Title Financial System in Poland

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EXECUTIVE SUMMARY

1. In the period 1945-1989, Poland constituted a typical centrally planned economy. Its inherent inefficiency brought about, among others, lowering of incomes and growing poverty, permanent shortage of basic goods and services, external imbalances and hidden inflation. Economic problems, along with limited freedom and democracy caused social tensions, which contributed to many political crises. Ultimately, after the Round Table Talks (February-April of 1989) and the first semi-free parliamentary election (June of 1989), Poland was the first Central European country to start thorough institutional and economic reforms. The introduction of the democratic system, the transition from the state-controlled economy to the free market one, and the undertaking of far-reaching, drastic in some cases, reforms have been the driving force behind the new Polish economy.

2. The basis for the economic transformation had been the so-called Balcerowicz plan, which came into effect on January 1st, 1990. The plan, strictly monetarist in character, included three main tasks: (1) to reduce inflation, in order to stabilize monetary conditions and to introduce convertibility of the Polish zloty; (2) to set market mechanisms in motion and thus to abandon the methods and principles of central planning and (3) to privatize the economy. All the tasks were realized immediately and simultaneously. Since 1992, the macroeconomic situation has been gradually improving, but social costs, in terms of growing unemployment, poverty and increasing inequalities within Polish society, have been higher than expected.

3. All the Polish governments after 1989 conducted economic policy on the same premises. These drew from mainstream macroeconomics including the so-called New Macroeconomic Consensus. In effect, Polish economic policy since transformation has been rather liberal and oriented towards market reform. At first sight, in the classification of Hall and Soskice (2001), Poland should be counted as a liberal market economy (LME). However, due to the existence of many features of coordinated market economy (CME), Poland might be better classified as a hybrid (Mediterranean) model. This reflects certain features of Poland’s economy such as the
large scope of the public sector, the extensive involvement of the government in the economy, rather high level of administrative burdens for enterprises, intense protectionism, dominance of small firms and single proprietorships, and a relatively high level of social protection. At the same time in Poland there are moderate levels of employment protection, decentralized wage-bargaining, low levels of coordination, generally non-confrontational relations between managers and workers, and drastically high and still increasing inequalities of wages, which are typical for the LME countries.

4. Before 1989 the financial system in Poland hardly existed. With a lack of markets and an effective price mechanism, money existed just as an unit of account and only to a limited extent as a means of payment. The financial system consisted then only of the banks, acting under non-market rules, with all significant parameters determined by the government. There were no other types of financial intermediation (only one, state-owned, insurance company) nor other financial markets than the loan-deposit one. Thus, the Polish financial system had to be created from near zero.

5. Since the beginning of the transition in 1989, the institutional structure of the Polish financial sector features the dominant position of the banking sector. It is a natural consequence of accepted sequence of changes: when other types of financial intermediaries were created, banks had already been well rooted in the market. Banks are the largest financial intermediaries in Poland and play a predominant role in financing the needs of the real sector of the economy transferring non-financial sector’s deposits into credits. However, since the mid 1990s, a significant growth in the assets of non-bank financial institutions has been observed. The main reason for this increase, apart from growth of prices of stocks, was the development of the capital part of the pension system (in 1998).

6. A natural consequence of nearly fifty years of a non-market reality, central management and a closed economy (until the end of 1980s Poland remained out of worldwide trends of globalization, internationalization and deregulation) is the relatively low potential (small size and funds) of financial institutions and scale of their
activity. Almost all the measures of financial activities and development of financial markets (assets of financial institutions, loans and deposits with reference to GDP, level of private and public debt, capitalisation of the stock exchange, etc.) exhibit levels significantly lower than in countries with mature market economy. Moreover, even among other emerging markets there are countries (e.g. Hungary, Czech Republic) with higher scale of financial intermediation than Poland.

7. Taking it into account, there is little to say about financialisation in the Polish economy. At first sight, when one analyses the levels of the basic financial categories and variables, compared with the countries of the eurozone, not to mention USA or Japan, there is rather a need for further developing financial system. However, a closer look at the development of financial institutions and changes in the main financial data reveals a much more ambiguous picture. The dynamics of financial categories are worthy of special attention. The assets of the financial sector amounted to about 20% of GDP in 1991, to about 50% in 1995, whereas in 2011 it already exceeded 120% of GDP. Employment in the financial sector also rose, independently of rather unfavourable conditions in the labour market. Its share in total employment increased to nearly 10% in 2010, growing even during the global financial crisis. Moreover, the following increased significantly also:

- capitalisation of the Warsaw Stock Exchange – from only PLN 161 million (about 3% of GDP) to its peak of more than 1 trillion in 2007 (about 90% of GDP);
- debt of public sector – within the years 2007 to 2011 it rose by more than 50% – from PLN 527.4 billion to 815.3 billion. At the end of the first quarter of 2012 the debt amounted PLN 554 billion, increasing year to year by almost 14% [NBP 2012];
- the ratio of households loans to GDP – from approximately 7% to 31%, while for the group of euro area countries it rose from 39% to 48%;
- debt of domestic and foreign enterprises – in 2004 total liabilities of enterprises amounted to PLN 528.3 trillion and in 2011 it reached 739.6 trillion.
8. Thus, although financialisation did not constitute an important issue in the Polish economy so far, it can be seen that situation begins to change. If the dynamics of changes would be as large as it has been recently, one may expect the supremacy of finance to develop also in the Polish economy, with all consequences of such situation.

9. Competition in the Polish financial sector and its subsectors is relatively modest. This reflects the low level of financial intermediation in Poland and the relative underdevelopment of the finance sector. Many households and enterprises still use only basic financial products and services. Another reason for the not so intense competition between financial institutions is the prevailing role of commercial banks. They dominate within the system, having the largest financial potential, resources, technology, human capital and experience. Moreover they control many other groups of financial intermediaries. Competition among banks themselves also has been rather moderate. Nevertheless, there are slight signs of growing competitive pressure.

10. Commercial banks have had a good performance during the recent years. This resulted from lower net charges to specific provisions, higher interest and fee income, good performance of the banks’ subordinate companies, reduction in the tax burden and increasing the loans to non-financial customers, mainly residential loans to individuals, and enhancing their quality. Most of the profitability and efficiency ratios have improved since 2001. It is important to note that the global financial crisis did not affect negatively the profitability of the Polish banking sector. Rate of return on assets (ROA) and rate of return on equity (ROE) indicators declined, but they still remained higher than in other Central and Eastern European Countries (CEECs). Due to focusing on core credit-deposit activity, the Polish banking sector in 2007-2010 appeared to be more stable than banking sectors in advanced European economies.

11. An obstacle hampering development of the financial sector in Poland has been the low level of financial knowledge. Many people do not know and barely understand simple economic phenomena and links between them. Therefore they can-
not figure out how to behave in free market economy and in modern financial system and they lack knowledge of saving and investing. This is a hangover from the old system of centrally planned economy, reinforced also by unsatisfactory financial education, affecting negatively the level of financial competences of the whole society, thus enlarging the number of those unable to access financial services.

12. Issues of inequality are almost entirely absent in research and discussion on the Polish financial system. Inevitably, this is a consequence of the lack of suitable data. Only some basic research has been conducted, mainly of a quantitative character, dealing with simple financial categories and phenomena (structure and ownership of the financial system, legal and technical frameworks, costs and profits, etc.). Gender, ethnical or minority issues are not so far raised. However, that applies not only to the financial sector, but to almost all sectors of the Polish economy.

13. The entry into the European Union (EU) on May, 1, 2004 did not change significantly the institutional and regulatory frameworks, as the de facto integration had, to a large degree, already been made. The integration process moved along with the transformation of the economic and political system. Moreover, since the very beginning of the transformation process, financial institutions from the EC/EU were present in the Polish financial system, being one of the most active investors in the process of privatization. Thus, many links with the financial systems in other EU countries were already established, even prior to Poland’s formal accession to the EU.

14. Since the beginning of the economic transformation, the Polish financial sector has been the subject of a deep restructuring, privatisation and consolidation, leading to the increase of competition. This is especially evident in the Polish banking sector. Substantial changes in the ownership structure of this sector occurred as a result of the privatisation of large state-owned banks, started in 1991. The privatisation was expected to contribute to the modernisation of management methods and technology, as well as to ensuring the access to new capital, raising the effectiveness of banks and thus increasing their competitiveness. Such results were in principle achieved, but a consequence of privatisation is a large share of foreign capital.
in the financial (mainly banking) sector, ambiguously assessed in the domestic liter-

ature.

15. The onset of the global financial crisis did not directly influence Poland. Po-

land avoided heavy losses brought about by the global financial crisis. Some prob-
lems occurred and the growth rate was lower, but still the Polish economy func-
tioned well, especially when compared to other European countries. No financial
institutions were bankrupted, and there were no drastic tensions in the financial
market. There are five points that explain this relatively good performance:

- the Polish economy has a relatively large internal market and is less open in
  comparison to other EU economies. It is also characterised by a relatively
  high level of diversification (among other things, no large enterpris-
  es/conglomerates which decide about the development of the whole economy)
  and by a high degree of flexibility among domestic firms that helped them to
  adapt to difficult external conditions;

- high investment outlays made by the public sector played an important stabi-
  lizing role. These replaced the reduction of investment by the private sector.
  The reduction of personal income tax rates and high indexation of pension
  benefits, and the earlier lowering of the pension contribution acted in a simi-
  lar manner. These actions have helped to sustain internal demand;

- the floating exchange rate helped to absorb the external shocks – a decline in
  orders was largely offset by higher proceeds resulting from the weakening of
  the zloty, and growth in orders due to the increase in the competitiveness of
  Polish exports. Thus the exchange rate acted as a “buffer”, protecting the
  economy from a decrease of demand;

- due to the aforementioned relatively low development and rather local char-
  acter of the financial market, the banking sector did not suffer large losses in
  foreign markets that required the involvement of public funds. At the same
  time, parent companies did not withdraw funding and household deposits ex-
  perienced strong growth;
• a reason closely connected with the previous one, is the generally lower scale of financialisation in Poland. There hardly exists on the domestic market sophisticated financial instruments, securities etc. Investment banks and large, global investment funds also do not function within Poland. Demand for financial services, formulated by the households and enterprises is limited rather to traditional loans, accounts and settlements. Thus, somewhat paradoxically, this relative underdevelopment turned out to be benefit for the Polish economy.

16. The monetary policy has been of special importance after 1989, whereas fiscal policy has been relatively less exploited. Moreover, fiscal policy was perceived as rather less important. It resulted from both ideological and factual premises. Consecutive changes in frameworks, principles and instruments of monetary policy made it consistent with the so-called New Monetary Policy Consensus. The last step towards the consensus was adopting the direct inflation targeting (DIT) strategy and switching to a floating exchange rate regime in 2001. The direction of changes has been perceived in the Polish literature as correct. Such a statement is confirmed by plain facts: decreasing of the inflation rate from circa 650% in 1989 to 1.4% in 2006 and avoiding – as one of only a few countries in Central and Eastern Europe – currency and financial crisis. However, the general assessment of monetary policy cannot be so obvious. The question arises whether focus on price stability was in fact beneficial or it was rather harmful, generating avoidable economic costs in terms of unemployment and lower economic growth. Moreover, the restrictiveness of monetary policy generated social costs, mainly in the first stage of transformation, creating a climate of distrust and limited confidence in policymakers decisions. Simultaneously, the coordination between monetary and fiscal policy was insufficient, generating inconsistencies and conflicts between the both policies.

17. The macroeconomic policy did not change significantly since the global financial crisis. Monetary policy still focused on price stability, conducting inflation targeting strategy (but with more attention paid to financial stability) and influencing short term interest rates. The NBP has been trying to manage liquidity of banks by
offering some additional forms of refinancing and investing potential surpluses. Fiscal policy, on the other hand, relaxed shortly before the onset of the crisis, was rather strict during the crisis.
1. **Historical, political economic and international background**

As a result of political agreements, after World War II Poland was included in the communist bloc and broke most of its economic links with non-communist countries. The Polish post-war economy was reconstructed in a Soviet way, becoming a socialist, centrally managed economy, with emphasis put on nationalization, collectivization and development of heavy industry. All the political powers were held by the Polish United Worker’s Party (Polska Zjednoczona Partia Robotnicza – PZPR) that controlled all aspects of political, cultural and economic life.

With time, such a centrally planned economy continued to be less and less effective. Its inherent inefficiency brought about, among others, lowering of incomes and growing poverty, permanent shortage of basic goods and services, external imbalances and hidden inflation. Economic problems, along with limited freedom and democracy caused social tensions, which contributed to many political crises and social protests against the Party and its politics. The turning point was the rise of Solidarity, a working class movement of protest against the austerity policies of the PZPR in the late 1970s.

The 1980s started with the initially successful confrontation of Solidarity (supported also by intellectuals) with the regime. It however ended with the imposition of martial law in Poland. The opposition was actually suppressed, but that did not eliminate any of the economic and social problems. All attempts to recover the economy and improve the performance of the socialist system by partial and modest reforms failed. Eventually, even the regime itself officially acknowledged the situation as an economic crisis.

The growing scale of the crisis was one of the main factors contributing to profound political changes in Poland. The PZPR realized, however, that it had lacked the legitimacy to carry out inevitable large-scale reforms. Therefore it attempted to

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1. According to Wilczyński [1992], the Polish economy should be characterized – with reference to Eucken (1965) – rather as “centrally managed”, not as a “planned” one. Its distinctive feature was rather direct, day-to-day management of economic phenomena by the Party and government, instead of commitment to a plan.

2. For more detailed characteristics of the Polish economy and society within the period 1945-1981 see for example Łukowski and Zawadzki [2001], Zamojski [1993], Davies [1982], Shen [1992], Landau and Tomaszewski [1985], Simon and Kanet [1980], Kenney [1997].
acquire at least some support from the opposition side. From February till April of 1989 Round Table Talks between the government and the opposition took place, concerning, among other things, economic issues. It allowed for a peaceful transition of political power to the democratically-elected government. Briefly after the negotiations, in June of 1989, the first semi-free parliamentary election was conducted. As a result of the Civic Committee’s election victory Poland was the first Central European country to start thorough institutional and economic reforms. The introduction of the democratic system, the transition from the state-controlled economy to the free market one, and undertaking thorough, drastic in some cases, reforms have been the driving force behind the new Polish economy.

The basis for the economic transformation had been the so-called Balcerowicz plan, which came into effect on January, 1, 1990. The plan included three main tasks. The first one was to reduce inflation, in order to stabilize monetary conditions and to introduce full convertibility of the Polish zloty. It was aimed at restoring the role of the zloty as a national currency after a long period of informal dollarization. The second task was to set market mechanisms in motion and thus to abandon non-market methods of regulating the economy and the principles of central planning. The third task contained a rapid privatization of the Polish economy, perceived as a main form of its micro-economic organisation and thus creation of a background for effective decision making at the level of individual firms (Wilczyński 1992).

The Balcerowicz plan was, by no means, strictly monetarist in character: monetary conditions and the growth of the money supply were at the very centre of it. It also assumed both monetary and fiscal policies being restrictive and influence of the government over the economy being strictly limited. This new plan resulted,
among other things, in the liberalization of domestic prices, in the reduction of pay controls in state enterprises, harder financial and budgetary policy towards the existing companies, and significant reduction of social benefits and budget subsidies. Moreover, all the task were realized immediately and simultaneously and they had dramatic effects on citizens [rapid decline in standard of living, much lower incomes and growth of uncertainty]. For this reason, it was perceived as the typical example of "shock therapy".  

The initial results of the Plan were rather disappointing. However, since 1992 the macroeconomic situation has been gradually improving. Gross Domestic Product increased (Figure 1). The rate of inflation decreased significantly and the Polish currency was perceived as relatively stable and worth holding on to. The monetary and financial systems, as will be presented below, already functioned just like in developed market economies. Still, high levels of unemployment constituted a serious problem (see Figure 2). Moreover, social costs, in terms of growing unemployment, poverty and increasing inequalities within Polish society, have been higher than expected (Milanovic 1991).

![Figure 1. Growth rate of GDP in Poland, 1991-2011 (%)](source: GUS [2012].)

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6 More detailed discussion of the Balcerowicz plan, circumstances that stood behind preparing it, its implementation and its effects is far beyond the scope of the report. For more detailed analysis see e.g. Sachs [1993], Wilczyński [1995] and Kotodko [1992].
The symbolic point and proof that the main part of economic transformation had ended, that the market economy had been established, and that monetary stability had been restored, was the introduction of the New Polish Zloty (Polski Nowy Zloty – PLN) in 1995. Another milestone, concluding in a way another stage of development and confirming the international position of Poland, was entering the European Union (EU) in 2004. However, in many areas and branches of the economy, the situation is still far from satisfactory. According to some authors transformation has not been completed and further changes are necessary, especially with reference to quality of institutions, legal arrangements and models of behaviour (see e.g. Battowski and Miszewski 2006, Woźniak 2012).

![Figure 2. Inflation and unemployment, 1991-2011](image)

Source: GUS (2012).

Nevertheless, Poland has been often pointed out as the example of a successful transformation and evidence of an appropriate stabilization program. But assessments of the Balcerowicz plan are very diverse. Detailed discussion of this issue is beyond the scope of this report. In short, supporters of the Polish variant of shock therapy argue that it allowed the economy to be more balanced and pushed it onto the path of fast economic growth. In their opinion, without the shock therapy that

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7 One New Polish Zloty amounted to 10000 of Polish zlotys.
sacrificed short-term gains for long-term growth, modern Poland would be a much poorer country, with unstable currency and weak institutional frameworks (see Balcerowicz 1992, Gomulka 1993, Wilczyński 2000, Kowalski 2010).

On the other hand, opponents of the Balcerowicz plan criticise it as being too restrictive and too far reaching in the scale of adjustment. They stress its heavy social costs: unemployment, one of the highest in post-communist countries, exclusion of many social groups from the benefits of transformation\(^8\) and increasing inequalities within the Polish society (see: Hardy 2009, Kowalik 2009, Tittenbrun 1993, Kiezun 2012, Kotodko 1993, Rosati 1993, Hunter et al 1994).

Apart from those disagreements, it is indisputable that the very construction and features of the Balcerowicz plan (mainly the ideology that stood behind it) influenced the economic system in Poland after 1989. As one of the first transformation packages based on the so-called Washington Consensus it was rather neoliberal in character. Its strong market-based approach was shared and supported by the then politicians and decision-makers.\(^9\) Moreover, all the subsequent governments conducted economic policy in a very similar way and based on the same premises. These drew from the mainstream economics, mainly monetarist and then, with the progress in macroeconomic theory, based on the principles of so-called New Macroeconomic Consensus or New Neoclassical Synthesis.

In effect, Polish economic policy since transformation has been rather liberal and oriented towards market reform. At first sight, in the classification of Hall and Soskice (2001), Poland should be counted as a liberal market economy (LME). However, due to the existence of many features of coordinated market economy (CME), Poland might be better classified as a hybrid (Mediterranean) model. This reflects certain features of Poland’s economy such as the large scope of the public sector, the extensive involvement of the government in the economy, rather high level of administrative burdens for enterprises, intense protectionism, dominance of small firms and single proprietorships, and a relatively high level of social protection. At

\(^8\) Somewhat paradoxically, the social group whose situation got radically worse were workers, who started deconstruction of the regime (for more see Ost 2005).

\(^9\) The open question which remains is the attitude of the Polish society that was rather mix.
the same time in Poland there are moderate levels of employment protection, de-centralized wage-bargaining, low levels of coordination, generally non-confrontational relations between managers and workers, and drastically high and still increasing inequalities of wages, which are typical for the LME countries.

Thus, a precise classification is a rather hard task and needs much more thorough research than possible in this report. But of special importance is that Poland, with so many features of a LME, has a bank-based financial system, not a market-based one. Adoption of such institutional arrangements resulted from political choice made in the very beginning of the transformation. The idea to establish in Poland a bank-based financial system was further reinforced by direction and timing of other institutional changes. It was often argued that such a system suits better the national culture and features of Polish society and, simultaneously, is consistent with historical experience. (Knakiewicz 1992, Jaworski 1996).

Without any doubt, the establishment of a modern financial system, adjusted to conditions of a market economy, was perceived as one of the most important factors influencing the transformation process. In turn, adequate changes within the financial sector had been seen as crucial for the success of the overall stabilization program. At the same time, such a task seemed to be extremely hard as the financial system before 1989 hardly existed. In the socialist economy, money and financial system were denounced as purely capitalistic devices. With a lack of markets and an effective price mechanism, money existed just as an unit of account and only to a limited extent as a means of payment. In the latter function and in the function of a store of value, Polish zloty was replaced (unofficially) by the Deutsche mark and US dollar.

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10 Separate problem constitute some specific processes, features and factors typical for post-communist countries, e.g. models of behaviour, low level of social capital, culture of distrust, etc.
11 However, it must be stressed that – due to rather complicated history and prolonged periods of lost sovereignty in the past – building of the homogenous national financial (and monetary as well) system was an extremely hard task.
12 Lack of confidence in Polish currency was, among other things, a consequence of currency reform of 1950 that actually turned to be simply the confiscate of a huge amount of private savings. Since then, citizens were deeply suspicious to government’s actions.
Under the rule of the Communist Party, the financial system in Poland was poorly developed. In fact, it consisted only of the banking system. Apart from banks, there was only one state-owned insurance company – Polish Insurance Company (Polski Zakład Ubezpieczeń – PZU). No other types of financial intermediation existed nor other financial markets than the loan-deposit one. Moreover, even banks acted under the non-market rules, with all significant parameters (interest rate, exchange rate, credit restrictions, etc.) determined by the government.

During the years 1946-1982 predominant in Poland was the so-called monobank system, typical for communist countries with centrally planned economies. In such a system privately-owned banking institutions did not exist. At the same time state-owned banks were highly specialized, in principle not offering services to society. They just realized strictly government plans and decisions. The National Bank of Poland (NBP) acted as the main actor in the financial market. Apart from its activity as the subject of monetary policy, it made loans, accepted deposits and conducted payments and settlements.

The transformation of the Polish financial system started even earlier than the overall systemic change. Moreover, changes in the domain of finance were much deeper and complex than in other subsystems of the economy. The first partial attempts to rebuild the banking system were made in 1982, but more profound changes within the banking system were enforced at the end of January, 1989 (that is, even before the Round Table Talks). Two new acts were passed then: Banking Law that determined the creation and functioning of commercial banks, and the Act on the National Bank of Poland, redefining the role and responsibilities of the Polish central bank. Both acts made it possible to form a two-tier banking system, typical of market economies. Building such a system, consisting of universal instead of specialized, banks was recognized as the fundamental objective of banking reform.

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13 Some consequences of this underdevelopment seem to last even until now.
14 However, according to Kokoszczyński (2006), in the Polish banking system a classic example of a monobank had never existed. There were, as it will be described, few so-called specialized banks, formal monopolists in particular fields of banking activity (e.g. foreign currency operations or agriculture).
15 Some financial services for the society were offered by cooperative banks. Form its very nature, however, and rather small potential, scale of their activity was rather limited.
At the same time nine commercial banks were created. Those new institutions had capital excluded from the regional branches of the NBP that ceased to make financial services for households and enterprises. At the same time all existing forms of by-operator and by-business-type constraints were lifted and clients became free to choose their banks and shape their relationship with banks on the contract basis. Another important step was the liberalization of the terms of entry into the banking system. Broad opportunities were provided for potential – domestic and foreign – investors to run banking activities in Poland, especially very mild license policy – legal barriers to create a bank were relatively small. As a result, in 1991 already 72 commercial banks functioned in the Polish market.

In the next stage, as it will be further described, the capital market and other segments of financial intermediation were established. Commercial banks were already well rooted in the market. An obvious consequence of such sequence of changes was dominant position of banks in the Polish financial sector since the very beginning of transformation (see Figure 3). Supremacy of banks eroded in subsequent years, but, rather surprisingly banks restored their position during global financial crisis.

16 In 1989 initial capital required for establishment of new bank amounted only circa one million of USD.
17 There was only one bank with dominant foreign capital. However, the situation changed very fast and foreign investor started to prevail within the banking system (more in Section 3).
18 It will be further discussed in the Section 16.
The availability of domestic capital at the beginning of transformation was negligible. Thus, the foundation of the financial system could not have been possible without the broad involvement of foreign investors, mainly from the EU countries and the USA. They participated actively in the process of privatisation of the Polish banks and insurance companies.

With the strengthening of the Polish economy and currency, Poland opened up to trade and economic relationships with other countries. Until 1989 the main partner was of course the Soviet Union and other countries of ‘Comecon’ (CMEA, Council for Mutual Economic Assistance). The volume of trade and capital flows between Poland and non-communist countries was limited due to many reasons, both political and economic ones. Thus, globalization and internationalization processes did not influence the Polish economy, which was then relatively closed, especially to the capitalist countries.\footnote{In 1970s relations with Western countries intensified, but it amounted just to borrowing money in order to finance large investment conducted by the then government (which turned to be ineffective} The situation changed after 1989. Foreign capital entered the
Polish market. It acted in many branches of economy, actively participating in the privatization process. Increasing openness of the Polish economy is illustrated in Figures 4 and 5.

**Figure 4. Foreign investments in Poland, 1995-2010**


**Figure 5. Export and import in Poland, 1995-2010 (as a % of GDP)**


and did not create any significant results in categories of higher competitiveness of the Polish economy).
With progress on reforms, greater macroeconomic stability in Poland fostered the inflow of foreign investors. One of the most intense processes was massive internationalization of the financial sector – mainly commercial banks and insurance companies, as will be further described below. But it must be noted that Poland is still a country with a chronic scarcity of capital. Its International Investment Position (IIP) is permanently negative since the very beginning of the transformation (NBP 2012).

---

20 Inflow of foreign investments accelerated after Poland’s accession to EU (see section 15).
2. The growth in finance and its role in the decades of financialisation

A natural consequence of nearly fifty years of a non-market reality is the relatively low potential (small size and funds) of financial institutions and scale of their activity, as well as the relative small size of individual parts of the financial market in Poland. It is a common feature of Poland and other economies of the region, having the same track record of socialism, central management and closed economy (all the communist countries until the end of 1980s remained out of worldwide trends of globalization, internationalization and deregulation).

Almost all the measures of financial activities and development of financial markets (assets of financial institutions, loans and deposits with reference to GDP, level of private and public debt, capitalisation of the stock exchange, etc.) exhibit levels significantly lower than in countries with mature market economy. Moreover, even among other emerging markets there are countries (e.g. Hungary, Czech Republic) with higher scale of financial intermediation than Poland. (see Table 1).

Table 1 Financial system assets in selected CEECs in 2002-2010 (as a % of the GDP)

<table>
<thead>
<tr>
<th>Country</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Czech Republic</td>
<td>118.6</td>
<td>114.7</td>
<td>119.3</td>
<td>126.7</td>
<td>125.6</td>
<td>134.3</td>
<td>137.3</td>
<td>138.4</td>
<td>136.0</td>
</tr>
<tr>
<td>Hungary</td>
<td>87.7</td>
<td>99.3</td>
<td>100.0</td>
<td>114.9</td>
<td>128.5</td>
<td>141.4</td>
<td>152.3</td>
<td>165.0</td>
<td>162.0</td>
</tr>
<tr>
<td>Poland</td>
<td>74.8</td>
<td>78.5</td>
<td>78.6</td>
<td>85.0</td>
<td>96.5</td>
<td>103.1</td>
<td>110.3</td>
<td>111.0</td>
<td>117.6</td>
</tr>
</tbody>
</table>


The volume of traded derivatives and other “sophisticated” securities was also relatively low. Generally speaking, the variety and supply of financial instruments was rather modest – traditional financial products and services (accounts, loans, payment cards, money transfers) dominated. For instance, the first structured products were offered in 1996, first Forward Rate Agreement contracts in 1998, and then Interest Rate Swaps – in 1999 (NBP, 2002). The situation changed slightly with the greater openness of the Polish economy, but still financial engineering has not constituted a serious challenge. This means that Polish banks are rather conservative
and do not undertake risky financial operations with the use of derivatives. They do not offer complex derivative structures to their clients as well. On the other hand, research revealed that about 40% of citizens still do not use even typical banking products. A noticeable large part of them do not even have a bank account, preferring to use cash. It is even said that a part of the Polish society is permanently “financially excluded”. (See more in Section 8)

From this point of view there is little to say about financialisation in the Polish economy. At first sight Poland lags behind other countries. However, the dynamics of financial categories are worthy of special attention here. A closer look at the development of financial institutions and changes in main financial data reveals a much more ambiguous picture. Figures 6 and 7 present a continuous increasing trend of financial assets in Poland, from the very beginning of the transformation. The assets of the financial sector amounted to about 20% in 1991, whereas in 1995 it was already about 50%, and in 2000 about 70% of GDP. Higher assets of banking institutions, as well as fast development of non-banking financial intermediaries contributed to this increase. The trend continued also in the next decade, when financial assets in relation to GDP nearly doubled (Figure 7). Surprisingly, even the global financial turmoil did not affect negatively (with some temporary exceptions – mainly investment funds in 2008) Polish financial institutions.

---

21 Development of the individual institutions and markets will be characterized in the next section.
Figure 6. Assets of main types of financial institutions in Poland, 1993-2011 (PLN billion)


Figure 7. Pace of financial assets growth in relation to GDP in Poland, 2002-2011 [%]

Apart from assets, employment in the financial sector also rose. The share in total employment of the FIRE (finance, insurance and real estate) sector increased to nearly 10% in 2010 (Figure 8). This growth occurred despite rather unfavourable conditions in the labour market. Even within the period 2008-2010, i.e. during the global financial crisis, employment in finance increased, whereas in the overall economy the unemployment rate rose by about 3 percentage points (see Figure 2 above).

![Figure 8. Employed in finance sector as a % of total employed, 1995-2011](source: OECD database.)

In the same period the relation of banking loans and deposits to GDP (Figure 9) also increased. Moreover loans reached their highest level ever, growing since 2007 by more than 20 percentage points. Also visible, but not so impressive, was the growth of banking loans. Thus, 2009 was the first year in which loans constituted a higher share of GDP than bank deposits.
In addition to the last few years, both categories of loans and bank deposits increased, particularly within the years 1997 to 2003. Though both of them remain at relatively low level, their growth is remarkable, especially when one takes into account the growing variety of alternatives to bank deposits mainly investment funds and credit unions and borrowing funds (factoring and leasing companies and, again, credit unions).

Having a bank-based financial system does not preclude having a strong capital market in the country. This is the case in Poland, where nearly all the period of transformation is marked by the quantitative and qualitative development of Warsaw Stock Exchange (WSE). It was restored in 1991 and nowadays is the largest national stock exchange amongst the CEE countries and one of the fastest-growing exchanges in Europe, offering a wide range of products and services within its trading markets of equity, derivative, fixed income and structured products. Development of the WSE is shown in Figures 10 and 11.

---

22 Investment funds collected in 2010 circa PLN 75.7 billion, whereas credit unions – circa 13 billion.

23 Polish capital market traditions go back to 1817, when the Warsaw Mercantile Exchange was established.
It follows that capitalisation of the WSE increased significantly, from only PLN 161 million (about 3% of GDP) to its peak of more than 1 trillion in 2007 (about 90% of GDP). Then, after a rapid decrease as stock market prices fell, it slowly rose to reach a level it had before the crisis (Fig. 10). Since 2002 the measure of capitalisation has included foreign companies listed on the WSE and, what is interesting, their capitalisation after 2007 indicates an inferior capitalisation level and pace of growth, than domestic companies.

![Figure 10. Warsaw Stock Exchange capitalization, 1991-2012 (PLN billion)](source)


The growth of capitalisation was due to the increasing number of listed companies. At the inaugural first trading session on the WSE that took place on April 16, 1991, only five companies were listed and seven brokerage houses took part in trading. In 2011 the number of listed companies exceeded 400 on several markets (see subsection 3.3.2). Only the years of 2002 and 2003 were marked by an outflow of companies from the WSE.

---

24 The total turnover during the session was around $2,000, with 112 orders to buy and sell.
An important feature of the Polish financial market is also growing debt of both public and private sectors. The former, altogether with balance of general government sector,\textsuperscript{25} is presented in Figure 12. The general government debt in relation to GDP is still lower than the average in the European Union, but it has grown extremely fast in the last few years. Within the years 2007-2011 it rose by more than 50\% – from PLN 527.4 billion to 815.3 billion.\textsuperscript{26} One of the factors contributing to such a tendency was the global financial crisis and its consequences, as it will be further described in the report. In consequence, the borrowing needs of the government have been one of the most important factors influencing the situation in the financial market.

Continuous and growing deficits of the government in consecutive years (Figure 12) had to be financed with issuing of Treasury securities, purchased by foreign investors and domestic financial institutions – mainly banks and open pension funds. It influenced to a large degree credit market and accessibility of credit, as banks were rather reluctant to make loans to the private sector, as they had opportunity to

\textsuperscript{25} It must be stressed that all considerations concerning public finance in Poland must be treated with some reserve, due to many changes in methodology of debt and deficit and so-called "creative accounting" on the side of Ministry of Finance, which has been trying to avoid constitutional limits of debt.

\textsuperscript{26} In 2012, September the general government debt exceeded already more than PLN 860 billion.
buy profitable, riskless treasury securities. Thus, the share of those securities in banks’ portfolios remained relatively high.

Figure 12. Debt and deficit of the general government sector in Poland, 1995-2011
Source: ESA, Ministry of Finance website.

The debt of the private sector has also grown. It concerns both enterprises and households. Debt of the latter at the end of the first quarter of 2012 amounted to PLN 554 billion, increasing year to year by almost 14%. (NBP 2012). In 2000 total liabilities of Polish households amounted to only circa PLN 52 billion. Interestingly, in the period preceding the beginning of the global financial crisis, the growth rate of household debt in Poland (and other new EU members as well) was higher than the average growth rate for eurozone countries. It resulted from the expansion of international banking groups in the markets of host countries and a large demand for loans, supported by expectations of a continued high economic growth rate. As a consequence, from 2004 to 2010, the ratio of households loans to GDP increased in Poland from approximately 7% to 31%, while in the group of euro area countries it rose from 39% to 48% (Financial Stability Report, 2011).

Debt of enterprises, domestic and foreign, also increased. In 2004 total liabilities of enterprises amounted to PLN 528.3 trillion and in 2011 it was already 739.6
trillion. At the end of 2010 loans granted to enterprises by domestic banks amounted to PLN 204 tn, while Polish enterprises’ foreign debt amounted to PLN 378 trillion. However, ratio of enterprise debt to GDP in Poland is still lower than in other EU countries. Moreover, the value of bank loans to enterprises is also low in relation to the size of the economy. At the end of 2010, loan liabilities of enterprises were equivalent to approximately 35% of GDP in Poland, i.e. relatively lower than in the Czech Republic (40%) or in the euro area (90%). Additionally, in 2009-2010, enterprises in Poland limited their debt with respect to the domestic banking sector. Other funding sources (e.g. leasing, trade credit) became more important, particularly in the case of large enterprises. But since January 2011, the value of loans granted to enterprises again started to grow (Financial Stability Report, 2011).

Bringing it all together, one may observe that financialisation did not constitute an important issue in the Polish economy so far. The levels of presented in the section basic financial categories and variables, compared with those characterizing countries of the eurozone, not to mention the US or Japan, are rather moderate, if not low. Nevertheless, situation appears to change. If the dynamics of changes would be as large as it has been recently, one may expect the supremacy of finance to develop also in the Polish economy, with all consequences of such situation. Open issue remains, however, whether changes in the scale of financial operations and growing potential of financial intermediaries will be followed by changes in attitudes and schemes of thinking of the Polish citizens.
3. The structure of the financial sector in Poland

3.1. Polish financial sector – a general overview

As it was already mentioned, the modern financial sector has been developing in Poland since the beginning of the 1990s. The first to develop was the interbank deposit market. The next to develop was the Treasury bill market. The introduction of partial convertibility of the Polish zloty in 1994 resulted in the emergence of the FX market. The stock exchange was developing simultaneously with the interbank market, mainly as a result of privatization.

The institutional structure of the Polish financial sector features, as it was stressed, the dominant position of the banking sector. Since the beginning of the transformation, the banking industry has been dominant in the financial sector in Poland. Although the banking system existing before 1989 was adjusted to function within the centrally-managed economy, banks still had appropriately qualified staff. In contrast, institutions in the capital market were created only after 1990. However, since the mid-1990s, a significant growth in the assets of non-bank financial institutions had been observed until 2008. In that year, due to the stock market crash, a significant fall in assets of investment funds and 'open pension' funds was observed. Since 2008 these institutions once again have started rebuilding their assets [Narodowy Bank Polski 2010, 2011b, 2011c], despite the turmoil observed worldwide again in 2011. The volume of assets and number of financial institutions operating in Poland are presented in Tables 2 and 3.

The data presented in Table 3 reflect the concentration process. The phenomenon was particularly visible in the banking sector, with the process of consolidation being extremely strong in the cooperative banks sector.

Poland’s accession to the European Union in 2004 was an important event from the standpoint of development prospects for the Polish economy, but did not have a significant impact on the size and structure of the financial sector because this system has been shaped by long-term processes, including Poland’s preparations for participation in the common market. Like other economies of the region, the Polish economy still exhibits a relatively low level of financial intermediation.
However, as it was mentioned in the precious section, the trend towards the growing significance of the financial sector has been pronounced.

Table 2 Assets of financial institutions in Poland in 1996-2011 (PLN billions)

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial and cooperative banks</td>
<td>197.1</td>
<td>247.7</td>
<td>318.7</td>
<td>363.4</td>
<td>428.4</td>
<td>469.7</td>
<td>466.5</td>
<td>489.0</td>
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<tr>
<td>Credit unions (SKOK)</td>
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<td>0.4</td>
<td>0.6</td>
<td>0.9</td>
<td>1.2</td>
<td>1.8</td>
<td>2.5</td>
<td>3.4</td>
</tr>
<tr>
<td>Insurance companies</td>
<td>8.1</td>
<td>13.2</td>
<td>20.7</td>
<td>28.9</td>
<td>37.9</td>
<td>48.0</td>
<td>57.5</td>
<td>65.7</td>
</tr>
<tr>
<td>Investment funds</td>
<td>1.4</td>
<td>1.9</td>
<td>1.8</td>
<td>3.1</td>
<td>9.5</td>
<td>12.1</td>
<td>22.8</td>
<td>33.1</td>
</tr>
<tr>
<td>Open pension funds</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>2.3</td>
<td>9.9</td>
<td>19.4</td>
<td>31.6</td>
<td>44.8</td>
</tr>
<tr>
<td>Brokerage houses</td>
<td>1.8</td>
<td>3.0</td>
<td>3.2</td>
<td>3.6</td>
<td>3.9</td>
<td>2.9</td>
<td>2.8</td>
<td>3.7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>208.6</td>
<td>266.2</td>
<td>345.0</td>
<td>402.2</td>
<td>490.8</td>
<td>553.9</td>
<td>583.7</td>
<td>639.7</td>
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<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial and cooperative banks</td>
<td>538.5</td>
<td>586.4</td>
<td>681.8</td>
<td>792.8</td>
<td>1039.1</td>
<td>1059.6</td>
<td>1158.5</td>
<td>1295.1</td>
</tr>
<tr>
<td>Credit unions (SKOK)</td>
<td>4.2</td>
<td>5.3</td>
<td>6.0</td>
<td>7.3</td>
<td>9.4</td>
<td>11.6</td>
<td>14.1</td>
<td>n/a</td>
</tr>
<tr>
<td>Insurance companies</td>
<td>77.9</td>
<td>89.6</td>
<td>108.6</td>
<td>126.9</td>
<td>137.9</td>
<td>139.0</td>
<td>145.1</td>
<td>145.2</td>
</tr>
<tr>
<td>Investment funds</td>
<td>37.5</td>
<td>61.3</td>
<td>99.2</td>
<td>133.8</td>
<td>73.9</td>
<td>93.4</td>
<td>116.5</td>
<td>n/a</td>
</tr>
<tr>
<td>Open pension funds</td>
<td>62.6</td>
<td>86.1</td>
<td>116.6</td>
<td>140.0</td>
<td>138.3</td>
<td>178.6</td>
<td>221.3</td>
<td>227.5</td>
</tr>
<tr>
<td>Brokerage houses</td>
<td>5.5</td>
<td>6.9</td>
<td>10.9</td>
<td>11.9</td>
<td>8.6</td>
<td>9.9</td>
<td>9.2</td>
<td>n/a</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>726.2</td>
<td>835.6</td>
<td>1023.0</td>
<td>1214.8</td>
<td>1407.0</td>
<td>1492.1</td>
<td>1664.7</td>
<td></td>
</tr>
</tbody>
</table>


Table 3 Structure of financial institutions in Poland in 1996-2011

<table>
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<tbody>
<tr>
<td>Commercial banks</td>
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<td>81</td>
<td>83</td>
<td>77</td>
<td>73</td>
<td>69</td>
<td>59</td>
<td>58</td>
</tr>
<tr>
<td>Cooperative banks</td>
<td>1394</td>
<td>1295</td>
<td>1189</td>
<td>781</td>
<td>680</td>
<td>642</td>
<td>605</td>
<td>600</td>
</tr>
<tr>
<td>Credit unions</td>
<td>168</td>
<td>198</td>
<td>220</td>
<td>228</td>
<td>146</td>
<td>144</td>
<td>120</td>
<td>109</td>
</tr>
<tr>
<td>Insurance companies</td>
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<td>54</td>
<td>56</td>
<td>66</td>
<td>71</td>
<td>72</td>
<td>76</td>
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<tr>
<td>Investment firms</td>
<td>5</td>
<td>10</td>
<td>14</td>
<td>15</td>
<td>21</td>
<td>17</td>
<td>19</td>
<td>16</td>
</tr>
<tr>
<td>Pension companies</td>
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<td>0</td>
<td>0</td>
<td>21</td>
<td>21</td>
<td>17</td>
<td>16</td>
<td>16</td>
</tr>
<tr>
<td>Brokerage houses</td>
<td>50</td>
<td>47</td>
<td>46</td>
<td>48</td>
<td>49</td>
<td>42</td>
<td>38</td>
<td>36</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>1739</td>
<td>1681</td>
<td>1606</td>
<td>1226</td>
<td>1056</td>
<td>1002</td>
<td>929</td>
<td>911</td>
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<tr>
<th>Institution</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
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<th>2009</th>
<th>2010</th>
<th>2011</th>
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<tbody>
<tr>
<td>Commercial banks</td>
<td>57</td>
<td>61</td>
<td>63</td>
<td>64</td>
<td>70</td>
<td>67</td>
<td>70</td>
<td>66</td>
</tr>
<tr>
<td>Cooperative banks</td>
<td>596</td>
<td>588</td>
<td>584</td>
<td>581</td>
<td>579</td>
<td>576</td>
<td>576</td>
<td>574</td>
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<tr>
<td>Credit unions</td>
<td>83</td>
<td>75</td>
<td>70</td>
<td>67</td>
<td>62</td>
<td>62</td>
<td>59</td>
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<tr>
<td>Insurance companies</td>
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<td>68</td>
<td>65</td>
<td>67</td>
<td>66</td>
<td>65</td>
<td>63</td>
<td>63</td>
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<tr>
<td>Investment firms</td>
<td>20</td>
<td>23</td>
<td>26</td>
<td>33</td>
<td>39</td>
<td>43</td>
<td>50</td>
<td>n/a</td>
</tr>
<tr>
<td>Pension companies</td>
<td>15</td>
<td>15</td>
<td>15</td>
<td>15</td>
<td>14</td>
<td>14</td>
<td>14</td>
<td>14</td>
</tr>
<tr>
<td>Brokerage houses</td>
<td>40</td>
<td>42</td>
<td>47</td>
<td>53</td>
<td>58</td>
<td>59</td>
<td>64</td>
<td>51</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>872</td>
<td>880</td>
<td>870</td>
<td>880</td>
<td>888</td>
<td>886</td>
<td>896</td>
<td></td>
</tr>
</tbody>
</table>

Despite the fact that the Polish financial sector is characterised by a low ratio of financial institutions’ assets to the GDP, the structure of the sector is similar to that in other new EU Member States. In all these countries the financial sector is dominated by monetary financial institutions. The dominant role of the banking sector in selected Central and Eastern European countries is shown in Table 4. However, the share of monetary institutions in the structure of the Polish financial sector is lower than in other new EU Member States. This is a result of a faster increase of the importance of non-banking financial institutions in Poland, as compared to the markets of other new EU Member States (National Bank of Poland 2007, 2009).

Table 4 Banking sector development in selected countries of Central and Eastern Europe (%)

<table>
<thead>
<tr>
<th>Country</th>
<th>Assets/GDP</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Czech Republic</td>
<td>99.0</td>
<td>93.5</td>
<td>98.9</td>
<td>97.5</td>
<td>105.4</td>
<td>109.1</td>
<td>112.9</td>
<td>114.2</td>
<td></td>
</tr>
<tr>
<td>Hungary</td>
<td>78.0</td>
<td>72.0</td>
<td>79.7</td>
<td>87.3</td>
<td>95.9</td>
<td>109.1</td>
<td>111.3</td>
<td>103.7</td>
<td></td>
</tr>
<tr>
<td>Poland</td>
<td>60.0</td>
<td>58.2</td>
<td>59.6</td>
<td>64.3</td>
<td>67.4</td>
<td>81.5</td>
<td>78.9</td>
<td>81.8</td>
<td></td>
</tr>
<tr>
<td>Loans/GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Czech Republic</td>
<td>32.0</td>
<td>32.5</td>
<td>37.6</td>
<td>43.2</td>
<td>50.3</td>
<td>52.2</td>
<td>53.9</td>
<td>54.7</td>
<td></td>
</tr>
<tr>
<td>Hungary</td>
<td>39.0</td>
<td>35.1</td>
<td>39.3</td>
<td>43.0</td>
<td>47.7</td>
<td>54.2</td>
<td>52.5</td>
<td>52.0</td>
<td></td>
</tr>
<tr>
<td>Poland</td>
<td>27.0</td>
<td>24.7</td>
<td>26.3</td>
<td>30.5</td>
<td>35.9</td>
<td>46.5</td>
<td>46.7</td>
<td>49.2</td>
<td></td>
</tr>
<tr>
<td>Deposits/GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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The Polish banking sector absorbs most of the financial surpluses accumulated by citizens and companies and funds most business projects. However, the ratio of assets of the banking sector to total assets of the financial sector is decreasing steadily. In 2007, this ratio decreased to 65.4% [in 2002 – 79.9%]. At the same time, the importance of non-banking financial institutions was growing steadily. In 2007, the ratio of non-banking sector’s assets to total assets of the financial sector rose to
34.6%. For the sake of comparison – in 1998 it was 7.6% (National Bank of Poland 2006b, 2010). This tendency was reversed in 2008, as a result of the global financial turmoil. Decline of prices of stocks, risk aversion and outflow of capital from the Warsaw Stock Exchange and from investment funds to safer banking deposits allowed the banking sector to increase its share in total assets of the financial sector to 73.8% (Narodowy Bank Polski 2010). However, since 2009, along with the rise of prices of stocks, risk aversion has declined and capital has started inflowing to investment funds once again. This in turn led to a further decrease of the ratio of banking sector’s assets to total assets of the financial sector. As a consequence, in 2010 the ratio of assets of non-banking sector to total assets of the financial sector went up to 30.4% (Narodowy Bank Polski 2011c).

The main reason for the increase of importance of non-banking financial institutions in Poland in recent years, apart from growth of prices of stocks, was the development of the capital assets of the pension system (see Section 6). The growth of prices of stocks increased the interest in investing savings in investment funds and unit-linked products. It also contributed to the increase in the value of the investment portfolio of non-banking financial institutions which, contrary to the banks, invest a significant part of their assets in stocks. The functioning of the reformed pension system was related to the constant inflow of funds to open pension funds. Moreover, interest in typically banking products gradually decreased for the benefit of other investment instruments, particularly those offered by investment funds (National Bank of Poland 2009).

The reform of the pension system implemented in 1999 undoubtedly contributed to a growing interest in savings with institutions other than banks. Pension funds appeared on the market, raising the demand for financial instruments. The development of investment funds also provided an alternative to the services offered by banks. The number of funds and their assets increased significantly. Due to changes in the saving habits of the public (a drop in demand for bank deposits), a further increase in the value of funds deposited with investment funds can be expected.
The securities markets in Central and Eastern European countries still do not play an important role as a source of financing for investment projects. However, in terms of capitalisation and the number of listed companies, the Polish stock market remained the largest capital market in Central and Eastern Europe. On the contrary, the ratio of the capitalisation as well as liquidity of the Polish stock market to GDP is still lower than the ratio for EU-15 countries (National Bank of Poland 2006b, 2007b, 2009, 2010).

In 2001 to 2011 only in Poland did the number of companies listed on the stock exchange grow, partially due to public offerings of stocks. For the sake of comparison, in the Czech Republic and Hungary, the increase in capitalisation was due to a rise of stocks prices, as well as the appreciation of currencies of these countries. Basic indicators related to the degree of development of capital markets in all these countries are presented in Table 5.

Table 5 Capital markets in CEECs in 2001-2011

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<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
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</tr>
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<td>14.56</td>
<td>23.65</td>
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<td>36.38</td>
<td>19.20</td>
<td>22.10</td>
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<th>2007</th>
<th>2008</th>
<th>2009</th>
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<tbody>
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<tr>
<td>Poland</td>
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<td>248</td>
<td>267</td>
<td>328</td>
<td>349</td>
<td>354</td>
<td>569</td>
<td>n/a</td>
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</table>

Source: Eurostat, World Bank.

The underdeveloped market of non-government tradable instruments is attributable, inter alia, to high borrowing needs of the public sector. A comparison between the markets of Treasury securities and non-government debt securities indicates a great difference between them (National Bank of Poland 2004). Apart from large borrowing needs of the central budget, many other factors have determined
the current shape of the capital market. The beginnings of the Polish stock exchange market were combined with the privatisation of the state-owned corporations. The interest in the stock exchange market was relatively poor. Only the year 1997 brought a significant rise in the number of listed companies and the privatisation of large corporations. The decisive role of privatisation of state-owned corporations in the development of the market influenced the extent to which the capital market should perform specific functions in the economy (National Bank of Poland 2004). As the segment of Treasury securities was undergoing a significant development, due to the increasing borrowing needs of the central budget and a simultaneous decrease in privatisation revenues, this weakened development in other segments of the capital market.

The capital market was created in line with the solutions implemented in developed countries, which will facilitate its integration into the European structures. It should also be stressed that although the legislative framework for the Polish capital market complies with international standards, it can be stated that its size is still unsatisfactory in comparison with the scale of capitalization in advanced economies.

3.2. Institutions of the Polish financial sector

3.2.1. The banking sector

Banks in Poland can operate as state banks, cooperative banks and joint-stock banks. The Banking Act also permits the operation of foreign banks’ branches and representative offices. A credit institution intending to perform the business within Poland must notify competent supervisory authorities of the home country, which shall transfer a notification to the Polish Financial Supervision Authority.

According to the Banking Act a state bank may be established by ordinance of the Council of Ministers, at the request of the Minister of State Treasury, which should have obtained the opinion of the PFSA. A joint-stock bank could be established on the basis of authorization of the PFSA. The provisions of the Code of Commercial Companies are applicable to the establishment and organization of a bank to the extent that they are not contradictory with the provisions of the Banking Act. A
cooperative bank may be established on the basis of authorization of the PFSA, taking into account provisions of the *Act on the Operations of Cooperative Banks, Their Affiliation, and Affiliating Banks*.

An opening of a branch of a foreign bank in Poland requires the authorization of the PFSA, granted in agreement with the Minister of Finance, at the request of the interested bank. Foreign banks may also establish their representative offices in Poland. Authorizations to establish representative offices of foreign banks are granted by the PFSA in agreement with the Minister of Finance.

Since the accession to the European Union, the principle of mutual recognition of licences for conducting lending activities has been introduced in Poland. According to it, a credit institution that has obtained a banking licence in any EU country is allowed to act on the territory of another member state without the need to be the subject of the licensing procedure in Poland. It is only required to notify the supervisory authorities in the host state of its intention to commence activity on its territory (National Bank of Poland 2006b, 2007b).

The principles of the establishing procedure, as well as the basic elements of internal organisation and the organisational structure of banks, are strictly regulated. The establishment of a bank depends on: ensuring that the bank would be furnished with own capital adequate to the size of the intended operations, together with other resources necessary to conduct those operations, as well as with premises adapted due to safekeeping of the valuables held in the bank (see Section 6).

Banks in Poland are functioning as universal banks. The one and only exception are mortgage banks, which have been functioning since 1998 on the basis of the *Act on Mortgage Bonds and Mortgage Banks*. The scope of activities of mortgage banks is strictly limited. Instead, they have the privilege of issuing mortgage bonds in form of long-term debt securities. The basic activity of mortgage banks consists of granting loans secured by a mortgage and issuing respective mortgage bonds, as well as in granting loans to entities of high creditworthiness (e.g. the Polish Treasury, territorial local government units) or loans guaranteed by those entities, and issuing public mortgage bonds based on them (National Bank of Poland 2004). Mort-
gage banks can be established as joint-stock banks only. The role of mortgage banks in financing the property market in Poland has been relatively small to date.

Banking activity has been described in the Section 5 of the *Banking Act*. The definition of such activity is basically closed, although there is a possibility for separate regulations to determine other activities that could only be performed by banks [Kowalski, Matysek-Jędrzych 2010]. Forms of active banking business are divided into three categories:

- operations that may be performed only by banks (inter alia taking deposits payable on demand or at a specified maturity, operating bank accounts, extending loans and guarantees, issuing bank securities, performing bank monetary settlements, issuance of electronic money),
- operations that may be performed also by non-banks but they turn to banking operations when performed by banks (inter alia operations on cheques and bills of exchange, issuing bank cards and performing operations using such cards, forward financial operations, safekeeping valuables and providing safe deposit facilities, purchase and sale of foreign exchange),
- other forms of business not considered to be banking operations by the *Banking Act* (inter alia, taking up or purchasing shares and the rights conferred by shares of other non-bank legal persons or units in mutual funds, undertaking commitments connected with the issue and trade of securities, purchasing and selling real property and debts collateralised by mortgages, providing financial consulting and advisory services).

The minimum capital necessary to obtain banking authorisation, equivalent to EUR 5,000,000 and the competition in the banking sector, reduced the opportunities for entering the market by employing solely Polish capital. The abolition of formal restrictions against foreign banks since Poland joined the OECD has led to an inflow of foreign capital to the Polish banking sector, as shown in Table 6. The share of foreign capital in the equity capital of commercial banks in Poland exceeded 72.0% in 2008 and declined in 2010 to the level of 66.2%. In 2010, domestic investors controlled 10 commercial banks (the State Treasury controlled 4 banks) and all the co-
operative banks. Measured by assets, their share in the market increased from 31.9% in 2009 to 33.8% in the next year. Foreign investors controlled 39 commercial banks and all the branches of credit institutions. The leading role was played by Italian investors (controlling 12.4% of the sector’s assets), followed by German (10.4%), Dutch (8.6%), American (6.9%) and French (5.8%) investors. It should be noted however that the sale of BZ WBK by Allied Irish Banks (Ireland) to Banco Santander (Spain) that took place in 2010 is going to change presented foreign capital’s structure in the forthcoming years (Polish Financial Supervision Authority 2011).

As a result of impulses from the real economy, the growth rate of the banking sector accelerated in the last decade. The ratio of assets of banking sector to GDP amounted to 82.0% in 2010. Changes to the structure of assets are the continuation of earlier trends. The further increase in claims on non-financial customers are mainly due to the extended activity of banks in the segment of retail banking, particularly in the segment of residential loans to households. Share of claims to non-financial customers increased to 56.9% in 2010 from 55.7% in 2008 (Narodowy Bank Polski 2011c).
Table 6 Number of banks and relative share of particular groups in the total system in 1993-2010

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<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.3</td>
<td>0.6</td>
<td>1.8</td>
<td>1.9</td>
<td>2.6</td>
</tr>
<tr>
<td>Cooperative banks</td>
<td>7.6</td>
<td>5.9</td>
<td>5.5</td>
<td>5.5</td>
<td>5.2</td>
<td>5.2</td>
<td>5.0</td>
<td>5.2</td>
<td>5.6</td>
<td>6.2</td>
<td>6.6</td>
<td>7.0</td>
<td>7.7</td>
<td>8.6</td>
<td>8.8</td>
<td>8.3</td>
<td>8.1</td>
<td>8.7</td>
</tr>
<tr>
<td>Total banks</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Total net assets (total assets less accumulated depreciation, specific provisions and valuation allowances) in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial banks:</td>
</tr>
<tr>
<td>banks with majority public sector interest, of which:</td>
</tr>
<tr>
<td>• directly owned by Treasury:</td>
</tr>
<tr>
<td>• with majority Polish equity</td>
</tr>
<tr>
<td>• with majority foreign equity</td>
</tr>
<tr>
<td>Branches of credit institutions</td>
</tr>
<tr>
<td>Cooperative banks</td>
</tr>
<tr>
<td>Total banks</td>
</tr>
<tr>
<td>Total capital base (core and supplementary capital) in %</td>
</tr>
<tr>
<td>Commercial banks</td>
</tr>
<tr>
<td>Cooperative banks</td>
</tr>
<tr>
<td>Total banks</td>
</tr>
</tbody>
</table>

| 93.4 | 94.7 | 95.2 | 95.4 | 95.5 | 95.7 | 95.8 | 95.8 | 95.4 | 95.0 | 94.8 | 94.7 | 94.2 | 93.8 | 93.8 | 94.6 | 94.2 | 93.9 |
| 80.4 | 76.1 | 68.3 | 66.5 | 49.3 | 45.9 | 23.9 | 22.9 | 23.5 | 25.1 | 24.4 | 20.6 | 20.3 | 19.8 | 18.3 | 17.3 | 20.8 | 21.5 |
| 76.1 | 70.8 | 63.0 | 51.1 | 38.2 | 36.7 | 22.1 | 21.1 | 21.7 | 22.9 | 22.3 | 18.4 | 18.6 | 18.1 | n/a  | n/a  | n/a  | n/a  |
| 13.0 | 18.6 | 26.9 | 28.9 | 46.2 | 49.8 | 71.8 | 72.9 | 71.9 | 69.9 | 70.4 | 73.5 | 73.1 | 71.0 | 71.2 | 71.9 | 68.1 | 67.9 |
| 10.4 | 15.4 | 22.7 | 15.1 | 30.9 | 33.2 | 24.6 | 3.4  | 3.2  | 2.5  | 2.6  | 6.6  | 4.0  | 4.3  | 4.6  | 5.0  | 5.3  | 6.2  |
| 2.6  | 3.2  | 4.2  | 13.7 | 15.3 | 16.6 | 47.2 | 69.5 | 68.7 | 67.4 | 67.8 | 66.9 | 69.1 | 66.6 | 66.6 | 66.9 | 62.8 | 61.5 |
| 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  |
| 6.6  | 5.3  | 4.8  | 4.6  | 4.5  | 4.3  | 4.2  | 4.2  | 4.6  | 5.0  | 5.2  | 5.3  | 5.8  | 6.2  | 6.2  | 5.4  | 5.8  | 6.1  |
| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0|
| 92.0 | 94.3 | 94.6 | 95.1 | 95.2 | 95.6 | 95.6 | 95.5 | 95.4 | 95.2 | 94.6 | 94.4 | 93.9 | 93.6 | 92.8 | 93.3 | 93.2 | 93.1 |
| 8.0  | 5.7  | 5.4  | 4.9  | 4.8  | 4.4  | 4.4  | 4.5  | 4.6  | 4.8  | 5.4  | 5.6  | 6.1  | 6.4  | 6.7  | 6.8  | 6.9  |
| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0| 100.0|

- Banks where the Treasury, other state institutions or the NBP hold equity entitling them to exercise at least 50% + 1 votes at a shareholders general meeting;
- Banks where the Treasury directly holds equity entitling it to exercise at least 50% + 1 votes at a shareholders general meeting;
- Banks where foreign parties jointly hold equity entitling them to exercise 50% + 1 votes at a shareholders general meeting.

The size and structure of the balance sheets of commercial banks are also influenced by securitisation transactions. In Poland, securitisation mostly takes place in the form of selling irregular loans to non-standardised securitisation funds by banks. New loans of high quality at initial stages of repayment are not the object of securitisation, as well as dividing loans into tranches (National Bank of Poland 2009).

3.2.2. Insurance institutions

Insurance institutions are offering insurance products and pursuing their own objectives and tasks through an insurance company, operating in the form of a joint-stock company or as a mutual insurance company, under the Law on Insurance Activities. The category of insurance institution does not cover entities that operate in the area of social insurance in Poland (the Social Insurance Institution, the Agricultural Social Insurance Fund, the National Health Fund or the Labour Fund), which are treated as a part of the sector of government and local government institutions (National Bank of Poland 2004). Number of insurance companies in operation is shown in Table 7.

Table 7 Number of insurance companies in operation in Poland in 1999-2010

<table>
<thead>
<tr>
<th>Year</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life insurance companies</td>
<td>30</td>
<td>32</td>
<td>35</td>
<td>35</td>
<td>35</td>
<td>32</td>
</tr>
<tr>
<td>chief branches</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Property and casualty insurance companies</td>
<td>33</td>
<td>34</td>
<td>34</td>
<td>35</td>
<td>38</td>
<td>36</td>
</tr>
<tr>
<td>branches</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life insurance companies</td>
<td>32</td>
<td>31</td>
<td>32</td>
<td>30</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>chief branches</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Property and casualty insurance companies</td>
<td>35</td>
<td>33</td>
<td>34</td>
<td>35</td>
<td>34</td>
<td>33</td>
</tr>
<tr>
<td>chief branches</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>


In 2010 there were 63 insurance companies conducting business activity, including 30 life insurance companies and 33 non-life insurance companies. There was one chief branch of a foreign insurance company operating in the Polish insurance market, offering non-life insurance products (Narodowy Bank Polski 2011c). Insurance products were also sold by the branches of insurance companies from EU.
This project is funded by the European Union under the 7th Research Framework programme (theme SSH) Grant Agreement nr 266800

Member States, which do not fall under the authority of the Polish insurance supervision, as the Insurance Activity Act stipulated the conditions according to which foreign insurance companies may conduct their activities on the territory of Poland and introduced the freedom to provide insurance services. According to the Act, a foreign insurance company may pursue activity via its chief branch. However, this does not apply to companies from EU countries, which may operate via branches. Chief branches are subject to Polish insurance supervisory authorities, whereas branches are subject to supervision in their home country (National Bank of Poland 2006b).

The insurance market in Poland is characterized by a faster growth in the assets of the life insurance sector as compared to the property and casualty insurance sector. The main reason for such development is a high demand for life insurance with an insurance capital fund. These insurance contracts are usually long-term ones, and the funds are accumulated for the entire duration of the contract. The property and casualty insurance sector is dominated by motor insurance contracts that are concluded on a yearly basis. The short time period of these agreements does not cause such a significant increase in the asset value, as it is observed in the life insurance sector (National Bank of Poland 2004).

Entities from several countries, mainly from Germany, are present in the Polish insurance sector. The share of the domestic capital has significantly decreased since the beginning of the nineties. It stemmed from the fact that new insurers were granted licenses to run insurance business as well as from the fact that the existing property and casualty insurers received capital injections from their foreign shareholders. However, the whole sector is still dominated by the entity with the majority of Polish capital – the PZU Group (National Bank of Poland 2004, 2006b, 2007b).

3.2.3. Collective investment institutions

Collective investment sector consists of two types of institutions: investment funds and open pension funds. Investment funds are legal persons, as defined in the Act on Investment Funds, whose business focuses on investing moneys, raised by public, or in circumstances specified in the Act by private, invitations to acquire par-
This project is funded by the European Union under the 7th Research Framework programme | theme SSH | Grant Agreement nr 266800

Participation units or investment certificates, in securities, money market instruments and other property rights. Open pension funds are institutions the subject of whose business is collecting moneys and investing them with a view to making payment to members of the funds after they reach retirement age, acting under the Act on Organization and Operation of Pension Funds.

The significance of the collective investment institutions increased in the last years. The strongest and the most sustainable factor that ensures this growth are the old age pension savings, the volume of which will be expanding under the compulsory and voluntary old age pension capital formation system. The size of the whole sector is shown in Table 8.

Table 8 Size of sector of collective investment institutions in 2001-2010 (PLN billion)

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Open pension funds’ assets, net</td>
<td>19</td>
<td>32</td>
<td>45</td>
<td>63</td>
<td>86</td>
</tr>
<tr>
<td>Investment funds’ assets, net</td>
<td>23</td>
<td>33</td>
<td>38</td>
<td>48</td>
<td>61</td>
</tr>
<tr>
<td>Year</td>
<td>2006</td>
<td>2007</td>
<td>2008</td>
<td>2009</td>
<td>2010</td>
</tr>
<tr>
<td>Open pension funds’ assets, net</td>
<td>117</td>
<td>140</td>
<td>138</td>
<td>179</td>
<td>221</td>
</tr>
<tr>
<td>Investment funds’ assets, net</td>
<td>99</td>
<td>134</td>
<td>74</td>
<td>93</td>
<td>117</td>
</tr>
</tbody>
</table>


Assets managed by investment fund management companies increased significantly, and the structure of the sector continued to diversify. In 2010, net assets of domestic investment funds increased by 24.7% as compared to 2009, and amounted to PLN 116.5 billion as at the end of December. The growth resulted mainly from the net inflows to funds (53%) and, to a lesser extent, from the change in the value of assets (47%). In 2010, the assets of foreign investment funds whose units were offered in Poland also increased, amounted to PLN 2.1 billion (Narodowy Bank Polski 2011c).

As at the end of 2010, 50 management companies operated in Poland (an increase by 7 entities), and they managed 417 funds. In 2010, the PFSA granted 115 licenses for the establishment of an investment fund, including 105 licenses for the establishment of a closed-end investment fund. In 2010, 77 foreign investment funds could sell their units in Poland; most of them were registered in Austria and Luxembourg. The notified entities often had the form of umbrella funds. Taking into account
the number of all sub-funds, the offer of foreign funds available in Poland was wider than that of Polish ones (Narodowy Bank Polski 2011c).

The majority of new resources contributed to investment funds was invested in the stock market, and figures for 2010 illustrate this. The stock portfolios of investment funds and open pension funds were different (PLN 55 billion and PLN 80 billion respectively), and their total share in free public floatations amounted to 16.1% and 31.7% respectively, which, with the limited supply of stocks, could have had an impact on the valuation of some stocks (Narodowy Bank Polski 2011c).

Open pension funds have recorded a significant increase in net assets since their creation. Partially this increase is a result of increase in the prices of debt instruments held in the portfolios of open pension funds, as these funds became the main domestic investor in the Treasury bond market (National Bank of Poland 2008). In 2010, open pension funds posted an increase in net assets by 23.9% to the level of PLN 221.3 billion. In 2010, the number of participants of open pension funds increased by 530 thousand and amounted to 15 million (11.72 million in 2005). Fourteen pension companies operated in this 2010 (Narodowy Bank Polski 2011c).

In 2010 funds invested their resources mainly in two classes of assets: domestic Treasury bonds (52.4%) and stocks of companies listed on the WSE (36%). The value of the Treasury bonds portfolio increased as compared to 2009 by approximately 5% to the level of PLN 115.9 billion. Pension funds became the second investor in the Polish Treasury bonds market in terms of value, after foreign investors (Narodowy Bank Polski 2011c).

3.2.4. The credit unions sector

This sector consists of Co-operative Saving and Credit Unions, which, according to the Polish law, are not banks. However, they are classified as monetary institutions by the National Bank of Poland. As non-banks, credit unions are not the subject of surveillance performed by the PFSA, nor members of the Bank Guarantee Fund. The one and only supervisory authority is National Co-operative Saving and Credit Union. The National Association and TUW SKOK (the mutual insurance company) are

Credit unions have been operating since 1992 under the Act on Cooperative Savings and Credit Institutions and under the provisions of the Act on the Cooperative Law. The purpose of the credit union is to collect cash only from its members, providing them with loans and credits, to carry out on their behalf accounts and to negotiate the conclusion of contracts of insurance. It should be underlined that according to the law credit unions operate as non-profit institutions. Credit unions offer their members most of the services provided by banks. Customers of credit unions may open personal accounts with attached payment cards. Credit unions may also maintain accounts of civil partnerships and natural persons conducting business activity. They operate predominantly in the retail customer segment, holding primarily consumer loans in their portfolios (with short maturities). Since May 6, 2002, the National Association of Credit Unions has held its account with the NBP, thus the customers are provided with access to the electronic clearing system via the National Clearing House (National Bank of Poland 2004).

Members of the credit union may be private persons, connected with professional or organization links and, in particular, the workers employed in one or more enterprises, or persons belonging to the same social or professional organization. However, it is enough to associate in one of communities organized by credit unions (inter alia the Association Promoting Financial Education or the Association Supporting the Credit Unions) to become a member of the chosen credit union.

Since 1992 the number of branches and members of credit unions has increased steadily, although the number of credit unions has decreased in subsequent years as a result of consolidation, as shown in Table 9. The main reason for this process was the fact that stronger credit unions took over smaller, less effective, single-branch credit unions (National Bank of Poland 2007b, 2009, 2010).
Table 9 Number of credit unions and their members in 1997-2010

<table>
<thead>
<tr>
<th>Year</th>
<th>1997</th>
<th>1998</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of credit unions</td>
<td>198</td>
<td>220</td>
<td>228</td>
<td>146</td>
<td>144</td>
<td>120</td>
<td>109</td>
</tr>
<tr>
<td>Number of credit unions inclusive of their branches</td>
<td>237</td>
<td>290</td>
<td>420</td>
<td>560</td>
<td>680</td>
<td>923</td>
<td>1285</td>
</tr>
<tr>
<td>Number of members (in million people)</td>
<td>0.19</td>
<td>0.26</td>
<td>0.31</td>
<td>0.39</td>
<td>0.53</td>
<td>0.70</td>
<td>0.92</td>
</tr>
<tr>
<td>Year</td>
<td>2004</td>
<td>2005</td>
<td>2006</td>
<td>2007</td>
<td>2008</td>
<td>2009</td>
<td>2010</td>
</tr>
<tr>
<td>Number of credit unions</td>
<td>83</td>
<td>76</td>
<td>70</td>
<td>67</td>
<td>62</td>
<td>62</td>
<td>59</td>
</tr>
<tr>
<td>Number of credit unions inclusive of their branches</td>
<td>1461</td>
<td>1553</td>
<td>1589</td>
<td>1658</td>
<td>1757</td>
<td>1801</td>
<td>1851</td>
</tr>
<tr>
<td>Number of members (in million people)</td>
<td>1.17</td>
<td>1.39</td>
<td>1.55</td>
<td>1.67</td>
<td>1.86</td>
<td>2.03</td>
<td>2.2</td>
</tr>
</tbody>
</table>


The assets of credit unions increased in 2010 by PLN 2.5 billion, reaching the level of PLN 14.1 billion. The assets of credit unions still constitute less than 15% of the balance sheet of the co-operative banking sector. As at the end of 2010, the value of loans and advances to non-financial customers, declared in the balance sheets of credit unions, exceeded PLN 9.8 billion. The value of deposits of non-financial customers placed at credit unions increased to PLN 13 billion. Households constituted the most numerous group of credit unions’ customers. Their share in loans and advances amounted to almost 78%, and in deposits to 99%. The maturity structure of receivables was dominated by loans and advances with the maturity of 1 to 5 years (Narodowy Bank Polski 2011c).

3.2.5. Brokerage houses and offices

There are two types of institutions conducting brokerage activity: brokerage offices and brokerage houses. According to the classification of the NBP, “brokerage houses” are independent entities operating in accordance with the rules of the Code of Commercial Companies, whereas “brokerage offices” are banks conducting brokerage activity within the framework of financially and organizationally isolated units. There is also a possibility enabling banks whose structure does not include brokerage offices to offer brokerage services (National Bank of Poland 2004, 2006b). Apart
from this, foreign investment companies are also operating in Poland under licenses granted by the home country supervisory authorities, after having informed the Polish Financial Supervision Authority of their intention to launch investment activities.

Number of brokerage houses and offices is relatively stable. The offices achieve higher returns due to their systemic advantage over the brokerage houses, resulting from the fact that they belong to banks and can use the banks’ extensive customer service network. They also provide services to the largest and most active investors, including institutional and foreign ones (National Bank of Poland 2004).

In 2010, the number of domestic brokerage institutions increased to 64 (from 42 in the previous year). They included 50 brokerage houses and 14 banks which conducted brokerage activities. It is worth noticing that the share of the five largest brokerage entities in the stock market turnover decreased to less than 50% in 2010. The distribution of brokerage services continued to grow. The number of accounts maintained by brokerage offices and houses increased from around 1,133,000 in 2009 to 1,477,000 in 2010 (Narodowy Bank Polski 2011c).

3.2.6. Other financial intermediaries

Other financial intermediaries are financial institutions whose primary activity is financial intermediation carried out by incurring liabilities in forms other than cash, deposits and/or substitutes for deposits in institutional entities other than monetary financial institutions. Services provided by other financial intermediaries are an alternative to the services provided by banks. A steady growth in the sales volume of financial intermediaries indicates the growing importance of these forms of business financing (National Bank of Poland 2004).

The activity of leasing and factoring companies is targeted at customers with legal personality (enterprises, companies, sole proprietors). Leasing may cover any type of goods, e.g. means of transport, equipment, office space. The possibility to make an investment and purchase goods makes leasing attractive for emerging business entities as well as for small and medium-sized enterprises (SME). For this
reason leasing companies target their offering mainly at this group of customers (National Bank of Poland 2004, 2006b). In Poland, leasing companies which are bank subsidiaries prevail, although their share decreases in favour of other entities (National Bank of Poland 2007b, 2008, 2010).

Leasing was one of the fastest-developing segments of the Polish financial market. In 2010 the value of assets leased increased by 19% as compared to 2009 and amounted to PLN 27.3 billion, which accounted for 1.9% of the GDP. The share of leased assets in gross fixed capital formation incurred in the national economy in 2010 amounted to around 12.6%. In 2010, there were 84 leasing companies. The majority of these companies belong to banking groups (Narodowy Bank Polski 2011c).

Factoring is an alternative to bank loans in the scope of financing current company activities. Both banks and factoring companies provide factoring services in Poland. The latter offer customers a broader range of additional services apart from the purchase of receivables and the potential assumption of the debtor’s insolvency risk, i.e. conducting settlements, debt collection or assistance in collecting past due debts. The importance of factoring for the Polish economy is still relatively small (National Bank of Poland 2004, 2006b, Narodowy Bank Polski 2010). The development of factoring in Poland is being affected by failing to meet payment deadlines due to low financial discipline of domestic entrepreneurs as well as low efficiency of debt recovery through courts of law (National Bank of Poland 2007b, 2010).

In 2010, the value of purchased invoices in Poland amounted to PLN 88.6 billion. It remained at a low level as compared to the GDP. In other countries of the region factoring is used more often. The services provided by companies were used mostly by companies from such sectors as the automotive industry, the foodstuffs sector, metallurgy, steel metallurgy, construction and trade sector (Narodowy Bank Polski 2011c).

The customers of loan brokers are individuals. The presence of brokers is designed to make it easier for the consumer to make a loan decision, as well as to accelerate the loan procedure. The Polish loan brokers market has been growing since the beginning of the 1990s. They are mostly small enterprises which cooperate with
one or a few banks, being usually controlled by banks. The activity of loan brokers is supplementary to the traditional distribution channels of banking products. The loan sold by an intermediary is extended by a bank, as the customer concludes a loan agreement with a bank. The role of the broker depends upon the type of cooperation agreement: it may act solely as a link between the lender and the borrower, but it may also be responsible for monitoring due claims collection. The customers of intermediaries usually include persons, which are not creditworthy enough to obtain a bank loan, or who want to obtain such a loan within a shorter period of time (National Bank of Poland 2004, 2006b, Narodowy Bank Polski 2010).

In 2010, the value of loans granted by banks with the participation of financial intermediation companies exceeded PLN 13 billion. The most important group of products sold by intermediaries were housing credits. Customers signed loan agreements of the value reaching more than PLN 11 billion. This market is characterized with the high level of concentration. Three largest entities from the sector had a 65% share in the market, in terms of both the value and the number of signed agreements (Narodowy Bank Polski 2011c).

Another form of intermediary financial institutions are private equity/venture capital funds. In Poland the venture capital sector started to form at the beginning of the 1990s. This segment of the Polish financial sector is characterized by a high volatility of annual capital raised and investments carried out. The ratio of venture capital investment to GDP in Poland is very small (0.1-0.2% in previous few years). A vast part of funds invested in Poland comes from foreign institutional investors. The lack of domestic capital resources is a significant obstacle to the development of this market (National Bank of Poland 2004, 2006b, 2007b, 2010).

In 2010, the value of investments initiated in Poland by domestic and foreign private equity funds reached the level of PLN 2 billion, while the value of new funds raised by funds which operate in Poland amounted to PLN 0.5 billion. Public sector capital prevailed among financing sources of private equity funds based in Poland (55.1% of capital raised by funds in 2010 was the public capital). Polish private equity funds predominantly invested in the domestic market.
3.3. Financial instruments

3.3.1. Money market instruments

Money market instruments are debt instruments with maturities of up to 1 year. The money market instruments used in Poland are: 1) Treasury bills, 2) NBP bills, 3) short-term debt issued by the corporate sector and bank short-term debt instruments, 4) repo, and buy-sell-back transactions, 5) interbank deposits and 6) FX swaps. The largest segment of the short-term debt securities market is the Treasury bills market.

Treasury bills are bearer securities, with maturities ranging from 1 week to 52 weeks. Maturities of T-bills offered during the Ministry of Finance auctions are mainly 52 weeks. Starting from July 1995, only dematerialized bills are issued (in electronic, book entry form). Treasury bills are sold with a discount, and the nominal value of one bill is PLN 10,000. Treasury bills are issued by the Ministry of Finance. The auctions for T-bills are organized by the National Bank of Poland NBP, which plays the role of a government agent. The primary market is based on agreements concluded between the issuer of Treasury securities (the Ministry of Finance) and selected banks, so-called Primary Dealers. Starting from 1996, the NBP selects a group of banks, which are money market dealers. The main participants of the secondary market are domestic banks acting on behalf of their customers. All transactions executed in the secondary market are registered in the Central Register of Treasury Bills, operated by the NBP [National Bank of Poland 2002, 2004, 2006b, 2010]. In 1990s T-bills were the main instrument of funding the borrowing requirements of the budget. In time, their role was taken over by T-bonds [National Bank of Poland 2002, 2007b, 2009, Narodowy Bank Polski 2010]. In 2010, the average value of Treasury bills outstanding amounted to PLN 40 billion, falling by PLN 16 billion as compared with year 2009 [Narodowy Bank Polski 2011c].

NBP bills (issued since 1990) are bearer securities. The issues of NBP bills are an instrument of the monetary policy, as with the use of this instrument, the central bank absorbs excess liquidity in the banking system and controls short-term in-
terest rates. In the beginning the NBP issued 28-day bills, then their maturity was shortened to 14 days, but in 2004, the Monetary Policy Council decided that from January 1st, 2005 the maturity of the main open market operations consisting in the issue of money market bills would be reduced to one week. Money market bills are sold at a discount. Nominal value of one bill is PLN 10,000. Since May 1996, NBP bills are issued in dematerialized form. Money market bills are sold in auctions, mainly to banks which have the status of money market dealers (assigned on the basis of the Dealers Activity Index), although the NBP reserves the right to sell the bills on a bilateral basis. The auctions are organized irregularly, in the periods when the excess of liquidity in banks put a pressure on market interest rates. Only the money market dealer banks and the Bank Guarantee Fund have the right to participate in money market bills auctions. Secondary trading in money market bills took place on the non-regulated interbank market. The trade takes form of outright transactions, repos and sell-buy-backs. All transactions in the secondary market are recorded in the Register of Money Market Bills operated by the NBP. The bills are not available for domestic non-bank institutions and foreign entities (National Bank of Poland 2002, 2004, 2006b, 2007b, 2009, 2010). In 2010, in annual average terms, the value of NBP bills issued and outstanding amounted to PLN 75 billion and was by 135.1% higher from the average level in 2009 (Narodowy Bank Polski 2011c).

Commercial debt has been issued since 1992. The securities take both the material and dematerialized form. There are two types of commercial paper: discount and coupon papers. They are issued both as bearer and registered securities, with different maturities, although the dominant type are papers with maturities up to 3 months. The legal basis for an issue of commercial paper are Civil Code, Bill of Exchange Act or the Bonds Act. The issues of the instrument are not public, because they are usually offered to less than 100 investors. The main reason for this is the high cost of public issue and long procedures of public trading. The main group of issuers are enterprises and non-bank financial institutions. Issues are organized by agent banks, which distribute the securities among investors. The secondary market for commercial papers is illiquid, since investors hold commercial papers until ma-
turity. A large portions of the securities is held by banks, which perform the function of agents. An important weakness of this segment of financial market is the lack of a centralized depository for commercial papers. Most frequently, the register of investors is managed by the agent bank, which distributes the issue. The small role of the short-term commercial debt instruments as a source of financing results from the relatively small demand for those instruments on the part of institutional investors (National Bank of Poland 2002, 2007b, 2009, Narodowy Bank Polski 2010). In 2010, the outstanding value of short-term corporate bonds amounted to PLN 11.7 billion (0.8% of the GDP), which meant an increase by approximately 88% as compared to 2009. Such a fast growth was an evidence of increasing enterprises’ interest in this form of furnishing themselves with new capital (Narodowy Bank Polski 2011c).

Certificates of deposit and short-term bank debt securities have been issued in Poland since the second half of the 1990s. All bank securities of which issue is based on the Banking Law (including certificates of deposit) must include the phrase “bank security” in the name of the security. This name distinguishes bank securities from other securities, which may also be issued by banks. Bank securities may have a material and dematerialized form. In practice, they are bearer instruments and have a material form. Households are the dominant investors purchasing securities and certificates of deposit. However Polish banks are rather uninterested in their issue due to the excess of liquidity in the banking system and the mandatory reserve requirement regarding the liabilities, when they are purchased by non-bank or foreign entities. The distribution of securities is usually conducted by other bank than the issuer. Secondary market is practically non-existent due to the limited size of the issue. There is no central register of bank debt instruments. The issuing bank performs the depository functions (National Bank of Poland 2002, 2006b, 2007b, 2009, 2010). In 2010, the outstanding value of short-term debt securities issued by commercial banks amounted to PLN 2.6 billion, which was PLN 0.4 billion less than in 2009 (Narodowy Bank Polski 2011c).

There are two basic types of conditional transactions: repurchase agreements (repo) and sell-buy-back and buy-sell-back (SBB/BSB) operations. Repo and
SBB/BSB are transactions where one of the parties sells securities, simultaneously agreeing to repurchase the securities at an agreed price and on a date specified in the agreement. The fundamental difference between repo and SBB is that the former is based on one agreement, while the latter on the two agreements (sale of securities in spot market and purchase of securities in forward market). The deposits obtained in the repo market are subject to mandatory reserve requirement. No such requirement applies for SBB. For these reasons, repo is used mainly to obtain funds in the interbank market, while the SBB operation is used by banks in transactions with non-bank institutions. Repos and SBB are short-term operations which are not consistently regulated in Polish legislation, because regulations concerning the functioning of specific financial institutions treat those transactions differently. A majority of operations are operations with maturities less than 7 days. The SBB (BSB) transactions are conducted almost exclusively with the use of Treasury bills. Majority of repos and SBBs/BSBs are concluded on the unregulated OTC market (National Bank of Poland 2002, 2004, 2006b, 2007b, 2009, 2010). In 2010, the average daily value of conditional transactions concluded in the domestic money market increased by 23% from 2009 to PLN 10 billion in 2010. SBB/BSB operations accounted for more than 90% of net turnover (Narodowy Bank Polski 2011c).

Interbank deposits are the key instrument for liquidity management in banks. Transactions in interbank market are based on Article 49 and 50 of the Banking Law. Unsecured deposits are being borrowed with the use of funds held with central bank. They bear relatively high credit risk. As a result, bank management boards impose limits on operations: as conditional transactions and FX swaps charge the credit limit of up to 10% of the nominal value of the transaction, for a classical interbank deposit it is 100% of the nominal value. Mainly the domestic banks are participants in the market, since only domestic banks hold accounts with the NBP, as current accounts held with the central bank are used inter alia to clear items related to the settlement systems maintained by the National Depository for Securities and the National Clearing House. The amount of funds that banks are able to deposit changes on a daily basis, therefore overnight (O/N) transactions account for the largest share of turno-
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The average daily turnover on the market of interbank deposits as at the end of 2010 was PLN 7 billion, being 3% lower than in 2009 (Narodowy Bank Polski 2011c).

The average interest rates in interbank deposit market are WIBOR/WIBID (Warsaw Interbank Offered Rate/Warsaw Interbank Bid Rate). The system of WIBOR rates fixing is used since 1991. The reference WIBOR rates are set for the following maturities: O/N, T/N, 1W, 1 month, 3, 6, 9 and 12 months. WIBOR (or WIBID) rate is calculated as the arithmetic mean of the rates quoted by the participants, after rejecting two outliers (National Bank of Poland 2002). In 2004, the NBP finished work undertaken in co-operation with the Polish Bank Dealers Association on the introduction of the POLONIA (Polish Overnight Index Average) rate, the equivalent of the EONIA (Euro OverNight Index Average) rate, i.e. the effective overnight reference rate for the euro. The participants of the POLONIA rate fixing include banks operating in Poland which participated in the fixing of WIBID and WIBOR reference rates (National Bank of Poland 2006b, 2007b, 2009).

FX swap is a purchase of the zlotys with foreign currencies in the market and a simultaneous repurchase of the foreign currencies in forward transaction. The swap market has been developing in Poland since 1999, after the introduction of the Foreign Exchange Law, which made Polish zloty externally convertible, as well as standardized agreement for FX swap transactions, introduced in November 1999 by the Polish Banks Association and the Polish Association of Bank Dealers. Majority of FX swaps involve the zloty and they have maturity up to 7 days. However, as opposed to the interbank deposit market, which is liquid for transactions for up to three months, the FX swap market is also moderately liquid for longer maturities of up to one year. The currency composition of turnover on the domestic FX swap market is stable: USD/PLN deals dominate. An important role is played by several foreign banks operating from London and Frankfurt. These banks perform the functions of intermediaries in the FX swap market (National Bank of Poland 2002, 2006b, 2007b, 2009, 2010, Narodowy Bank Polski 2010). In 2010 the average daily net turnover increased and amounted to PLN 54.9 billion, although the daily net turnover on the domestic inter-
bank market was responsible for 21% of the total turnover (Narodowy Bank Polski 2011c).

3.3.2. The capital market instruments

Capital market instruments are instruments with maturities exceeding 1 year: 1) Treasury bonds, 2) National Bank of Poland bonds, 3) local government bonds 4) corporate bonds and bank short-term debt instruments, 5) mortgage bonds and 6) stocks. The equity market and the Treasury bond market remain the most important segments of the Polish capital market. The other segments still are much less significant (Narodowy Bank Polski 2011c).

The Treasury bond market is the most important segment of the Polish debt securities market. Treasury bonds are debt instruments with maturities exceeding 1 year, which are issued by the State Treasury represented by the Ministry of Finance. The interest income is offered in the form of discount or coupon payments. Depending on the type of the investor, to whom the issue is directed, Treasury bonds may be classified as retail bonds, dedicated for individual investors, and wholesale bonds, dedicated for domestic and foreign institutional investors. Par value of a bond is equal to PLN 100 or PLN 1,000, depending on the type of the issue and its tranche. Bonds may be issued as fixed-rate or floating-rate, zero coupon or inflation-indexed ones. They may be issued during an auction, through the retail points of sale (POS), and through the securitisation of the public debt. The primary T-bond market is organized in the form of auctions at the NBP, which plays a role of the Ministry of Finance agent. Starting from May 1992, all issues of bonds are conducted in the dematerialized form, both for the institutional and individual investors. Treasury bonds transactions are settled in the National Depository of Securities. Only a small proportion of bonds are traded in the domestic organized exchanges: the Warsaw Stock Exchange and Bondspot. The secondary market is divided into the segments of institutional investors and individual investors. The former purchase wholesale bonds, while the latter savings bonds and retail bonds distributed by the POS network (National Bank of Poland 2002, 2006b, 2009, 2010). In 2010, the outstanding value of
Treasury bonds issued increased by 15% as compared with 2009 and amounted to PLN 479 billion, out of which marketable bonds accounted for PLN 471 billion. Fixed-rate bonds are the basic instrument for the financing of the State budget borrowing needs. In 2010, they accounted for 81.6% of all outstanding bonds. In terms of liquidity, the Polish Treasury bond market was the strongest one among all the CEECs markets (Narodowy Bank Polski 2011c).

Apart from the Treasury, another public agency, which issued long term securities, was the National Bank of Poland. The NBP bonds were issued on September 30, 1999, to absorb liquidity from banks, which was released after the central bank lowered the mandatory reserve requirement. The bonds had initial maturities between 6 and 10 years and interest indexed to the inflation rate. They were issued as non-public securities (National Bank of Poland 2002, 2004, 2010). Since 2002 10-year NBP bonds worth PLN 7.82 billion are traded. They were repurchased on March 1, 2012 (National Bank of Poland 2009).

Local governments issue their debt on the provisions of the Bonds Act. The main issuers of municipal bonds are cities with poviat status.27 Municipal bonds allow to obtain financing at a cost lower than the interest on bank credit, but pursuant to the Public Finance Act, the debt of local government units may not exceed 60% of their revenue (this does not apply to the tasks which are co-financed by the EU). Municipal bonds are usually floating rate securities. Issuers usually address their offers to selected investors (in non-public issue). Therefore, similarly as in case of corporate debt instruments, the market for municipal bonds is organized by banks. In practice there is no secondary market for municipal bonds. Municipal bonds are mainly purchased by domestic investors, of which banks constituted the vast majority (National Bank of Poland 2002, 2004, 2006b, 2007b, 2010). At the end of 2010, the value of municipal bonds issued amounted to PLN 10.9 billion (Narodowy Bank Polski 2011c).

Similar to local government authorities, corporations issue long-term bonds based on the Bonds Act. The maturities of such bonds vary from 2 to 10 years. Corpora-

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27 Poviat is a medium unit of three-level territorial division in Poland; poviat may consist of several municipalities or it may be a single city.
rate bonds may be fixed or floating rate instruments. The size of issue remains small compared to both Treasury bonds and short-term corporate securities. Market organization, both in the case primary and secondary trade, is the same, as described in the part on commercial papers. In Poland, long-term commercial bonds are issued as public offers and private placements – the latter predominate. Similarly to the market for short-term debt instruments, there is no centralized depository and settlement system for the corporate bonds. The settlement of transactions is conducted by banks, which maintain the depository accounts for the buyers of bonds, and who perform the operations associated with the initiation and redemption of an issue (National Bank of Poland 2002, 2004, 2006b, 2007b, 2009, 2010). In 2010, outstanding value of LCBs amounted to PLN 19.9 billion (1.4% of the GDP), increasing by 29% from 2009. The share of long-term corporate bonds in the whole market of non-Treasury bonds in Poland amounted to 35%. The value of new issues of long-term bonds amounted to PLN 7.8 billion, majority was sold as a result of non-public offers on the OTC market (Narodowy Bank Polski 2011c).

Long-term bank debt securities are securities issued by commercial banks with maturities of at least one year. Primary market of these securities is organized similarly to the long-term commercial debt instruments primary market. Bonds issued by commercial banks may be traded both on the regulated and on the unregulated market. Public bank bond issues have been targeted mainly at individuals. Private placements, on the other hand, have been targeted at institutions (National Bank of Poland 2007b, 2009). In 2010 there was a rapid increase of the outstanding value of long-term debt securities issued by domestic banks in Poland. At the end of the year, this value exceeded PLN 5.2 billion, of which vast majority (about 90%) was nominated in PLN and was issued in the form of bank bonds (Narodowy Bank Polski 2011c).

The legal basis for the issue of mortgage bonds is the Law on Mortgage Bonds and Mortgage Banks of August 29, 1997. Mortgage bond is a registered or bearer security, backed by receivables of a mortgage bank. Bank issuing mortgage bond is obliged to make strictly defined payments. The payments of the mortgage bonds are divided into core payments (nominal value of the bond, according to which the bond is
redeemed) and secondary payments (interest payable on dates identified in the conditions of the issue). Mortgage bonds may be issued only by mortgage banks, established under the rules of the law. The issue of mortgage bonds is organized by banks, which own mortgage banks. They perform the functions of a dealer, payment agent and custodian. Mortgage bonds, both denominated in zlotys and in foreign currencies, are a part of the domestic bank asset portfolios. Secondary trading in mortgage bonds can take place both on the public and non-public markets, however in practice this market is illiquid (National Bank of Poland 2002, 2004, 2006b, 2007b, 2009). In 2010, the outstanding value of mortgage bonds issued by banks did not change significantly as compared to previous years and amounted to PLN 2.5 billion at the end of the year, out of which majority were the public issues (Narodowy Bank Polski 2011c).

A stock is an equity instrument, giving the owner the right to a dividend and participation in voting at the general assembly of shareholders. The equity instruments took a dematerialized form (electronic book entry) from the very beginning. In August 1998, a new instrument was introduced at the Warsaw Stock Exchange in the form of subscription warrants (PDA). Subscription warrants allow the buyer of new issues of stock to sell the shares before they are listed on the exchange (National Bank of Poland 2002).

Public trading in securities is regulated by the Law on Public Trading in Securities. The issuers are obliged to place an application to the Polish Financial Supervision Authority. A company planning to list its shares on the exchange, places an appropriate application with the Board of the Warsaw Stock Exchange. Listing requirements, which are different for each of the markets, are determined in the Rules and Regulations of the Exchange. These include, inter alia, minimum value of shares to be listed, minimum book value and share capital of the company. The criteria for listing of a security on Bondspot are much less stringent than on the WSE. Organized secondary trading in securities is conducted at: the Warsaw Stock Exchange and the BondSpot Publicly traded shares are dematerialized. The settlement of transactions is conducted in a T+3 settlement cycle (settlement within three business days) based
The dominant role among investors in the stock market is played by domestic individual and institutional investors (National Bank of Poland 2002).

The main institutions of the Polish capital market are: 1. the Warsaw Stock Exchange (WSE), which organises the trading in financial instruments, 2. the National Depository for Securities (NDS), which handles clearing and settlement of transactions, processes corporate actions and provides safekeeping of financial instruments, and 3. Brokerage houses, which serve as intermediaries in transactions. The NDS uses the National Bank of Poland as its clearing bank (Warsaw Stock Exchange 2010). The capital market is supervised by the Polish Financial Supervision Authority.

The regulated off-exchange market, involving mostly wholesale transactions, is organised by BondSpot. This company engages in wholesale trading of bonds and Treasury bills on the Treasury BondSpot Poland platform and in trading in municipal, corporate and mortgage bonds in a regulated off-exchange market which is part of Catalyst. The minimum value of an issue, equalling PLN 5 million, is the key admission criterion for those markets. By definition, both BondSpot-operated markets are wholesale markets, i.e. bids can be placed only if they reach or exceed a minimum threshold of PLN 100,000 of nominal value. The BondSpot is part of the WSE group of companies: at the end of 2010 the WSE held a 92.47% stake in the BondSpot (Warsaw Stock Exchange 2011).

In 2010 the WSE became a public company, its shares being traded on the WSE Main List since November 2010. The Treasury sold 26,786,530 shares in a public offering, out of which 8,035,959 were taken up by individual investors and 18,750,571 shares were purchased by institutional investors. At the end of 2010 the State Treasury hold a 35.81% stake in the share capital, having 51.40% share of votes at the General Meeting of Shareholders.

The WSE Group organizes and operates trading on the following markets:

- Main Market (trade in equities, other equity-related securities, cash markets instruments and derivatives), notified to the European Commission as a regulated market;
• NewConnect (trade in equities and other equity-related securities of small and medium-sized enterprises), launched on August 30, 2007, organised and maintained by the WSE as an alternative trading system, designed for start-ups and developing companies;

• Catalyst (trade in corporate, municipal, co-operative, Treasury and mortgage bonds), founded on September 30, 2009, it consists of two trading platforms organised by the WSE as a regulated market and as an alternative trading system (ATS) for retail customers, and two analogous markets operated by the BondSpot and designed for wholesale clients;

• Poee WSE Energy Market (trade in electric power).

The role of the WSE is to supervise listed companies’ compliance with disclosure requirements and to ensure that market participants have equal access to information published by issuers. The WSE also supervises members’ compliance with applicable WSE rules. Operations on the WSE are open only to its members. Under the current rules and regulations, the following entities may become WSE members: an investment firms, as defined in Article 3(33) of the Act on Trading in Financial Instruments, which conducts transactions on their own account or on the account of its clients; any other entity which is a participant of the National Depository for Securities (NDS) and conducts transactions only on its own account; any other entity which is not a participant of the NDS and which conducts transactions only on its own account, provided that it indicates a NDS participant which has committed itself to meeting the transaction clearing and settlement obligations (Warsaw Stock Exchange 2009).

At the end of 2010 the WSE calculated and published 6 WSE indices, 10 sub-indices, 2 strategy indices and one external index. The values of four of those indices are reported on an on-going basis (Warsaw Stock Exchange 2010, 2011):

• WIG20 – calculated since 16 April 1994, the price index of the largest quoted companies (blue chips) and has a base value of 1,000 points, WIG20 values are calculated on the basis of share prices of 20 listed companies,
• mWIG40 – covers medium size companies (by market value and turnover), this price index has been published by the WSE since 31 December 1997, its base value being 1,000 points, mWIG40 values are calculated on the basis of share prices of 40 listed companies,
• sWIG80 – its portfolio covers listed companies which are smaller than the WIG20 and mWIG40 constituents, this price index has been published by the WSE since 31 December 1994, its base value being 1,000 points, sWIG80 values are calculated on the basis of share prices for 80 listed companies,
• WIG – total return index calculated since the first ever WSE session on 16 April 1991, its portfolio covers all listed companies except those whose free float is under 10% and EUR 1 million and those in a special situation, as defined in the WSE Rules, the base value of the WIG is 1,000 points.

3.3.3. Spot FX market instruments

The domestic foreign exchange market is for transaction involving the Polish zloty. Such transactions are executed not only by domestic entities with domestic or foreign entities, but also between non-residents, as it is the case in the London foreign exchange market. After several years the dominant trading currency in the Polish foreign exchange market become euro because it is the basic currency in the Polish foreign trade, thus replacing USD. Other currencies, mainly the pound sterling and Swiss franc, are also traded in the FX market (National Bank of Poland 2002, 2007b, 2009).

Foreign exchange market is an interbank market. Several banks perform the function of market-makers, which publish quotes and conclude transactions on a continuous basis. The remaining domestic banks are price takers on the FX transactions between residents are concluded on the basis of bilateral agreements drawn up by the Polish Banking Association and the Polish Bank Dealer Association. Active foreign participants in the zloty market include Deutsche Bank, Citigroup, UBS, JP Morgan, HSBC. Banks conclude transactions on the zloty market mainly via an electronic broking system (National Bank of Poland 2004, 2007b).
Since 2005 the Ministry of Finance has become a very important player on the domestic FX market, exchanging currencies obtained from the issue of Eurobonds. Due to the growing scale of the trade, the liquidity of the domestic foreign exchange market is constantly improving (National Bank of Poland 2002, 2007b). The FX market in Poland is the largest and most liquid among the currency markets in the region. It is estimated that in 2010 the average daily turnover on the offshore zloty market amounted to over USD 8 billion (Narodowy Bank Polski 2011c).

3.3.4. Derivative instruments

Financial derivatives are traded both on the stock exchange and over-the-counter markets. The advantage of the stock exchange market over over-the-counter (OTC) results from centralisation of trade and functioning of clearing houses, which contribute to reduction of credit risk borne by the parties to the transactions. The activity on the OTC market is mainly focused on transactions involving FX derivatives. In Poland the derivatives include: 1) FRA contracts, 2) forward transactions, 3) future contracts, 4) foreign exchange futures, 5) derivatives on stocks, 6) interest rate swaps, 7) currency interest swaps, 8) interest rate options, 9) foreign exchange options, 10) options on securities, 11) credit default swaps.

The most frequently used instrument of hedging against short-term interest rate risk are FRAs (Forward Rate Agreement), which have been traded in Poland since 1998. The reference rate for FRA contracts in Poland is WIBOR. FRA contracts allow for hedging against short-term interest rate risk for various periods, which are quoted as 1x2, 9x12, 6x12 etc.\textsuperscript{28} The nominal value of a transaction is subject to a contractual agreement. A majority of transactions is classified by banks as speculative. Both foreign and domestic institutions actively participate in the PLN denominated FRA market (National Bank of Poland 2002, 2004, 2009). The value of the domestic

\textsuperscript{28} FRAs are quoted in the format AxB, with (A) representing the number of months until the loan is set to begin, and (B) representing the number of months until the loan ends. To find the length of the loan, subtract A from B. For example, 1x4 quote would mean a 3 month loan, set to begin 1 month in the future. Common formats for these quotes include 1x4, 1x7, 3x6, 3x9, 6x9 and 6x12.
banks’ positions in the FRA contracts on the domestic zloty market amounted to PLN 390.2 billion in 2010 (Narodowy Bank Polski 2011c).

Outright-forward transactions are agreements on a delivery of a specified amount of currency at a pre-agreed exchange rate at a given time in the future. It is possible to enter also non-delivery forwards (NDF) where there is no obligation to deliver currency, but, instead, to settle the differential between the initial forward exchange rate and the future spot rate on the day of settlement. The size of individual transactions is adjusted to the needs of customers and is contractually negotiable. Standard maturity of transactions range from 1 week to 12 months. The main role in outright-forward market is played by banks. A large proportion of their transactions is executed with non-residents (National Bank of Poland 2002, 2006b).

Interest rate futures are standardized forward contracts where the parties agree to settle the difference between future price of the purchased (sold) contract and the initial price of the contract. The first interest rate futures were introduced by the Warsaw Commodities Exchange (WCE) in February 1999. Futures are traded at the WCE in an open-outcry system. Financial institutions, most of all banks, do not use futures contracts to hedge themselves against risk. The majority of their transactions is executed in the interbank FRA market (National Bank of Poland 2002).

In February 2005 the WSE introduced bond futures. Underlying instruments are fixed-rate Treasury bonds. The value of issue cannot be less than PLN 5 billion, while the date of redemption has to be fixed within the obligatory time limit: not shorter than two years and nine months but not longer than five years and six months following the date of contract execution. There are only a few market makers on the bond futures contracts market (National Bank of Poland 2007b).

Foreign exchange rate futures contract is an agreement between two parties, which promise to settle the differences between the future price of the contract and its initial price. Foreign exchange rate futures have been trading in the two exchange markets: the Warsaw Commodities Exchange and the Warsaw Stock Exchange. EUR/PLN and USD/PLN futures are traded on the WSE while EUR/PLN, USD/PLN, CHF/PLN, EUR/USD, EUR/HUF and EUR/CZK futures are traded on the WCE. All for-
eign exchange futures contracts traded in the organized exchanges in Poland are settled in cash without the physical delivery of the underlying instrument. The WSE was the first market to start the trade in exchange futures in September 1998. However, the Warsaw Commodities Exchange won a dominant position in the market. Individual investors play a dominant role in the foreign currency futures market. Banks and other companies prefer the OTC outright-forward market, which is more liquid (National Bank of Poland 2002, 2007b).

Futures on stock market indices and individual stocks allow for an effective hedging of investment portfolios against changes of equity securities prices. The first to be traded in 1998 was the futures contract on the WIG20 index. To assure safety of trading and to guarantee the settlement of transactions, a separate Derivative Instruments Settlement Chamber was established within the National Depository of Securities. After each session on the WIG20 futures contracts market, DICS settles open positions of each investor. The first futures on stocks were introduced by the Warsaw Stock Exchange in January 2001. These contracts, similarly to other derivatives, are listed in the continuous trading market. NDS is responsible for the settlement and guaranteeing of transactions. Futures on stocks, despite a short history, became popular mainly among individual investors (National Bank of Poland 2002).

Interest rate swap (IRS) is an agreement on the exchange of interest payments (fixed against floating). The first interest rate swaps in PLN were concluded in London interbank market around 1998. On the domestic market, the first interest rate swaps were offered in 1999. By mid-1999, IRS transactions on WIBOR 6M became a standard in Poland. Typical maturities for IRS range from 1 year to 10 years, less frequent are quotations of longer maturity, mainly with non-bank clients in London, and the market for them is illiquid. Majority of IRS transactions is classified as speculative. The liquidity of this market is ensured by the participation of foreign (mainly London-based) banks. Interest rate swap market is dominated by foreign investors (National Bank of Poland 2002, 2004).

A new transaction of this form, called the Overnight Index Swap, has been introduced since 2004, extending the offer of available derivatives by an instrument
involving short-term interest rates (National Bank of Poland 2007b, 2009). Banks use OIS transactions to hedge against changes in financing costs on the money market and to speculate on interest rate and exchange rate movements (National Bank of Poland 2010).

CIRS is a combination of interest rate swap and foreign exchange swap. The parties of the swap exchange the principal amounts the spot exchange rate. During the life of the swap, the counterparties make interest payments in two currencies. Typical maturities of such transactions range from 1 to 10 years. Payment streams are based on 1, 3, and 6-month WIBOR or LIBOR. In case of basis swaps (subject to transactions in the interbank market), the minimum value of the transaction equals USD 25 million. Typical maturities for such transactions range from 1 year to 10 years. Payments are usually based on 3 or 6 month WIBOR, LIBOR or EURIBOR. The EUR and USD have a similar share in the total number of transactions. CIRS transactions are offered mainly for bank clients. Basis swaps are subject to transactions in the interbank market, mainly as transactions between domestic and foreign bank. Such transactions are sporadic and the terms of such transactions are negotiated between the parties. Domestic counterparties in CIRS transactions are mostly the largest telecommunication industry companies, which use the instrument to hedge against foreign exchange rate and interest rate risk (National Bank of Poland 2002, 2007b, 2009).

Interest rate option is an instrument which gives the buyer the right to buy (call option) or sell (put option) interest rate assets at a pre-determined price. The price of the option is the premium payable on the second day after the conclusion of the transaction. Futures contracts on WIBOR rate are usually the underlying assets for interest rate option. Banks and brokers are quoting volatility of prices of underlying assets. The interest rate option market is an over-the-counter market. Options are written by banks. PLN denominated options are also written by London investment banks. Domestic and foreign banks participate in the market. The dominant role in the market for interest rate options is played by domestic banks. The interest
rate options market in Poland is much less liquid than the foreign exchange options market (National Bank of Poland 2002).

Foreign exchange option is an instrument giving the buyer the right to buy or sell foreign currency in the future at a pre-determined exchange rate. In Poland clients (banks, which only buy options and do not write options and non-bank entities) prefer to buy entire option strategies to buying particular options. The benefit of such solution is the lower cost of purchase and the possibility of shaping profit making and loss limiting profiles depending on individual needs. Banks offer options contracts with maturities from 1 week to 1 year. The FX options market is a typical dealer market. Options are offered by domestic and foreign banks. Only a few domestic banks managing portfolios of FX options perform regular transactions in such instruments. In almost all transactions non-residents are parties to the contracts concluded. Most domestic banks owned by foreign companies are only intermediaries in the FX option market (National Bank of Poland 2002, 2007b).

A securities option gives the buyer a right to buy or sell the underlying instrument (stock, debt security) at a pre-agreed price. European style options are traded in the over-the-counter market in Poland. An instrument, which has many characteristics common with the option, and which is traded at a stock exchange is warrant. Warrant is a financial instrument, the price of which depends on the price or value of the underlying instrument. Warrant is an unconditional and irrevocable obligation of the issuer to pay the owners the settlement amount. Banks offer the securities options to clients. The interbank market practically does not exist. Securities options are purchased mainly by domestic entities, and the zloty is the settlement currency. Warrants may be issued by banks and other financial institutions. The underlying instrument are stocks of publicly traded companies. The execution of warrants on stocks may only be realized through the cash settlement. The National Depository of Securities is the clearing chamber for the instrument. Warrants are traded in the continuous trading system for the derivatives market. The instruments were introduced by the Warsaw Stock Exchange. The first listing was organized in March 1997.
Until October 2000, warrants were also traded on Bondspot (National Bank of Poland 2002, 2007b).

In 2005 in the off balance sheet positions of banks there appeared credit default swaps. However, the nominal value of such transactions confirms that the credit derivatives market has not developed in Poland yet (National Bank of Poland 2007b, 2009).
4. The nature and degree of competition between financial institutions in Poland

Competition in the Polish financial sector and its subsectors is relatively modest. Such a state of things results mainly from, as already mentioned, low levels of financial intermediation in Poland and the relative underdevelopment of the domestic financial market. Many households and enterprises still use only basic financial products and services. Thus, there is still a large part of the market to share and a number of potential clients to activate. In other words, the cake is still sufficiently big for all interested parts.

Another reason for the not so intense competition between financial institutions is the prevailing role of commercial banks. They dominate within the system, having the largest financial potential (assets and funds), resources, technology, human capital and experience. Moreover, they control many other groups of financial intermediaries. In fact, almost all of them are, more or less, dependent upon banks. Pension and investment funds are co-owned by banks, and in many cases even established (or co-established) by them. Insurance companies have the same distribution channels (e.g. bank branches) and their offering is to a large degree complementary to those of banks (e.g. insurance of mortgage loans, collateral), due to so-called bancassurance (i.e. cooperation in different forms and on different levels between banks and insurance companies) activity (see Śliperski 2000). Factoring and leasing companies are also owned by banks or, at least, finance their activity with banks’ loans. With this, banks are able to influence scale and directions of their activity. Moreover, links between banks and other financial intermediaries have sometimes also a personal character.

At the same time, cooperative banks in Poland do not constitute competition to commercial ones, as their range of activity is limited, as it was described in the previous section. Moreover, cooperative banks are small and their products are rather simple and classical. Some services are barely offered29 by those groups of banks or their quality leaves much to be desired (if one concerns, for instance, electronic

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29 In offering some services and products cooperative banks are even prohibited by law.
banking). Additionally, cooperative banks, from their very nature are aimed at rather different clients than commercial institutions.

Thus, somewhat surprisingly, it is only the SKOKs credit unions which have competed, and the credit unions have become very popular within the last few years, with number of clients exceeding 2 million. However, their legal status has been unclear, especially with reference to supervision of them and fulfilling by the SKOK sector requirements concerning safety and risk management.

The degree of competition among banks themselves has also been rather moderate.\(^{30}\) It increased in some periods and with reference to some products (e.g. mortgage loans in 2005–2006 or deposits during the period of problems with liquidity and confidence in the interbank market, at the onset of global financial crisis), but usually any significant competitive pressure on banks did not exist. It is reflected in high margins between deposit and loan interest rates. For example, it amounted, on average, to 8.9% in 2005 3.9% in 2009 and to 4%.

However, competition between banks (as well as among other financial intermediaries) probably will grow in the future. This may be so due to three factors. The first one is inevitable “saturation” of clients’ financial needs and consecutive decrease of the growth of demand. In such situation banks will have to intensify their activity aimed at building relations with clients, as well as improve quality of their services and also, perhaps, decrease prices.

The second reason for higher competition between banks has been the growing concentration within the sector (see Figure 12). So far, the concentration of the banking sector is low as compared to other CEECs and EU countries. The situation in the Polish insurance market is quite different. The market is highly concentrated:. C5 (the share of five the biggest insurance companies in the overall insurance sector), measured by insurance premium, amounted to 98% at the end of the 1990s, and still exceeded 70% in 2009 (Kozak, 2010). Such high level of concentration is a conse-

\(^{30}\) According to Pawłowska and Kozak (2007), commercial banks in Poland operated even in the conditions of monopolistic competition.
sequence of quasi monopolistic position of the PZU SA, the only insurance company that functioned in Poland before 1989.

![Figure 12. C5, C10, C15 for net assets of the commercial banks, 1996–2007](image)

Source: General Inspectorate of Banking Supervision (2007); Polish Financial Supervision Authority (2012).

As Figure 12 shows, concentration in the Polish banking sector was increasing, however not linearly, until 2002. It was a result of consolidation between banks. Then concentration decreased and started to grow again after 2007 (but looking only at C10 and C15). Similar tendencies occurred with reference to concentration of deposits and loans.31

Higher concentration can also be observed in the cooperative banks sector, being aimed at meeting capital requirements (EUR 1 million by the end of 2007, as a result of entering the EU). As a result, in 2010 all cooperative banks met the capital requirements (Narodowy Bank Polski 2011c).

However, concentration may go further as a result of consolidation process, affected by takeovers of local Polish-owned banks by local subsidiaries of foreign banks, mergers and acquisitions abroad resulting in the local subsidiaries of interna-

31 The only difference is that for deposits C5 amounted in some years even 60%. It is the aftermath of historical factors, namely privileged role of the PKO BP SA. This institution was the only deposit bank before 1989, collecting then almost all loans and after systemic change it retained its dominant position.
tional banks being amalgamated, heightening competition, and pressure for rising
cost efficiency.

The third factor that has contributed to growth in competition in the banking
sector is integration of Poland with the European Union. The same channels, i.e. con-
solidation and financial deregulation, that were observed in the EU during the adop-
tion of the euro, influenced the banking efficiency and competition of Polish banking
sector during Poland’s accession to the EU. It was mainly the consequence of the
consolidation process, strictly connected to the process of privatization of Polish
banks, in which, as it will be presented in details in the Section 12, first and foremost
was involved foreign capital from the euro area.

It seems that Poland’s entry into the EU resulted in an increase in competition
and efficiency mainly in the segment of corporate banking. The retail banking, on the
other hand, continued to be of a local character owing to bank lending relationship
with individual customers and SMEs.
5. Profitability of the financial sector and sub-sectors

5.1. Banking institutions

In 2010, the banking sector pre-tax earnings amounted to PLN 14.27 billion whereas net earnings amounted to PLN 11.48 billion, which means a growth of 40% over the previous year. (Narodowy Bank Polski 2010). Despite this significant improvement, the profits of the sector were still lower than in 2007-2008 as banks’ results came under pressure from write-offs as credit risks materialised in the aftermath of the global financial crisis. The main sources of improvement were an increase in net interest income and in net fees and commissions and a reduction in the negative balance of write-offs and provisions (Polish Financial Supervision Authority 2011).

Improved results were recorded by 440 entities in 2010 holding 80.1% of the sector’s assets. The results of the entire sector continued to be determined by the two largest banks, i.e. PKO BP and Pekao, which at the end of 2010 controlled c.a. 25% of the assets of the sector and were responsible for over 45% of the profits generated. It is worth underlining, however, that in 2010 seven commercial banks, eleven branches of credit institutions, and two cooperative banks showed a net loss amounting to PLN 1.3 billion. In five entities losses exceeded PLN 100 million (Polish Financial Supervision Authority 2011).

Good performance of commercial banks during the recent years resulted from lower net charges to specific provisions, higher interest and fee income, as well as good performance of the banks’ subordinate companies. Achieving such results was also possible due to increasing the loans to non-financial customers, mainly residential loans to individuals, and enhancing their quality. Moreover, the 2004 reduction of the corporate income tax (CIT) rate to 19% significantly reduced the income tax burden on earnings (National Bank of Poland 2006b, 2009). In 2010, according to recommendations of the NBP and the PFSA, commercial banks retained achieved incomes, without paying dividends to shareholders or restricting the scale of these dividends. This was made in order to be able to cope with possible negative consequences of the global financial crisis and forthcoming economic slowdown in
Poland, that could lead to impairment of loans portfolio (Narodowy Bank Polski 2010).

Most of the profitability and efficiency ratios have improved since 2001, as shown in Table 10. In 2010, net interest margin increased from 2.57% in 2009 to 2.78% (with the exception of co-operative banks – because of their substantial share of subsidized loans they were under pressure from the NBP’s low interest rates and simultaneously must cope with competition in the deposit market). The ratio of the balance of write-offs and provisions to average assets fell from 1.14% to 1.02%. Aggregated ROA increased from 0.81% to 1.05%. (Polish Financial Supervision Authority 2011).

It is worthwhile underlining the significant differences between the efficiency of commercial banks and cooperative banks. Cooperative banks were and still are characterized by a dominant role of net interest income and commission income in profits from banking activity and a lower share of irregular loans in total claims. The lower efficiency of cooperative banks is an effect of the difference in scale of operations and scope of activities, and the structure of customers served (mostly local society).

The increase in banks’ interest income as compared to services rendered to non-financial customers was mainly due to the lowering of interest costs. From among banks’ non-interest revenues, incomes from fees and commissions were the most important, as a result of bancassurance activity and the sale of non-banking products, among others, units in investment funds and insurance policies. This phenomenon mimics the European trend to gradually increase the significance of non-interest revenues in the structure of banks’ income (National Bank of Poland 2006b, 2009).

Changes in the banks’ interest income in relation to their assets have been accompanied with changes of NBP interest rates. The decrease of net interest margin was also a result of intensified competition particularly in housing and consumer loan markets (National Bank of Poland 2004, 2007b). Growing competition along with
the lack of possibilities of further decrease in margins induced banks to search for non-interest sources of income (National Bank of Poland 2010).

The global financial crisis did not negatively affect the Polish banking sector. ROA and ROE indicators declined, but they still remained higher than in other CEECs. Due to focusing on core credit-deposit activity, the Polish banking sector in 2007-2010 appeared to be more stable than banking sectors in European advanced economies (Narodowy Bank Polski 2011b).
Table 10 Profitability and efficiency ratios for banking sector in 1999-2010 (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>The whole sector</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
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<tbody>
<tr>
<td>ROA (net gain/loss to average asset value)</td>
<td>n/a</td>
<td>n/a</td>
<td>1.0</td>
<td>0.5</td>
<td>0.5</td>
<td>1.4</td>
<td></td>
</tr>
<tr>
<td>ROE (net gain/loss to average core capital)</td>
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<td>n/a</td>
<td>12.1</td>
<td>5.8</td>
<td>5.8</td>
<td>17.2</td>
<td></td>
</tr>
<tr>
<td>NIM (net interest income/assets)</td>
<td>n/a</td>
<td>n/a</td>
<td>3.7</td>
<td>3.4</td>
<td>3.2</td>
<td>3.3</td>
<td></td>
</tr>
<tr>
<td>Irregular loans to non-financial sector/gross claims</td>
<td>13.3</td>
<td>15.0</td>
<td>17.9</td>
<td>21.1</td>
<td>21.2</td>
<td>14.9</td>
<td></td>
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<table>
<thead>
<tr>
<th>Year</th>
<th>The whole sector</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
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<tbody>
<tr>
<td>ROA (net gain/loss to average asset value)</td>
<td>1.6</td>
<td>1.7</td>
<td>1.7</td>
<td>1.5</td>
<td>0.8</td>
<td>1.1</td>
<td></td>
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<tr>
<td>ROE (net gain/loss to average core capital)</td>
<td>20.6</td>
<td>22.5</td>
<td>22.5</td>
<td>21.2</td>
<td>11.3</td>
<td>12.7</td>
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<tr>
<td>NIM (net interest income/assets)</td>
<td>3.3</td>
<td>3.3</td>
<td>3.1</td>
<td>3.2</td>
<td>2.6</td>
<td>2.8</td>
<td></td>
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<tr>
<td>Irregular loans to non-financial sector/gross claims</td>
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<td>7.4</td>
<td>5.2</td>
<td>4.5</td>
<td>7.9</td>
<td>8.8</td>
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<table>
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<th>2004</th>
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<td>1.1</td>
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<td>0.5</td>
<td>1.4</td>
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<td>ROE (net gain/loss to average core capital)</td>
<td>14.2</td>
<td>14.5</td>
<td>12.8</td>
<td>5.2</td>
<td>5.4</td>
<td>17.1</td>
<td></td>
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<tr>
<td>NIM (net interest income/assets)</td>
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<td>3.5</td>
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<td>3.1</td>
<td>3.1</td>
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<tr>
<td>Irregular loans to non-financial sector/gross claims</td>
<td>13.7</td>
<td>15.5</td>
<td>18.6</td>
<td>22.0</td>
<td>22.2</td>
<td>15.6</td>
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<th>2008</th>
<th>2009</th>
<th>2010</th>
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<td>1.8</td>
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<td>1.6</td>
<td>0.8</td>
<td>1.1</td>
<td></td>
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<tr>
<td>ROE (net gain/loss to average core capital)</td>
<td>20.8</td>
<td>23.1</td>
<td>22.9</td>
<td>21.2</td>
<td>11.2</td>
<td>n/a</td>
<td></td>
</tr>
<tr>
<td>NIM (net interest income/assets)</td>
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<td>3.3</td>
<td>3.1</td>
<td>3.1</td>
<td>2.5</td>
<td>n/a</td>
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<tr>
<td>Irregular loans to non-financial sector/gross claims</td>
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<td>7.7</td>
<td>5.5</td>
<td>4.8</td>
<td>8.3</td>
<td>9.0</td>
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<th>2002</th>
<th>2003</th>
<th>2004</th>
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<tbody>
<tr>
<td>ROA (net gain/loss to average asset value)</td>
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<td>n/a</td>
<td>1.6</td>
<td>1.6</td>
<td>1.2</td>
<td>1.8</td>
<td></td>
</tr>
<tr>
<td>ROE (net gain/loss to average core capital)</td>
<td>n/a</td>
<td>n/a</td>
<td>19.4</td>
<td>18.2</td>
<td>12.2</td>
<td>18.3</td>
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</tr>
<tr>
<td>NIM (net interest income/assets)</td>
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<td>n/a</td>
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<td>Irregular loans to non-financial sector/gross claims</td>
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<th>Year</th>
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<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
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<tbody>
<tr>
<td>ROA (net gain/loss to average asset value)</td>
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<td>1.3</td>
<td>1.5</td>
<td>1.7</td>
<td>1.2</td>
<td>1.1</td>
<td></td>
</tr>
<tr>
<td>ROE (net gain/loss to average core capital)</td>
<td>17.6</td>
<td>14.5</td>
<td>17.2</td>
<td>19.3</td>
<td>12.7</td>
<td>n/a</td>
<td></td>
</tr>
<tr>
<td>NIM (net interest income/assets)</td>
<td>5.6</td>
<td>4.8</td>
<td>4.8</td>
<td>5.2</td>
<td>4.2</td>
<td>n/a</td>
<td></td>
</tr>
<tr>
<td>Irregular loans to non-financial sector/gross claims</td>
<td>4.9</td>
<td>4.0</td>
<td>3.0</td>
<td>2.8</td>
<td>4.3</td>
<td>5.2</td>
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</tbody>
</table>

The share of irregular (non-performing) claims in gross claims at banks was highly dependent on economic and financial standing of borrowers. However, better credit risk management and the constant introduction of new principles and guidelines by supervisory authorities improved banks’ portfolios. The reason for a deep fall of share of irregular claims in gross claims in 2004-2005 was also writing off by some banks their past lost claims to the off-balance sheet (National Bank of Poland 2007b). Moreover, the share of irregular claims to non-financial sector in gross claims decreased due to the change in the type structure of loan exposures, along with the rise of new residential loans to households, which were usually characterised by high quality. The improvement of the quality of the loans portfolio was also influenced by an improvement in the income of individuals and the sale of irregular claims to securitisation funds (National Bank of Poland 2009).

In commercial banks, which constituted circa 95% of the banking sector, the same trends as in the entire banking sector were observed. The performance in the cooperative banking sector, despite similar trends, was better (the share of irregular loans was smaller, in some years ROA and ROE were higher). This could be achieved because cooperative banks were not involved in financing large enterprises, which could have problems with repaying the liabilities, and they were focusing on providing services to the local market (National Bank of Poland 2004, 2006b). Moreover, due to the different type structure of the loan portfolio, particularly the lower share of residential loans with lower interest rates, the interest margin was higher in cooperative banks than in commercial banks (National Bank of Poland 2009).

The process of consolidation has strengthened in Poland in recent years. As a result of changes in the banking system (bank mergers, acquisitions and liquidations) the number of commercial banks conducting operational activity diminished at the end of 2010 to 646 banks and branches of credit institutions. The number of commercial banks remained unchanged at 49, the number of branches of credit institutions increased from 18 to 21 and the number of cooperative banks remained unchanged at 57 (Polish Financial Supervision Authority 2011).
After 2010 several mergers and acquisitions took place in the banking sector, however, the process was the most intensive in the years 1999-2002 (National Bank of Poland 2004, 2006b). In the first half of the nineties, take-overs of banks in poor financial condition by stronger banks were the major reason for consolidation process. On the other hand, the mergers conducted in the years 1997-2002 were a consequence of the privatisation of domestic banks as well as global-scale mergers including parent banks – foreign investors in Polish banks. However, the consolidation processes did not have a great impact on the condition of the banking sector or on its concentration. A slower development of large banks and a more rapid development of small and medium banks caused the drop in the concentration, which was also in line with the worldwide decline in the consolidation process (National Bank of Poland 2004, 2006b, 2007b). The most influential merger in the Polish banking sector took place in 2007, when Italian UniCredit took over Bank BPH SA. The merger of Bank BPH and Bank Pekao with the part of the divided Bank BPH slightly increased sector concentration measured by the share of 5 largest banks. Consolidation was intense also in the cooperative banks sector, aimed at meeting capital requirements: EUR 500,000 by the end of 2005 and EUR 1 million by the end of 2007 (National Bank of Poland 2009, 2010, Polish Financial Supervision Authority 2008b).

In 2010 share of five biggest banks in overall assets of the banking sector declined to 43.9% from 44.5% in 2009, however, their share in credit activity increased from 44.7% to 45.3% (Narodowy Bank Polski 2011c). The leading position was occupied by PKO BP (with balance sheet totals close to PLN 170 billion), followed by Pekao (PLN 130 billion) and BRE (PLN 85 billion). The assets of most cooperative banks were smaller than PLN 100 million and only 15 of them had balance sheet totals exceeding PLN 500 million. The leaders in this sector were Krakowski Bank Spółdzielczości and Podkarpacki Bank Spółdzielczy, whose assets were close to PLN 2 billion (Polish Financial Supervision Authority 2011).

Since the second half of the 1990s the Polish banking sector has exposed a decline in concentration. This decline was due to the higher growth rate of smaller

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32 See Section 11.
commercial banks’ assets than the growth rate of assets of largest banks. The concentration level of the Polish banking sector, measured by the share of five largest entities in the overall sector’s assets, was lower than the average for EU countries (National Bank of Poland 2009, Narodowy Bank Polski 2011b).

5.2. Collective investment institutions

In 2010, there were 50 investment companies managing over 400 investment funds, operating in the Polish market. The weighted average rate of return of investment funds equalled to 10.5%, declining from 20.5% in 2009. All types of funds achieved positive rates of return, but only funds investing in the domestic bond market recorded higher rates of return than in 2009. Such a modest growth of rates of return resulted from the bear stock market and the related low profits generated by funds involved in this market. However, in 2010 aggregate ROA for the investment funds sector achieved 30%, improving by 2.7 percentage points as compared with 2009. Aggregated ROE also increased from 33.7% in 2009 to 37.6% in 2010 (Narodowy Bank Polski 2011c, Urząd Komisji Nadzoru Finansowego 2011b).

The results achieved by equity investment funds since the beginning of this century have been changing in line with economic performance. The improvement of the economic climate on the stock exchange usually caused a significant rise of rates of return of these funds. The lowest rates of return were achieved at times of stock exchange market turmoil, in 2001 and 2008. On the contrary, the structure of the investment portfolio of steady-growth funds proved to be less dependent on volatile market conditions. They had good investment results despite volatility of the economic cycle. Performance of bond funds was highly dependent on situation on debt market. Downward price trends prevailing in the debt securities market always caused delayed reaction of investors and massive outflow of capital from these funds. Stable upward trends resulted in delayed investors’ responses to these tendencies as well (National Bank of Poland 2004, 2006b, Narodowy Bank Polski 2010). Rates of return achieved by foreign funds were highly associated with the volatility of the EUR/PLN and the USD/PLN exchange rates. Profitability of these funds
decreased along with the appreciation of the zloty against the euro and the US dollar (National Bank of Poland 2007b).

Table 11 Rates of return achieved by investment funds and open pension funds in 2001-2010 (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>Investment funds</th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2001</td>
<td>2002</td>
<td>2003</td>
<td>2004</td>
<td>2005</td>
</tr>
<tr>
<td>Equity funds</td>
<td>-17.7</td>
<td>1.1</td>
<td>35.0</td>
<td>23.8</td>
<td>22.9</td>
</tr>
<tr>
<td>Bond funds</td>
<td>15.9</td>
<td>13.9</td>
<td>2.8</td>
<td>6.0</td>
<td>6.5</td>
</tr>
<tr>
<td>Money market funds</td>
<td>16.7</td>
<td>9.8</td>
<td>5.0</td>
<td>5.0</td>
<td>4.7</td>
</tr>
<tr>
<td>Balanced funds</td>
<td>-5.5</td>
<td>4.3</td>
<td>17.9</td>
<td>14.4</td>
<td>18.1</td>
</tr>
<tr>
<td>Stable growth funds</td>
<td>6.0</td>
<td>11.0</td>
<td>11.6</td>
<td>10.7</td>
<td>11.6</td>
</tr>
<tr>
<td>Foreign equity funds</td>
<td>-27.4</td>
<td>-27.9</td>
<td>23.7</td>
<td>-11.8</td>
<td>12.2</td>
</tr>
<tr>
<td>Foreign bond funds</td>
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<td>10.5</td>
<td>-14.9</td>
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<td>Equity funds</td>
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</tr>
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<td>4.2</td>
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<td>Balanced funds</td>
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<td>-15.1</td>
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<td>Stable growth funds</td>
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<td>-16.4</td>
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<tr>
<td>Foreign equity funds</td>
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<td>-44.5</td>
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<td>7.8</td>
<td>16.1</td>
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<td>2001</td>
<td>2002</td>
<td>2003</td>
<td>2004</td>
<td>2005</td>
</tr>
<tr>
<td>The best open pension fund</td>
<td>10.0</td>
<td>17.4</td>
<td>16.8</td>
<td>16.7</td>
<td>16.4</td>
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<tr>
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<tr>
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<td>5.5</td>
<td>13.6</td>
<td>10.9</td>
<td>14.0</td>
<td>15.0</td>
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<td>2007</td>
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<td>2009</td>
<td>2010</td>
</tr>
<tr>
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<td>11.9</td>
</tr>
<tr>
<td>The worst open pension fund</td>
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<td>2.2</td>
<td>-17.9</td>
<td>12.5</td>
<td>9.3</td>
</tr>
<tr>
<td>Weighted average for all open pension funds</td>
<td>16.4</td>
<td>6.2</td>
<td>-14.3</td>
<td>13.7</td>
<td>11.2</td>
</tr>
</tbody>
</table>

It is worth noticing that since 2003 the method of distributing units of participation in investment funds has been changed. The funds pay the intermediaries commission on the funds obtained and also share the management fee with them. That is why, for example, some of the banks offered units of participation in funds belonging to several pension companies. It even happened that banks linked by equity with an investment company offered units of participation in competitive funds (National Bank of Poland 2004).

Since 2004, open investment funds may invest in derivatives, including OTC ones. Such investments should allow them to effectively hedge against investment risk. However, the use of derivatives was very limited. This was caused by very strict regulations concerning investment risk management (National Bank of Poland 2006b).

The mobility of investment fund customers is high. Investment fund sector is still at early stage of development. This results in high correlation between volatility of rates of return on investments in different types of investment funds and individual decisions made by the investment funds’ members on switching over to a different fund, without keeping long term investment perspective. Such decisions make the investment funds get rid of instruments that yielded unsatisfactory rates of return, increasing at the same time the market tendencies, as other market participants usually follow similar strategy (National Bank of Poland 2004).

In 2010, open pension funds generated positive rates of return, with lower risk level compared to that in 2009. As a result variances of rates of return generated by open pension funds declined. The average rate of return amounted to 11.2%. This result was achieved due to the high prices of debt instruments, which constituted a major part of portfolio of open pension funds (Narodowy Bank Polski 2011c). However, it is worth to underline a deep fall in aggregate return on assets (ROA) from 17% in 2009 to 8.5%. Aggregated return on equity (ROE) also decreased from 19.8% in 2009 to 8.9% in 2010 (Urząd Komisji Nadzoru Finansowego 2011c). This may be an evidence of change of investment strategies and building safer portfolios, less susceptible to market turmoil, but also less profitable.
In analysed period the investment performance of pension funds was progressing. Even in 2001 and 2007, years of drastic fall in prices on the Warsaw Stock Exchange, all open pension funds were able to generate positive rates of return, allowing them to meet the criterion of minimum 36-month required rate of return. However, it is worth underlining that funds, that achieved the highest rates of return under the circumstances of stock bull market, due to investments in stocks of small and medium enterprises, suffered heavily along with the decrease of stock prices (National Bank of Poland 2010). This appeared to be extremely evident in 2008, the year in which all funds incurred loses. But even then all open pension funds were able to achieve rates of return exceeding aforementioned minimum 36-month required rate of return (Narodowy Bank Polski 2010).

In the analysed period differences between rates of return within the entire sector were reduced. Differences between investment performance of pension funds with the highest and the lowest rates of return diminished – to 2.6 percentage points in 2010. This is the sign of growing similarity of investment strategies. The investment strategy of pension funds is similar to that of stable growth funds. The inclination to imitate strategies was reflected in rates of return, which reached nearly identical levels and small discrepancy in risks undertaken. Such behaviour was influenced also by limits on investment in particular categories of deposits and concentration limits for investments in instruments issued by one entity, as well as the structure of stock supply (National Bank of Poland 2006b, 2009).

The Polish investment fund and pension fund sectors are characterized by concentration which is higher than in the banking sector and smaller than in the insurance sector. Furthermore, investment fund sector is distinguished by smaller concentration than the open pension sector. However, the gap between the three largest investment companies in terms of net assets as well as the one between the

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33 The mandatory minimum rate of return for open pension funds is equal to either 50% of the weighted average rate of return of all open pension funds or that weighted average rate of return minus 4 per cent, whichever is lower. The weighted average rate of return must be calculated for a 36-month period twice a year (i.e. in March and September). The calculation method takes into account the return and market share of each pension fund. The weighted average rate of return must be published by the Polish Financial Supervision Authority (PFSA).
largest company and other companies has been widening constantly since 2000 [Narodowy Bank Polski 2011c]. The cause for it could be the fact that the largest entities were better prepared to take advantage of the opportunity brought about by an inflow of new funds into the sector.

Small changes were observed in the concentration of the open pension sector. Despite one merger that have occurred since 1998, the market concentration decreased – in 2010 three biggest open pension funds controlled 61.9% of overall assets, whereas in 2008 they controlled almost 64%. The reason for the drop in market concentration was the diminishing market share of the largest entity and the increase in the share of smaller management companies which attracted new investors [National Bank of Poland 2004, 2006b, 2007b, 2009, 2010, Narodowy Bank Polski 2010, Narodowy Bank Polski 2011c].

The number of open pension funds remained stable in the period analysed. Fifteen pension companies operated until 2009, since then fourteen funds have been operating as a result of the merger of two pension companies. Competition in the pension fund is protected due to the system of lottery of those persons who have not selected a pension fund themselves. According to this system, only funds which achieved rates of return higher than the respective weighted average rates of return for all funds in the last two calculation periods and their assets do not exceed 10% of total sector assets can take part in the draw. This solution prevents the largest and underperforming funds ones from participating in the lottery. At the same time, excessive concentration in the open pension fund system is hampered because of fees charged for switching funds [National Bank of Poland 2006b, 2010]. In 2010, the number of transfers of members between pension funds exceeded 600,000. It means that funds have to attach much importance to this form of acquiring new customers [National Bank of Poland 2007b, 2009, Narodowy Bank Polski 2011c].

What is of great importance to the future evolution of the collective investment services sector is the fact that capital groups having a large life insurance company within their structures are becoming ever more important shareholders. These groups have been dominating in the open pension sector since 1999 and constitute an
increasingly important part of the investment fund sector (National Bank of Poland 2004).

5.3. Insurance institutions

In 2011, the premium amount grew both in the life insurance sector (by 1.4%) and in the non-life insurance sector (by 11.7%). The total gross written premium in the entire sector amounted to PLN 57.2 billion, which was an increase of PLN 3 billion over 2010. Net financial result of life insurers in 2011 decreased by 20% to PLN 2.9 billion, while in the case of non-life insurance companies their net result grew by over 3.7% in comparison to 2010 reaching the amount of PLN 3.2 billion (Urząd Komisji Nadzoru Finansowego 2012).

The earnings of life as well as non-life insurance companies indicated an enhancement. Both the balance on the technical account and earnings improved. The items which influenced insurance companies revenues to the highest extent were earned premiums, net of reinsurance and investment income. On the other hand, the most important entries in equity and liabilities were paid claims and changes in technical provisions as well as operating costs time (National Bank of Poland 2007b). In general, larger insurance companies achieved better earnings. The strong brands and market positions of such insurers guaranteed high premium income without the need to offer competitive prices (National Bank of Poland 2006b).

It should be noticed, that at the beginning of this century the Polish insurance sector faced the problem of mass resignations from life insurance with an insurance capital fund. The failure to adjust the insurance and investment products to the needs and financial capacity of the customers during an economic slump of 2000-2001 resulted in massive resignations from this type of insurance (National Bank of Poland 2004). The second wave of resignations from unit-linked products occurred in 2008, as a result of collapse of the stock exchange market. However, since 2009 this trend has been reversed, as earnings from selling unit-linked products increased in 2010 by more than PLN 30 billion (Narodowy Bank Polski 2011c).
Table 121 Selected financial indicators of insurance companies in 2001-2010

<table>
<thead>
<tr>
<th>Year</th>
<th>Life insurance companies</th>
<th>Property and casualty insurance companies</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Premium (in PLN billion)</td>
<td>Premium (in PLN billion)</td>
</tr>
<tr>
<td></td>
<td>Net profit (in PLN billion)</td>
<td>Net profit (in PLN billion)</td>
</tr>
<tr>
<td></td>
<td>ROE (%)</td>
<td>ROE (%)</td>
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<tr>
<td></td>
<td>ROA (%)</td>
<td>ROA (%)</td>
</tr>
<tr>
<td>2000</td>
<td>8.3</td>
<td>12.5</td>
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<tr>
<td>2001</td>
<td>9.3</td>
<td>13.1</td>
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<tr>
<td>2002</td>
<td>9.9</td>
<td>13.2</td>
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<td>2004</td>
<td>12.7</td>
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<td>15.3</td>
<td>15.7</td>
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<tr>
<td></td>
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<td>0.2</td>
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<td></td>
<td>0.4</td>
<td>0.7</td>
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<td>2006</td>
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<td>2007</td>
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<td>2008</td>
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<td>2009</td>
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<tr>
<td>2011</td>
<td>3.3</td>
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In 2000-2011 the profitability indicators remained at safe levels. In 2011, aggregated ROE remained at the level of 19.8% – 22.9% in the sector of life insurers and 17.6% in the sector of non-life insurance companies. Aggregated ROA reached 4.2%: 3.3% in the sector of life insurers and 5.7% in the sector of non-life insurers (Urząd Komisji Nadzoru Finansowego 2012).

Concentration of the Polish insurance sector is systematically decreasing. However, in comparison to other sectors, the insurance sector is characterized, as it was mentioned in the Section 4, by a high level of concentration. The reason for this is a very high share of the PZU Group in the both sectors. However, this concentration tends to decrease due to the fact that smaller insurers respond to market needs more rapidly and flexibly by offering new products. They are also more competitive and attract customers by minimizing insurance costs (National Bank of Poland...
This is why the share of five biggest life insurers in the premiums decreased from 71.5% in 2008 to 58.7% in 2011 and share of five biggest insurers in the property & casualty sector decreased to approximately 63.4% in 2011 (Urząd Komisji Nadzoru Finansowego 2012).

In terms of premiums, the PZU Życie still holds the leading position, however, its share in the Polish insurance market dropped from 32.8% in 2009 to 30.8% in 2011. The company maintains its dominating status on the market thanks to group insurance services. PZU retained its leading market position also in the property & casualty market. Its share measured by insurer's share was equal to 32.6% in 2011. For many years PZU Group has been a dominating entity on the Polish insurance market. In view of the current level of concentration its status seems safe (National Bank of Poland 2007b, Narodowy Bank Polski 2011c, Urząd Komisji Nadzoru Finansowego 2012).

The insurance market concentration in Poland is higher than in EU countries, where the liberalized insurance market has been functioning for a longer time. A high concentration in Poland results from a small number of insurance companies or and a high market share of 1 insurer (National Bank of Poland 2004). Polish insurance market can be classified, both in terms of premium amount per capita and the ratio of premium to GDP, as a less developed (National Bank of Poland 2007b).
6. The present regulatory framework and the key changes in financial regulation

6.1. Introduction

The Constitution of the Republic of Poland (1997) specifies the frameworks within which legal regulations of the financial services sector are created. It introduces the principle of freedom of business activity as the basis for the whole economic system. As regards the financial sector, this freedom is expressed in the following:

- freedom to conclude contracts of any subject and of any contents,
- freedom to select business partners and a possibility to perform cross-border activities,
- freedom of competition.

According to the Constitution, provision of financial services is subject to control and supervision by the State, while “entities put funds entrusted to them by other entities (natural and legal persons) at risk of their operations”.

The need to adjust the Polish legal system to EU law and to the commitments stemming from Poland’s membership in the Organization of Economic Cooperation and Development (OECD) was the main reason for the amendments introduced to Polish legislation. The process of adjustment of the Polish law was very dynamic, since regulations regarding the financial sector in the European law have been frequently changed. This was reflected in numerous amendments to acts or in the creation of new acts (National Bank of Poland 2004). Moreover, some changes have been introduced as a result of EU laws, and not of domestic legislation, like for example regulations which have introduced the single license (passport) principle in the financial sector of EU countries.

6.2. Regulations regarding the entire financial sector

6.2.1. Changes in the Foreign Exchange Law

The Foreign Exchange Law specifies the rules of exchanging the Polish currency to foreign currencies and procedures for the issuance of permissions to perform market operations that are related to spending in terms of the foreign currency.
Changes in the *Foreign Exchange Law* were mainly related to the fulfilment of Poland’s obligations towards the OECD and the EU.

Until 2002, foreign exchange operations were regulated by the *Foreign Exchange Law of 1998* ([Act of December 18, 1998 – Foreign Exchange Law](#)). The adopted legal solutions, despite their contribution to the liberalisation of foreign capital flows, did not meet the standards of the European Union. Non-residents were not able to purchase short-term securities or financial derivatives in Poland without a foreign exchange permit. However, these restrictions did not pertain to purchases by non-residents of Treasury securities and financial derivatives offered on stock exchange markets, nor to the purchase of short-term securities and financial derivatives offered by authorized banks.

The new law ([Act of July 27, 2002 – Foreign Exchange Law](#)) implemented in 2002 have met the obligations stemming from European Union law. The abolition of restrictions in the flow of capital to countries within EU, countries within the European Economic Area and other countries in the OECD, made it possible for residents to freely invest on capital markets of these countries. As a result of these changes, residents obtained the right to maintain accounts with foreign banks and to deposit funds on such accounts.

Restrictions on capital flows have been additionally lifted since 2007. Amendments introduced in this very year to the *Foreign Exchange Law* ([Act of 26 January 2007 Amending the Foreign Exchange Law Act and Other Acts](#)) resulted from obligation to ensure compliance of Polish legal regulations with EU law. The most important solutions lifted restrictions on (National Bank of Poland 2010): disposal and acquisition of securities and participation units of joint investment funds by non-residents from third countries, as well as granting and taking loans and lending facilities in trading between residents and non-residents.

The amendment to the *Foreign Exchange Law* didn’t remove restrictions on settlements in foreign currency between residents. Removing restrictions imposed on agreements and on performing other activities which result or may result in domestic settlements in foreign currency was put on hold.
6.2.2. Amendments to the *Bankruptcy Law*

A crucial issue for entities that execute transactions on the financial market is the guarantee of settlement of mutual claims. Thanks to the regulations of the *Bankruptcy and Recovery Act* effective from October 1, 2003 and amended in 2009, such settlements are guaranteed through netting (mutual compensation of claims and liabilities in the case of insolvency of one of the parties to the transaction). Thanks to the netting, the solvent party is able to close transactions concluded, but yet not executed by the parties and the compensation of all mutual payments resulting from all executed transactions is possible. Another important regulation introduced to strengthen the security of trade is the legal guarantee that an order placed by a participant of the financial market in the payment system will be performed even in the case the participant’s bankruptcy is announced (National Bank of Poland 2004).

6.2.3. Implementation of the European Directive MiFID

On 17 June 2010 the requirements of European Directive MiFID (*Markets in Financial Instruments Directive*) entered into force in Poland. The MiFID has been introduced into the Polish legal system through the *Act on Trade in Financial Instruments* together with its implementing provisions. Its implementation means that investors are entitled to the same level of protection in Poland’s financial markets as they are in other EU states. The protection offered to clients in line with the implementation of the MiFID in Poland consists of, inter alia:

- submission and preparation of detailed information on the products and services in a way which is comprehensible and not misleading,
- assessment of the client’s understanding of the product, particularly the risks involved,
- verification whether the services or products to be provided are suitable by establishing client’s level of investment knowledge and experience.
6.3. Regulations regarding the banking sector

6.3.1. National Bank of Poland

The reform of Polish banking system started in 1989 when the domination of the mono-bank centralized system was overcome with the Act on the National Bank of Poland of January 31, 1989. Since then, the NBP has started to be a central bank functioning in a market-oriented economy (Janc 2004).

The year 1998 was a milestone for the legal and institutional framework for Polish central bank and the banking sector. This framework was first outlined by the new Constitution of the Republic of Poland of April 2, 1997, and then fleshed out by two acts adopted on August 29, 1997: the Act on the National Bank of Poland and the Banking Act. The legislation previously in force in this regard, put in place in 1989 and since then constantly amended, no longer corresponded to the requirements of the economic transformation process in Poland, nor to the needs of the developing banking sector. The necessity of implementing new legislation also stemmed from the commitments undertaken by Poland under the agreement on association with the EU, which was accomplished in 1994 (National Bank of Poland 1999).

The new Constitution took effect on October 17, 1997, while the aforementioned banking legislation took effect on January 1, 1998. The Constitution and the Act on the NBP specify the position of Poland’s central bank. They define the NBP as the country’s central bank, which has the “exclusive right to issue currency, and to determine and implement monetary policy”. According to the Constitution, the NBP is responsible for the value of the zloty, which is the Polish currency. The Act on the NBP stipulates that the basic objective of NBP activity is to “maintain price stability”, and the Bank is at the same time to act in support of government economic policies, as long as this does not put a constraint on fulfilment of the basic objective of the central bank.

The Constitution, and following on from it the Act on the NBP, also identified the directing bodies of the central bank, which include the President, the Monetary Policy Council (MPC) and the Management Board. These new legal provisions have changed the position, role and powers of the NBP President and Management Board,
and vested major powers in the MPC. Changes also occurred in the position of banking supervision. The Act entrusted supervisory powers to a Commission for Banking Supervision. Since January 1, 2008, this Commission has replaced with the Polish Financial Supervision Authority (see point 6.6).

The most important reasons which lay behind these changes included the need to establish and protect the independence of the central bank. The implemented changes established new operational interrelationships between the principal directing bodies of the NBP and modified the operating conditions for the whole central bank.

According to the existing legal framework, the President of the National Bank of Poland is appointed by the Sejm (the lower house of the Polish parliament) at the request of the President of the Republic of Poland for a six-year term of office, and chairs the Monetary Policy Council and the NBP Management Board. The President is authorised to represent the Bank in its external contacts and is the superior of all NBP staff. The President of the NBP is also entitled to participate in the debates of the Sejm and Council of Ministers. The President may serve the maximum of two terms. Recall of the President is possible only in rare cases enumerated in the law.

The MPC convened for its first session on February 17, 1998. The MPC is composed of the President of the NBP as Chairperson and nine other members, specialists in the field of finance, appointed in equal numbers by the President of the Republic of Poland, the Sejm and the Senate (the upper house of the Polish parliament). The basic responsibility of the MPC is to prepare annual monetary policy guidelines and submit these to the Sejm, for the information thereof, alongside the submission by the Council of Ministers of the draft Budget. The Council’s responsibilities also include:

- establishing the parameters of monetary policy, which primarily involves setting NBP base interest rates, determining the procedures governing the reserve requirement and setting the reserve ratio, and determining the principles applicable to open market operations,
• setting ceilings on the liabilities arising from loans and advances drawn by the NBP from foreign banking and financial institutions,

• approving the NBP budget and the report on the activity of the NBP, and accepting the Bank’s annual accounts.

At the beginning of its term, the Council drafted and adopted the *Medium-Term Monetary Policy Strategy, 1999-2003*, in which the Council laid out Poland’s monetary policy strategy for the period preceding membership in the European Union. This document specified that the medium-term monetary policy objective was to be a reduction in annual inflation to below 4% by the year 2003 (Monetary Policy Council 1998). In 2003 new strategy has been implemented. According to *Monetary Policy Strategy beyond 2003*, “the monetary policy is targeted to attain a stable inflation rate of 2.5% after year 2003 with a permissible volatility band of ±1 percentage point either side of this target” (Monetary Policy Council 2003).

The activity of the National Bank of Poland is directed by its Management Board, composed of the President of the NBP as Chairperson, and from six to eight other Board members, of which two are Vice Presidents of the NBP. The NBP Management Board is charged with implementing resolutions of the MPC, performing responsibilities with respect to exchange rate policies, supervising open market operations, and performing assessments of foreign currency trading, the operations of the banking system, the circulation of currency and monetary settlements. The Board also adopts resolutions on other matters, which include resolutions on the licensing of banks to conduct foreign exchange operations.

### 6.3.2. Commercial banks

Commercial banks, as it was mentioned in Sections 2 and 3, have substantially developed following the 1989 reforms. The *Banking Law of 1989* made it possible to form a two-tier banking system typical of market economies. In the beginning the Polish banking sector included 9 regional commercial banks, independent of the NBP. However, shortly afterwards the key process for banks turned to be the privatization connected with the increase of foreign capital’s share in the whole sector.
Such increase was a result of seeking strategic foreign partners, which would be able to support banking transformation by sharing their practical knowledge on how to conduct banking activity under the circumstances of market economy (Janc 2004).

The reform of the banking sector was one of the crucial components of the 1989 reforms. In January 1989 the Sejm passed two acts: the *Banking Act* and the *Act on the National Bank of Poland*. The basic importance of the first of them was to be seen, among others, in the reconstruction of the banking sector, as the act allowed for the operation of state banks, joint stock banks and cooperative banks, an abolition of the mechanism of automatic lending for governmental purposes, as well as the extension of the catalogue of banking activities and services (National Bank of Poland 2001).

The Acts of 1989 were complex in the way they set out to regulate the operation of the banking system. However, as the time went by banking legislation became a component of a larger whole, which forced the introduction of new acts in 1997, specifically aforementioned the *Act on the NBP* of 1997 and the *Banking Act* of 1997. These acts have become the source of principles of conducting banking business, as well as the principles of performing banking supervision, and bank liquidation and bankruptcy procedures (National Bank of Poland 2001).

The term “bank” is the basic notion used by the *Banking Act*. The bank is defined as a legal person, operating on the basis of authorisation to perform banking operations that expose to risk funds which have been entrusted to the banks. The legal-penal protection of banking operations is maintained by assigning banks a monopoly to use the term “bank” and to perform banking operations consisting of collecting funds from other natural or legal persons or other organisational units that do not possess the status of a legal person.

According to the *Banking Law*, banks may operate as state banks, joint stock banks and cooperative banks. Pursuant to the provisions introduced in 2007, it is possible to divide a bank, providing that permission is given by the supervisory body. The supervisor can refuse to give such permission, however, if such division would be
unfavourable to the prudent and stable management of the divided bank or banks to which the assets of the divided bank are transferred (National Bank of Poland 2009).

Pursuant to the Banking Act, a bank may be established, if:

- it is ensured that the bank will be provided with own funds, at the amount which shall not be less than zloty equivalent of 5 million EUR, calculated at the exchange rate published by the NBP on the date of granting the authorisation to establish the bank, the initial capital shall be contributed in cash considerations (in Polish zloty), non-cash contributions may be contributed only in the form of equipment and property holding related to banking business and subject to the condition that their value shall not exceed 15% of the initial capital;
- at least two persons proposed to take up positions of the management board members possess the education and professional experience necessary to manage the bank and possess a fluent command of Polish language; two members of the management board, including the president, shall be appointed with the consent of the PFSA, which have considered the request submitted by the supervisory board;

According to the provisions implemented in the Banking Act, each bank shall maintain the sum of own funds at a level that represents not less than 8% of risk-weighted assets and off balance sheet commitments. A bank starting operations shall maintain the risk based capital ratio at a level not lower than 15% for the first 12 months of operations, and for the next 12 months at a level not lower than 12%.

The changes that have been introduced to the Banking Act since 1997 have been largely a consequence of gradual adaptation of Polish regulation to EU requirements (Kowalski, Matysek-Jędrzych 2010). Significant regulatory changes took place in Polish banking sector. These changes were related to the implementation of the New Capital Accord, prepared by the Basel Committee (Directive 2006/48/EC, Directive 2006/49/EC). Then, on April 2011, the parliament passed amendments to the Banking Act and the Act on Trading in Financial Instruments, which are the first steps towards the implementation of the Directive 2010/76/UE (the so-called CRD III).
However, some changes in a domestic legislation have been introduced not for purpose of the adjustment to the EU law. Among them, one can distinguish the amendment to the Polish banking legal framework not linked with EU legislation is the Act on the so-called Prevention of Usury, which has been passed by Polish parliament in 2005. According to the Act the maximum interest rate which can be charged on bank loans, trade credit and cash loans cannot be higher than four times the lending credit rate of the NBP. This regulation limits also the total value of all fees and commissions arising from a conclusion of a consumer loan agreement (excluding costs of credit insurance and security) to 5% of the value of a consumer credit.

6.3.3. Cooperative banks

After 1989, the cooperative banking sector, due to its fragmentation and poor situation, was the area that required the restructuring. Until the Act on Changes in the Organisation and Operation of the Cooperative Movement of 20 January 1990 came into effect, the cooperative banks must affiliate in the Bank Gospodarki Żywnościowej (BGŻ), a then state cooperative bank. In September 1992 the President of the NBP decreed that all cooperative banks should be affiliated to one of the about to be created regional banks or to the BGŻ. Shortly after, co-operative banks had started establishing three affiliating banks.

However, a deep crisis was observed in the cooperative banks sector in the second half of the nineties forced legislators to establish a new legal framework for its secure operation. The new Act (Act on the Restructuring of Cooperative Banks and of Bank Gospodarki Żywnościowej of June 1994) implemented the three-tier structure of the cooperative banking sector, consisting of cooperative banks, of regional banks and with the BGŻ at the top. By the end of 1997 nine regional banks, provided for in the aforementioned Act, had been established, as cooperative banks were obliged to affiliate to one, geographically appropriate, regional bank. Additionally, two existing earlier affiliating banks were operating outside the three-tier structure, while one adopted the status of a regional bank in accordance with the Act on the
Restructuring of Cooperative Banks. Consequently, BGŻ was transformed into a joint-stock company (National Bank of Poland 2001).

The implementation of the Act improved the effectiveness of the cooperative banking sector. However, a few negative aspects also occurred, such as the creation of too many relatively weak regional banks. The consolidation of regional affiliations of the cooperative banks through a system of mutual guarantees was one of the main assumptions made in the construction of the Act. However, this assumption was not met, due to reluctance of stronger cooperative banks to take over the responsibility for the liabilities of smaller banks (National Bank of Poland 2001).

This situation required further changes. In January 2001 a new act regulating cooperative banking sector was implemented (Act on the Operations of Cooperative Banks, Their Affiliation, and Affiliating Banks of December 7, 2000). Since 2001 a two-tier structure of cooperative banks sector has been established and the cooperative banks have been burdened with the requirement of the increase of own funds, to the level of EUR 1,000,000 by 31 December 2010. Cooperative banks have still been obliged to affiliate – only a co-operative bank that reached minimum EUR 5,000,000 of own capital can decide to remain free with no affiliation. According to the new Act it is easier for affiliating banks to merge, as they do not need to make an affiliation agreement with the BGŻ anymore.

6.3.4. The Bank for the Domestic Economy (BGK)

The Bank for the Domestic Economy (Bank Gospodarstwa Krajowego – BGK) is Poland’s only state-owned bank. The BGK’s status is defined by the special law of 14 March 2003 (Act on Bank Gospodarstwa Krajowego). The regulations enable the BGK to maintain the central government budget’s account as well as the accounts of the state administration and state legal persons within the sector of public finance. This activity, however, will become effective only upon Poland’s accession to the euro area.

The primary business objective of the BGK is to provide banking services for the public sector entities, in particular through the support of the government’s eco-
onomic programs, as well as local government and regional development programs implemented with the use of public funds, including those of the EU. The BGK is currently authorized to provide services to the central budget as regards current accounts of budgetary establishments, their auxiliary units and special funds, as well as the accounts of central or local legal persons. It should be underlined, however, that the BGK is not the only bank providing such services, as non-budgetary institutions and government agencies have freedom to select a bank.

6.3.5. The Bank Guarantee Fund

The reconstruction of the Polish banking system required the establishment of an institution that would deal with banking deposit guarantees. On February 1995 such an organisational body in form of the Bank Guarantee Fund was established (Act on the Bank Guarantee Fund of 14 December 1994). The legal provisions on the BGF are in full in compliance with the Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009, which amends the Directive 94/19/EC on deposit-guarantee schemes. According to the law, the basic tasks of the Fund include, inter alia: reimbursement of funds accumulated on bank accounts in the event of the bankruptcy of a bank which is a participant in the deposit guarantee scheme as well as financial assistance to banks which have found themselves faced with a loss of solvency and are engaging in independent reforms. The entities covered by the guarantee system contribute compulsory annual payments to the Fund and are obliged to establish a protection fund for guaranteed funds.

The legislator specified the deposit guarantee principles. Deposits maintained in all banks with their registered offices within the territory of the Republic of Poland are covered by the Fund. In the event of the bankruptcy of a domestic bank, the BFG is obliged to pay the guaranteed funds up to the amount determined by law, except for the deposits of, inter alia: the State Treasury, banks, brokerage houses, pensions funds, investment funds, entities providing insurance services, managers of the bank and its main shareholders (holding at least 5% of the shares). Since 2010, a deposit amount not exceeding the equivalent of EUR 100,000 has been guaranteed in full, but
the guaranteed amount is as before calculated from the total funds located in all the accounts of a single person in a given bank, while in the case of a joint account, each account holder is entitled to a separate guaranteed amount.

6.4. Regulations regarding the non-bank institutions sector

6.4.1. Insurance companies

A package of four acts (Insurance Business Act of May 22, 2003; Act on Compulsory Insurance, the Insurance Guarantee Fund and the Polish Motor Insurers’ Bureau of May 22, 2003; Act on Insurance and Pension Funds Supervision and on Insurance Ombudsman of May 23, 2004; Insurance Intermediation Act of May 22, 2004), to become effective on January 1, 2004 was adopted in 2003, creating legal framework for insurance activity. Changes introduced to aforementioned acts are of a systemic nature. They are aimed at eliminating the contradictions in the provisions of the acts, Ordinances of the Minister of Finance and the Polish Civil Code, by moving civil law regulations regarding the insurance agreement to the Civil Code, as the previous Insurance Business Act (Insurance Business Act of July 28, 1990) and the accompanying executive acts regulated civil law issues.

Polish insurance law was adjusted not only to EU legal requirements, but also to international conventions. In line with the provisions of relevant EU Directives, the position of Polish insurance firms and their solvency have been strengthened. The first step aimed at achievement of this target was the introduction of Solvency I. According to Polish law, the Solvency I increased the amount of a minimum guarantee capital for limited companies in Group I (life insurance) from EUR 800,000 to EUR 3,000,000, for Group II (non-life insurance) groups of 1-9 and 16-18 from EUR 300,000 and EUR 200,000 to EUR 2,000,000. It also introduced an annual indexation of the minimum guarantee capital. The new assessment system on solvency is to be introduced in form of the Solvency II.

New regulations introduced the single passport principle. The Investment Services Directive (93/22/EEC) has helped create a single market in securities by eliminating a first set of legal obstacles. It introduced the ‘single passport’ for investment
firms whereby a firm can operate EU-wide on the basis of mutual recognition of supervision by its home Member State. This 'single passport' is widely used and access to “regulated markets” and exchanges has been liberalised. It enables the Polish insurers to conduct business activity on the territory of EU Member States in a direct manner (cross-border services) or by opening branches, and foreign insurance companies to launch their products on the Polish market (as branches of foreign insurance companies).

The separate statutory regulation of insurance intermediation resulted from the fact that this is a type of activity different from insurance activity. The most important provisions introduced by amendments to the Insurance Intermediation Act included (National Bank of Poland 2006b), inter alia:

- the precise stipulation of the requirements insurance agents must satisfy and their qualifications,
- the introduction of compulsory professional indemnity insurance for so-called multi agents that perform agency services for more than one insurance company with regard to the same type of insurance,
- the stipulation of the principles of an insurance broker’s liability.

6.4.2. The Insurance Guarantee Fund

According to the law, the primary task of the Fund is to meet claims arising from the compulsory liability insurance of motor vehicles holders and civil liability of farmers for damage caused on Polish territory (Compulsory Insurance, the Insurance Guarantee Fund and the Polish Motor Insurers’ Bureau Act of May 22, 2003):

- for bodily injuries – when the damage was caused in circumstances justifying the liability of motor vehicle holder or driver, when their identities have not been identified;
- for property damage, in case where the consequence is death of any participant, injury of an organ or loss of health that lasts longer than 14 days and the damage was caused in circumstances justifying the liability of a motor vehicle holder or driver, and when their identities have not been identified; in case of vehicle’s dam-
age, benefit funds shall be reduced by the amount of 300 EUR, determined by using the average rate announced by the Polish National Bank in the day of settling the compensation;

• for both personal injuries and property damage, if:
  o the holder of the identified motor vehicle, the movement of which caused the loss, has not been insured by the compulsory insurance of motor vehicles holders;
  o the holder of the identified motor vehicle, the movement of which caused the loss, registered abroad in a country whose National Bureau is a signatory of the Uniform Agreement between the National Bureaus – Internal Regulations, has not been insured by compulsory insurance of motor vehicles holders and whose motor vehicle has not had any motor vehicle registration numbers or these numbers have not been assigned to that vehicle by the competent authorities at the time of the event;
  o a farmer, a person staying with him in one mutual household or a person employed on his farm caused a loss resulting in death, bodily injury, health disturbance as well as a loss, a destruction or a damage of property and the farmer has not been insured by the compulsory insurance of farmers.

The Insurance Guarantee Fund meets claims of personal injury and property damage caused by uninsured motor vehicle holder, if the damage happened within 30 days from the date of vehicle’s purchase in the EU and the vehicle should be registered in Poland. For damages caused to foreigners, citizens of the countries whose National Bureaus are not the signatories of the Uniform Agreement between the National Bureaus – Internal Regulations, the Insurance Guarantee Fund shall pay compensation on the basis of reciprocity.

The Fund pays out 100% of due compensations under compulsory civil liability agreements of vehicle owners, farmers and the insurance of farm buildings. In the case an obligation to conclude an insurance agreement results from provisions of other acts or international agreements ratified by Poland, and in the case of life in-
surance policies, the Insurance Guarantee Fund pays out funds in the amount of 50% of receivables (but not more than the zloty equivalent of EUR 30,000).

6.5. Regulations concerning investment funds

The first investment fund in Poland was established in 1992. However, since then important changes in the organisation and operation of the investment funds have been introduced also. Due to the considerable number of amendments introduced and in order to ensure transparency, a new Act on Investment Funds was developed. The Act took effect on July 1, 2004 (Act on Investment Funds of May 27, 2004). According to this Act, an investment fund is “a legal entity whose sole area of activity is the collective investment of capital raised from the public – and also through private offerings, in instances defined in the Act – of offering the sale of units or investment certificates, in the securities, money market instruments and other property rights defined in the Act”.

From July 1, 2004, investment funds may operate as:

- open funds;
- specialised open funds;
- closed-end funds.

The hitherto operating mixed and specialised closed-end investment funds became closed-end investment funds by end-June 2005.

Investment funds may also be divided into several categories from the point of view of their investment strategies. In the Polish market, the following types of funds operate:

- equity funds;
- bond funds;
- balanced funds;
- stable growth funds;
- money market funds.
In order to give investors access to a wider range of investment funds and diverse asset management forms, the Act on Investment Funds introduced new fund forms and types. These are:

- funds with various participation unit categories;
- funds with separate sub-funds (so-called umbrella funds);
- master-feeder (hub and spoke) funds;
- funds of funds.

The most important provisions that affect the investment fund market included enabling (National Bank of Poland 2006b):

- investment companies to provide asset management services and consulting services with regard to securities trading;
- open funds to use a wider range of derivatives, including derivatives traded on the OTC market;
- the establishment of funds consisting of separate sub-funds which implement their own investment policies (umbrella funds);
- the establishment of securitisation funds and portfolio funds;
- the transformation of specialised open investment funds into open funds.

Pursuant to the Act on Investment Funds, funds may operate as a securitisation funds in the closed-end form. These funds can be established as standardised or non-standardised. A standardised fund has a form of a fund with separate subfunds which allows it to differentiate the risk level in individual subfunds. A non-standardised fund cannot be an umbrella fund. Such a structure increases the investment risk, hence its offer may be addressed on condition than the issue price of one certificate is an equivalent of at least 40,000 EUR. A standardised fund has to invest at least 75% of the assets of a subfund in one pool of receivables unless the statutes state otherwise. In the case of non-standardised funds, investments may concern various receivables (National Bank of Poland 2007b).

According to Polish law, investment funds may invest up to 5% in foreign investments and maximum of 42.5% in domestic equities (increased from 40%). No limits are put on the purchase of the domestic Treasury securities. However, on De-
cember 15, 2011, the European Court of Justice has ruled that Poland must lift the restrictions it placed on foreign investments.

6.6. Regulations concerning open pension funds, individual pension accounts, employees’ pension schemes

Open pension funds were created in Poland in 1999. They started working on April 1999. Any person covered by the national social security system and born after 31 December 1968 is required to join an open pension fund and sign a contract, otherwise one will be randomly assigned to one of the funds. People born between 1 January 1949 and 31 December 1968 were allowed to choose whether or not to opt into the new mandatory system introduced in 1999. Their decision was, however, irreversible (OECD 2008).

The retirement age is now set in Poland at 67 for women and for men. Before reaching that age, the insured cannot withdraw their retirement assets. However, in case of death of the insured, the assets are subject to inheritance law (Act of 28 August 1997, On Organization and Operation of Pension Funds).

Open pension funds constitute the so called II pillar of pension system (pension in the I pillar is based on the distributional system which has the character of the generation agreement). For persons participating in the open pension funds contributions for the pension plan in part are counted in the individual account led by the ZUS (the Social Insurance Institution) and in part handed over by the ZUS to the open pension fund chosen by the employee. These contributions are counted in the individual account. Contributions paid in the II pillar are exempt from the income tax. On May 1, 2011, a new amendment to social insurance law went into effect. According to, employees now contribute 2,3% of their monthly salaries to the II pillar. Starting in 2013, contributions to II pillar will be gradually increased until reaching 3,5% in 2017.

Open pension funds can invest assets without any limits solely in securities issued by the Polish Treasury or the National Bank of Poland and loans and advances granted to those entities, as well as in securities, loans or advances guaranteed by those entities. Funds can also invest up to (National Bank of Poland 2004):
• 20% of the assets in bank deposits and bank securities,
• 40% of the assets in shares listed on a regulated stock exchange market,
• 45% of the assets in publicly traded municipal bonds (20% in non-publicly traded bonds),
• 40% of the assets in secured and publicly traded commercial bonds (10% in non-publicly traded bonds),
• 10% of the assets in unsecured bonds and other debt securities issued by public companies,
• 40% of the assets in publicly traded mortgage bonds,
• 10% of the assets in closed-end investment funds.

A series of other changes have been introduced to the functioning of pension funds after 1999. Changes in the law were aimed to reduce the costs borne by the system users, to streamline the operation of the funds and to provide maximum return on investment. Among others, since April 1, 2004 (Act Amending the Act on the Organisation and Operation of Pension Funds and Other Acts of August 27, 2003), regulations have been in force, which introduced a new method for calculating the minimum required rate of return (reaching lower rate of return may lead to deficit that has to be covered by universal pension society that manages the particular fund). The amendments to the Act have limited also the amount of charges deducted from open pension fund members’ contributions. These charges should decline to 3.5% for contributions made in 2014 and further years.

In 2004 the Individual Pension Account Act was introduced as a III pillar of the Polish pension system in order to enable citizens to accumulate additional funds towards their old age pensions (Individual Pension Account Act of April 20, 2004). An Individual Pension Account (IPA) is a separate account maintained for the saver by bank, brokerage house, investment fund or insurance company. A single person may only have one IPA. Income from the funds deposited in IPA is exempt from capital gains tax. This exemption applies only to persons who withdraw the savings after they attain the retirement age. Such persons must, however, accumulate savings in their Individual Pension Accounts for at least five (any five) years, or over half of the
amount paid into the IPA must be deposited not later than five years before an application for fund withdrawal is submitted.

Since 2012, a new III pillar voluntary savings vehicle, called individual pension insurance accounts (or IKZEcs), has been introduced in order to complement IPA. Clients may set up an IKZE with an authorized institution (investment company, insurance company, bank or open pension fund). Contributions on the first 4% of gross salary are tax free (Poland Will Open..., 2011).

The III pillar of pension system in Poland captures also the employees’ pension schemes sector. Privately managed pension funds may be established by employers on a voluntary basis. Up to the equivalent of 7% of monthly salary may be paid in by the employer and contributions are exempt from the social security levy. Additional payments by an employee are possible, but the whole contribution is subject to an income tax (OECD 2008). Since 2005 employees’ pension funds have been allowed to manage funds entrusted them by foreign employers who carry out employees’ pension schemes on the basis of Polish regulations (The Act of 20 April 2004 on Occupational Pension Programs).

It is worth underlining, that after the license process had finished, in 1999 21 financial institutions created open pension funds. Since then 7 open pension funds have been wound up. Further consolidations in this sector are inevitable, especially amongst the small and medium-sized companies (Komisja Nadzoru Finansowego 2008, National Bank of Poland 2003).

6.7. Regulations concerning the Pension Guarantee Fund

The basic resource of the Pension Guarantee Fund is administered by the National Depository for Securities, and consists of contributions of pension companies calculated on the basis of assets managed and revenues from depositing of own assets. A payment from the basic resource of the Guarantee Fund is made in the case of a shortfall, to open pension funds’ members to cover damage caused by the non-performance or improper performance of obligations by a pension company (Act on the Organization and Functioning of Pension Funds).
6.8. Regulations regarding the capital market

6.8.1. Regulations regarding the stock exchange market and the OTC market

The capital market in Poland is regulated by the following legal acts: the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies and the Act on Trading in Financial Instruments. These acts address the principles and scope of operations of capital market.

The first Act defines rules and conditions for carrying out a public offering of securities, for conducting subscription or sales of such securities and for seeking admission and introduction of securities or other financial instruments to trading on a regulated market, obligations of issuers of securities and other entities participating in trade in such securities or other financial instruments. It also stipulates consequences of obtaining the status of a public company as well as special rights and obligations relating to the holding of and trading in shares of such companies.

The second Act explains the meaning of financial instruments and rules of trade with the use of these instruments. According to it, financial instruments include:

- securities;
- any of the following instruments other than securities, inter alia: units in collective investment undertakings, money market instruments, options, futures contracts, swaps, forward rate agreements;
- derivatives, financial indices or financial measures which are delivery- or cash settled,
- options, futures contracts, swaps, forward rate agreements and other derivatives which are based on commodities and which are cash-settled or may be cash settled at the option of one of the parties as well as those which are based on commodities and delivery-settled, provided that they are admitted to trading on a regulated market or in an multilateral trading facility,
• options, futures contracts, swaps, forward agreements and other derivatives that are not admitted to trading on a regulated market or in an multilateral trading facility and which are based on commodities and may be delivery-settled, which are not intended for trading purposes and have the characteristics of other derivative financial instruments;
• credit risk transfer derivatives;
• contracts for difference;
• options, futures contracts, swaps, forward rate agreements, climate change, freight rate and emission allowance derivatives, as well as derivatives based on interest rates or other official statistics, which are cash-settled or may be cash settled at the option of one of the parties, as well as any other derivatives based on assets, rights, obligations, indices and other ratios which have the characteristics of other derivative financial instruments.

The main component of the Polish capital market is the Warsaw Stock Exchange (WSE). It operates under the Act on Trading in Financial Instruments of 29 July 2005, as amended, under the supervision of the Polish Financial Supervision Authority. Following the introduction of stabilization program and market-oriented reforms after the collapse of centralized economy in 1989, the WSE was created as a joint-stock company on April 12, 1991 by the State Treasury. The first trading was held on April 16, 1991 with five listed companies. In 1996 the OTC market was established under the name of Centralna Tabela Ofert SA (Central table of offers – CeTO). As it was noticed in the Section 5, since November 2000 it has been the member of the WSE capital group as a BondSpot SA. It organizes and manages a regulated market and alternative trading system.

Amendments to legal foundations of the Polish capital market set forth in more detail the information requirements to be met by issuers, depending on the type of issued securities. The information requirements towards the issuers whose securities were listed in the CeTO have been eased. Other amendments extended, among other matters, competences of the supervisory authority, giving it the right to demand a securities account be blocked when a well-founded suspicion exists that
an offence consisting of the manipulation of a financial instrument or the use of confidential information has been committed (Act Amending the Act on Public Trading in Securities and Other Acts of March 12, 2004).

Moreover, new regulations concerning transactions of qualified holdings were also introduced. One of the most important changes was the repealing of previous regulations concerning the need to obtain a permit of supervisory authorities in order to exceed the threshold of 25%, 33% and 50% of the total number of votes in a public company (Act on Trading in Financial Instruments of 29 July 2005). However, the obligation to notify reaching or exceeding the threshold of 10%, 20%, 33% or 50% of the total number of votes in a public company was kept.

According to new rules, short selling was allowed on the WSE starting from 1 July 2010. Short selling means that investors sell securities which are not held on their investment accounts at the moment of sale. However, short selling is not available to all customers and is offered under the contract signed with the brokerage house which maintains the investor’s securities account. Not all securities can be involved in short selling. In 2010 this type of trading was available for shares of 140 companies (Warsaw Stock Exchange 2011).

Some changes were not related to the adjustment of Polish law to EU regulations. Especially, until December 31, 2003, income arising from the transfer of listed securities against payment was exempt from income tax pursuant to the provisions of the Personal Income Tax Act. Since January 1, 2004, such income obtained by persons (who do not engage in business activity) has been taxed (Art. 30b, Para. 1 of the Personal Income Tax Law of July 26, 1991, as amended). After a given fiscal year has ended, taxpayers who have obtained income from the transfer of securities against payment are required to include this income in their annual tax returns as well as calculate the amount of income tax due and transfer it to the account of the competent tax authority. The changes aimed to make the tax system neutral with regard to all instruments available on the financial market, as in November 2001, amendments to the Personal Income Tax Act were adopted, which introduced a tax on savings deposits and funds in bank accounts.
Apart from the commonly binding legal acts that regulate the operation of the capital market, certain customs of no binding nature were adopted and accepted by the market participants (National Bank of Poland 2004). The first document specifying corporate governance rules for listed companies was adopted by the WSE in 2002. Amended rules were implemented in „Best Practices in Public Companies 2005”. Starting from 1 January 2009, a new corporate governance document, entitled „Code of Best Practice for WSE Listed Companies”, has been put into practice (Warsaw Stock Exchange 2009).

Capital gains earned by Polish individuals are taxed at a flat rate of 19%. The same rate applies to capital gains earned by legal persons. Foreign investors are subject to the same regulations as domestic ones, with their tax obligations being additionally regulated by the respective double taxation avoidance treaties (Warsaw Stock Exchange 2009, 2010, 2011).

6.8.2. The Compulsory Investor Compensation Scheme of the National Depository for Securities

Brokerage companies are required to pay annual contributions to the compensation system that guarantees pay-outs of funds to investors and to compensates for the value of lost financial instruments deposited by investors in brokerage institutions. Payments are made in the case of declared bankruptcy of a brokerage house, of a valid rejection of a motion to declare bankruptcy due to the fact that assets held by a brokerage house are insufficient to cover the costs of proceedings, or inability of a brokerage house to fulfil its obligations. If a foreign investment company that pursues brokerage activities on the territory of Poland participates in a compensation system established in the country of its registered office and the system complies with the requirements specified in the Law on the Public Trading in Securities, the institution is not required to participate in the domestic compensation system.

The value of investors’ funds secured in 100% equals to 3,000 EUR. The compensation system also guarantees the payment of 90% of investors’ funds exceeding
the zloty equivalent of EUR 3,000. The maximum amount of funds covered by the system is the zloty equivalent of EUR 22,000 (National Bank of Poland 2004).

6.8.3. Settlement Guarantee Fund of the National Depository for Securities

The settlement guarantee fund safeguards protect fulfilment of obligations stemming from transactions concluded on the regulated securities market. It consists in contributions paid by its participants and is divided into four functionally separated parts, each of them guaranteeing settlement of specific types of transactions. The amount of contributions to the clearing fund is established depending on the level of liabilities, which may arise in result of the participant’s activities on the regulated market, settled by the National Depository for Securities (National Bank of Poland 2004).

6.9. Regulations regarding supervision over financial sector

6.9.1. The Polish Financial Supervision Authority

Significant changes have been introduced to the institutional structure of financial supervision since 2007. The Act on Financial Market Supervision, provisions of which entered into force on 19 September 2006, has changed the rules of supervision in Poland (Act of 21 July 2006 on Financial Market Supervision). The new solutions are aimed at integrating the supervisory bodies overseeing the financial market. One organizational body is now responsible for the tasks and powers that formerly belonged to several bodies supervising the individual sectors of the financial market. The Polish Financial Supervision Authority comprises the Chairperson, two Vice-Chairpersons and four members: the minister competent for financial institutions or his/her representative; the minister competent for social security or his/her representative; the President of the NBP or a delegated Deputy President of the NBP; a representative of the President of the Republic of Poland. The activity of the PFSA activity is being supervised by the President of the Council of Ministers.

The Polish Financial Supervision Authority (PFSA), which on 19 September 2006 replaced the Insurance and Pension Funds Supervisory Commission and the
Securities and Exchange Commission, was entrusted with conducting integrated supervision. The PFSA initiated its activity on 19 September 2006. In the second phase of the merger of financial supervision, on January 1, 2008, the PFSA took over the powers of the Commission for Banking Supervision together with its Office – the General Inspectorate of Banking Supervision. Thus, there occurred an establishment of authority separate from the structure of the National Bank of Poland and unifying all supervisory bodies into single authority, the task of which is to provide a surveillance over the financial sector (Kowalski, Matysek-Jędrych 2010).

The PFSA supervises credit institutions, insurance firms, investment companies, exchanges, pension scheme as well as payment institutions. Its supervision also covers the Warsaw Stock Exchange, the National Depository for Securities, investment advisors and issuers of WSE-listed financial instruments. The tasks of the PFSA include:

- undertaking measures aimed at ensuring development and regular operation of the financial market;
- participation in the drafting of legal acts related to financial market supervision;
- creation the opportunities for settlement of disputes which may arise between financial market actors, in particular disputes resulting from contractual relations between entities covered by the PFSA supervision and recipients of services provided by those entities.

As it was underlined, before January 2008, supervisory authorities were separate. The Commission for Banking Supervision supervised the activities of banks since January 1, 1998. The supervision was aimed to secure funds deposited on bank accounts and to protect compliance of banking activity with legislative acts, articles of association, other legal regulations as well as with the binding financial standards. The Commission fulfilled three basic functions: licensing, regulatory, and the one involving examination and administrative management. Executive body of the Commission was the General Inspectorate of Banking Supervision, an organizational unit of the NBP (National Bank of Poland 2004).
The Securities and Exchange Commission was a central government authority that performed with the help of the Office of Polish Securities and Exchange Commission. Its primary tasks included supervising the observance of the rules of fair trading and competition in the public trading in securities and commodities and providing public access to reliable information on the securities and commodities markets. It was within the competences Commission to conduct licensing of activities of market participants and issuance of permits for admission of securities to public trading. The Commission was entitled to supervise operation of investment funds and brokerage activities (National Bank of Poland 2004).

The Insurance and Pension Funds Supervisory Commission was another central government authority. Its supervision covered insurance companies, insurance intermediaries, open pension funds and occupational pension schemes. The Commission was established on April 1, 2002 and took over the responsibilities of the State Office for Insurance Supervision and the Office for Pension Funds Supervision. The supervision over the insurance market included, inter alia, protection of interest of the insured, issuance of permits to perform brokerage and agent activities, control of operation of insurance companies and insurance intermediaries. The supervision and regulation of the operation of pension funds involved, among others, protection of interest of the open pension funds’ members and participants of occupational pension schemes, issuance of permits to establish a pension fund and a pension company (National Bank of Poland 2004).

The three Commissions cooperated with each other. The purpose for such cooperation was to exchange information on particular segments of the financial market, thus increasing the efficiency of supervision and surveillance over this market in order to ensure the compliance of financial institutions’ operations with the provisions of the law.

6.9.2. The Council for Financial Market Development

In 2006, the Minister of Finance established the Council for Financial Market Development (Order No. 25 of the Minister of Finance of 14 September 2006) The
body issues opinions and advice in matters related to the development of the Polish financial market. The Council is composed of the representatives of financial market participants and supervisory institutions. The formula of the Council’s operation assumes establishing working groups and holding consultations with the market. The task of the working groups and teams is to prepare proposals of amendments to regulations aimed at improving conditions for financial system development in Poland and adapting them to EU legislation (National Bank of Poland 2008).

Generally speaking in the Polish literature the development of regulation is perceived positively. Supervisory authorities were assessed to work satisfactory. Controversy arose only in 2006-2007 when legislation setting up a new integrated financial supervisory authority came into force. The new authority (KNF, Polish Financial Supervisory Authority) combined the functions of the existing insurance and pension fund supervisor, securities commission and the banking supervision commission. However, it is too early to formulate any general remarks on this matter and assess efficiency of the new supervisory authority.
7. Relationship between the financial sector and other components of finance, insurance and real estate

The circulation of funds in the Polish financial sector takes place through different channels, as shown in Figure 13. However, as the Polish financial sector is a bank-oriented one, banks play a predominant role in financing the needs of the real sector of the economy transferring non-financial sector’s deposits into credits. Taking into account the available voluntary and obligatory forms of savings in Poland, the financial assets of households include the following (National Bank of Poland 2009):

- deposits with banks and credit unions,
- participation units of investment funds,
- unit-linked assets and life insurance saving premiums,
- funds on accounts with open pension funds,
- Treasury securities,
- stock listed on the WSE,
- cash in circulation excluding bank vault cash,
- other financial instruments (e.g. non-Treasury debt instruments).

Investments of Polish enterprises – especially SMEs – are first and mostly financed from internal funds. The deficit of own funds is covered from external sources, with the special consideration of bank loans and other non-bank sources, including, as the most important (National Bank of Poland 2009):

- issue of stock,
- issue of debt securities,
- loans from foreign parent undertakings,
- leasing.

The decisions of households concerning financial investments are influenced by, e.g., the macroeconomic situation, the level of interest rates, tendencies in the capital market, legal regulations, knowledge about the financial market and familiarity with products offered by financial institutions and financial intermediaries (National Bank of Poland 2009, 2010, Narodowy Bank Polski 2010). The financial assets of households have been increasing – the value of assets held by households increased to
This project is funded by the European Union under the 7th Research Framework programme | theme SSH | Grant Agreement nr 266800

PLN 963 billion in 2011, from PLN 280 billion in 2000. In the same period, the ratio of those assets to GDP increased from 37.7% to 62.0% (Table 13). In 2011 household assets increased by over PLN 52 billion. Out of this amount, PLN 6.8 billion accounted for the increase in bank deposits. Changes in the value of savings deposited with banks were correlated with the increasing risk aversion and bullish stock market as well as the outflow of funds from investment funds (Analizy Online 2012).

Table 13 Financial assets of households in 2000-2011

<table>
<thead>
<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial assets of households (in PLN billion)</td>
<td>280.4</td>
<td>335.5</td>
<td>365.9</td>
<td>400.4</td>
<td>434.7</td>
<td>509.1</td>
</tr>
<tr>
<td>of which: funds on accounts with open pension funds (in PLN billion)</td>
<td>2.3</td>
<td>19.4</td>
<td>31.6</td>
<td>44.8</td>
<td>62.6</td>
<td>86.1</td>
</tr>
<tr>
<td>Financial assets of households (% of GDP)</td>
<td>37.7</td>
<td>43.1</td>
<td>45.3</td>
<td>47.5</td>
<td>47.1</td>
<td>51.9</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial assets of households (in PLN billion)</td>
<td>636.5</td>
<td>751.2</td>
<td>739.8</td>
<td>859.2</td>
<td>911.0</td>
<td>963.0</td>
</tr>
<tr>
<td>of which: funds on accounts with open pension funds (in PLN billion)</td>
<td>116.6</td>
<td>140.0</td>
<td>138.3</td>
<td>178.6</td>
<td>221.3</td>
<td>224.7</td>
</tr>
<tr>
<td>Financial assets of households (% of GDP)</td>
<td>60.0</td>
<td>63.8</td>
<td>58.0</td>
<td>63.9</td>
<td>68.3</td>
<td>62.0</td>
</tr>
</tbody>
</table>

Deposits with banks remain the main item of the financial assets of Polish households (Table 14). The total share of this form of saving in total assets amounted to more than 44% in 2010. Since 2008, a return to saving at banks has been observed as a result of the global financial turmoil and searching for so-called safe havens (National Bank of Poland 2009, Narodowy Bank Polski 2011c).

The participation units of investment funds were an item which grew in the assets of households in the first half of the last decade. The large interest in these instruments resulted from several factors: the bull stock market in 2003-2006 and the high rates of return as well as the diminishing attractiveness of bank deposits and Treasury bonds in the face of falling interest rates (National Bank of Poland 2009). At the end of 2010, the value of funds held by households in investment funds amounted to PLN 75.5 billion. Households also invest directly in the capital market. The exposure of individual investors on the stock market exceeded PLN 51 billion in 2010. The flow of funds in this market is of pro-cyclical nature and is linked with the tendencies observed on the stock exchange and the privatisation of state-owned enterprises. Events that took place in 2007 had a significant impact on the structure of house-
holds’ assets. The outburst of the global financial turmoil in the last quarter of 2007 and a bear stock market caused a steep fall in the interest received by households from unit-linked products and units of investment funds (National Bank of Poland 2009, 2010, Narodowy Bank Polski 2011c).

The only category of financial assets of households of decreasing volume were Treasury securities. As their profitability has been continuously decreasing and the gains have become subject to the personal capital gains income tax since 2004, the value of Treasury bonds held by households exceeded only PLN 10 billion in 2010. Households preferred other forms of investment, especially bank deposits, due to intense advertising activity of commercial banks despite a lower interest paid on bank deposits (National Bank of Poland 2009, 2010, Narodowy Bank Polski 2011c).

The funds on accounts with open pension funds constituted an important item of the financial assets of households. The savings in open pension funds are, however, different than other forms of investment, as participation in pension funds is mandatory for people born after 31 December 1968 (see Section 6). Funds collected on accounts with open pension funds are non-liquid and long-term savings. Their value increased from PLN 2.3 billion in 2000 to PLN 224.7 billion at the end of 2011 (National Bank of Poland 2009, Analizy Online 2012).

Bank term deposits have been losing out to other forms of savings. However, the share of bank deposits in total financial assets of Polish households is still at a higher level than in most developed countries (National Bank of Poland 2009). In the future, as the Polish financial sector develops, the structure of financial assets of households is likely to change, in line with the structure observed in the euro area. This implies a great challenge for domestic banks which would be in need of searching funds for financing the growing lending activity, other than declining deposit base (National Bank of Poland 2009).
Table 14 Structure and changes of selected items of the financial assets of households in 2001-2010 (in %)

<table>
<thead>
<tr>
<th>Year</th>
<th>Share in the total assets of households</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2001</td>
</tr>
<tr>
<td>Bank deposits</td>
<td>65.4</td>
</tr>
<tr>
<td>Funds on accounts with open pension funds</td>
<td>5.8</td>
</tr>
<tr>
<td>Participation units of investment funds</td>
<td>3.0</td>
</tr>
<tr>
<td>Unit-linked assets and life insurance saving premiums</td>
<td>6.2</td>
</tr>
<tr>
<td>Stock listed on the WSE</td>
<td>2.9</td>
</tr>
<tr>
<td>Treasury securities</td>
<td>4.8</td>
</tr>
<tr>
<td>Deposits with credit unions</td>
<td>0.5</td>
</tr>
<tr>
<td>Cash in circulation (excluding bank vault cash)</td>
<td>11.4</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Growth rate (y/y)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2001</td>
</tr>
<tr>
<td>Bank deposits</td>
<td>12.6</td>
</tr>
<tr>
<td>Funds on accounts with open pension funds</td>
<td>760.7</td>
</tr>
<tr>
<td>Participation units of investment funds</td>
<td>61.3</td>
</tr>
<tr>
<td>Unit-linked assets and life insurance saving premiums</td>
<td>30.0</td>
</tr>
<tr>
<td>Stock listed on the WSE</td>
<td>-40.8</td>
</tr>
<tr>
<td>Treasury securities</td>
<td>70.0</td>
</tr>
<tr>
<td>Deposits with credit unions</td>
<td>56.6</td>
</tr>
<tr>
<td>Cash in circulation (excluding bank vault cash)</td>
<td>12.0</td>
</tr>
</tbody>
</table>


As it has been argued above, the Polish financial sector is a bank-oriented one. This means that financial markets do not play a key role in providing funds. This
is due to the fact that the Polish financial sector is determined by preferences of households as regards the allocation of capital – a vast part of the deposit base (especially of longer maturity) belongs to them. As shown in Table 14, Polish households still prefer to deposit their surpluses of funds within banks. However, it should be noticed that the Polish financial sector has been constantly evolving since 1990, which results in the growing importance of financial markets. The pace of this evolution will be largely conditioned by the development of corporations and the development of the real economy (National Bank of Poland 2004).

Households’ savings are being converted into different forms of financing of enterprises. The majority of funds for enterprises came from bank loans. In 2010, enterprises obtained more funds from bank loans than from market sources. At the end of 2010, the debt of enterprises due to bank loans amounted to PLN 107.9 billion and was PLN 1.1 billion lower than in the previous year (National Bank of Poland 2009, Narodowy Bank Polski 2011c).

Table 15 Market financing vs. bank financing of Polish enterprises in 1999-2006 (PLN billions)

<table>
<thead>
<tr>
<th>Year</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source of financing</td>
<td>-6.9</td>
<td>-5.8</td>
<td>4.8</td>
<td>1.8</td>
<td>1.6</td>
<td>19.8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source of financing</td>
<td>12.8</td>
<td>-8.9</td>
<td>-8.1</td>
<td>-37.8</td>
<td>30.7</td>
<td>n/a</td>
</tr>
</tbody>
</table>

* Predominance means a difference between financing from market sources and bank financing in a given year. Market sources include: stock issues on the WSE, bond issues on the domestic market and bond issues on foreign markets. Positive value means that financing from market source was dominant in a given year, whereas negative value exposes predominant nature of banking financing.


Stock issues on the WSE were another important market source of financing. During the period of a favourable situation on the WSE, enterprises were financing their operations by means of equity issues on the stock exchange. However, in 2010 value of new issues on the WSE amounted only for PLN 5.6 billion, being circa. PLN 9 billion lower than in 2009. (Narodowy Bank Polski 2011c), despite the fact that new segment of the capital market, established in 2007, in form of the New Connect (see Section 3.3.2.), has been developing significantly in order to allow SMEs with short
business track record to gather funds with the use of the stock market. The reasons for the insignificant use of the stock exchange include, among others, still high costs of entering the market (National Bank of Poland 2009, 2010, Narodowy Bank Polski 2011c).

Polish enterprises use bond issues on the domestic market to finance their activities only to a small extent. Only enterprises from chemical, construction and energy sectors were active bond issuers. The small popularity of this source of financing resulted from excessively complex, in the view of enterprises, legal regulations concerning those instruments, and from the high costs of issues in the form of public offering (National Bank of Poland 2009, 2010). Enterprises obtained capital also through bond issues on foreign markets, although the value of those issues was systematically decreasing, which was related to the increased availability of capital on the domestic market. An important source of capital for Polish enterprises were also loans from direct foreign investors. However, this form of financing was used only by a relatively small group of enterprises (National Bank of Poland 2009).

Leasing was another non-bank source of financing. In 2010, the value of leased assets amounted to PLN 21.3 billion. The increased interest in leasing in the recent years resulted from the favourable economic situation in Poland and a higher demand of SMEs for external financing. Small and medium-sized enterprises constitute the main group of recipients of leasing companies’ services (National Bank of Poland 2009, 2010, Narodowy Bank Polski 2011c).

In forthcoming years bank loans will remain the most important source of external financing of enterprises in Poland, especially from the SME sector. Due to high entrance costs, stock market financing is relatively too expensive for the majority of SMEs (National Bank of Poland 2009). However, the tendencies observed in the recent years point to a gradual increase in the importance of market sources of financing for enterprises. This will be supported by the increasing similarity of the structure of assets of households in Poland to the structure in more developed countries, characterized by the high share of funds invested through collective investment institutions (National Bank of Poland 2009).
8. The culture and norms of the financial system

The processes of globalization enforce a deep evolution of the financial systems worldwide. Financial institutions and their clients must be prepared to cope in a more and more rapidly changing environment. This phenomenon is explicitly evident in Central and Eastern European countries. Since the beginning of the nineties these countries, among them Poland, have been transforming their economies in order to catch up with advanced economies. This catch-up process is present also in different segments of the financial sector. However, it must be emphasized that in some segments (capital market, FX market, derivatives market) this process is slow due to low level of financial knowledge concerning the functioning of these elements of financial sector among Poles. Many people don’t understand simple economic phenomena and links between them and therefore they can’t figure out how to behave in free market economy.

In practice, very important barrier for the above mentioned catch-up process is unsatisfactory financial education, affecting negatively the level of financial competences of the whole society, thus enlarging the number of excluded in access to financial services (Solarz 2007). This is a hangover from the old system of centrally planned economy. Hence one can identify the lack of saving and investing habits in Poland. Studies carried out in October 2011 by Pentor on behalf of the Kronenberg Foundation and the Polish Financial Supervision Commission reveal that (*Postawy Polaków wobec oszczędzania*, 2011):

- although the Poles in the face of unfavourable macroeconomic phenomena (the economic downturn in 2008, the sovereign debt crisis, volatility of prices on the stock exchange) often declare strong saving habits (67% in 2011 versus 58% in 2010), this point of view is more frequently shared by people with higher education, earning over PLN 4000 a month;
- however, the above mentioned declarations do not go hand in hand with actual behaviour: more than half of the Poles (52%) spends all their earnings in order to satisfy current needs;
- 45% of the Poles saves, but only 7% of the Poles do it regularly each month;
• savings usually serve a consumption purpose: the purchase of dwelling equipment or car (35%), holiday (28%), 49% of the Poles saves for less than 1 year;
• in the aftermath of the outburst of the global financial crisis and economic slowdown the Poles have started trusting their intuition: more than a quarter of the respondents (27%) believes that the success in investing relies mainly on their own decisions, and 39% of the respondents is not able to determine the reasonable reasons affecting the probability of success;
• as a consequence of global financial turmoil less Poles trust the employees of financial institutions (the fall from 16% in 2010 to 14% in 2011);
• according to the respondents, a safe investments include basic financial instruments (current accounts – 17%, time deposits – 12%), 42% of the respondents pay regularly their financial surpluses into their current accounts or keep them under the mattress.

Therefore, the level of financial education in Poland can hardly be assessed as an appropriate, especially if compared with advanced economies. This general remark is supported by the analysis conducted by the National Bank of Poland. According to results of studies (Koźliński 2010):

• rudimentary cashless payment instruments such as direct debiting or payment orders, are still not popular among the Poles;
• despite an access to the various payment instruments and services, Poles still opt for the cash payments;
• often opening a current account doesn’t limit the preference for cash payments because of so-called “cult of cash”, understood as a preference of possession cash and making cash payments regardless of costs, and the lack of willingness to broaden knowledge on cashless means of payments.
• The lowest level of financial education can be recognized within poorly educated older people, the unemployed or people with low disposable income.

Following research on the level of the use of banking products and services,
measured by the access to a bank current account, it appears that such an access is the lowest among (Koźliński 2009): people aged 60 or more,

- people who got only primary education,
- households earning a net income of PLN 1600 a month;
- farmers;
- the unemployed;
- low-qualified personnel.

Low inclination to use financial services and products in Poland is supported also by Eurobarometer research. Results of this study show explicitly that 87% of the Europeans aged 20 or more have bank accounts. In this research Poland took 22nd place, as only 76% of the respondents had opened a current account. This level is significantly lower than EU27 average (Consumers’ views on switching service providers..., 2009). The access to bank account in Poland is similar to this observed in other Central and Eastern European Countries, such as Hungary, Slovenia, Lithuania and Latvia, but significantly lower than in Slovakia and the Czech Republic (Koźliński 2009).

The most important reasons, identified in the NBP’s research, for not opening the bank current account, are the following (Koźliński 2009):

- lack of such a need,
- preference to keep money in form of cash;
- belief that monthly earnings are too low to have an account;
- fear of high costs related to opening and keeping a bank account.

Increasing the level of financial knowledge among Poles constitutes a serious challenge for all units that carry out activities in the sphere of financial education. Otherwise it would be extremely difficult to broaden the knowledge of the society concerning the economy market mechanisms and financial system, thus increasing the number of excluded, which do not have a bank account, nor use financial instruments (Maison 2010a, Maison 2010b, Narodowy Bank Polski 2009, Narodowy Bank Polski 2011a). Among factors causing long-term financial exclusion one can include
the lack of financial consciousness, credit dysfunction or intergenerational exclusion. It is necessary then to disseminate the financial knowledge by public institutions and non-governmental organizations to contribute to faster economic growth and the utilization of innovative potential, thus improving the competitiveness of the economy as a whole (World Economic Forum 2010). Financial education should be an important source of knowledge about the realities of the functioning of the economy and the financial system, as well as the opportunity to improve certain skills easing functioning on the financial market. Fulfilment of these targets is extremely important especially while taking into account older people who finished schools in realities of centrally-planned economy or in the beginning of the transformation of the Polish economy. Hence, they often did not even have the possibility to benefit from the opportunities offered by modern finance. Lack of adequate knowledge and “avoiding” financial institutions and services results in a great exposure to the financial exclusion. Therefore a significant difference between the generations arises concerning the understanding of the mechanisms of the contemporary economy as well as the use of financial services and products.

Broader educational offer directed to different social classes can therefore be seen as a tool that limits financial exclusion. This activity should be particularly important in the context of opposite phenomenon, which appears to be the financialisation, observed in many advanced economies and discussed already in the Section 2. The most important feature of the financialisation phenomenon can be defined as the increasing impact of the markets and the financial elites on the macroeconomic policy. Thus the financialisation can be considered as a new stage of capitalism in form of “coupon capitalism” (Ratajczak 2009).

As was noted in other Sections, in the Polish bank-oriented financial system banks are the main providers of funds for households and enterprises. Thus the fulfilment of needs of the Polish society is highly dependent on the level of bank’s activity. Therefore, since the beginning of the nineties bank loans have become an important part of the culture of everyday life. This phenomenon can be observed while
analysing changes in loans to households as well as changes in the number of credit cards and value of card payments in Poland.

Since the beginning of the 1990s volume of bank loans have been increasing continuously. As a result, as at the end of 2010, loans to households reached the value of PLN 467.6 billion, and loans to enterprises – PLN 204.1 billion (Narodowy Bank Polski 2011c). Nothing distinguished the year 2010 from previous years, as in 2010 a further increase in the growth rate of loans to non-financial customers was observed. As in the previous year, indebtedness resulting from loans to households grew at the fastest pace (13.9%). The growth rate of loans to households in the analysed years was higher than that in the case of enterprises (National Bank of Poland 2004, 2006b, 2009).

Property loans grew the most rapidly of all the categories of loans to households. Even in the beginning of the first and second decade of this century, which were characterized by economic slowdown resulting in deterioration of financial condition of many households, growing unemployment and a drop in the disposable incomes, property loans grew by 35.1% in 2002, and by 22.5% in 2010. As a result, the share of property loans in total loans to households grew from 17% in 2001 to 58.0% in 2010 (Narodowy Bank Polski 2011c). Moreover, it should be underlined that yet in 2004, more than 60% of the amount of housing loans to households was secured by mortgages, and this ratio even increased in the forthcoming years. This indicates the growing role of mortgages in the securing of property loans taken out by households (National Bank of Poland 2004, 2006b, 2009, Polish Financial Supervision Authority 2008).

It is worth underlining, that in 2006 the indebtedness of individuals due to property loans for the first time exceeded the total value of their indebtedness due to all other loans. As compared to other countries of the region, the indebtedness of Polish households due to property loans increased the most and amounted to PLN 271.5 billion in 2010. The quick growth of these loans was caused by the strong demand for flats among households and improvement of their financial situation, declining costs of purchasing dwellings financed with a mortgage-backed loan (particu-
larly in large cities) as well as the prospect of liquidating the interest allowance in 2006 and increasing the VAT rate on construction materials in 2008. The demand for housing loans remained high despite the outburst of the global financial crisis, which forced application of more strict criteria and terms and conditions for granting mortgage loans by banks, thus eliminating the households without sufficient creditworthiness from the market (National Bank of Poland 2004, 2006b, 2009, Polish Financial Supervision Authority 2008).

Table 2 Structure of selected types of loans to households in 2002-2010 (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real property loans</td>
<td>23.3</td>
<td>30.4</td>
<td>34.0</td>
<td>38.6</td>
<td>44.3</td>
<td>48.3</td>
<td>54.0</td>
<td>54.0</td>
<td>58.0</td>
</tr>
<tr>
<td>Authorised overdrafts</td>
<td>16.0</td>
<td>13.7</td>
<td>12.7</td>
<td>10.7</td>
<td>8.3</td>
<td>7.0</td>
<td>5.6</td>
<td>5.5</td>
<td>5.1</td>
</tr>
<tr>
<td>Credit card lending</td>
<td>1.9</td>
<td>2.1</td>
<td>2.7</td>
<td>3.1</td>
<td>3.2</td>
<td>3.5</td>
<td>3.4</td>
<td>3.6</td>
<td>3.2</td>
</tr>
<tr>
<td>Other loans, of which:</td>
<td>39.7</td>
<td>36.0</td>
<td>34.0</td>
<td>33.5</td>
<td>31.7</td>
<td>30.5</td>
<td>28.4</td>
<td>28.7</td>
<td>25.9</td>
</tr>
<tr>
<td>Investment loans</td>
<td>12.0</td>
<td>11.5</td>
<td>11.2</td>
<td>10.0</td>
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Table 3 Changes in selected types of loans to households in 2002-2009 (%)

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<th>2003</th>
<th>2004</th>
<th>2005</th>
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<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
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<tr>
<td>Real property loans</td>
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<td>47.7</td>
<td>21.2</td>
<td>40.6</td>
<td>54.8</td>
<td>59.2</td>
<td>62.4</td>
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<td>Authorised overdrafts</td>
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<td>-2.5</td>
<td>4.0</td>
<td>4.3</td>
<td>4.6</td>
<td>16.5</td>
<td>17.0</td>
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<td>6.0</td>
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<tr>
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<td>41.1</td>
<td>45.2</td>
<td>37.3</td>
<td>53.0</td>
<td>42.0</td>
<td>18.3</td>
<td>-1.1</td>
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<td>Other loans, of which:</td>
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<td>2.2</td>
<td>8.6</td>
<td>22.5</td>
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<td>23.3</td>
<td>35.9</td>
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<td>11.6</td>
<td>18.8</td>
<td>19.0</td>
<td>16.5</td>
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<tr>
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<td>14.0</td>
<td>11.9</td>
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<td>34.5</td>
<td>38.7</td>
<td>45.0</td>
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</table>


Since 2004 individuals have become the dominant group of borrowers (National Bank of Poland 2006b). This is the result of a strong demand impulse accompanying Poland’s accession to the European Union. In the first half of the first decade of the 21st century this impulse was also related to concerns regarding a possible increase in indirect tax rates, as well as the easing of credit standards and loan terms and conditions for loans by banks. The structure of loan types to households didn’t change significantly, however, except for the doubling the share of real property loans in overall loans (Tables 16-17). Similarly, in the whole analysed period, except
for the year 2010, two types of loans of the fastest growth were aforementioned real property loans and credit card loans. (National Bank of Poland 2006b).

However, despite fast growth, in 2010-2011, the number of payment cards issued in Poland decreased, mainly due to introduction of more strict criteria by banks to be fulfilled while putting in for a credit card. As at the end of 2011, there were 24.7 million payment cards (credit, debit and charge cards) in circulation, i.e. 8.9% more than in 2010 (Table 18).

With regard to the number of payment cards issued and the amount of transactions executed, debit cards still prevail in Poland (Tables 18-19). In 2011, their share in the total number of cards issued was 77.4%. However, in 1998-2011 credit cards exhibited the fastest growth with regard to transaction value (from PLN 364 million in 1998 to PLN 30.4 billion in 2011) and the number of cards issued (from 91 thousand in 1998 to almost 7 million in 2011). As a result, the share of credit cards increased in the structure of payment cards. In 2002, it was equal only to 4.8%, while in 2011 it amounted to 21.7%. This means that on average every fifth citizen of Poland was the holder of a credit card. The sharp rise of share of credit cards was mainly a result of the reduction of the fees by banks for issuing and using credit cards, lowering the minimum income required of a future card holder, increasing the non-price attractiveness of the offered cards, and most importantly intensive promotion of credit cards (National Bank of Poland 2006b, 2007b). However, it has to be emphasized that this ratio is still very low in comparison to advanced countries (National Bank of Poland 2006b, 2007b, 2009).
### Table 18 Number of payment cards in Poland in 1998-2011

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<tr>
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<td>87.8</td>
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<td>88.0</td>
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<td>67.6</td>
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<td>77.4</td>
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### Table 4: Value of card transactions in Poland in 1998-2011

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<td>89.6</td>
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<td>3711</td>
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<td>7.7</td>
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<td>Total (PLN mn)</td>
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</tbody>
</table>

As has been noted, although the fastest growth in the number of transactions performed was observed in credit cards, debit cards accounted for the majority of transactions performed with payment cards. This is triggered by specific social habits. Some holders of payment cards still use them only in extraordinary situations, considering them as an indication of prestige but in everyday life preferring cash payments. Payment cards are often used only in order to withdraw cash from ATMs, and not as a means of cashless payments (National Bank of Poland 2007b). However, this tendency has been significantly weakening since the second half of the 1990s. The increase in the number of issued cards (especially credit cards) resulted in an increased share of the number of transactions with their use in the total number and volume of payment card transactions. In 2011, volume of card transactions amounted to 389 billion, rising by 377 billion as compared with 1998 (Table 19).

Acceleration of credit card lending to non-financial customers indicates that the lifestyle of the society is changing and that this form of payment is more often used in everyday transactions. This is related to a change in bank policies concerning the issue of cards, the growing demand of customers, and the rising number of points of sale accepting cards. Credit cards have ceased to be financial instruments targeted only at high-net-worth individuals (National Bank of Poland 2006b). Due to strong competition in this segment of the market banks gradually ease requirements and accessibility of payment cards. Consequently more customers can apply for payment cards. The observable change in the lifestyle of customers, i.e. the fact that the service timeline of durable devices becomes shorter, also affects the market (National Bank of Poland 2007b).

In order to better adjust the functionalities of payment cards to the customers’ needs an agreement concerning cashpoint services was signed in 2005 between settlement agents, banks issuing credit cards and international payment organisations (Visa and MasterCard). According to it, payment card holders are able to withdraw cash in shops and services centres (National Bank of Poland 2007b). In the next few years banks increased functionality of cards, improving security of transactions with
the use of advanced technologies, such as PayPass technology or implementation of the 3D-Secure service (National Bank of Poland 2010).

But despite that cards in Poland are used in order to fulfil only short-term financial needs. The average value of a transaction performed with a credit card has been relatively stable (and low) over the last few years. Credit cards are used only in emergency situations. It is also worth stressing that the repayment of debt within the credit limit on the card usually takes place within the so-called grace period (National Bank of Poland 2009). Therefore, there is no significant increase in household spending in relation to the use of credit cards, as the share of transactions performed with them in the total value of card transactions in Poland is insignificant, amounting to 7.8% in 2011 (Table 19).

Studies surveyed in this Section show the culture and norms that exist in the Polish financial system. Despite wide access to innovative financial products and services a part of the Polish society deliberately refuses to use them due to lack of trust of financial institutions and lack of appropriate knowledge. This conservative approach results in, inter alia, very limited use of credit cards in favour of debit cards and use of bank credit as a primary source of financing only in specific and extraordinary circumstances, for example while purchasing durable goods (especially cars) or dwellings. This phenomenon forces financial institutions to compete for clients, with a special consideration of financially excluded ones, such as retired persons with constant monthly incomes.
9. The availability and sources of funds in the Polish financial sector

Despite the fact, that the Polish financial sector is a bank-oriented one, the predominance of the banking sector has been constantly decreasing. However, as shown in Table 20, banks’ position as a providers of funds for non-financial sector remains solid. This leading position can hardly be put into a danger, as sources of funds other than bank loans are also supplied by Polish banks to a large extent. This is a consequence of the ownership structure of financial institutions. As it was underlined in the Section 3, it is very often the case that financial intermediaries, such as leasing and factoring companies, as well as loan brokers are in fact bank subsidiaries.

Table 5 Net incurrence of liabilities in non-financial corporations in Poland in 1995-2010 (in PLN million, current prices)

<table>
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<td>941</td>
<td>-306</td>
<td>4680.6</td>
<td>4800.7</td>
<td>5382.1</td>
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<tr>
<td>Securities other than shares, except financial derivatives</td>
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<td>941</td>
<td>-306</td>
<td>4675.8</td>
<td>4760.8</td>
<td>5424.6</td>
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<td>815</td>
<td>-507.9</td>
<td>1250.1</td>
<td>1715</td>
<td>-201.5</td>
<td>-1490.7</td>
<td>566.6</td>
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<td>126</td>
<td>201.9</td>
<td>3425.7</td>
<td>3045.8</td>
<td>5626.1</td>
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<td>0</td>
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<td>10.4</td>
<td>37.8</td>
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<td>18418</td>
<td>13738.1</td>
<td>32952.7</td>
<td>15578.9</td>
<td>23224.6</td>
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<td>1346.1</td>
<td>10066.1</td>
<td>-200.4</td>
<td>2892.1</td>
<td>879</td>
<td>950.1</td>
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<td>15779.3</td>
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<td>Shares and other equity</td>
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<td>5909</td>
<td>13353.8</td>
<td>17189.1</td>
<td>25330.7</td>
<td>-18484.5</td>
<td>-1792</td>
<td>11469.6</td>
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<tr>
<td>Shares and other equity, except mutual funds shares</td>
<td>214</td>
<td>5909</td>
<td>13353.8</td>
<td>17189.1</td>
<td>25330.7</td>
<td>-18484.5</td>
<td>-1792</td>
<td>11469.6</td>
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<td>Quoted shares</td>
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<td>1246.9</td>
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<tr>
<td>Mutual funds shares</td>
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<td>0</td>
<td>0</td>
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<td>22561.2</td>
<td>56561.1</td>
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</table>
Taking the above mentioned into account it is not surprising that claims on non-financial customers have the biggest share in the assets of the Polish banking sector, and loans constitute a vast majority of these claims. While analysing the
structure of banks’ claims on non-financial sector, one can notice that initially the amount of these claims grew, mainly due to a rapid growth of claims on individuals (Tables 21-22). Just in 1999 major component of outstanding loans to the non-financial sector were loans to corporates, although the pace of growth of this lending was continuously declining. On the other hand, slower growth in personal real incomes and desire to maintain or expand the level of consumption led to further increase in demand for consumer loans. At the end of 1999, these loans made up 82.9% of total personal borrowings (General Inspectorate of Banking Supervision 2000, 2001).

The pace of growth in loans to the non-financial sector slowed in 2000-2002. This was the result of weakening economic growth and of higher real interest rates. As a consequence, loan demand declined due to a deterioration in corporate finances and the gloomy perspectives for future household incomes. Companies with sound credit capacity also accessed external funding by borrowing from foreign banks and by issuing commercial papers. Furthermore, banks introduced more selective procedures aimed at more sound analysis of clients’ credibility. All these phenomena led to a decline in consumer loans as compared with the previous year (General Inspectorate of Banking Supervision 2001, 2002, 2003). However, banks managed to keep the expansion of their claims on non-financial customers thanks to the growing demand for foreign currency loans, as they were offered at relatively low interest rates. The strongest increase was seen in the sector of housing loans and loans indexed to foreign currencies (General Inspectorate of Banking Supervision 2003).

Since 2003, along with the improvement of the macroeconomic situation, bank loans and other claims on households have started to increase dynamically. The most important factor supporting the growing demand for loans was the boom in the property market, partially brought about by the announcement that the VAT rate on construction materials would be significantly raised. Demand for housing loans remained high also in the next few years (General Inspectorate of Banking Supervision 2004, 2005).
At year-end 2004, the shares of claims on enterprises and claims on households in banking sector assets became similar (National Bank of Poland 2006b). In 2005 for the first time the value of claims on households exceeded the value of claims on enterprises (National Bank of Poland 2007b).

The growth of debt of households was stimulated by higher availability of loans as a result of easing loan terms and conditions as well as credit standards by banks. It was also accompanied with improving financial standing of households (General Inspectorate of Banking Supervision 2006, 2007). As a result, in 2006, for the first time in history, the value of claims on individuals exceeded the value of claims on enterprises (Table 20). This occurred mainly due to the significant increase in the value of loans extended to individuals (National Bank of Poland 2009). Such a high growth rate of lending occurred not only as the consequence of high demand for loans, but it was also fuelled by the significant depreciation of Polish currency in the second half of 2008 (Polish Financial Supervision Authority 2009b). This depreciation made loans denominated in foreign currencies (especially mortgage loans) more attractive. High interest in these loans continued for the next two years, due to high optimism among consumers, despite the MPC’s change of attitude and introduction of tight monetary policy, what in turn led to a further loan interest rate rise.

Table 21 Bank loans and other claims on non-financial sector (in PLN million)

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<td>1130</td>
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<td>2007</td>
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<td>2244</td>
<td>2718</td>
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<td>4177</td>
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Table 22 Structure of bank loans and other claims on non-financial sector (in %)

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<tr>
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<td>46.5</td>
<td>44.0</td>
<td>42.4</td>
<td>39.9</td>
</tr>
<tr>
<td>Non-profit institutions serving households</td>
<td>0.4</td>
<td>0.4</td>
<td>0.6</td>
<td>0.8</td>
<td>0.6</td>
<td>0.4</td>
<td>0.3</td>
<td>0.2</td>
</tr>
<tr>
<td>Year</td>
<td>2004</td>
<td>2005</td>
<td>2006</td>
<td>2007</td>
<td>2008</td>
<td>2009</td>
<td>2010</td>
<td>2011</td>
</tr>
<tr>
<td>Households</td>
<td>33.6</td>
<td>35.6</td>
<td>37.3</td>
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<td>39.0</td>
<td>40.3</td>
<td>41.3</td>
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<tr>
<td>Individuals</td>
<td>25.4</td>
<td>28.0</td>
<td>30.1</td>
<td>31.6</td>
<td>33.2</td>
<td>34.5</td>
<td>35.6</td>
<td>35.2</td>
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<tr>
<td>Individual entrepreneurs</td>
<td>4.8</td>
<td>4.5</td>
<td>4.2</td>
<td>4.0</td>
<td>3.8</td>
<td>3.9</td>
<td>3.9</td>
<td>3.9</td>
</tr>
<tr>
<td>Non-financial corporations</td>
<td>36.0</td>
<td>31.7</td>
<td>28.2</td>
<td>26.0</td>
<td>23.7</td>
<td>21.1</td>
<td>18.9</td>
<td>19.7</td>
</tr>
<tr>
<td>Non-profit institutions serving households</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
<td>0.3</td>
<td>0.3</td>
<td>0.3</td>
</tr>
</tbody>
</table>


It was impossible to sustain the growth of lending because of the outburst of global crisis that occurred in 2007. Another problem was the growing importance of lending barriers in form of exhaustible and limited sources of financing lending. Moreover, maintaining such a high pace of growth of lending could pose a risk of a formation of asset price bubble, especially in the property market, due to relatively cheap and easily available loans in foreign currencies (Polish Financial Supervision Authority 2010b). Fortunately, this negative scenario was avoided, as negative outcomes of the global financial turmoil affected also the Polish financial sector, forcing financial institutions to put a halt to the credit activity.

As a result, although in 2009-2010 loans for households were still characterised by the positive rate of growth, pace of growth of bank loans and other claims on companies appeared to be negative, partially due to the fact that some newly granted loans were related to the settlement of foreign exchange derivative transactions. A crucial role has undoubtedly been played by the effects of the financial crisis, leading to limitation of activity by some entities, worsening of their financial situation and, at the same time, increasing uncertainty concerning the macroeconomic perspectives.
At the same time awareness of risk related to credit activity increased both among banks and borrowers. As a consequence enterprises reduced their demand for credit (Polish Financial Supervision Authority 2010b, 2011b).

Despite the fall in companies’ interest in bank loans, in 2011 the increase in loans and other claims on households (11.9%) appeared to be lower than in loans and other claims on corporates (18.1%). This was really a significant change as compared with the previous year, in which loans and other claims on corporates declined by 0.9%. However, one should be aware that in 2011 loans and other claims on households more than doubled respective claims on corporate clients. As at the end of 2011, loans and other claims on households reached the value of PLN 526.0 billion, and loans and other claims on enterprises – PLN 253.3 billion. Presented changes didn’t change significantly the structure of loans to non-financial sector. Loans and other claims on households still play a key role in bank’s assets (National Bank of Poland 2012a). It is worth noticing, however, that the bank debt of Polish households still remains relatively low. At year-end 2011, the ratio of loans and other claims on households to GDP stood at 35%, and ratio of loans and other claims on individuals achieved 30%, while the average for euro area countries was around 60%.

Households became the main group of customers using bank financing. This phenomenon is not a country-specific one. The growing importance of retail banking compared to corporate banking can be observed also in other European countries. In the last years there has been a dynamic development of retail banking on the international scale. Cross-border mergers and takeovers can be treated as and evidence of this process (National Bank of Poland 2007b).

As was noted in the beginning, role of other segments of the financial sector in Poland is considerably lower. Among segments other than banking sector, the Polish capital market appears to be the fast developing one. Dynamic progress of the Warsaw Stock Exchange provides favourable circumstances for the growth of non-banking corporate financing, as well as stride of the investment funds. This may create a foundation for a stronger competition for banks, additionally fuelled by foreign financial institutions using the single passport principle and starting business in Po-
land. This phenomena also facilitate deepening cooperation between banks and insurance institutions (which are very often members of the same capital group) in form of mentioned bancassurance, aimed especially at insurance of long-term mortgage loans and constructing long- and medium-term savings schemes for clients (National Bank of Poland 2004).

Taking into account financial market development, one may assume that the convergence of interest rates to the level similar to the one observed in the euro area is going to enhance the attractiveness of capital market long-term debt securities. A further increase in the outstanding value of these financial instruments issued predominantly by groups of companies may be expected. However, according to the NBP’s forecasts, the structure of both markets with regard to the outstanding value of individual instruments will not change considerably. Treasury securities will continue to dominate on the Polish debt securities market, and enterprises’ interest in raising funds through the issue of short- and long-term bonds will rise at a moderate pace (National Bank of Poland 2004).

However, despite the aforementioned trends, in Poland banks will remain the key element of the financial system. Their role in providing capital for non-financial sector appears to be unthreatened, as clients’ preferences are apparently not flexible. The share of bank deposits in all financial assets of Polish households is still higher than in other developed countries. This share is expected to remain high in the forthcoming years of financial turbulence, as just in 2011, the inflow of resources to investment funds registered in Poland was negative, as difference between sales and redemptions of investment funds’ units and investment certificates amounted to PLN -4.2 billion, while the value of bank deposits and other liabilities to households both in zloty and foreign currencies increased by PLN 54.7 billion (National Bank of Poland 2012a, 2012b). It seems that bank deposits as a form of gathering savings are regaining their popularity once again.
The sources of funds for business investment in the Polish financial sector

In the second half of the 1990s the GDP growth appeared to be considerably slower than in years 1996-1997, falling to the 0.4% y/y in the fourth quarter of 2001. Year-on-year GDP growth in 2002 achieved 1.3% (as compared with 1.0% in 2001). This resulted in mounting current account deficit, increase in inflation rate up to two-digit levels in the end of the second half of the 1990s (mainly due to increase in fuel prices and food), and higher cost of implementing of four big structural reforms (concerning local government, health care, education and social insurance). This in turn brought about a rise of the unemployment rate and a fall in the propensity to save. The consequences of the slowdown turn out to be severe, as the joint impact of the Asian and Russian currency crises on the Polish economy proved to be much painful than initially expected. In addition, slower growth in the EU countries, especially in Germany, dampened external demand for Polish goods. Thus, exports shrank not only to Central and Eastern Europe but also to Germany, Poland’s most important trading partner. Recovery both in Western Europe and in Central and Eastern European Countries allowed for faster growth of exports only in 2000 (General Inspectorate of Banking Supervision 2000, 2001, 2002, 2003).

Relatively high inflation rate, together with slower growth in disposable incomes and business activity resulted in deterioration of corporate finances and in the fall of their creditworthiness as many companies reported worse performance than in the previous years. Therefore availability of bank loans also declined, putting at the same time a halt to new investments. The decrease of the gross fixed investment in constant prices reached its maximum in 2001, falling by 8.8% year on year, it remained also significant in 2002 (-5.8% y/y). Moreover, as presented in Table 23, in 2001-2002 the fall of gross fixed investment and gross fixed capital formation as well was observed not only in real terms, but also in nominal ones. As the propensity to invest vanished, a decline was seen also in industrial output (General Inspectorate of Banking Supervision 2001, 2003).
The situation improved only in 2003-2004. The GDP grew by 3.7% in 2003 and by 5.3% in 2004 and this growth was markedly faster than during the previous years. The growth of the GDP remained strong also in the next few years. The accelerated growth was caused both by an increase in domestic demand and exports. This resulted in the fall in unemployment rate and suppression of the inflation rate increase (1.7% as of the end of 2003). However, immediately after Poland’s accession to the EU, an acceleration was seen in consumer price growth, primarily attributable to the increase in food and transportation prices (General Inspectorate of Banking Supervision 2004, 2005, 2006).

Table 63 Non financial accounts by sectors in Poland in 1995-2010 (in PLN million, current prices)

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Gross</td>
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<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>capital</td>
<td>35269</td>
<td>52556</td>
<td>71924</td>
<td>91962</td>
<td>105031</td>
<td>120134</td>
<td>90029</td>
<td>77368</td>
</tr>
<tr>
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<td></td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>Gross fixed</td>
<td>32749</td>
<td>48435</td>
<td>67129</td>
<td>86690</td>
<td>99930</td>
<td>113129</td>
<td>89246</td>
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<td></td>
<td></td>
</tr>
<tr>
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<td>4086</td>
<td>4757</td>
<td>5240</td>
<td>5029</td>
<td>6926</td>
<td>732</td>
<td>-1537</td>
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<tr>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Acquisitions</td>
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</tr>
<tr>
<td>less disposals of val</td>
<td>48</td>
<td>35</td>
<td>38</td>
<td>32</td>
<td>72</td>
<td>79</td>
<td>51</td>
<td>49</td>
</tr>
<tr>
<td>Acquisitions</td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>less disposals of val</td>
<td>82622</td>
<td>99618</td>
<td>101363</td>
<td>126190</td>
<td>167539</td>
<td>168836</td>
<td>134951</td>
<td>140914</td>
</tr>
<tr>
<td>Gross fixed</td>
<td>79132</td>
<td>85472</td>
<td>92078</td>
<td>110422</td>
<td>136611</td>
<td>150045</td>
<td>140145</td>
<td>130431</td>
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<tr>
<td>formation</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in</td>
<td>3444</td>
<td>14110</td>
<td>9225</td>
<td>15730</td>
<td>30887</td>
<td>18746</td>
<td>-5234</td>
<td>10439</td>
</tr>
<tr>
<td>inventories</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Acquisitions</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>less disposals of val</td>
<td>46</td>
<td>36</td>
<td>60</td>
<td>38</td>
<td>41</td>
<td>45</td>
<td>40</td>
<td>44</td>
</tr>
</tbody>
</table>

Source: OECD.

Industrial output also improved noticeably, whereas construction industry output was still falling, although its drop was smaller than in 2002. Gross fixed investment decreased only by 0.5% in 2003, increasing in the next year by 5.1%. However, despite a significant improvement in gross fixed investment, capital expenditure in the entire economy slowed down further (General Inspectorate of Banking Supervision 2004, 2005). But in the next few years situation of corporates gradually improved
and their financial results as well as their core economic indicators improved significantly. Subsequently investment growth (not only in corporates but also investments carried out by the government) reached levels that had not been recorded for years [General Inspectorate of Banking Supervision 2006, 2007].

In 2007 the growth of the GDP reached the highest value in the whole decade – 6.6%. Economic growth was triggered by very strong domestic demand (both consumption and investment demand). Gross fixed capital formation grew by 17.6%, which was the highest growth rate since the 1990s (Table 23). Industrial production increased and international trade continued to intensify consequently allowing the value of exports to exceed the level of EUR 100 billion in 2007 for first time in history. Very good economic condition favoured further improvement of situation on the labour market. High domestic and foreign demand caused increase in financial results of enterprises, allowing them to generate record-breaking profits (Polish Financial Supervision Authority 2008b).

However, the outburst of the global financial crisis led to serious deterioration of economic situation.34 In 2008 the GDP increased only by 4.8% and in 2009 by 1.9% (in real terms). This signified a considerable decrease of the growth rate as compared to 2006-2007. Slight recovery has been visible only since 2010. A slowdown of the Polish economy, the increase of the unemployment rate and deterioration of perspectives for future economic performance occurred as a consequence of decreasing demand for Polish products, what in turn brought about adjusting responses of enterprises and the limitation of investments, as profits of enterprises waned. Deterioration of economic situation in the Euro zone, the main commercial partner of Poland, resulted in significant weakening of exports, especially due to the German economy entering into recession. The deficit on the current account increased to 5.4% of GDP in 2008. As a result, the pace of growth of gross fixed capital formation gradually declined. A reduction of gross fixed capital formation was observed in 2009, with an insignificant increase in investment been seen in the second half of the 2010. This occurred due to worsening macroeconomic situation as well as a result a result

34 It will be discussed in a more details in Section 16.
of tightening the credit policy by the banks (Polish Financial Supervision Authority 2009b, 2010b, 2011).

Similarly as in the case of households, external funds for enterprises in the analysed years were provided primarily by the banking sector. However, the changes observed in availability of bank loans for business investment were highly dependent on abovementioned macroeconomic phenomena that influenced real and financial sectors’ performance. Hence, in years 2000-2002, the growth rate of loans granted to corporates was low, and in 2004 even negative (Table 25). On the contrary, in 2006-2007 growth rate of bank loans granted to enterprises was very high due to faster economic growth. But in the next years, volume of abovementioned loans increased in a slower pace due to tightening credit policy by banks as a result of mounting credit risk, increasing costs of refinancing and uncertain macroeconomic perspectives in the aftermath of the outburst of the global financial crisis. The negative impact of the crisis on lending to businesses entities was larger than in the case of loans to households due to both supply (the tight credit policy of banks), and the demand factors (lower profitability and liquidity of enterprises, limiting their creditworthiness). In the fourth quarter of 2008 corporate lending significantly slowed down. This was related to deterioration of economic growth prospects due to the rapid escalation of the global financial crisis (Narodowy Bank Polski 2010, 2011b, Polish Financial Supervision Authority 2009b).

Operating loans and investment loans appeared to be the most important categories in loans to business entities, and their total share amounted to 50% (Table 24). The stagnation observed in both categories in 2003 and fall in 2004 resulted from a slump in the economic climate, loan rationing by the banks, as well as from the use of companies’ own funds resulting from relatively good financial standing of Polish enterprises, which enabled them to repay their liabilities from internal sources of financing. Polish enterprises preferred to use own funds and short term liabilities to non-banking institutions to finance their operational activity rather than bank loans (National Bank of Poland 2004, 2007b).
Table 24 Structure of loans to business entities in 2001-2010 (in %)

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overdrafts</td>
<td>12.8</td>
<td>16.9</td>
<td>16.5</td>
<td>18.6</td>
<td>21.6</td>
<td>21.9</td>
<td>23.1</td>
<td>23.2</td>
<td>22.1</td>
<td>22.1</td>
</tr>
<tr>
<td>Operating loans</td>
<td>65.1</td>
<td>34.4</td>
<td>33.8</td>
<td>32.6</td>
<td>30.4</td>
<td>28.3</td>
<td>26.5</td>
<td>24.1</td>
<td>21.9</td>
<td>21.3</td>
</tr>
<tr>
<td>Investment loans</td>
<td>n/a</td>
<td>34.2</td>
<td>34.1</td>
<td>31.8</td>
<td>31.8</td>
<td>30.8</td>
<td>27.2</td>
<td>28.0</td>
<td>29.4</td>
<td>30.5</td>
</tr>
<tr>
<td>Real property loans</td>
<td>n/a</td>
<td>7.9</td>
<td>10.3</td>
<td>12.1</td>
<td>11.9</td>
<td>15.4</td>
<td>20.0</td>
<td>21.6</td>
<td>23.2</td>
<td>22.4</td>
</tr>
<tr>
<td>Other loans</td>
<td>n/a</td>
<td>6.6</td>
<td>5.3</td>
<td>4.9</td>
<td>4.3</td>
<td>3.6</td>
<td>3.2</td>
<td>3.1</td>
<td>3.4</td>
<td>3.7</td>
</tr>
<tr>
<td>Total</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>


Table 25 Changes in loans to business entities in 2001-2010 (in %)

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overdrafts</td>
<td>-6.7</td>
<td>11.7</td>
<td>-0.6</td>
<td>8.6</td>
<td>18.9</td>
<td>16.8</td>
<td>31.1</td>
<td>27.9</td>
<td>-8.7</td>
<td>-1.6</td>
</tr>
<tr>
<td>Operating loans</td>
<td>6.0</td>
<td>-3.6</td>
<td>1.3</td>
<td>-7.4</td>
<td>-7.3</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>Investment loans</td>
<td>n/a</td>
<td>13.8</td>
<td>2.8</td>
<td>-10.5</td>
<td>3.8</td>
<td>10.4</td>
<td>9.5</td>
<td>36.8</td>
<td>0.9</td>
<td>2.1</td>
</tr>
<tr>
<td>Real property loans</td>
<td>n/a</td>
<td>15.4</td>
<td>33.3</td>
<td>13.7</td>
<td>16.8</td>
<td>28.4</td>
<td>62.4</td>
<td>36.9</td>
<td>3.1</td>
<td>-5.1</td>
</tr>
<tr>
<td>Total</td>
<td>8.5</td>
<td>2.4</td>
<td>3.0</td>
<td>-4.0</td>
<td>3.6</td>
<td>14.1</td>
<td>24.1</td>
<td>29.6</td>
<td>-4.0</td>
<td>-1.6</td>
</tr>
</tbody>
</table>


However, the improvement of the economic climate in 2006 resulted in significant growth in demand for bank loans for enterprises. As a result the increase in Polish enterprises’ indebtedness in 2006 amounted to PLN 17.5 billion, being highest since 1998 (National Bank of Poland 2009). The situation changed along with the intensification of the negative results of the global financial crisis. In 2009 operating loans decreased by 14.2% and investment loans rose insignificantly – only by 0.8% (Narodowy Bank Polski 2011b). But the cycle of tightening credit policy by banks was terminated in 2009. Hence, despite still negative annual growth rate of loans granted to businesses and the fall of the volume of loans granted to large firms, loans for SMEs remained stable in 2009-2010: the value of the portfolio of loans to SMEs decreased in 2010 only by 0.2%, and significant growth was observed in investment loans (3.0%). It should be underlined that new lending to SMEs developed most strongly in the cases of small and medium-sized banks as well as of cooperative banks (Narodowy Bank Polski 2011c, Polish Financial Supervision Authority 2011).
The observed changes in the growth rate of investment loans could have been the result of the hysteresis effect, i.e. the postponed undertaking of investment decisions, resulting among other things from the accumulation of funds for investments co-financed from EU structural funds. This was the purpose for the growth in investment loans during the economic slumps in 2002 and in 2009. However, it should be noted that retaining the positive dynamics of investment loans was related also to releasing subsequent tranches as part of loans granted in previous periods. Moreover, faster economic growth in the beginning of the second half of the first decade of this century and rising domestic demand appeared to be conducive to rebuilding and maintaining the portfolio of investment bank loans as retaining the market position required making constant additional investments by enterprises (National Bank of Poland 2009, 2010, Polish Financial Supervision Authority 2010b).

At the same time, increase of overdraft facilities despite periods of economic slowdown could be treated as a consequence of the deterioration of the business climate and to the problems companies experienced with maintaining financial liquidity. This brought about the need to search for new sources of short-term financing, including the short-term bank loans (National Bank of Poland 2004). But overdraft facilities has become popular also due to their accessibility and fewer formal requirements as compared to other types of credit. The main advantage of an overdraft facility is that it is not necessary to undergo formal procedures every time, and that it is cheaper than other types of loans (National Bank of Poland 2007b). Moreover, interest rates on overdraft facilities were significantly lower than interest rates on long-term loans (National Bank of Poland 2009).

Property loans to business entities (including mortgage-backed loans) were another fast growing loan category. They were mostly loans to property developers, i.e. entrepreneurs investing in housing premises and office space for sale. Export loans were among the loans whose volume and thereafter significance decreased. Considering the high growth of the Polish export in the analysed period, it may be suspected that the exporting companies did not report demand for bank loans due to
the improvement in their financial situation and the use of other, mostly foreign, sources of financing their activities (National Bank of Poland 2004).

Apart from banking financing, enterprises used also non-banking financing, using among others stock exchange financing and increasing the amount of leased assets. Table 26 shows the tendencies in the structure of leased assets, whereas Table 27 presents number of companies listed on the Warsaw Stock Exchange and their market capitalization.

The improvement of the economic conditions contributed to the increase in domestic demand and thus to the increase in the leasing of movables and real property assets. The structure of leased goods has been changing since the beginning of the nineties. The data presented in Table 26 indicates a clear domination of leased road transport means. The shift in the structure of leasing sector assets towards vehicles used for transport has resulted from the increased interest in the leasing of passenger cars certified as lorries and increasing interest in the leasing of the means of transport on the part of small and medium-sized enterprises (SMEs) as well as the development of car fleet management. But other categories, among them volume of leased industrial machinery and apparatus as well as of office equipment (including hardware) or aircraft, ships and rail transport means were of significantly smaller importance. The situation was similar also in the case of real property leasing. The reason may be that leasing of land and buildings requires more sophisticated and expensive procedures than purchasing movables through leasing. The structure of leased assets was dependent also on the fact that entrepreneurs postponed investment decisions under uncertain economic prospects, hence they did not declare additional demand for financing construction of new industrial facilities or purchases of machinery and apparatus. Moreover, as the economic situation in 2008-2009 negatively affected the turnover of the largest customers of leasing companies, they limited their development plans. The lower tendency of firms to invest, however, did not changed substantially the structure of leased assets (National Bank of Poland 2004, 2006b, 2007b, 2009, Narodowy Bank Polski 2010, 2011b).
Enterprises used stock exchange financing especially in periods of bull stock market. At times of economic slowdown, number of listed companies increased slowly, reflecting reluctance to debut on the stock exchange market. For example, due to the slump on the equity market observed from the second quarter of 2000 until the end of the first quarter of 2003, market capitalization decreased in 2001 and in 2002-2003 the number of listed companies decreased for the first time in the history of the Warsaw Stock Exchange (Table 27). This tendency reversed only in 2005, under the influence of improving economic situation in Poland as well as increasing the confidence in the Polish market after the accession to the EU. Low interest rates worldwide and capital availability contributed to the increased capital inflow on the WSE, resulting in rise in stock prices and market capitalization. High valuations of the listed companies along with relatively low costs of introducing new companies rendered the stock issue on the WSE one of the cheapest sources of fundraising. This enhanced the interest of companies in entering the stock market (National Bank of Poland 2006b, 2007b).

Therefore, in 2007 the capitalization of domestic and foreign companies increased by 70% and reached record-breaking PLN 1.080 billion at the end of this year. At the end of December, there were 328 companies listed on the WSE, i.e. 61 entities more than at the end of 2006. As a result, the WSE found itself among the top European stock exchanges in terms of the number of IPOs. The companies listed on the WSE conducted secondary public offerings (SPO) worth PLN 8 billion, highest since 2004 (National Bank of Poland 2009, 2010).

This favourable tendency reversed in 2008. In this very year the development of the stock market was determined by the mounting negative effects of the global financial crisis. Serious disturbances in many segments of the world financial market caused the outflow of capital from the stock markets, reflected in the sharp drop in the prices of these instruments. Due to price decreases the capitalization of the WSE declined by 47.6%. The scale of the problems soon appeared to be more severe, as many enterprises had problems in obtaining financing as declining confidence among
participants in the financial markets led to problems with renewal of bank loans [Narodowy Bank Polski 2010, 2011b].

Table 7 Structure of leased assets in 2001-2010 (in %)

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Movables leased</td>
<td>79.6</td>
<td>92.9</td>
<td>94.3</td>
<td>85.9</td>
<td>84.8</td>
<td>90.6</td>
<td>90.7</td>
<td>90.1</td>
<td>91.0</td>
<td>94.2</td>
</tr>
<tr>
<td>Industrial machinery and apparatus</td>
<td>25.6</td>
<td>23.6</td>
<td>21.1</td>
<td>20.4</td>
<td>26.2</td>
<td>29.8</td>
<td>27.1</td>
<td>29.6</td>
<td>33.3</td>
<td>31.3</td>
</tr>
<tr>
<td>Computers and office equipment</td>
<td>4.6</td>
<td>3.9</td>
<td>2.2</td>
<td>2.0</td>
<td>2.0</td>
<td>1.7</td>
<td>1.5</td>
<td>1.6</td>
<td>2.0</td>
<td>1.7</td>
</tr>
<tr>
<td>Rail, air, water, transport means</td>
<td>3.5</td>
<td>1.4</td>
<td>0.6</td>
<td>1.0</td>
<td>2.1</td>
<td>2.7</td>
<td>1.8</td>
<td>1.6</td>
<td>2.4</td>
<td>2.4</td>
</tr>
<tr>
<td>Means of road transport</td>
<td>42.5</td>
<td>63.1</td>
<td>68.7</td>
<td>61.5</td>
<td>54.0</td>
<td>55.8</td>
<td>59.6</td>
<td>56.5</td>
<td>52.7</td>
<td>58.3</td>
</tr>
<tr>
<td>Real property leased</td>
<td>20.4</td>
<td>7.1</td>
<td>5.7</td>
<td>14.1</td>
<td>15.2</td>
<td>9.4</td>
<td>9.3</td>
<td>9.9</td>
<td>9.0</td>
<td>5.8</td>
</tr>
<tr>
<td>Total movables and real property leased</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>


Table 27 Companies listed on the Warsaw Stock Exchange, their market capitalization and equity index in 2001-2010

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Listed companies</td>
<td>9</td>
<td>16</td>
<td>22</td>
<td>44</td>
<td>65</td>
<td>83</td>
<td>143</td>
<td>198</td>
<td>221</td>
<td>225</td>
</tr>
<tr>
<td>Market capitalization (USD million)</td>
<td>144</td>
<td>222</td>
<td>2710</td>
<td>3060</td>
<td>4564</td>
<td>8390</td>
<td>12135</td>
<td>20461</td>
<td>29577</td>
<td>31279</td>
</tr>
<tr>
<td>S&amp;P global equity index (annual change)</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>71,80</td>
<td>-18,51</td>
<td>-12,25</td>
<td>22,30</td>
<td>-3,53</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Listed companies</td>
<td>230</td>
<td>216</td>
<td>203</td>
<td>225</td>
<td>248</td>
<td>267</td>
<td>328</td>
<td>349</td>
<td>354</td>
<td>569</td>
</tr>
<tr>
<td>Market capitalization (USD million)</td>
<td>26016</td>
<td>28750</td>
<td>37165</td>
<td>71102</td>
<td>93873</td>
<td>149054</td>
<td>207322</td>
<td>90233</td>
<td>135277</td>
<td>190234</td>
</tr>
<tr>
<td>S&amp;P global equity index (annual change)</td>
<td>-24,95</td>
<td>2,19</td>
<td>29,49</td>
<td>59,30</td>
<td>20,79</td>
<td>38,13</td>
<td>23,22</td>
<td>-57,80</td>
<td>41,90</td>
<td>11,26</td>
</tr>
</tbody>
</table>

Source: GPW (2012)

Summing up the analysis undertaken, it is worth underlining that the main source of financing newly established investments are the own funds of enterprises. According to the survey conducted cyclically by the National Bank of Poland among Polish entrepreneurs, almost a half of the respondents (47.9%) preferred to fund new
investments from their own resources in the third quarter of 2012. This ratio appeared to be stable as compared with the previous years (49.5% in the fourth quarter of 2011). The second popular source of financing of investments are bank loans which cover c.a. 25% of the needs of enterprises. However, some companies as the main source of financing of the new investments use foreign financing from their mother companies (Narodowy Bank Polski 2012).

The global financial crisis brought about some changes in the structure of investment’s financing. Namely, in the last three years the use of bank loans by large companies was descending, while in the sector of SMEs there was at that time an increase of interest in bank loans as a source of the financing of new investments. The third quarter of 2012 brought a deep reduction in the use of bank loans as a source of financing of investments undertakings by large companies. As a result, role of bank loans in the financing of investments in this sector of companies is currently the lowest in history (Narodowy Bank Polski 2012).
11. The involvement of the financial sector in the restructuring of the economy

The Polish financial sector played an important role in the process of the rebuilding of the economy in Poland in two ways. Firstly, the Polish financial sector itself has been the subject of a deep transformation since 1989, referring particularly to the privatization processes. This phenomenon is going to be analysed in the next Section. Secondly, development of segments and institutions of the Polish financial sector facilitated the achievement of a target of the restructuring of the whole economy (National Bank of Poland 2001).

This second target has been mainly accomplished by the privatisation of the Polish economy (Table 28). As it was noticed, since 1989 Poland has entered into a period of economic transformation. In order to foster this process, successive governments and the Ministry of the Treasury, created in 1996, have launched the privatisation process. The largest privatisations took place in the 1990s. In particular years, the property worth more than USD 10 billion was sold (around 6% of the Polish GDP then). Privatisation in Poland very often took form of the sale of state-owned property to foreign owners: the biggest Polish telecom operator and many banks went into the hands of foreign investors. In the latter half of the nineties, the status of most of the inefficient state enterprises of that time altered, with these enterprises being restructured or privatised. Very often new private firms have survived, but at a price of growth of unemployment. Because of a difficult economic environment, the condition of many of them has again deteriorated; this includes companies involved in shipbuilding, mining and transport. Partially this was also due to the fact that frequently the motive for the intensification of privatisation process was not the increase of economic efficiency, but meeting the budgetary needs (National Bank of Poland 2003).

Since the very beginning the Polish capital market has been highly involved in the restructuring of the national economy. As it was stressed in Section 3, in the early days of the Polish capital market a huge stimulus to its development was provided by the planned privatisation of the state-owned enterprises. The largest company privatised in this period was Bank Śląski SA. It was then the largest company in
terms of market valuation. However, as first quotations of Bank Śląski SA in 1994 were more than 13 times the issue price, suspicions of a fraud arose among the public (Warsaw Stock Exchange 1993, 1994).

Despite that, as a result of the privatisation new stocks on the Polish capital market appeared, as well as the inflow of capital to budget. In order to maintain the scale of this inflow, in 1995 the Mass Privatisation Programme had been launched, making the use of the experience of the “voucher privatisation scheme” applied earlier in the Czech Republic. The main target was to transfer some of state-owned companies to Polish citizens, while management firms, which were also the element of the programme, would be responsible for restructuring the privatised enterprises. Such management firms in form of the National Investment Funds (NIF) were created in 1994, as joint stock companies. Each fund hold 33% of the shares in 33-34 companies and had a minority stake in all of the programme’s other companies. All funds hold altogether 60% of shares in each of 512 privatised companies. The remaining part of shares was divided into pools of 15% and 25%: the first was distributed among employees and the latter one was retained by the State Treasury. The distribution of the NIF certificates started on November 1995 and finished year after. Each adult Pole was eligible to take up one certificate for a standardized fee of 20 PLN. The NIF certificates were distributed among 26 million citizens (more than 95% persons eligible) that participated in the program. Certificates were issued in form of physical bearer documents that could be sold or purchased on the secondary market without any restrictions. Such a construction led to the concentration of the certificates, as many people got rid of the certificates immediately after purchasing them (Warsaw Stock Exchange 1995, 1997, 1998).

In 1995 the NIF certificates were introduced to exchange trading provided that they were dematerialised by the National Depository for Securities. This was the first step of the Mass Privatisation Programme. The second step was to admit 15 NIF’ shares for exchange trading in 1997. Each NIF certificate could be converted into one share in each of the 15 NIF in accordance with the Act of 30 April 1993 on the National Investment Funds. The conversion process started on May 1997 and finished in
December 1998. In this very month the NIF certificates were traded on the Warsaw Stock Exchange for the last time. All the certificates were converted into NIF shares and those who did not manage to dematerialize them had only souvenir of historical value (Warsaw Stock Exchange 1995, 1997, 1998, 1999).

The shares of NIF were listed on the stock exchange on June 12, 1997 (National Bank of Poland 2002). Since admission to public trading, the funds had been subject to the same disclosure requirements as other public companies. The total capitalisation of these funds stood then at PLN 4.96 billion (Warsaw Stock Exchange 1998). The accomplishment of the programme allowed for maximizing the value of privatised companies along with bringing more Poles into the ownership transformation process. The Mass Privatisation Programme is going to be officially accomplished on January 1, 2013, as the Act of 30 April 1993 on National Investment Funds is valid until December 31, 2012 (Act of 30 April 1993 on the National Investment Funds).

Along with the accomplishment of the Mass Privatization Programme, a privatization through sale of stakes in state-owned companies was extended. As a result, the years 1996-1998 brought a significant rise in the number of listed companies and the privatisation of further large corporates. The decisive role of privatisation of state-owned corporates in the development of the capital market influenced the rising abilities of this market to perform its functions in the market economy. However, every halt in the inflow of large offerings from the Polish Treasury companies resulted in hampering of the development of the capital market along with the rapid development of the segment of Treasury securities as a consequence of increasing borrowing needs of the central budget and a simultaneous decrease privatisation revenues.

Without any doubt one can find out that the growth rate of the capitalization of the capital market in the second half of the nineties was dependent on the privatization of large state companies, such as: Bank Pekao SA (one of biggest Polish banks), Telekomunikacja Polska SA (main telecom operator) and Polski Koncern Naftowy Orlen SA (large fuel company). This resulted from the manner in which state-owned
companies were privatised: state-owned companies entered the market mainly through new stock issues. Such policy allowed the partial privatisation of state-owned companies and obtaining new capital necessary for further development simultaneously with keeping the control over those companies by the State Treasury (National Bank of Poland 2007b). But along with changes in the Polish political arena intensification of privatisation process through entering the WSE waned. The years 2000-2003 were the first in the WSE history without any State Treasury privatisation (Warsaw Stock Exchange 2001, 2002, 2003, 2004).
### Table 8: State-owned enterprises covered by the privatisation programme (from August 1, 1990 to December 31, 2010)

<table>
<thead>
<tr>
<th>Period</th>
<th>Total</th>
<th>Commer-cialisation*</th>
<th>First stake of shares made available</th>
<th>Sale of shares</th>
<th>Direct privatisation</th>
<th>Liquidation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Indirect privatisation</td>
<td>Acquisition of share in the increased capital</td>
<td>Gratuitous transfer to local government units</td>
<td>Sale of further stakes in companies with Treasury share-holdings</td>
</tr>
<tr>
<td>in years</td>
<td></td>
<td></td>
<td>Indirect privisation</td>
<td>Acquisition of share in the increased capital</td>
<td>Gratuitous transfer to local government units</td>
<td>Sale of further stakes in companies with Treasury share-holdings</td>
</tr>
<tr>
<td>1990-1995</td>
<td>3619</td>
<td>1062</td>
<td>160</td>
<td>220</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1996</td>
<td>425</td>
<td>131</td>
<td>567</td>
<td>24</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1997</td>
<td>314</td>
<td>61</td>
<td>58</td>
<td>44</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1998</td>
<td>297</td>
<td>118</td>
<td>41</td>
<td>16</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1999</td>
<td>303</td>
<td>97</td>
<td>26</td>
<td>18</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2000</td>
<td>258</td>
<td>37</td>
<td>26</td>
<td>21</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2001</td>
<td>134</td>
<td>9</td>
<td>32</td>
<td>21</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2002</td>
<td>100</td>
<td>12</td>
<td>22</td>
<td>21</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2003</td>
<td>83</td>
<td>12</td>
<td>6</td>
<td>6</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>2004</td>
<td>98</td>
<td>23</td>
<td>11</td>
<td>10</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>2005</td>
<td>84</td>
<td>16</td>
<td>11</td>
<td>6</td>
<td>5</td>
<td>-</td>
</tr>
<tr>
<td>2006</td>
<td>32</td>
<td>9</td>
<td>6</td>
<td>6</td>
<td>0</td>
<td>-</td>
</tr>
<tr>
<td>2007</td>
<td>62</td>
<td>32</td>
<td>25</td>
<td>20</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>2008</td>
<td>100</td>
<td>78</td>
<td>10</td>
<td>3</td>
<td>0</td>
<td>6</td>
</tr>
<tr>
<td>2009</td>
<td>51</td>
<td>36</td>
<td>20</td>
<td>12</td>
<td>2</td>
<td>6</td>
</tr>
<tr>
<td>2010</td>
<td>15</td>
<td>10</td>
<td>97</td>
<td>56</td>
<td>0</td>
<td>31</td>
</tr>
</tbody>
</table>

* together with 117 Sole Shareholder Companies of the Treasury created by other Misters and taken over by the Mister of Treasury pursuant to the reforms of government economic centre 1997.

Source: Ministry of Treasury (2010).
In 2004, for the first time since 2000, new privatised companies came to be listed on the WSE. One of them was Powszechna Kasa Oszczędności Bank Polski SA (the then largest Polish bank). It was the largest public offer in the history of the Polish capital market. Moreover, in April 2004, the Polish government made a decision to initiate the process of privatizing the Warsaw Stock Exchange itself (Warsaw Stock Exchange 2005).

In the next year 7 state-owned companies were privatised (including large fuel and energy companies, such as PGNiG SA and the Lotos Group SA), but in 2006 the privatisation process once again was dampened. Only one company owned by the State Treasury (Ruch SA – the then largest press distributor) was privatized through the WSE (National Bank of Poland 2004, 2009). The reason – as in years 2000 to 2003 – was the change of political climate. The conservative and populist parties, reluctant to sell away the Polish state property to the private (especially foreign) investors, came then to power and put a halt to the denationalization process. In 2006-2008 only one important company was privatised by the State Treasury to be listed on the WSE (Warsaw Stock Exchange 2007, 2008, 2009).

However, the turn of political events has brought an intensification of the privatisation process since 2009. In that year the privatised energy company, PGE Polska Grupa Energetyczna SA, former state-owned company, made its debut on the Warsaw Stock Exchange, becoming the second largest public offering ever to be launched on the Polish capital market and the largest one in Europe in 2009 (Warsaw Stock Exchange 2010).

2010 was a breakthrough year in the history of Polish privatisation. In terms of revenues from privatisation, 2010 turned out to be the record year. The value of concluded and/or initialled privatisation agreements in 2010 amounted to PLN 29.7 billion, which was the highest result in the history of Polish privatisation. Three state-owned companies were floated on the Warsaw Stock Exchange. Among them was a historic offering, described as the ‘IPO of two decades’, i.e. the Warsaw Stock Exchange’s floatation on its own trading floor. This public offering elicited record interest among investors. Over 320,000 individual investors submitted their subscriptions
and the issue was 25 times oversubscribed among institutional investors. The other two privatised enterprises were the leading Polish insurance company, PZU SA (the largest IPO in the history of the WSE), and Tauron Polska Energia SA, an energy company. The value of stocks listed under those three offerings accounted for PLN 13.5 billion. In the case of PZU’s IPO – the biggest insurer in the region – institutional investors oversubscribed available shares over 9 times. In the transaction for the 10% of shares in PGE Polska Grupa Energetyczna, SA institutional investors from four continents participated [Ministry of Treasury 2011, Warsaw Stock Exchange 2011].

It is worth underlining, that since 2010 a new programme, Civic Shareholding, has been launched by the Ministry of Treasury. It is a long-term programme continued during further IPOs and subsequent sale of shares of state-owned companies through secondary public offering. The idea of the Civic Shareholding is to allow individual investors to participate in the privatisations carried through the WSE. For state-owned companies, each time a fixed number of shares which may be purchased by individual investors is set (c.a. 20%-30%), as well as a maximum number of shares that one person may subscribe for. It allows to ensure that there is no credit leverage when buying shares. Unlike previous forms of mass privatisation, individual investors buy shares learning the mechanisms of the capital market. The interest in the shares of companies debuting through the Civic Shareholding programme was higher than expected. Altogether, 323,000 individuals subscribed for shares of the WSE, 251,000 for PZU shares, and 230,000 for Tauron PE shares. Mass participation of Poles contributed to the success of these transactions and strengthened the Warsaw Stock Exchange as an important element of the Polish capital market [Ministry of Treasury (2011).

The role of mergers and acquisitions as well as takeovers in the process of the restructuring the Polish economy was significantly lower. First transactions of this type on the capital market appeared only in the beginning of this century. Moreover, the Polish banking-oriented financial sector supports M&A transactions. Hostile takeovers happen seldom, as presented in Table 29.
Hostile takeovers are hindered also due to the activity of the open pension funds. As noticed in Section 6, these funds have been operating since 1999, as they were created as part of the pension system reform started in January 1999. Their involvement in the restructuring of the economy is of highly stabilizing character. With the establishment of these funds, a new and very important category of institutional investors appeared, as the open pension funds are allowed to invest up to 40% of premiums collected in shares of publicly traded companies, and an additional 10% in shares of the NIF stocks. The rising share of investments by pension funds in securities listed on the WSE is an important factor stabilising the market, influencing the shareholder structure in many listed companies (Warsaw Stock Exchange 2000).

Table 29 Number of delisted companies from the WSE main list and reasons for delisting in 2001-2011

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forced buyouts</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>3</td>
<td>0</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Annulments of dematerialisation/withdrawal from public trading upon request of the issuer</td>
<td>2</td>
<td>10</td>
<td>4</td>
<td>8</td>
<td>5</td>
<td>0</td>
<td>3</td>
<td>0</td>
<td>0</td>
<td>7</td>
<td>3</td>
</tr>
<tr>
<td>Change of legal status</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Bankruptcies by liquidation</td>
<td>1</td>
<td>3</td>
<td>4</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>3</td>
<td>1</td>
<td>1</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>Delisting on the home market</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td>0</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Mergers and acquisitions</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>9</td>
<td>10</td>
<td>4</td>
<td>6</td>
<td>3</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Safety of trading/breach of regulations</td>
<td>0</td>
<td>3</td>
<td>1</td>
<td>1</td>
<td>5</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>No trading</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td></td>
</tr>
<tr>
<td>Total</td>
<td>4</td>
<td>19</td>
<td>9</td>
<td>10</td>
<td>9</td>
<td>14</td>
<td>10</td>
<td>8</td>
<td>13</td>
<td>12</td>
<td></td>
</tr>
</tbody>
</table>


Open pension funds’ investments focus mainly on Treasury securities and shares listed on the WSE. The average share of Treasury securities in the open pension funds’ portfolios accounted for circa 60% in 2009-2011, and share of stocks –
circa 30%. Investments in foreign securities are negligible. Among the most important changes in the structure of portfolios of the open pension funds one can include drastic reductions of share of stocks in overall assets in the first quarter of 2009 and at the end of September 2011. The first reduction was the result of the bear stock market as a consequence of the outburst of the global financial crisis. The second reduction resulted from sharp stock prices fall in the third quarter of 2011 triggered off by the sovereign debt crisis in the euro zone. This particular crisis along with the volatility on the foreign exchange and debt securities markets as well as forecasted rise of the inflation rate brought about also the reduction of the volume of a fixed-rate bonds in the open pension funds’ portfolios in favour of zero-coupon bonds (Urząd Komisji Nadzoru Finansowego 2011a).

The constantly increasing compulsory pension contributions paid to the open pension funds raise the potential impact of the funds on the valuation of shares listed on the WSE. Thus increasing the supply of instruments in which open pension funds may invest, such as corporate shares on the WSE, gains particular significance. This target can be accomplished by nothing more but the accomplishment the process of privatisation (National Bank of Poland 2006a).
12. The processes of privatization of the Polish financial sector

Since the beginning of the economic transformation in Poland, the Polish financial sector has been the subject of a deep restructuring, privatisation and consolidation, leading, in principle, to the increase of competition. This is especially evident in the Polish banking sector.

Taking into account this very sector one can observe that the reduction in bank number presented in Section 3 resulted mainly from consolidation, initiated by Polish banks, to strengthen their market position. The consolidation in the sector has resulted from the amalgamation of foreign banks’ subsidiaries and branches operating in Poland. Substantial changes in the ownership structure of this sector occurred also as a result of the privatisation of large state-owned banks, started in 1991. The privatisation was expected to contribute to the modernisation of management methods and technology, as well as to ensuring the access to new capital, raising the effectiveness of banks and thus increasing their competitiveness (National Bank of Poland 2001).

As already mentioned, since 1989 a two-tier structure of Polish banking has been established. Initially, there were 9 regional commercial banks which took over around 400 branches of the NBP. In the next years these state-owned banks were privatised. Initially commercial banks sought for strategic foreign partners, which would be able to provide technical assistance. This allowed for modernisation and reconstruction of the structure of individual commercial banks. However this cooperation was gradually evolving, involving modernisation of banking operational principles and preparation for operation in a market economy. Additionally, prospects of the accession to the EU made an increase of banks’ own funds a priority. As a consequence, banks in Poland were compelled to attract new capital into the sector. In the face of lack of the domestic capital it had to be a foreign capital (National Bank of Poland 2001).

The cooperative banking sector, because of its fragmentation and poor situation was also a sector that underwent restructuring. Different forms of financial and technical assistance were implemented. As a result, the number of banking failures
was reduced. Consolidation processes, which started intensifying in 1996, was also a response to the increase in competition of commercial banks. The consolidation process accelerated even more in the end of the 20th century due to the resolution of the Commission for Banking Supervision, according to which the capital minimum for cooperative banks established before January 1, 1999 was set at EUR 300,000. However, as opposed to commercial banks, in the privatisation of cooperative banks almost exclusively domestic capital was involved, due to the lack of a legal arrangements regarding participation of foreign capital. Thus foreign investors influenced the situation in the sector of cooperative banks only indirectly, by taking part in the privatisation of the bank BGŻ SA, in which until 1990 all cooperative banks were affiliated (National Bank of Poland 2001).

As was already underlined, the establishment of 9 commercial banks with head offices in main regions and in the biggest Polish cities was the main factor supporting the removal of the banking sector monopoly. Initially these were state-owned banks, equipped with capital by the NBP. In 1991 they were transformed into sole state shareholder companies. The 1989 Banking Act also created the legal background for the creation of new banks. The liberal licensing policy of the NBP in the period 1989-1992 resulted in the establishment of 70 banks. Both public and private capital participated in this process. An important role was played by the State, which wanted to achieve specific social and economic goals by creation of particular banks responsible for, inter alia, conducting state business transactions, financing the housing construction industry, supporting development of SME, financing pro-ecological investment projects, support privatisation. In many cases these banks were not competitive enough as compared to large commercial banks and they quickly transformed into institutions of more universal character. Apart from them, several banks were established as a result of local initiatives in order to provide servicing and financing selected sectors of the economy or to support the development of a given region. As the time went by, they were usually taken over by larger institutions (National Bank of Poland 2001).
Years 1990-1992 appeared to be favourable for the establishment of foreign banks due to several incentives and facilities (tax reliefs during the initial years of operations, possibility of contributing and holding the capital in foreign currency, and the freedom of transferring 15% of profit) were an additional factor encouraging foreign investors. However, as shown in the Table 30, the process that influenced the structure of the Polish banking sector to the highest extent was the privatisation of the nine state-owned banks. The privatisation programme that was set out in 1991 encompassed two stages of this process, namely: 1) commercialisation and 2) capital privatisation, i.e. making bank shares available to third parties. In 1991 the government decided on the transformation of the nine banks into commercial companies. The then adopted legal acts created a framework within which banks could appoint supervisory boards, conduct asset restructuring, increase operational effectiveness, and implement the reconstruction of organisational structures (National Bank of Poland 2001).

Initially in the adopted privatisation strategy foreign strategic partners, that would take over the holding of no more than 30% of the total shares issued but actively participate in bank management were favoured. It was also agreed that the State would retain about 30% of shares with voting rights limited to strategic decisions and the remaining shares would be offered to individual investors in a public offer and to employees, on privileged terms. The change of the government’s policy occurred in 1998. Then significant equity holdings (36.7% and 33.3% of capital, respectively) in two of the banks were sold to foreign investors. This resulted in the first in history exertion of sole control over these banks by foreign institutions (General Inspectorate of Banking Supervision 2000).

The strong position occupied by banks controlled by foreign investors is commonly observed in the banking sectors of various CEEs. In the initial period of transition, these countries lacked domestic investors agents with sufficient capital to participate in bank privatisations. Moreover the privatisation strategies focused on a search for strategic investors in order to protect financial system stability and increase the quality of corporate governance (National Bank of Poland 2003).
The sale of majority interests in Bank Polska Kasa Opieki SA and Bank Zachodni SA by the State Treasury in 1999 completed the privatisation of the 9 banks that emerged from the NBP structure. As a result, at the end of September 2001 the State controlled directly only PKO Bank Polski SA, Bank Gospodarki Żywnościowej SA and Bank Gospodarstwa Krajowego SA, which enjoy state bank status (see Section 6). The latter bank was not included in privatisation plans, because its business focused on carrying out government transactions. The banks indirectly controlled by the Treasury comprised only a few banks. Among them there were Bank Pocztowy SA, controlled by the Polish Post Office (General Inspectorate of Banking Supervision 2002).
Table 30 The privatisation of the biggest commercial banks in 1990-2010

<table>
<thead>
<tr>
<th>Name and registered office of the bank</th>
<th>Privatisation method</th>
<th>Year</th>
<th>Shareholders structure during the privatisation (share in the capital)</th>
<th>Important changes of shareholders in the following years</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>&quot;The nine&quot; banks</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank Zachodni SA</td>
<td>Takeover by selected foreign investor</td>
<td>1999</td>
<td>AIB European Investment Limited (Ireland) 80%, State Treasury 4.29%, other shareholders 15.71%.</td>
<td>2001: the merger with Wielkopolski Bank Kredytowy SA, subsidiary undertaking of Allied Irish Bank European Investments Ltd.</td>
</tr>
<tr>
<td>Powszechny Bank Gospodarczy w Łodzi</td>
<td>Amalgamated with Bank Polska Kasa</td>
<td>1999</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Bank Name</td>
<td>Operation Type</td>
<td>Year</td>
<td>Description</td>
<td>Notes</td>
</tr>
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<tr>
<td>Bank Depozytowo-Kredytowy w Lublinie SA</td>
<td>Amalgamated with Bank Polska Kasa Opieki SA</td>
<td>1999</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Pomorski Bank Kredytowy w Szczecinie SA</td>
<td>Amalgamated with Bank Polska Kasa Opieki SA</td>
<td>1999</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Bank Rozwoju Eksportu (later BRE Bank SA)</td>
<td>Stock market launch</td>
<td>1992</td>
<td>Individual private and institutional investors 85%, State Treasury 15%. 1995: Commerzbank AG bought in the market 21%; 1997: 48.7% (taking up new issue); 2000: 50%, other shareholders 50%; 2002: the merger with LG Petro Bank SA, increase in the equity interest of Commerzbank AG in BRE Bank SA from 50% to 72.2% (primarily through the announcement of a tender offer for BRE Bank SA shares); 2005: the equity interest of BRE Bank SA in BRE Bank Hipoteczny SA raised from 50% to 100%, for an interim period.</td>
<td></td>
</tr>
<tr>
<td>Bank Handlowy w Warszawie SA</td>
<td>Stock market launch</td>
<td>1997</td>
<td>State Treasury 7.9%, ZC Netherlands BV 6.2%, Sparbanken SverigeAB 5.0%, JP Morgan &amp; CO 14.8%, Bank of New York 16.9%, other shareholders 49.2%. 2000: 87.83% buy out of shares by City Group’s subsidiary the Citibank Overseas Investment Corporation; 2001: the merger of Citibank (Poland) SA and Bank Handlowy w Warszawie SA, both directly controlled by Citibank Overseas Investment Corporation; 2005: decrease of the Citigroup interest in the equity of Bank Handlowy w Warszawie SA and its share of voting rights at that bank’s shareholders’ general meeting, cutting these to 75%.</td>
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<tr>
<td>Bank Polska Kasa Opieki SA</td>
<td>Selection of a strategic investor</td>
<td>1999</td>
<td>UniCredit Italiano and Allianz AG (together) 52.09%, EBRD 5.25%, State Treasury 13.9%. 2000: 53.17% UniCredit Italiano, EBRD 6.63%, State Treasury 7.98%, other shareholders 32.22%; 2005: the take-over of control over the German Bayerische Hypo- und Vereinsbank AG by the Italian UniCredit; 2007: Commission for Banking Supervision’s consent for the division of Bank BPH, which allowed the merger of Bank Pekao SA and the part of Bank</td>
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</tbody>
</table>
This project is funded by the European Union under the 7th Research Framework programme (theme SSH) Grant Agreement nr 266800.

Pryzemia-Handlowy SA, conclusion of agreement between UniCredit and GE Money concerning the purchase of 66% of stocks of the so-called mini-BPH.

However, the partial privatisation of PKO Bank Polski SA was launched in 2004 [National Bank of Poland 2006b]. 37.7% of the equity was sold through a public share offering, thereby beginning bank’s privatisation. Moreover, just in 2005 Bank Gospodarki Żywnościowej SA received a capital infusion of PLN 510.8 million thanks to a new share issue taken up by the EBRD and Rabobank Nederlanden BV which additionally purchased shares of BGŻ SA also from cooperative banks. A decrease in the equity stake of the State Treasury in state-owned banks declined also as a result of planned gradual transfer of shares of these banks to their employees (General Inspectorate of Banking Supervision 2005, 2006).

As a result of the intensification of the privatisation process, in 2005 the share of the State Treasury in the share capital of PKO Bank Polski SA decreased from 62.3% to 52.0%, and in the share capital of Bank Gospodarki Żywnościowej SA from 49.5% to 43.5% (National Bank of Poland 2007b).

In years 1997-2003, the bulk of foreign capital invested in the Polish banking sector came from Germany and the USA. Initially the inflow of investments from these two countries reached jointly 60% of all foreign capital invested in the Polish banking sector. In the subsequent years this share was gradually falling to 40% in 2004 (General Inspectorate of Banking Supervision 1999, 2000, 2001, 2002, 2003, 2004). However, in 2005 the equity involvement of investors from Belgium increased the most, thus these investors reached second position as providers of foreign capital. Their investments accounted for almost 17% of all foreign capital invested in the Polish banking sector in 2005. Next years the inflow of capital from Belgium was even stronger as compared with other countries, allowing investors from Belgium to leave the American and German investors at second and third places (General Inspectorate of Banking Supervision 2005, 2006, 2007). The situation changed in 2007. Since then, investors from Italy have started controlling the largest part of assets in the Polish banking sector, which accounted for more than 12% in this and subsequent years (Polish Financial Supervision Authority 2008b, 2009b, 2010b).

As a result of the constant inflow of the foreign capital, at the end of 2011, foreign investors controlled 37 commercial banks and all branches of credit
institutions. Majority holdings were in the hands of investors from 18 countries, whereas the dominant role was played by Italian investors (12.5% of the sector’s assets), followed by German (10%), Dutch (8.5%), American (6.2%), Spanish (5.7%) and French (5.1%). In 2011 domestic investors controlled only 10 commercial banks and all cooperative banks (The State Treasury controlled 4 commercial banks: PKO Bank Polski SA, Bank Gospodarstwa Krajowego SA, Bank Pocztowy SA and Bank Ochrony Środowiska SA). Their market share measured in assets increased from 33.8% in 2010 to 35% in 2011 (Polish Financial Supervision Authority 2012).

The increasing domestic and foreign competition created a background for establishment banking groups and financial conglomerates. In 1989, at the beginning of the transformation, a mono-bank sector dominated. The dismantling of this structure required introduction of commercial banks. The approval of the establishment of numerous private banks and the broadly planned privatisation of existing state-owned banks resulted in the removal of the initial disproportion between capital and organisational concentration and the mechanism of competition in the inter-bank market (National Bank of Poland 2001). The process of consolidation has strengthened in Poland since the second half of the 1990s. This process was the most intensive in the years 1999-2002. In the first half of the 1990s, takeovers of banks in poor financial condition by stronger banks dominated. On the contrary, the mergers conducted in the years 1997-2002 were a consequence of the prior privatisation of domestic banks and winning over strategic investors, as well as global-scale mergers including parent banks (National Bank of Poland 2004). Evolving situation in the banking sector, influenced by the Poland’s membership in the EU, created a favourable circumstances for new trends, according to which new banking capital groups and financial conglomerates are being established.

The last huge M&A transaction was launched in 2006, when Italian UniCredit commenced the merger procedure of Bank Pekao SA and Bank BPH SA. This was the result of the announcement of the takeover of the German HypoVereinsbank (HVB) by the Italian UniCredit group in 2005 (see Table 30). In Poland, UniCredit and HVB were strategic investors of Bank Pekao SA and Bank BPH SA, respectively. The merger of
the HVB and UniCredit groups triggered action aimed to merge Polish banks. As a result, in 2007 Bank BPH SA was divided. One part was integrated with Bank Pekao SA in the form of an organised part of the enterprise in exchange for the shares of Bank Pekao SA, while remaining part was sold to GE Money Bank SA. The split of Bank BPH SA took place by the end of 2007. As a result of this merger, the value of assets of Bank Pekao SA appeared to be higher than the asset value of the then largest Polish bank – PKO BP SA (National Bank of Poland 2009, 2010, Narodowy Bank Polski 2010).

In the next years mergers and acquisitions were of far lower influence on the structure of the Polish banking sector. Only the merger between Getin Bank SA and Noble Bank SA, finalised in January 2010, could have the sizable impact on this structure, as well as changes of strategic investors in some banks as a result of their parent banks being taken over (for example, in 2009 BNP Paribas took over a part of the Fortis group), or necessary sales of some foreign assets by parent banks following independent decisions aiming at improving the financial situation (Polish Financial Supervision Authority 2010b).

Consolidation observed in the Polish banking sector is one of the major factors that could trigger off the increase in concentration in the future. However, since the beginning of the functioning of the two-tier banking sector, an level of concentration has remained stable. In 1998, at the end of December, the 11 largest banks jointly held nearly 68.7% of net assets at the commercial banks, while 42 small banks held merely 4.7% of net assets at the commercial banks (General Inspectorate of Banking Supervision 1999). For the sake of comparison, in 2011 10 largest banks controlled 63.4% of the sector’s assets (Polish Financial Supervision Authority 2012). Even the aforementioned merger of the Bank Pekao SA and Bank BPH SA did not cause the significant rise in the concentration level, which is still relatively low in comparison with other European countries (National Bank of Poland 2004, 2009).

As was mentioned in the beginning of this section, the denationalization and restructuring processes were the deepest in the Polish banking sector. Privatization in other financial sectors was less dynamic and changes in their structure occurred
in a more smooth way. This can be observed while analysing for example the Polish insurance sector.

The Polish insurance market, due to the number of citizens, location and economic reforms implemented in the country was very attractive for foreign investors. The first of these appeared in 1990: two American entities along with the Polish shareholder formed insurance companies. In the following year four other companies were allowed to conduct insurance activity. At the end of 1991, only 6 insurance companies with prevailing foreign capital had the authorization of the Minister of Finance to conduct insurance activity, but as at the end of 1996 their number equalled 14. In the following years, this number kept increasing. Starting from the year 1996 on the Polish insurance market there has been a sharp increase in the number of insurance companies with participation of foreign capital. As a result, the share of foreign capital in the Polish insurance sector exceeded 70% in 2011, in life insurance as well as in non-life. Some insurers continue to be controlled by the Treasury or have registered Polish companies as shareholders (Państwowy Urząd Nadzoru Ubezpieczeń 2001, Polish Chamber of Insurance 2011).

The first mergers and acquisition transaction in the Polish insurance sector was accomplished in 1994 via the purchase by foreign entity shares of the existing insurance company (a German entity purchased 27.5% of shares in Hestia Insurance SA). The process of mergers and acquisitions intensified in the end of the 1990s, being a result of the processes of consolidation in the Polish insurance sector. However, along with keeping the monopolistic position by the largest Polish insurance company (PZU SA), they led to relative petrification of the structure of the Polish insurance sector. Like in other Central and Eastern European countries this sector is characterized by a relatively high degree of concentration. The number of market players is relatively stable, it changes lately only as a consequence of decisions of insurance companies’ owners to pull out of the Polish market as a result of realignments among foreign shareholders (Insurance and Pension Funds Supervisory Commission 2003, Państwowy Urząd Nadzoru Ubezpieczeń 2001).
This project is funded by the European Union under the 7th Research Framework programme |theme SSH| Grant Agreement nr 266800
13. Inequality and the Polish financial system

Issues of inequalities are almost entirely absent in research and discussion on the Polish financial system. Inevitably, it is a consequence of a short period of functioning newly established the financial system. Many basic aspects and features have been hardly recognized. Under such circumstances, only some basic research have been made, mainly of quantitative character. Subject of analysis have been simple financial categories and phenomena, like structure and ownership of the financial system, organization of financial intermediaries, their legal and technical frameworks, costs and profits, assets and liabilities and their dynamic, etc.

Gender, ethnical or minority issues are not so far raised. It concerns not only complex, thorough analysis, but also even partial, fragmentary ones. Such question as a structure of incomes within the financial sector, gender structure, gender bias, education of staff, etc. are not subject of research. There is no data on those issues, both external and internal. Moreover, the question seems to be rather ignored by the Polish researchers. Survey of the articles published in Polish economic journals, as well as the topics of main finance and sociological conferences (and papers being their aftermath) from recent 10 years reveals no interest in the topic of inequalities within the financial sector.

There are only some exceptions, connected only with the banking sector. First, Institute of Banking from the Poznań University of Economics with cooperation with Związek Banków Polskich (ZBP, the Polish Banks Association) conducted in 2005 research on features of banks’ staff in Poland. Results revealed some differences between employees of the commercial and the employees of cooperative banks. The latter ones were older and worse educated than in the former ones (PBA 2006). Second, the ZBP (2007) researched structure of the employment in the banking sector. Their results showed that the women constituted in 2003 nearly 80% of employees in the banking sector. Finally, in the report Woman in Poland (2011) there were presented some data on the situation of the women in various segments of the Polish economy. Concerning banking, it turned out that in 2011 among the

35 Incidentally, some fragmentary data on salaries of banks’ chairpersons are published, but their reliability is questionable.
chairpersons of the banks listed on the WSE there was only one woman. There was also only a few women in the boards of those banks. Moreover, according to research made for the report, average salary in banks in 2011 amounted PLN 5750 for a man, and only PLN 4000 for a woman. Even more divergence was when one compares salaries of the branch managers – PLN 9000 and PLN 7400 respectively.

However, it must be stressed that lack of interest in inequalities applies not only to the financial sector, but in principle to all sectors of the Polish economy. Just recently have been presented first relatively complex publications on inequalities in education and health care. They are, among others, the subject of the most complex so far research on sociological and economic features of the Polish society – *Social Diagnosis (Diagnoza Społeczna 2011)*. This document discusses at length such problems as social exclusion, social capital, household living conditions, quality of life, use of information and communication technologies, inequalities in labour market, health care and education. However, there is no reference to financial exclusion or inequalities within the financial sector.

One might suppose that with consecutive development of the financial system, better understanding of importance that inequalities of various kind have, broader application to Polish conditions methodology of research on the issue, as well as with growing experience of researchers, more thorough, both quantitative and qualitative studies will be conducted. But at the moment, even a general outline of issues connected with inequalities within the financial sector, would demand distinct, long-lasting research, which is beyond the scope of this report.
14. **Survey of previous research on efficiency of the Polish financial sector**

Research on efficiency of the Polish financial sector have been relatively rare and concerned mainly the banking system.\(^{36}\) Moreover, the topic has been rather considered by domestic authors in articles prepared for domestic market. The method most often applied, apart simple analysis of earnings, costs and profitability, was data envelope analysis (DEA).

Havrylchyk (2006), using this very method, investigates the efficiency of the Polish banking industry between 1997 and 2001.\(^{37}\) The methodology allowed the author to distinguish between five different types of efficiency, such as cost, allocative, technical, pure technical, and scale. Additionally, a number of parametric and non-parametric tests was conducted in order to test whether foreign and domestic banks came from the same population. Finally, multivariate regression analysis was employed in order to detect the determinants of banking efficiency in Poland.

The average efficiency for banks operating in Poland has been 52.92% and 73.23% for domestic and foreign banks respectively. Foreign banks have exhibited higher productivity of their inputs (technical efficiency) and have been superior in choosing the right mix of inputs in light of given prices (allocative efficiency). Such results are consistent with other studies for transition and developing economies (e.g. Grigorian and Manole 2002, Hasan and Marton 2003, Bonin et al 2005). However, the results of the multivariate regression analysis indicated that the higher efficiency of foreign banks had been due to the successful performance of green field banks. Foreign banks that had acquired domestic banks did not appear to have enhanced their efficiency.

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\(^{36}\) One of the exceptions is Pawtowska and Kozak (2008). They analysed insurance sector in the context of entry to the EU. They followed Bikker and Leuvensteijn (2005) approach used in research on the Dutch insurance sector, and applied DEA and SFA methods for the period 2003-2006. Results revealed average efficiency of the Polish insurance companies slightly lower than average for the eurozone. However, the former increased in considered period.

\(^{37}\) The starting point in the research on bank efficiency are usually years 1995-1996. Just since then appropriate data exist that makes analysis possible.
Moreover, Havrylchuk’s results indicate that bank efficiency has not improved during the years analysed. The years when most of the decline in efficiency took place, 1999 and 2001, were marked by accelerating privatization and consolidation processes that imposed additional costs on banks. At the same time, the declining loan portfolio quality has added costs associated with monitoring and enforcement of loan contracts.

Pawłowska and Kozak (2008) run empirical analysis of the Polish banking sector for the longer period, namely 1997–2006. They used both DEA and SFA (Stochastic Frontier Approach) methods. They found that in the analysed period, the efficiency of Polish commercial banks increased. The average efficiency of Polish commercial banks was close to the efficiency of euro area banking sectors. In addition, retail banks were more efficient than corporate banks. As the main reason of increasing efficiency, the authors point at the adjustments during accessions and the Poland’s entry into the European Union. Another important factor, but in a sense, being the aftermath of entering the EU was consolidation process within the banking sector.

Gospodarowicz (2000) used DEA method to measure efficiency of 50 Polish commercial banks in the years 1997-1999. The results showed that average efficiency amounted 80%. Moreover the author used Malmquist index in order to identify changes in banks’ productivity within the research period. Analysis of the index indicated continuous fall of the overall productivity in researched banks. As a reason of such tendency Gospodarowicz perceived decreasing technical productivity.

Kopczewski (2000) and Kopczewski and Pawłowska (2000) analyses changes in efficiency of the Polish banking sector in the context of three factors: their size, ownership and conducted activity. The sample consisted of 65 banks, segmented by their technical efficiency, scale of activity. Then, Kopczewski and Pawłowska tried to identify influence of volatile market conditions on banks efficiency. They found that the main source of technical inefficiency was relatively high number of “small” banks. The latter ones, due to limited size of resources involved, were not able to reach optimal relation between costs and profits. Concerning ownership structure
both authors found that best parameters of technical efficiency had private banks, controlled by the foreign investors.

Similar results reached Opiela et al (1999). They analysed 56 commercial banks, functioning in Poland in the period 1996-1998. Taking into account cost efficiency and profit efficiency they searched for factors explaining differences in these two areas. Decisive impact had the ownership structure. Private banks were more effective than banks owned by the Treasury. At the same, within the former group more effective were banks with dominating foreign investor.

Kisielewska et al. (2005) develop six production models in which banks are mainly perceived as “producers” of deposit accounts and loan services in order to examine performance of the banks. They use DEA window analysis in order to accommodate relatively small sample size (only 10 banks) with a large number of performance variables. Then, they analyse cost efficiency of the banks within the years 1995-2003, based on these model. Moreover, similarly to Gospodarowicz, the authors use Malquist index in order to track changes in productivity. Results of their research indicated general improvement in the cost efficiency, as well as decline of the dispersion in efficiency between considered bank.

Mielnik and Ławrynowicz (2002) researched 34 commercial banks in 1999. In their analysis the variable that influenced efficiency was, rather surprisingly, the number of branches. The variable ceased to be important in explaining efficiency changes in mature market economies. Its relevance in Poland may constitute another argument for relative underdevelopment of the Polish banking sector.

Stępień (2004) and Pawłowska (2003) applied DEA method in order to assess efficiency of the banking sector in the context of its consolidation. The former author, analyzing the sample of 20 banks in 1997-2003, found that in a few cases consolidation contributed to greater efficiency. On the other hand, the latter did not find any significant influence of mergers and acquisitions between banks on their efficiency.

Apart from commercial banks, DEA was applied also to research on cooperative banks (Gospodarowicz 2009, Zychowicz 2001). Results revealed lower
efficiency of cooperative banks than commercial ones. It probably resulted from less qualified staff, limited resources and less developed organizational culture in cooperative banks. However, efficiency of cooperative banks varied between banks belonging to various cooperative associations.

The presented survey of previous research shows that efficiency of the Polish banks in principle increased, at least till the mid of 2000s. It differed however when type of bank and structure of the ownership was considered.
15. The impact of the processes of European integration on the national financial system

Poland was among the first CEEs to apply for membership of the European Union. Already on September 19, 1989, Poland signed the agreement for trade and trade cooperation with the then European Community. That agreement constituted a starting point for future negotiations on the subject of associating with the EC.

On May 19, 1990, Poland officially applied for a beginning of negotiations for an agreement of associating, and the negotiations began in December 1990. After eleven months, on December 16, 1991 the Polish government signed the Europe Agreement which established an associate relationship between the EC and the Republic of Poland. The document initiated Poland’s process of European integration, setting the legal grounds for the pursuit and implementation of economic, political, scientific, and cultural union. The agreements signed with the EC, which at this time was preparing for its transformation into the European Union (EU). The Europe Agreement came into force on February 1, 1994.38 The EC gave its consent to the Agreement foreword containing an additional point: “Poland’s ultimate aim is membership of the Community.” In this way the Polish partner established that the aim of the Agreement was the creation of frameworks for Poland’s gradual integration into the Community.

Another important stage on Poland’s way to the EU took place at the Luxembourg summit in 1997, when the EU accepted the Commission’s opinion to invite several Central and Eastern European states (Poland, Czech Republic, Hungary, Slovenia, Estonia and Cyprus) to start talks on their accession to the EU. The preliminary condition for the inauguration of negotiations was fulfilment of the so-called Copenhagen criteria.39

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38 The third part of the Agreement – on the mutual trade relations – came into force already since March 1992.
39 The Copenhagen criteria, prepared on the EC summit in June 1993, assumed, among others that candidate countries should achieve stable institutions that guarantee democracy, legality, human rights and respect for and protection of minorities, should have working market economy, capable of competing effectively on the EU markets, and, finally, that they are capable of accepting all the membership responsibilities, political, economic and monetary.
The negotiation process started on March, 31, 1998, when the first sitting of the International Accession Conference took place. After the meeting, screening sessions began to determine the extent to which Polish law was in accordance with community law, followed by the two parties developing position papers for each negotiating position. The opening of negotiations in given areas signified that the European Council has granted the European Commission the relevant mandate to conduct talks with the candidate states. After the final agreement negotiations were temporarily closed. In the final phase of all the negotiations their results took the form of entries in the accession treaty.

Poland finished the accession negotiations in December 2002. Then the Accession Treaty was signed in Athens on April, 16, 2003. After the ratification of that Treaty, Poland (and other 9 countries) became the members of EU on May, 1, 2004. At the same time Poland committed also to enter the Euro zone, but without any determined date.

The integration process moved along with transformation of the economic and political system. It was in a sense, convenient: many adjustment could have been made while creating brand new legal environment. Thus, in many cases, no special changes were needed – sufficient was just preparing and introducing laws consistent with the EC regulations. Moreover, since the very beginning of the transformation, financial institutions from the EC/EU were present in the Polish financial system, being one of the most active investors in the process of privatization (see section 1). Thus, many links with financial systems of the EU countries were already established, even prior to Poland’s formal accession to the EU.

However, some adjustments had to be made. Ongoing efforts of Poland’s consecutive cabinets government, central bank, supervisory institutions and financial institutions themselves were taken. It involved implementation of the EU *acquis communautaire* relating to free flow of capital and services, as well as to functioning of individual types of financial intermediaries, central bank and monetary policy, supervision authority, and settlements systems actions taken in order to reinforce
the stability and strengthen the capitalisation of the whole sector and to improve the quality of the legal, judicial and technological infrastructure.

With reference to the banking sector, the dominant part of the Polish financial system, the main part of adjustments was made with passing new Poland’s Constitution of April, 2 1997 and, in the same year the Act on National Bank of Poland and the Banking Act – both of August 29, 1997. These two adjusted almost entirely organization and functioning of the Polish banks to the EU directives. All remaining differences were eliminated by amendments, passed by the Act of 18 December 2003, which entered into effect on 1 January 2004. Since then it can be stated that the domestic regulations blend in with those of the EU. Necessary legal adjustments were also enforced with reference to other parts of the Polish financial system.\(^40\)

Thus, the very entry into the EU in 2004 did not change significantly instructional and regulatory framework.\(^41\) Despite of it, or maybe, due to reached earlier convergence, EU membership was another impulse for the development of Polish financial sector and its closer integration with financial markets of other Member States.

As was said above, many financial institutions from the EU already conducted activity in Poland. But after the accession, they were able to open branches in Poland on the basis of single passport rule. For instance, in 2003, credit institutions from the EU Member States had no branches in Poland, but in 2007 already 14 branches operated in Poland and their total assets exceeded EUR 9.5 billion. In 2012 there were 23 branches (see Section 3).

The value of assets of the Polish financial sector had been on the increase already in the pre-accession period, as it was described in the second section, and this trend was continued after the accession. In 2006, this increase reached a record-breaking level of 22.4% per annum. Better condition for growth resulted from two factors. The first one was the rise in the flow of foreign direct investment. In April

\(^{40}\) For instance, insurance market was re-regulated with passing Insurance Activity Act, Insurance Brokerage Act and Compulsory Insurance, Insurance Guarantee Fund and Polish Motors Insurers’ Bureau Act – all of them of May, 22, 2003. For more concise characteristic of legal changes, see Section 6.

\(^{41}\) Of course, some slight discrepancies still existed.
2005, FDI amounted to EUR 7.5 billion – about twice as much as in the previous year. In the period 2004–2007, the value of FDI inflows was much higher than in the five-year pre-accession period, reaching nearly EUR 51 billion. It meant that the average annual value of FDI inflows in four years after accession reached almost EUR 13 billion. In comparison, the inflows of FDIs in 1999–2003 reached 32.2 billion EUR, i.e. just 6.4 billion EUR per year on average. This growth in FDI was mainly due to a considerable increase in confidence in the Polish economy after its integration into the EU and its good economic perspectives. The second positive sign is a net inflow of structural founds amounting EUR 1.5 billion.\textsuperscript{42}

There were, however, also negative consequences. Among them, one should point at pressure on the appreciation of the Polish zloty, resulting from an increased demand for the currency. A higher exchange rate means, among others, more expensive goods and services, which in turn become less competitive on internal and external markets, with all the negative effects for production and unemployment. However, fortunately, it was not the Poland case, as the appreciation of the Polish zloty was accompanied by the rise of productivity.

The second problem, often mentioned, was pressure on the budget deficit. Structural funds provided by the European Union can finance accepted programs by definition up to 75% of their value. So, at least 25% of the value of the project is always accounted for by self-financing by the Polish government. In reality, self-financing means financial sources obtained from the local or central government, with the exception of those financed by private institutions. Where there is a huge budget deficit — paradoxically— a positive inflow of structural funds creates pressure to increase it. However, as it will be mention in the Section 16, it helped to avoid recession, when global financial crisis and following dampening of economic activity in Europe occurred. Altogether with inflow of funds it boosted internal demand and at the same time – demand for loans and financial services.

\textsuperscript{42} In 2006 net inflow amounted even more then EUR 10 billion.
16. Global financial crisis and its consequences for the Polish financial system

The onset of the global financial crisis did not directly influence Poland. Poland avoided heavy losses brought about by the global financial crisis. Some problems occurred and the growth rate was lower, but still the Polish economy functioned well, especially when compared to other European countries. No financial institutions were bankrupted, and there were no drastic tensions in the financial market. But as the crisis escalated, it started to interfere with economic processes in Poland. Disturbances were transmitted into domestic market through three main channels: (1) crisis of confidence and market seizure; (2) market dislocation and (3) spillover effects in the real economy.

In the first stage of the crisis it was mainly the Polish capital market which was affected. Initially, the market remained relatively autonomous and unaffected by growing global turmoil. In the first half of 2008 a sharp decline occurred mainly on the stock market. Events from July-September of that year covering, among others, US government taking control over Fannie Mae and Freddie Mac, bankruptcy of Lehman Brothers, announcing takeover of the Merrill Lynch by the Bank of America and actual nationalisation of American International Group (AIG) accelerated however the negative tendencies in financial systems. As a result, in September the negative tendencies in the Polish financial sector escalated, followed by rapid fall of market activity. A crisis of trust between market participants led to very strong disturbance on interbank market, great declines in stock markets and resources markets and “escape of the capital” from emerging markets.

The growing crisis resulted also in a sharp increase in interbank market rates, reduction of the transactions’ deadlines and decrease in limits for exposure for each

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43 Problems with confidence were, inter alia, a result of information and rumours about financial problems of Polish banks’ strategic investors on foreign markets.

44 It must be stressed that the situation on the Polish financial market has been not only a derivative of the country’s macroeconomic situation or the general climate on global markets, but also, to a significant extent, is a derivative of the situation of neighbouring countries, classified by foreign investors as belonging to one group. This makes unfavourable trends from other countries in the region transfer to Polish market. Moreover, because Polish market is the biggest and the most liquid among the CEEs, investors who want to open or close the exposure to CEE countries, often do this just in Poland. As a result, the scale of reactions to unfavourable trends in other countries is usually bigger in Poland than in countries directly related to these trends. Thus, Polish decisionmakers have to face a sort of “over-reaction” of the Polish market to external events.
entity. All of this led to the increase of financing costs and difficulties in managing current liquidity and securing the risk. Decline of mutual trust among market participants created a situation where banks in Poland, uncertain of contractors’ financial situation, preferred to invest available funds in central banks.

The situation on Polish interbank market in the fourth quarter of 2008 may be however perceived as quite good in comparison to the disturbances occurring in other countries. WIBOR 3M rate, i.e. a reference rate for majority of domestic currency loans, increased from 5.7% at the end of 2007 to 5.9% at the end of 2008. However, it is necessary to note that a decrease of mutual trust among market participants occurred also in Poland. (National Bank of Poland 2009).

As a result of the accelerating crisis, sale of assets (including currencies) of the countries from emerging markets took place together with strong decrease in prices on commodities and limitation of investment processes. Together with the previous symptoms of weakening of US and EU economy, it resulted in a sharp deterioration of economic situation and deterioration of perspectives for world economic upturn.

Thus the financial crisis transformed into the economic crisis. It also happened, to some degree, in Poland. The Polish GDP increased in 2008 by 4.8% in real terms, which signified a considerable decrease of the growth rate compared to 2006-2007 (see Section 1). The decline of GDP growth rate resulted from the natural weakening of economic conditions (highest phase of the cycle was in 2007) and from fast deterioration of world economy following the escalation of financial crisis. It translated into decline of demand for Polish products abroad, decline of production and weakening of enterprises’ financial situation as well as limitation of investments. Industrial production increased in 2008 only by 3.3% in total – the lowest growth rate since 2002. It resulted from reducing the portfolio of domestic and foreign orders, excessive stock, difficulties in acquiring funds and uncertainty concerning

45 However the most alarming thing was consecutive decline of growth dynamics. In first quarter GDP growth rate equaled 6.0% as compared to the same period of previous year, in second quarter 5.8%, in third 4.8% and in fourth only 2.9%.

46 In 2007 it amounted to 11.2%.
development of economic situation. Gross fixed capital formation per annum increased by 7.9% as compared to 17.6% in 2007. The rate of individual consumption remained however high, probably due to certain delay in transferring trends in enterprise sector to households’ level.

Deterioration of economic conditions in the Euro zone, especially in Germany (main commercial partner of Poland), resulted in significant weakening of foreign trade growth rate. Exports in PLN in current prices increased by 3.3%, and imports increased by 6.3%. As a consequence the negative balance of general trade decreased about almost PLN 20 billion with comparison to 2008. (National Bank of Poland 2010).

It is interesting that in the first half of 2008 the Monetary Policy Council (MPC) increased NBP interest rates (100 bps in total), justifying it with accelerated inflation processes, exceeding the top acceptable limit of deviations from inflation target by CPI and with increase in inflation expectations. But in the second half year, in the face of the “second wave” of the financial crisis moving through global financial markets and the resulting difficulties in accessing credit, as well as prognosis for decrease of inflation related to the expected slowdown of Polish economy, the MPC decided to reverse in a sense monetary policy and started a cycle of quick interest rates’ cuts. As a result of the cuts (100 bps in November–December of 2008 and 100 bps in January–February of 2009) NBP rates returned to the level of 2006, equalling respectively: 4.00% for reference rate, 5.50% for lombard rate, 2.50% for deposit rate, and 4.25% for rediscount rate. (MPC 2009, 2010).

Even earlier, in October of 2008, as a result of crisis escalation on global financial markets, a sale of Polish Treasury bills took place. As a consequence, the yield of bills jumped to 120-150 bps. Calming of global markets and starting aggressive cuts of interest rates by MPC translated into a sharp yield decline between November of 2008 and January of 2009, which was within 100-280 bps.

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47 Aggressive cuts of interest rates in Euro zone, US, Great Britain and Switzerland were an additional argument.
48 In the whole 2008 foreign investors decreased their exposure to T-bills issued on domestic market by 25% from PLN 74,5 billion at the end of 2007 to PLN 55,9 billion at the end of 2008.
However, in the subsequent weeks, as a result of another wave of investors’ pessimism and a very negative climate which was created around Central-East Europe countries, Polish Treasury bills were under pressure and its yield increased again. Another consequence of growing financial turmoil on global financial markets was also increase of difference between the yield on Polish T-bills and bills issued by the governments of the biggest and most stable countries (US, Germany, Japan) perceived as the most secure.49

One of the effects of the crisis was also a big reduction of market value of companies which were “icons” of the world and regional economy, particularly from the finance sector. Warsaw Stock Exchange (WSE) followed global markets. As a consequence, at the end of 2008 WIG (main index of the WSE) value was lower than in the end of 2007 by 51,1%. (WIG20 by 48,2%, mWIG40 by 62,5%, sWIG80 by 56.9%, and WIG-Banks by 44,8%). Breakdown on WSE was intensified by mass amortisation of investment funds’ participation units (the biggest in January of the previous year when about PLN 11 billion were withdrawn).50

By observing changes made by banks during 2008 it can be ascertained that for most of the year banks were adjusting significantly parameters of deposit-loan policy to changes of monetary policy’s parameters – increase of NBP interest rates was accompanied by increase of interest rates on deposits and loans offered to clients by the banks.

However, in the last quarter of 2008 banks tightened their loan policy and strengthened the pressure on acquiring deposits through increasing their interest rates. Just then was observed a peak phase of the “deposit war”: weighted average interest rate on term deposits in PLN amounted circa 6.0%.

Considerable tightening of the lending policy that occurred then was continued, to a lesser extent, until the third quarter of 2009. It was based on

49 It, however occurred also in most countries, including those in Euro zone (Spain, Austria, Greece, etc.).
50 About PLN 30 billion net were withdrawn from investment funds in the whole 2008, which together with the decline of stock exchange caused decrease in value of assets accumulated in funds from PLN 133,8 billion at the end of 2007 to PLN 73,7 billion at the end of 2008. [i.e. by 44.9%]. In fact investment funds were the group of Polish financial intermediaries that suffered most from the crisis.
increasing margins, increasing the level of required own contribution, increasing non-interest costs of loans, shortening the maximum lending period and tightening conditions regarding required collateral. At the same time, most banks ceased to grant foreign currency loans or subjected them to “prohibitive” margins which had the same effect. Banks also tightened the rules for calculating credit capacity, requirements regarding documents providing information on the income of a borrower and the rules of real estate valuation. Therefore, it may be said that all the elements of the lending policy were tightened, although the extent of such tightening was different for individual banks.

As a consequence, the reaction of banks to decreases of interest rates at the end of 2008 was insignificant. Banks decreased insignificantly interest rates on new loans for enterprises, they increased interest rates on new loans for households. At the same time for fear of losing deposits and thus liquidity, they made only slight corrections of interest rates on deposits for households. Thus, influence of classic instruments of monetary policy on bank policy was rather limited. Under such circumstances some special action had to be taken by both the central bank and the government. They are listed in the table 31

At the beginning of 2009, the aversion to risk continued to increase, which resulted in, among other things, further declines in share markets and the depreciation of currencies from emerging markets. At the end of February and the beginning of March, a fundamental change of atmosphere occurred, mainly due to actions taken by governments of particular countries and international organizations and slight improvements in the economic performance.

Table 31 Anti-crisis measures in Poland since 2008

<table>
<thead>
<tr>
<th>NBP “confidence package”</th>
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<tr>
<td>- In order to stabilise and improve situation on financial market the NBP developed a so-called “confidence package” which enabled banks to acquire assets in PLN for periods longer than one day, to acquire assets in foreign currencies and to expand the possibilities for banks to obtain liquidity in zloty by broadening the range of collateral in operations with the NBP.</td>
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<td>- To accomplish these goals The NBP planned to take the following steps:</td>
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<td>- providing open market operations in the form of repo transactions, with maturities of up to three months, introducing FX swaps, introducing FX deposits as collateral in refinancing credits,</td>
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<tr>
<td>- introducing modifications in the operational system of Lombard credits,</td>
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<tr>
<td>- increasing, if necessary, the frequency of open market operations to enable flexible response to changes in liquidity, and to stabilise the POLONIA rate around the reference rate.</td>
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At the same time, the National Bank of Poland reminded the banks of the possibility of redemption of NBP bills before their maturity.

Legislative activity of the Government of the Republic of Poland

In order to counteract the crisis:
- the Act on the Bank Guarantee Fund was amended, which increased guarantees for deposits to EUR 50 000;
- “Plan for stability and development” was developed, according to which the total amount of resources allocated for the support of economy in 2009-2010 could be PLN 91.3 billion. This amount constituted of the following: increase of guarantees and securities for loans from 3 months to 5 years of PLN 40 billion, creation of credit expansion for small and medium-sized enterprises through BGK of PLN 20 billion, advancement of investments co-financed from EU resources of PLN 16.8 billion, investments in renewable energy sources of PLN 1.5 billion, support of consumers’ demand through maintaining two PIT rates (PLN 8 billion) and VAT reform (PLN 2 billion);
- the Act on granting support for financial institutions by the State Treasury was passed, which determined the forms, conditions and procedures for granting support for financial institutions by the State Treasury, which was dedicated for undertakings aiming at the maintenance of payment liquidity, also in connection with the development of the National Bank credit expansion. The support was granted for national banks in the form of: guarantees of the State Treasury, treasury securities loans, treasury securities sale with deferred due rate, treasury securities sale with arranged instalments for payment, treasury securities sale through an offer for a certain financial institution.
- the bill on the change of Act on Bank for Domestic Economy was passed, submitted by the Minister of Finance. BGK was allowed to give securities or guarantees within national socio-economic programmes, especially within those concerning the support for small and medium-sized enterprises. Some of the areas of BGK activity were excluded from the public contracts procedure. This concerns, inter alia, the procedures connected with the service of State Treasury foreign debt. The exclusion from the disciplines of the Act on the public contracts law included also BGK services provided for the entities of public finance sector.
- the bill on recapitalisation of some financial institutions was passed, submitted by the Minister of Finance. According to the project, the State Treasury was allowed to give securities to the financial institutions, which are threatened with loss of liquidity. This concerned the injection of new capital into institutions, which were recommended the increase of equity funds in the rescue plan by PFSA. The bill included national banks and national insurance offices. In accordance with the bill, the performance of the guarantee contract would occur when shares, bonds or securities emitted by the financial institution are not taken up by current shareholders or third entities. The guarantee have been given by the Minister of Finance after receiving an opinion of the PFSA President and NBP Chief Executive Officer.

Source: NBP (2009)

As a result, some investors concluded that the most severe phase of the crisis was over and proceeded to buy overestimated Polish assets. This led to a very strong rebound in share markets, increase in prices of raw materials and the gradual strengthening of the zloty. Also, the improvement in functioning of the interbank market has been observed, which reflects the gradual rebuilding of trust among the participants of this market, and the decrease in risk premiums reflected in quoting CDS contracts.
The MPC continued to quickly mitigate the monetary policy with the aim to stimulate the weakening economy.\textsuperscript{51} As a result, the NBP interest rates were reduced by 150 bps and their levels were record low. The Monetary Policy Council also lowered the compulsory reserve ratio to 3.0\%, and the NBP continued its activities aiming at improving the situation on the interbank market and stimulating lending. To this aim, the NBP bonds related to the decrease in compulsory reserves were redeemed earlier and the range of instruments applied under the “Confidence Package” was expanded \textsuperscript{(Table 31).} The measures taken helped rebuild confidence in the market: the gap between rates in the interbank market and the reference rate of the central bank narrowed. However, the situation on the interbank market still was far from being normal, which was proved by, e.g. the lack of smooth functioning of operations with long dates of maturity.

Treasury bonds market reacted to the changes in monetary policy parameters only to a limited extent (mainly bonds with short maturity dates), being mainly under the influence of volatile investors’ mood, their risk assessments and expectations regarding future interest rates. Consequently, while the return on bonds with short maturity dates dropped (average return on 52-week treasury bills in the secondary market fell from 5.7\% in December 2008 to 4.2\% in December 2009), the return on bonds with long maturity dates increased (average return on 5-year bonds increased from 5.2\% to 5.8\%, and on 10-year bonds – from 5.6\% to 6.2\%). The spread between Polish and German 10-year bonds was maintained, or even increased.\textsuperscript{52} This unfavourable change may be explained by investors’ concerns about the state of Polish public finances, as well as the large issues of treasury bonds on a global scale, which made it necessary to pay higher costs for the placing of issues. Nevertheless, foreign investors returned gradually to the Polish treasury bond market.

\textsuperscript{51} It still however put lot of attention to inflation rate, believing that the probability for the inflation to fall below the inflation target in a medium period is greater than the probability that inflation will be higher than the target. Thus, some action aimed at boosting economic activity were possible.

\textsuperscript{52} It amounted 257 bps on average in December 2008, and 300 bps in December of the next year.
The situation in the PLN market in 2009 was characterized by two phases. During the first one (lasting until mid-February), the Polish currency depreciated, and this caused zloty to fall to the minimum level from the beginning of 2004. It was an aftermath of a very negative atmosphere in global financial markets and accumulation of negative outlooks for the CEE economies. But during the second phase, zloty stabilised and was gradually strengthened (particularly against USD), which was attributed to the general improvement in atmosphere in global markets. The strengthening of the Polish currency was additionally influenced by “media campaign”, the intervention sale of EU funds directly on the foreign exchange market, acquiring by Poland access to IMF flexible credit line (USD 20.6 billion), which was positively assessed by the investors. Moreover the Polish economy still indicated sustained growth. As a result, at the end of 2009, 1 EUR was 4.1018 (compared with 4.1724 at the end of 2008) and 1 USD was 2.8503 (2.9618), which meant that despite the high fluctuations during the year, the level of the exchange rate at the end of 2009 was close to the rate at end of 2008. Nonetheless, the value of zloty against euro was nearly 20% lower than at the peak of its appreciation (in mid-2008), and by about 25% against CHF and USD. However, despite a negative impact on the situation of some borrowers, companies and on the increase of the foreign debt, the depreciation mitigated, to a large degree the influence of the global recession adverse effects on the Polish economy. (MPC 2010).

It should be noted that despite a substantial change in atmosphere on the financial market, there was no significant inflow of resources to investment funds (on a net basis). A positive balance of payments and withdrawals in the whole year 2009 was only about PLN 3 billion. Therefore, the observed per annum increase in net assets of investment funds – from PLN 73.9 billion at the end of 2008 to 93.0 billion at the end of 2009 should be associated mainly with the increase in share prices.\(^\text{53}\) This reflected a change of preferences in the ways households invest financial surpluses. They started to prefer classical forms of investing money in a form of bank deposits,

\(^\text{53}\) The value of funds accumulated in investment funds increased from PLN 17.5 billion to PLN 27.1 billion.
as a result of negative experiences of the crisis. Thus, somewhat paradoxically, as it was already mentioned in the Section 2, banks in a way gained from the crisis.

However, a strong decline in economic activity, combined with the persistent uncertainty about future development of the situation and aversion to excessive risk-taking translated into decreased activity of the banking sector. Banks have reduced their expansion and concentrated on adjusting business models to the difficult external conditions. But despite the strong deterioration in financial performance, the situation of the banking sector in 2009 remained stable, and the capital position of banks was even strengthened. The main source of banks’ earnings were Treasury securities and loans for households. The latter had the highest rate of growth: in 2009 they increased by almost 12%, while loans for companies fell by 4.4%. As a result, at the end of 2009 the share of loans for households in the credit portfolio increased about 3.6 percentage points, to 65.7% [of previous year], and in case of loans for companies, it decreased to 33.9% [from 37.5%].54 (Polish Financial Supervision Authority, 2010b).

Banks reduced interest rates in 2009. The average interest rate on deposits in December 2009 was 3.2% against 6.0% in December 2008 and the average interest rate on newly granted loans decreased from 13.6% to 12.5%. As a result, the spread between lending and deposit interest rates increased from 5.6% to 6.5%. Such increase positively influenced the growth of interest income in subsequent periods. Changes in the deposit and credit policy of banks were in line, as far as the direction is concerned, with the changes of the monetary policy parameters. However, the scale of changes differed – interest on deposits was reduced more than the interest on loans.

Lower interest rates were however accompanied by steady tightening of credit policy. It consisted in increasing margins, non-interest costs of loans, limiting the availability of simplified procedures of credit capacity analysis (including documenting a borrower’s income with an income declaration) and tightening collateral procedures. The main reasons for tightening the lending policy were

54 Lending to non-profit institutions was only peripheral to the operations of banks, accounting at the end of 2009 for the mere 0.4% of the credit portfolio.
negative prospects of macroeconomic development and declined quality of consumer loan portfolio. It did not constitute an obstacle for households: the value of consumption loans increased by 13.2% (from PLN 136.5 billion at the end of 2008 to PLN 154.5 billion at the end of 2009).\footnote{Among those loans highest growth characterized by debt on credit cards (by 18.3%). The growth was associated with the fast development of these products and their strong promotion in previous periods. On the other hand, a sharp increase in non-performing loans (by nearly PLN 1 billion) indicated that some borrowers might use credit cards to pay other obligations.}

On the other hand, the dynamics of enterprise loans was low. It was caused not only by the tightened conditions of lending, but also by the decreased demand for loans from companies, which, in view of the decline in demand (domestic and foreign), were limiting production and verifying investment plans. Slowdown of lending had an adverse influence on the economic situation. The decrease in the growth of lending to corporates and households (mainly mortgage loans) contributed to a fall in investment. The deterioration in enterprises’ financial situation at the end of 2008 and the beginning of 2009 resulted in a significant slowdown of wage growth, a slight increase of unemployment and a fall in companies' investments. The growth rate of foreign direct investment in Poland also decreased. At the same time, slower growth rate of households’ disposable income had an impact on the reduction of consumption growth rate. (MPC 2010).

Thus, in 2009, the rate of economic growth slowed down drastically, the labour market was significantly weakened and the situation in the public finance sector deteriorated. The reasons were similar to the ones from the previous year: the recession in the economies of Poland’s main trading partners and the uncertainty about prospects for global and domestic economic growth. Yet, it still was the positive rate of growth and, despite the slowdown, the condition of the Polish economy was better than the economies of other EU countries.\footnote{In fact, Poland turned out to be the only EU country which managed to maintain a positive growth rate in spite of the crisis, while the remaining countries slipped into recession.}

After the slowdown that occurred in late 2008 and 2009, a recovery has been visible in the global economy with the strength of this recovery differing between particular regions and countries. Better situation in Poland’s main economic
partners has been conducive to an increase in the rate of growth of the Polish econ-
economy. The rate of growth in GNP in 2010 amounted to 3.8% and was among the
highest in the EU. What important, it accelerated from quarter to quarter (3.0%;
3.5%; 4.2%; 4.5%). The improvement in this area was influenced by strengthening in
domestic demand (by 4.3%), resulting primarily from growth in individual
consumption (of 3.2%) supplemented by growth in public consumption and an
increase in stock-building.57

Despite the real revival of the economy it remained still under strong pressure
from the external environment – in particular from uncertainty as to prospective
developments in Poland’s major trading partners and from the significant volatility of
moods in financial markets. Another serious problem was in this period rapidly
growing public sector debt. State public debt increased from about PLN 669.9 billion
at the end of 2009 to PLN 748.5 billion at the end of 2010. As a consequence public
debt rose from 50.9% of GDP to 55.1%. This meant that the first prudential threshold
provided for in the Act on Public Finances has been crossed.

The situation in the Polish financial market continued to be characterised by
increased volatility but was more stable than in 2009. The greatest influence on
moods and on the attitudes of investors was exerted by the flow of macroeconomic
data from the US, from the EU and from China. Such psychological factors
contributed to continued increased volatility in the zloty’s exchange rate. At the end
December 2009 and at the end of individual quarters of 2010, the average NBP
PLN/EUR rate was 4.1082; 3.8622; 4.1458; 3.9870 and 3.9603, the average NBP
PLN/CHF rate 2.7661; 2.7000; 3.1345; 2.9955 and 3.1639, and the average NBP
PLN/USD rate 2.8503; 2.8720; 3.3946; 2.9250 and 2.9641. (National Bank of Poland
2011)

In 2010 monetary policy was rather stable. The MPC left central bank rates
unchanged during all 2010, but in October it raised the compulsory reserve ratio by
half a percentage point from 3.0% to 3.5% (returning to the level before 30 June
2009). In spite of unchanged central rates, there was reduction of yields on Treasury

57 Important factor were broad investments connected with organization of Euro 2012 continued in
subsequent years.
bonds (the average secondary market yield on 5-year Treasury bonds fell from 5.8% to 5.5% and that on 10-year bonds from 6.2% to 6.0%). From the fourth quarter of 2010 a gradual increase in Treasury bond yields and in interbank interest rates was perceptible. It was related to investors’ expectations of tightening of monetary policy by the MPC, that actually took place in January 2011.58

Surprisingly, foreign investors’ involvement in purchases of Polish Treasury securities increased greatly (from PLN 81.8 billion at the end of 2009 to PLN 128.3 billion at the end of 2010). It “financed” almost all of the increase in their issuance.59 This was of course seen as positive phenomenon by the government, but on the other hand – it gave rise to an increase in systemic risk (given the current scale of the market withdrawal of a substantial part of these funds would certainly cause a rise in yields and weakening of the zloty).

There were also the reduction of interest rates in the interbank market (the average rate of 3M WIBOR fell from 4.1% in December 2009 to 3.8% in December 2010). In 2010 banks made a slight adjustment to their interest rates policy. On the basis of changes in the rates applying to new agreements one might state that the banks did not alter in principle what they offered depositors and kept the interest rate paid on deposits at a level only a little above 3%. On the other hand there was an appreciable reduction in the interest rate applied to newly arranged loans from about 9-10% at the end of 2009 go about 8% at the end of 2010, which reflected a reduction in margin, being consequence of growing competition in the sector.

What was crucial in determining banks’ results in this regard was, however, the interest rates applied during the year to all agreements in place. In relation to this it can be asserted that average interest rate applied to all deposits during the whole of 2010 was about 4.1% and was significantly lower than in 2009, when it was 5.1%. In turn the average interest rate applied to all loans during the whole of 2010 was about 8.4%, as against 8.5% in 2009. This contributed to the strong growth in

58 The MPC begun a gradual tightening of monetary policy in 2011. The reference rate was raised to 3.75% in January and to 4.0% in April. To such move led pronounced by the MPC increase in inflationary pressure.
59 The quantity of Treasury securities in the hands of domestic entities fell from PLN 380.5 billion to PLN 378.7 billion
profits on deposit-taking and lending activity by the banking sector that was seen in 2010 (see Section 5).

Despite the improvement in the functioning of financial markets in 2010 together with the global economy’s entering a growth path, a heightened level of risk continued to affect the business of the banking sector. Altogether with the substantial worsening in the quality of the loan portfolio and the uncertainty as to development of the macroeconomic situation seen in 2009-2010, it gave rise to tightening of lending policy in some areas (and above all in consumer loans, so popular in the previous year). Together with reduced demand for loans from certain entities (particularly some enterprises) this led to a further slowdown in new lending. The main areas of development were housing lending, loans to individual entrepreneurs and loans to the budget sector. On the other hand banks continuously increased their portfolio of NBP bills and Treasury bonds, which promised high liquidity and a safe income. At the same time banks increased their deposit base. (Polish Financial Supervision Authority, 2011).

The functioning of the interbank market in Poland gradually improved, but this market still continued to be less efficient than before the crisis. It manifested, among others, by low reciprocal credit limits and the reluctance of banks to accept risks. As a result banks managed liquidity primarily by using overnight transactions, the share of which in total interbank turnover exceeded 90% while before 2008 it was about 80% of turnover.

In 2011 the economic growth rate remained moderate. GDP grew by 4.3%. But, at the same time the unemployment rate remained relatively stable. strong inflationary pressure was maintained, and the indicators of the overall outlook for industry and construction and of consumer confidence were low or even negative. Condition of the state budget improved (the deficit amounted to PLN 25.1 nearly half of the previous year. On the other hands, there still were concerns about the rapidly-growing public finance sector debt (debt of the general government grew from PLN 747.9 billion at the end of 2010 to PLN 815.3 billion at the end of 2011).
Nevertheless situation of Poland still was relatively good, compared with most countries of the EU. This was evident in, among others, the highest economic growth rate in 2007-2011 out of all EU countries. The prospects for growth, however, deteriorated. This was a result of a global economic downturn, growing debt crisis in some eurozone countries as well as the tightening of the fiscal policy, necessary to back Poland from the path leading to an excessive deficit in 2012-2013.60

In the first half of the 2011, the situation on global financial markets was relatively stable. Despite volatility and uncertainty, this period marked the time of local all-time highs on equity and commodity markets, and reported a strengthening of CEEs currencies. But at the turn of the first and second half of 2011 the global financial market confidence deteriorated significantly. This resulted from many factors: the growing problems in eurozone countries’ public finance, delays in the process of enactment by the US Congress of the higher debt limits for the USA, concerns about the financial standing of certain European banking groups together with indications of an economic deceleration in the EU and the USA, and a loss of confidence among enterprises and customers. The process was intensified by a number of reductions to sovereign and financial institution ratings.61

A build-up of these negative phenomena resulted in very large markdowns on equity and commodity markets, selling of foreign currencies from emerging markets, reduction or loss of liquidity on the market for medium- or long-term unhedged financing, and increased costs of financing and CDS rates. Also the situation on the money market became more severe as a result of reduced exposure to Europe by US money market funds, which forced European banks to look for alternative sources of financing. Furthermore, confidence among banks again started to decline and banks’ deposits in ECB grew rapidly. At the same time the downturn of outlook on equity

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60 Actually, looking at the external data, the procedure should have been already started. But, as it was mentioned, the Ministry of Finance made number of activities, which blurred actual level of debt.
61 As an important factor contributing to the crisis, was often perceived media coverage, which, perhaps excessively, emphasised the issue of actual or potential threats. It affected the attitudes of financial market participants, entrepreneurs and consumers. As a result, a number of entities chose to reduce their investments and spending, and financial markets experienced increasing pressure which deepened the crisis (e.g. some entities reduced their exposures to institutions subject to negative media speculation).
markets reduced the possibility of obtaining funding. The liquidity situation improved slightly after the major central banks intervened by agreeing to provide the necessary liquidity.\textsuperscript{62}

Those developments were not without impact on the Polish economy. Moreover, the Monetary Policy Council, in response to the rapid growth of inflationary pressure, continued to tighten monetary policy. In January, April, May and June 2011 the reference rate was raised by 25 bps respectively and amounted to 4.5% at the end of 2011. All these steps caused increased interest rates on the interbank market (average WIBOR 3M rate increased from 3.8% in December 2010 to 4.9% in December 2011).\textsuperscript{63} The interbank market still was not fully effective, as reciprocal credit limits were low and banks were very reluctant to take risk and lend. As a result, in managing liquidity, banks used primarily overnight transactions, and the proportion of longer-term transactions was small.

Interest rate on deposits and loans also increased. Interest rates on new deposit agreements grew from about 3.1% in December 2010 to about 4.4% in December 2011, while interest rates on loan agreements grew within this period from circa 7.5% to almost 8%.

Still higher borrowing needs of the government resulted, with other factors, in increased profitability of treasury securities at. Thus, involvement of foreign investors’ involvement in purchases of Polish Treasury securities issued on the domestic market grew. At the end of 2011 those investors held nearly 30% of the securities issued on the domestic market. The increased involvement of foreign investors increased systemic risk associated with the possibility of rapid withdrawal of a portion of capital. It could be one of the factors contributing to a weaker zloty. After relative stability in the first half of 2011, in the third quarter of 2011, the Polish currency declined against the major currencies. The situation stabilised at the end of

\textsuperscript{62} In particular the ECB engaged in the so called LTRO program, offering circa EUR 500 billion in low interest long term loans to banks.

\textsuperscript{63} At the same time, in the first half of 2011 quotes for FRA rates indicated expectations of a further rise in interest rates, whereas since August there has been a decrease, which should be associated with lowered expectations of the tightening of the monetary policy or even expectations of its easing, that actually occurred in 2012.
the year due to a slight improvement to investor confidence, BGK and NBP interventions and the SNB setting a minimum exchange rate for the CHF against the EUR. However the zloty remained weak against the major currencies.64

The deterioration in confidence of the financial markets together with forthcoming decrease in the growth rate of the Polish economy and deterioration of the job market situation, carried a number of potential threats for banks. Despite a relatively good situation of them (see previous sections), an increase in operational risk occurred. Moreover non-performing loans started to grow significantly. Therefore, banks carried on efforts aimed at ensuring an appropriate liquidity buffer, stable sources of funding and strengthen their capital position. One of the results of such activity was, however, decreasing dynamics of loans to some groups of clients. As a result internal demand also showed some marks of decrease.

Summarizing considerations in this section, it must be noticed that Poland in principle avoided heavy losses brought by global financial crisis. Some problems occurred and the growth rate was lower, but still the Polish economy functioned well, especially when compared to other European countries. No financial institutions were bankrupted, there were no drastic tensions on the financial market. There are pointed many, intertwined to a large degree, reasons, of this relatively good performance.

First, Polish economy has a relatively large internal market and is less open in comparison with other economies in the region. It is also characterised by a relatively high level of diversification (among other things, lack of clear domination of one sector and no large enterprises/conglomerates which decide about the development of the whole economy) and by a high degree of flexibility among domestic firms that helped them to adapt to difficult external conditions.

Second, high investment outlays made by the public sector played an important stabilizing role. These replaced the reduction of investment by the private sector. The reduction of personal income tax (PIT) rates and high indexation of pension benefits, and the earlier lowering of the pension contribution acted in a

64 At the end of 2011 NBP average exchange rates for 1 EUR, 1 CHF and 1 USD against the zloty were: 4.4168; 3.6333; 3.4174 respectively as compared to: 3.9603; 3.1639; 2.9641 at the end of 2010.
similar manner. These actions, similar to the stimulus packages implemented in other countries, have helped to sustain internal demand.

Third, the floating exchange rate helped to absorb the external shocks – a decline in orders was largely offset by higher proceeds resulting from the weakening of zloty, and growth in orders due to the increase in their competitiveness. Thus the exchange rate acted as a “buffer”, protecting the economy from decrease of demand. At the same time, the depreciation of zloty did not cause significant inflationary tension.

Fourth, Poland is, as it was already emphasized, characterized by a low level of “banking” (relatively low development of the financial market) and the rather local character of the banking system. As a result, the banking sector did not suffer large losses in foreign markets that require involvement of public funds. At the same time, parent companies did not withdraw funding and household deposits experienced strong growth. Moreover, since the importance of financing enterprises by the banking sector or with funds raised on the capital market is lower than in other countries, limiting credit activity by banks and the downturn at the stock exchange did not have such negative impact as in many other countries. In other words, the channel transferring the crisis phenomena from the financial sector to the economy turned out to be narrower in Poland.

Fifth, strictly connected with the previous one, reasons is generally lower scale of financialisation in the Polish economy. There hardly exists on the domestic market sophisticated financial instruments, securities etc. Investment banks and large, global investment funds also do not function within Poland. Demand for financial services, formulated by the households and enterprises is limited rather to traditional loans, accounts and settlements. Thus, somewhat paradoxically, this relative underdevelopment turned out to be benefit for the Polish economy.
17. Monetary policy in Poland after 1989 – main issues

Transformation of the Polish economy has created a special and unique challenge for the policymakers, responsible for the individual areas of economic policy in Poland. Monetary disorder, urgent necessity to stabilize and rebuilt monetary regime, as well as the very construction and assumptions of the transformation program in Poland made the monetary policy (and strictly connected exchange rate policy) of special importance after 1989. The other main part of macroeconomic policy – fiscal policy – was relatively less exploited. Moreover, it was rather perceived as less important and inefficient. It resulted from both ideological and factual premises. The former were mainly the aftermath of conservative and (neo)liberal orientation of subsequent cabinets (even those formed by the left). The latter ones included, among others high level of indebtedness, its low transparency and credibility, high share of predetermined expenditures and, after joining the EU, necessity to fulfil the Maastricht criteria in unfavourable environment of global financial (and also debt) crisis. Thus fiscal policy, considered usually as too expansionary, was treated rather as an obstacle to price stability and overall economic performance. (Bratkowski 1995, Dąbrowski 1997, Marszatek 2006).

Under such circumstances, the main role in the macroeconomic policy has been playing by the NBP. Until 1989, as was already mentioned, it acted as a “monobank”. It was an issuer of money, central credit and settlement institution as well as central foreign exchange institution. (Knakiewicz 1997). In fact, the NBP became “typical” central bank in January of 1990, thanks to the beginning of the transformation of the Polish economy into the market one. (See Gronkiewicz-Waltz 1992, Knakiewicz 1997, Rutkowski 1997). Since then, the NBP has been aimed at becoming an independent institution. It was argued in the literature that after 1989 the Polish central bank had been consequently acting in order to obtain greater independence. (Baka 1990, Knakiewicz 1997, Wojtyna 1996, Ugolini 1996). Within a

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65 With time, the burden of the debt was less severe due to reduction, under agreements negotiated with the London and Paris Clubs [see Wijnbergen and Budina 2001]. However is started to increase again, even before the onset of the global financial crisis and even in the periods of high economic growth [e.g. 2006-2008].
dozen or so years, it has become fully independent a central bank, conducting mone-
monetary policy according to contemporary standards and making use of modern
(mainly mainstream) economic theories and experience of development economies.
It also used typical, market instruments as open market operations, reserve
requirements and credit-deposit operations.

Such a situation, however, had been achieved gradually. The Act on the NBP of
the January 31, 1989, legally binding until the end of 1997, decreased the degree of
subordination to the Council of Ministers and the Minister of Finance (Gronkiewicz-
Waltz 1992). The government stopped formulating monetary policy guidelines and so-
called credit plan. It kept, however, statutory mandate to fix principles and set the
level of the zloty exchange rate. The principles of the exchange rate setting against
other currencies were determined by „the Council of Ministers, at the request of the
NBP President, agreed with the Minister of Finance and the Minister of Cooperation
with Foreign Countries” (The Act on the NBP of 1989, art. 39). The NBP could only
inspire decisions-making process, taking into account the existing exchange rate
regime. Still, the final decision was always taken by the government. (Polański

The Act of January 31, 1989, left to the Parliament very important competence
within the area of the monetary policy. Although this act granted the NBP the
initiative in formulating the monetary policy, formal rights in this field were still in
the hands of the parliament. The NBP had just prepared projects of monetary policy
guidelines, which next were adopted by the parliament in the form of resolution.
What is worth noting is the government had a decisive impact on the guidelines. The
Minister of Finance played the main role. In order to increase budgetary incomes,
within the years 1990-1997 he usually underestimated the inflation rate in the Budget
Laws. Thus, the NBP was forced to adopt unrealistic inflation targets. (Polański
1998a, Szpunar 2000). Still, the responsibility for achieving the targets rested on this
institution. Thus, the central bank published its own estimates of inflation, to
maintain credibility in the event of, actually inevitable, overshooting inflation target.
Such activity, however, triggered off protests from the fiscal side. The NBP was accused of undermining, in turn, credibility of the government.

The Act of 1989 did not include clear rules for recalling the NBP President. Also, any limits of financing the government activity by the central bank were not anticipated. However, some quantitative limits of purchasing treasury bills on the primary market were enforced just in the amendment of the act, passed in the same year. According to this amendment, the value of purchased treasury bills could not exceed 2% of planned budget expenditures. (The Act of 1989, on the Amendments to the Act on the NBP). Unfortunately, such restriction was not respected.\(^{66}\) Thus, the NBP was not fully independent in this period. According to Gronkiewicz-Waltz (1992), the Parliament, within the confines of binding bills, decided every year on central bank independence.

The situation improved under the next amendment to the Act on the NBP, which was put into practice in 1992. It introduced, among other things, a six-year term of the NBP President and limited cases in which such person could be recalled only to those not connected with the conduct of monetary policy. (The Act of May 22, 1992, on the change of the Banking Law and on the change of the Act on the National Bank of Poland)\(^{67}\). However, the problems with fixing targets and deficit financing remained unresolved until 1997. This shortcoming was very often stressed in the literature. Nevertheless, many authors pointed at systematic increase in the independence of the Polish central bank, underlining gradual transformation from a formal independence to the actual one. (Pietrzak1999, Strzelec 1994, Ugolini 1996, Wojtyna1996).

New constitutional and legal arrangements on the monetary policy were adopted in 1997 and enforced on January 1st, 1998, strengthening the independence

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\(^{66}\)Actually, the NBP was forced to finance the budget deficit. Moreover, it was characteristic that the government treated the legal limit as applying to the balance at the end of the year. Such interpretation enabled much larger borrowing from the NBP during a given year.

\(^{67}\)In the opinion of Kokoszczyński (2004), such regulation took actually abilities to influence monetary policy away from the Parliament – although the regulation, according to which the parliament appointed and recalled the President of the NBP, formally still was in force. Even recognizing that monetary policy had been mistaken and rejecting by the parliament annual report from the monetary policy implementation did not entail any consequences for the NBP and its President.
of the NBP. These acts created institutional conditions for a more effective monetary policy. Understanding and precise (quantitative) formulation of the target however changed. It also expressed precisely in the new Act on the NBP its main goal. Namely, it was stated that “the basic objective of the central bank shall consist in maintaining price stability, supporting at the same time the economic policy of the government, insofar as this does not constraint the basic objective of the NBP”. (The Act on the NBP of 1997, art. 3). Such statement has been consistent with recommendation of the then European Monetary Institute.

On April, 7, 1998, the new Constitution of the Republic of Poland was adopted. It also strengthened significantly the independence of the NBP. Pursuant to the article 227, the central bank was granted exclusive right to issue currency and to formulate and implement monetary policy.

Then, since 1998 monetary and fiscal policies in Poland have been conducted by distinct and independent authorities. Such relations, in a sense, determined many problems, which both policies had made to each other. New arrangements have escalated conflicts between the central bank and the government. It has demonstrated weakness of coordination mechanisms. Situation has been tense, despite of removing responsibility for the government economic policy from the Ministry of Finance to the Ministry of Economy, Labour and Social Policy in 2003. Conflicts have resulted in an inappropriate policy mix, i.e. restrictive (tight) monetary and loose fiscal policy, to the detriment of investments and economic growth (OECD, 2004). What important, such combination of monetary and fiscal policy has been suboptimal for both the policymakers. They have been caught in a classical “prisoner dilemma” (Nordhaus, 1994).

68 However, some problems have not been solved yet. In particular, as Kowalski (1997) underlines, the act lacked regulations, which would specify methods of resolving potential conflicts with the government. It is also worth of noticing that the discussed act has not been fully adjusted to the European law. Namely, the NBP was given full personal and, to a large degree, functional independence. Some shortcomings were observed in the area of institutional independence. Necessary has been judged auditing financial reports of the NBP by professional auditors instead of commission, appointed by the Council of Ministers at the request of the Minister of Finance. Questionable remains also possibility of borrowing by the NBP to the Bank Guarantee Fund. (Convergence Report 2004).

69 Conflicts occurred also under the „old” arrangements. Probably the most famous example is the struggle over a desirable level of interest rates in 1994. For the “central bank” point of view see Knakiewicz (1994), and for the “government’s” – Kotodko (1995).
First and foremost, disagreements have resulted from different objectives of the monetary and fiscal authorities. The NBP has been criticised for a “dogmatic” focusing its attention on price stability, what, according to the fiscal authorities, created excessive costs of disinflation, mainly in terms of slower economic growth. The NBP replied for the critique, arguing that the lack of fiscal consolidation and actual fiscal policy different than the declared one (mostly less disciplined) have blurred situation and made decision process difficult, thus increasing uncertainty and probability of mistakes. Under such circumstances, according the NBP, high level of official interest rates was inevitable. [MPC 1999, Narodowy Bank Polski 1998].

The Act of 1997 has also extended entitlements of the NBP to pursuing exchange rate policy. The obligation to consult issues of the exchange rate with the Minister of Finance, imposed on the central bank by the Act on the NBP of 1989, was removed. The article 24 of the Act of 1997, however, still preserved the right of the Council of Ministers to establish frameworks of exchange rate policy. Thus, the division of competence in the field of exchange rate still has not been transparent.

It can be argued that during all the periods considered the government decided about the character of the exchange rate regime, whereas the NBP executed government’s guidelines. The exchange rate regime was used as an instrument of the overall economic policy. Taking into account that the exchange rate appeared to be also important instrument of the monetary policy, lack of consistency between the policymakers could have been expected. Targets, which had been intended to achieve by the means of the exchange rate, also varied. What should be stressed that they were often different from those of monetary policy.

Regardless of the controversies in the field of coordination between individual policies, it must be admitted that the Polish central banked had to operate in a difficult environment. Therefore it has been forced to make incessant adjustments to changeable economic and institutional conditions and to search for new, often very unorthodox actions and tools. Indisputably then, frequent changes of targets, strate-

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70 It occurred very clearly in years 2000-2001, when Leszek Balcerowicz, who became then the President of the NBP started policy of “cooling the economy that had been, according to him, “overheated”.
71 To this inconsistency, attention has been paid, among other, by Janc (2004) and Kowalski (1997).
gies and instruments of the Polish central bank have been indispensable. In principle in pursuit of monetary and exchange rate policy by the NBP may be distinguished three periods: (1) implementation of an “eclectic strategy” (the years 1990-1997); (2) conducting (direct) inflation targeting strategy (IT) with formally fixed exchange rate (1998-2000) and (3) IT strategy with floating exchange rate (since April 2001).

Since 1990, both monetary and exchange rate policies, have been subjected to frequent and striking transformations. Aside from fundamental changes, as switching to the new exchange rate regime or setting a brand new main target of monetary policy, strategies and specific operational arrangements have also been reformulated. The most important changes in field of both of these policies are presented synthetically in the Tables 32 and 33.

Monetary policy in 1990 was not an autonomous domain of the economic policy, but just a part of the broader stabilization program. An integral element of the program was adoption of a fixed nominal exchange rate. The fixed zloty exchange rate against the US dollar became a nominal anchor, intended to restrain inflation and reduce inflationary expectations. The relation of Polish zloty to US dollar was reduced to the level almost threefold lower, than the one resulting from the comparison of purchasing power of the both currencies in the end of 1989. While setting on January 1, 1990 the central “anchored” parity rate at the level of 9500 zlotys for one dollar, the policymakers stressed that a specific buffer had been created. The aim of this purpose-built buffer was to cover an expected rise in domestic prices.

Nevertheless, the fixed exchange rate was a source of serious problems with controlling money supply. Namely, in legal circumstances, applied then to the NBP, it was not able to control the increase of foreign exchange reserves and what follows – increase of money supply. But this very variable was treated then as an intermediate target of the monetary policy. Thus, in order to control money supply, limits of net credit to the government sector, net assets of the banking system and net foreign exchange reserves were brought into effect.72

72 Such limits were introduced with cooperation with the IMF and were treated as quarterly executive criteria of the stabilization program.
These limitations and other administrative instruments, applied to overcome problems with money supply, made at the beginning of the 1990s conducting of coherent monetary policy strategy impossible. However, as Kokoszczyński (2004) stressed, the then strategy already contained some elements of monetary targeting. Nevertheless, officially, the rank of intermediate target money supply gained just in another few years.

As results from the table 32, as early as 1991 the NBP’s strategy was to reduce inflation through control of money supply, treated as the intermediate target. In the subsequent years, the strategy was completed by including an immediate target. In this way, the classical triad of targets was established, initially informally and, in the years 1996-1997 – already officially73 (see Table 33). At the same time, along with the development of the money market, it became possible to extend range of available monetary policy instruments. Similarly to central banks in the countries of mature market economy, the NBP has started to make use of indirect, market instruments, mainly open market operations.74

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73 Elements of this strategy had already functioned. But just in The Monetary Policy Guidelines for the Year 1992 the statement had been expressed, according to which disinflation through control of money supply was recognized as the official strategy.
74 Causes and consequences of such attitude are described in Kiedrowska (2005).
Table 32. Changes of Polish exchange rate regime within the years 1990-2000

<table>
<thead>
<tr>
<th>Period of</th>
<th>Type of the regime</th>
<th>Main features of the regime</th>
</tr>
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<tbody>
<tr>
<td>1.1.1990-13.10.1991</td>
<td>Fixed exchange rate</td>
<td>Since January 1, 1990, till May 16, 1991 the fixed zloty exchange rate against the US dollar was in force. There was the official parity of the Polish zloty, called also “anchored” exchange rate. According to it, 1 USD = 9500 zł. May 17, 1991 – the zloty exchange rate was reduced by 16.8 %, thus 1 USD = 11100 złotys. May 20, 1991 – a switch of the peg to the collective unit, value of which was determined by the basket of five currencies. Basket 45 % USD dollar, 35 % DM, 10 % GBP, and 5 % both FRF and CHF</td>
</tr>
<tr>
<td>14.10.1991-15.10.1995</td>
<td>Pegged exchange rate, adjusted in dependence with changes of the main macroeconomic factors (crawling peg)</td>
<td>October 14, 1991 – introduction of peg with preannounced crawling devaluation at a monthly rate of 1.8 %. The zloty exchange rate was daily reduced by specific amount, equal to devaluation rate. Moreover, permissible deviations of the zloty exchange rate on the interbank market against the parity were established, in form of fluctuation band, amounting to ± 0.5 %. February 26, 1992 – 10.7 % devaluation of the zloty October 1, 1992 – the fluctuation band was widened to ± 1 %. August 27, 1993 – the rate of crawling peg reduced to 1.6 %. The zloty devaluated by 7.4 %. September 13, 1994 – the rate of crawling devaluation reduced to 1.5 %. November 30, 1994 – the rate of crawling devaluation reduced to 1.4 %. February 6, 1995 – the rate of crawling devaluation reduced to 1.2 %. March 6, 1995 – the fluctuation band was widened to ± 2 %.</td>
</tr>
<tr>
<td>16.5.1995-11.4.2000</td>
<td>Pegged exchange rate, adjusted within horizontal bands (crawling band)</td>
<td>May, 16, 1995 – the zloty exchange rate was partially floated. The central parity rate stopped serving as the official exchange rate. It became just the basis for determining the range of deviations of the zloty exchange rate in the interbank market to ± 7 %. The principles of crawling devaluation were still in force. The banks were allowed to setting on their own the exchange rates of buying and selling foreign exchange. December 22, 1995 – the zloty exchange rate was revaluated by 6 %. January 8, 1996 – the rate of crawling devaluation was reduced to 1.0 %. February 26, 1998 – the rate of crawling devaluation was reduced to 0.8 %. The fluctuation band was widened to ± 10 %. July 17, 1998 – the rate of crawling devaluation was reduced to 0.65 %. September 10, 1998 – the rate of crawling devaluation was reduced to 0.5 %. October 29, 1998 – the fluctuation band was widened to ± 12.5%. January 1, 1999 – the new currency basket was introduced; basket 55 % euro 45 % USD. March 25, 1999 – the rate of crawling devaluation was reduced to 0.3 %. The fluctuation band was widened to ± 15 %.</td>
</tr>
<tr>
<td>Since 12.4.2000</td>
<td>Independently floating</td>
<td>April 12, 2000 – the zloty exchange rate was fully floated. Since then, it is determined only by demand and supply on the foreign exchange market.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Primary target of monetary policy</th>
<th>Detailed target of monetary policy</th>
<th>Monetary policy strategy</th>
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</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Since December 28, 1989 formally monetary targeting; actually – atypical strategy, being a part of the stabilization.</td>
</tr>
<tr>
<td></td>
<td><strong>1991</strong></td>
<td>CPI [XII/XII] - 32.0%; increase of M2 aggregate -8.5 billion</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Since January 1, 1991 monetary targeting.</td>
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<tr>
<td></td>
<td><strong>1992</strong></td>
<td>CPI [XII/XII] – 36.9%; increase of M2 aggregate – 12.7 billion</td>
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<td></td>
<td><strong>1993</strong></td>
<td>CPI [XII/XII] – 32.2%; increase of M2 aggregate – 15 billion</td>
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<td></td>
<td><strong>1994</strong></td>
<td>CPI [XII/XII] - 23.0%; increase of M2 aggregate – 15.5-16.9 billion</td>
</tr>
<tr>
<td></td>
<td><strong>1995</strong></td>
<td>CPI [XII/XII] -17.0%; increase of M2 aggregate – 17.1 billion</td>
</tr>
<tr>
<td></td>
<td><strong>1996</strong></td>
<td>CPI [XII/XII] - 17.0%; increase of M2 aggregate – 23 billion increase of the so-called reserve money – 7 billion</td>
</tr>
<tr>
<td></td>
<td><strong>1997</strong></td>
<td>Since January 1, 1997 – maintaining price stability, supporting at the same time the economic policy of the government, insofar as this does not contradict the basic objective of the NBP</td>
</tr>
<tr>
<td></td>
<td><strong>1998</strong></td>
<td>CPI [XII/XII] 9.5%</td>
</tr>
<tr>
<td></td>
<td><strong>1999</strong></td>
<td>6.6-7.8% CPI[XII/XII]</td>
</tr>
<tr>
<td></td>
<td><strong>2000</strong></td>
<td>5.4-6.8%* CPI[XII/XII]</td>
</tr>
<tr>
<td></td>
<td><strong>2001</strong></td>
<td>6.0-8.0%, CPI [XII/XII]</td>
</tr>
<tr>
<td></td>
<td><strong>2002</strong></td>
<td>3.0% +/- 1 percentage point, CPI[XII/XII]</td>
</tr>
<tr>
<td></td>
<td><strong>2003</strong></td>
<td>3.0+/- 1 percentage point, CPI[XII/XII]</td>
</tr>
<tr>
<td></td>
<td><strong>2004</strong></td>
<td>From January 1, 2004 CPI (m/m) 2.5% +/- 1 percentage point</td>
</tr>
<tr>
<td></td>
<td><strong>2005</strong></td>
<td>Since January 1, 2004 direct inflation targeting with continuous target</td>
</tr>
</tbody>
</table>

* Formally, this strategy was adopted on January 1, 1999, but its pursuing has just started in 1998.
* Such level of target was adopted in March, at the beginning of the year it amounted 8-8.5%.
* Such level of target was adopted in June, at the beginning of the year it amounted 5% +/- 1 percentage point.

Source: authors’ work on the basis: The Act on the National Bank of Poland (1989); The Act on the National Bank of Poland (1997); MPC (1998) MPC (2003b), Infla-
tion Reports from the years 1996-2004; Reports on Monetary Policy Implementations from the years 1992-2006.

In spite of the constant improvement of strategy and increase in efficiency of tools, achieving of planned inflation targets caused many troubles.\textsuperscript{75} The disinflation process was disrupted and entailed high costs. Moreover, the NBP did not hit planned values of targets {see Table 34}.\textsuperscript{76} There were many reasons that stood behind these negative phenomena.\textsuperscript{77} They were additionally heightened by the exchange rate regime, which contributed to massive foreign capital inflows and – along with surplus of current account in the balance of payments – to increase of foreign exchange reserves. (Kokoszyński 2004, Polański 1999).

Table 34. Fulfilment of the monetary policy targets within the years 1991-1998

<table>
<thead>
<tr>
<th>Year</th>
<th>Actual inflation (CPI, XII/XII)</th>
<th>Planned inflation</th>
<th>Deviation from the target (percentage points)</th>
<th>Deviation from the target (per cent of the target)</th>
<th>Actual value (billion PLN)</th>
<th>Planned value (billion PLN)</th>
<th>Deviation from the target (billion PLN)</th>
<th>Deviation from the target (per cent of the target)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>60.4</td>
<td>32.0</td>
<td>28.4</td>
<td>88.8</td>
<td>9.0</td>
<td>8.5</td>
<td>0.5</td>
<td>5.9</td>
</tr>
<tr>
<td>1992</td>
<td>44.3</td>
<td>36.9</td>
<td>7.4</td>
<td>20.1</td>
<td>15.0</td>
<td>12.7</td>
<td>2.3</td>
<td>18.1</td>
</tr>
<tr>
<td>1993</td>
<td>37.6</td>
<td>32.2</td>
<td>5.4</td>
<td>16.8</td>
<td>14.8</td>
<td>15.0</td>
<td>-0.5</td>
<td>-1.3</td>
</tr>
<tr>
<td>1994</td>
<td>29.5</td>
<td>23.0</td>
<td>6.5</td>
<td>28.3</td>
<td>21.4</td>
<td>-1.4</td>
<td>22.8</td>
<td>16.6</td>
</tr>
<tr>
<td>1995</td>
<td>21.6</td>
<td>17.0</td>
<td>4.6</td>
<td>27.1</td>
<td>26.9</td>
<td>17.1</td>
<td>9.8</td>
<td>57.3</td>
</tr>
<tr>
<td>1996</td>
<td>18.5</td>
<td>17.0</td>
<td>1.5</td>
<td>8.8</td>
<td>32.4</td>
<td>23.0</td>
<td>9.4</td>
<td>33.0</td>
</tr>
</tbody>
</table>

\textsuperscript{75} Within the years 1991-1997 planned inflation target had been achieved not even once (Table 34). It is characteristic that three-digit inflation rate was eliminated relatively fast and twelve-month CPI decreased below 30%. But reducing inflation to single-digit rate turned out to be much more complicated. It happened just in 1998, in the ninth year of the transformation.

\textsuperscript{76} It must however, be kept in mind that – as was already mentioned in the second part – the NBP did not determine its targets on its own. It forcibly expressed in e.g. 1996, when the Parliament significantly changed values of targets, proposed by the central bank.

\textsuperscript{77} Problems posed, among others things, delays in privatization and demonopolisation of the Polish economy, external factors {e.g. inflation and growth in the key trading partners, movements in officially controlled process, indexation mechanisms strengthening inflationary inertia. (See Dąbrowski 1999; Kokoszyński 2004).
Gradual modifications of the exchange rate regime did not improve the situation. It turned out that keeping the zloty exchange rate against the US dollar fixed is no longer possible. Despite of progress in realization of stabilization program inflation rate still was high, bringing about the overvaluation of the zloty. In turn, it worsened terms of trade and caused a rapid increase of current account deficit. Thus, in the October of 1991 a new exchange rate regime was introduced, so-called crawling peg. (See Table 32).

Under the new regime the official parity was reduced daily by a small amount. It was so-called micro-devaluation. Within a month, it amounted to the fixed devaluation rate, initially equal to 1.8% per month. Moreover, a very narrow tolerance for deviations of the zloty rate on the interbank market was permitted. Originally, the width of the fluctuation band equalled to ±0.5%. It was supposed that thanks to adoption of this regime the exchange rate was going to stabilize inflationary expectations, as well as serve as an instrument of export supporting. (NBP 1992, Rosati 2001). To make fulfilment of these targets more plausible, the NBP had been constantly reducing the rate of the crawling devaluation, so finally it achieved in 1995 the level of 1.2%. The fluctuation band for deviations was being gradually widened to 2% as well. The two goals, however, were contradictory. According to Polański [1999, p. 45], “on the one hand managing the exchange rate made control of money supply difficult, an on the other administrative feedback between expected devaluation and inflation were conducive to formation of an inflationary spiral”. Such view was shared by Wojtyna (2004), recognizing that abandoning the fixed exchange rate deprived the stabilization program of one of the most important nominal anchors.

It is worth stressing that the crawling devaluation rates, according to which official parity was devaluated every month, were adopted jointly by the NBP and the

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78 In 1990 inflation rate amounted to 249%.
government. Therefore, they were included in the budget law. (Polański 1999). The exchange rate then was not only an instrument of the monetary policy, but also – or even first of all – the intermediate target of this policy. Achieving this target precluded however the central bank from controlling monetary aggregates. Yet, the aggregates constituted formal intermediate target (see Table 33). The exchange rate had such status only unofficially. For that reasons conducted strategy was called “eclectic”, since it included components of various attitudes.

Achieving both intermediate objectives – formal and informal – was unfeasible. Commitment to a systematic devaluation of the zloty’s rate was conducive to massive inflows of short-term foreign speculative capital. In 1995 such inflow brought about a rapid increase of foreign exchange reserves by circa USD 8.935 million, triggering serious inflationary tension (see Koronowski 1997). In response to this unfavourable phenomenon, in the May of 1995, the zloty was partially floated. The parity ceased to serve as the official exchange rate. Banks were allowed to set on their own zloty exchange rate, while buying and selling foreign exchange. However, they were under an obligation to resale foreign exchange to the NBP. This regulation, however, contributed again to increase of foreign exchange reserves. In order to prevent money supply to grow sterilization was conducted, in the form of open market operations (reverse repo and outright sale). It exposed the NBP to high losses (NBP 1996b) and contributed to overliquidity in the Polish banking sector.

Also the band, within which the market exchange rate could deviate on the interbank market from the official parity, was widened, initially to ±7 %. With time, the zloty was permitted to float within the fluctuation band of ±15 %. Thereby the basics of the regime of crawling band were created (Table 32). The intention was to increase

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79 According to Szpunar (2001), the exchange rate (or, more precisely, the rate of the crawling devaluation and widening of the fluctuation band) was, not to say, the main instrument of the NBP, at least till 1997.

80 As Kokoszczyński (2004, p. 233) states “the choice, that the Polish monetary authorities had in this situation, was limited to real appreciation of zloty, caused by inflationary consequences of rapid increase in money supply, combined with keeping the existing mechanism of exchange rate control unchanged, or to nominal (thus also real) appreciation in the event of introducing changes in the exchange rate mechanism, aimed at decreasing of capital inflows.

81 Overliquidity constrained significantly the effectiveness of the interest rates policy. The banks could do without borrowing from the central bank. Thus, the interest rates of the NBP did not determinate the cost of money on the interbank market. (See Knakiewicz and Marszalek 2001).
fluctuations of the market exchange rate so as to increase uncertainty about its future level and to reduce short-term capital inflows.\textsuperscript{82} (Polanński 1999, Rosati 2001, Stawiński 1999). Such target was successfully achieved. Since 1996 the structure of inflowing foreign capital changed. Direct investments began to play bigger and bigger role. (Jurek 2002). At the same time, the growth of foreign exchange reserves was curbed. Reserves increased within 1996 by USD 3.070 million.

All these efforts caused significant decline of unregistered trade turnovers, which in previous years had corrected \textit{in plus} the balance of current account. Thus, the balance worsened.\textsuperscript{83} Therefore, despite of widening the fluctuation band, the NBP had to conduct interventions and to stabilize the zloty within a narrower, unofficial band. (Lutkowski 2003, Rosati 2001).\textsuperscript{84} Such action was made in order to restrain the appreciation of the zloty so as to reduce deficit of the current account balance.

Despite the changes, a simultaneous achieving of the both goals still remained unfeasible. Moreover, lack of consistency between them even deepened. It must be stressed, however, that inflation rate systematically decreased. According to the statement included in the \textit{Medium-Term Strategy of Monetary Policy for years 1999-2003}, it had been possible as long as the investment risk did not decreased and connections of the Polish economy with international market did not become closer. As Szpunar (2001) explained, the reason behind this phenomenon was that, under the circumstances of a deepening financial market, affecting simultaneously the zloty exchange rate and interest rates was no longer possible. It required a greater scale of interventions, as changing the level of the exchange rate became more difficult. This, in turn, entailed – while attempting to avoid appreciation – increase in banks’ liquidity. The results were, as it was mentioned, low effectiveness of the interest rates policy and disruptions in the transmission mechanism. In the face of high over

\textsuperscript{82} At the same time, move towards gradual widening of the deviations band were perceived as elimination of “internal conflict between the intermediate targets”. [MPC 1998, p. 8].

\textsuperscript{83} In 1996, instead of surplus on the current account, deficit of USD 1.3 billion emerged. In the next year, this deficit deepened, amounting USD 4.23 billion. Deficit of the balance of trade rose from USD 4.5 billion to USD 7.3 billion. At the same time, positive balance of unregistered turnovers [mainly unregistered trade] decreased – in the August of 1997 it amounted to USD 3.7 billion, while in the 1996 to USD 4.9 billion (NBP 1998, Koronowski 1997).

\textsuperscript{84} In the banking practice there is a saying, according to which the NBP holds the zloty “on a tight lead”. (Sławiński \textit{et al.} 2001, p. 208).
liquidity, monetary policy tightening required a much higher increase in the interest rate, what resulted in foreign capital inflow and higher appreciation pressure. It led to a vicious circle of the constant growth of sterilization operations, as well as their costs.

Under such circumstances, continuous progress of disinflation was a result of granting by the NBP an informal priority to inflation targets. Namely, trying to keep a tight rein on inflation, the exchange rate was changed. To a lesser extent, however, changes in monetary aggregates were taken into account. Thus, their level exceeded significantly planned values. The intermediate target, i.e. money supply, was then, in a sense, “sacrificed”. What mattered most, was achievement of the final target. (Szpunar 2001).

According to Kokoszczyński (2004), the described manner of monetary policy was, in principle, effective. He argues, however, that understanding of mutual relations of money supply and the exchange rate as the intermediate targets of the monetary policy was rather difficult. Lack of consistency resulted in the critique of actions, undertaken by the NBP. Thus, decision was made to abandon the triad in favour of the direct inflation targeting (the DIT or just inflation targeting) strategy. It was guided by the practical considerations as well as by the newest results of empirical research.85

Since 1999 the Polish central bank has officially begun to conduct the DIT strategy.86 From the previous considerations it follows that changes in the monetary policy strategy extracted also, in a way, new attitude to the use of the exchange rate as the monetary policy instrument. It was also the case after the DIT had been adopted. Namely, the NBP gradually ceased to use the exchange rate channel in monetary transmission. It was rather painful, for this channel had probably been the most effective one from among all the monetary policy channels. (See Rybiński 2000).

Still, some actions were made, aimed at adjusting the exchange rate regime to the new strategy. It was necessary, because putting any restrictions on the exchange

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85 It is commonly shared point of view that, in contemporary conditions, adopting as the intermediary targets both the exchange rate and monetary aggregates cannot be effective.
86 In fact, such strategy has been already realised since 1998. (See Table 32).
This project is funded by the European Union under the 7th Research Framework programme (theme SSH) Grant Agreement nr 266800

rate (e.g. in form of adopting a narrow fluctuation band) would have been in practice equivalent to setting the second, parallel target of the monetary policy. It could have led to conflict between inflation target and some exchange rate target. Thus, it was officially stated that for effective conducting of the inflation targeting it would be beneficial to float the zloty exchange rate, thus making the monetary policy of the NBP consistent. (MPC 2000b).

Before taking decision on establishing the regime of a float exchange rate, features of the conducted exchange rate policy have been changing. First of all, it had to create conditions favourable to effective monetary policy in the changing environment of an external disequilibrium and instability in the global financial markets. Thus, in 1998 the fluctuation band was widened twice: on February 26 (to ±10%) and on October 28 (to ±12,5%). At the same time, foreign exchange interventions were taken rather seldom – for the last time in the first half of 1998. Also, the decision about changes in the fixing mechanism was made. The new principles limited space for conducting foreign exchanges transactions between the commercial banks and the NBP during so-called zloty fixing, mainly by imposing a margin between bid and offered exchanges rates and reducing a time set aside for making offers as well as their maximum volumes. (MPC 1999c).

In the June of 1999 the opportunity to make transactions between the NBP and the commercial banks was entirely eliminated. Thanks to this move, the zloty exchange rate was determined only by demand and supply on the market. Thus, in fact, the zloty exchange rate was almost completely floated. (Rosati 2000). The floating of the zloty became plausible because of reducing the rate of monthly devaluation and widening the fluctuation band to ±15% from official parity. (MPC 2000b).

On April, 11, 2000, a crucial switch of the exchange rate regime in Poland occurred. It was due to the common decision of the government and the Monetary Policy Council (MPC) – the new body, established on January 1st, 1998, in connection with reorganization of the NBP authorities. The resolutions of the MPC, which sanc-

87 As it was already indicated, the Council has special prerogatives in the field of the exchange rate. According to the Act on the NBP of August 1997, “the NBP conducts the exchange rate policy established by the Council of Ministers in consultation with the [Monetary Policy] Council. The procedure for
tioned abovementioned changes and introduced in Poland the floating exchange rate regime, came into effect on April 12, 2000. It was equivalent to abolition of the central parity rate for the zloty and the crawling band.

Formally, the new regime has been characterized as managed floating. In practice, however, the NBP has refrained from interventions aimed at influencing the zloty exchange rate. Therefore, in the literature the current regime is perceived as independently floating. [Matecki 2002, Rosati 2001]. The central bank desisted from the zloty exchange rate defence, focusing on price stability. Then, the NBP does not have any target in the form of the level of the zloty exchange rate against other currencies. Nor does it have any formal commitments concerning interventions on the foreign exchange market. [MPC 2000a]. The zloty exchange rate ceased to be employed as an instrument of the monetary policy. [MPC 2001b].

The NBP reserves, however, the right to carry out foreign exchange interventions, “for the sake of the low level of foreign exchange market development” and “if it recognizes them necessary for achievement of the inflation target”. [MPC 1999b, p. 15; NBP 2002, p. 6]. At the same time, the NBP emphasises clearly that floating the zloty exchange rate constituted the final stage in a policy of the gradual increase of exchange rate flexibility. [MPC 2001a].

Adopting the DIT strategy and switching to the float exchange rate regime in a way completed process of changes in the area of the Polish monetary policy. Since then, its frameworks have been consistent with the so-called New Monetary Policy Consensus. Such approach, recommended by most of mainstream economists, is nowadays treated as the most effective way of conducting monetary policy [see e.g. Woodford 2003 and for critique – Arestis and Sawyer 2005].

In principle, one may say that the direction of changes has been correct. Such statement is confirmed by plain facts: decreasing of the inflation rate from circa
650% in 1989 to 1.4% in 2006 and avoiding – as one of only few countries in Central and Eastern Europe – currency and financial crisis. However, general assessment of monetary policy cannot be so obvious. The question arises whether focus on price stability was in fact beneficial or it was rather harmful, generating avoidable costs. The latter view may be confirmed by the research of Schmidt-Hebbel and Tapia (2002). According to them, among 20 countries, realizing strategy of direct inflation targeting, Poland had highest sacrifice ratio. Moreover, restrictiveness of monetary policy generated social costs, mainly in the first stage of transformation, creating climate of distrust and limited confidence to policymakers decisions. Simultaneously, coordination between monetary and fiscal policy was insufficient.

Additionally, it is argued that the monetary transmission mechanism in Poland has been slow and weak. Different reasons made the transmission of monetary policy impulses in Poland ineffective, including specific features of the Polish banking sector and some behavioural factors, which are particularly important in transition economies and should be taken into consideration by monetary policy-makers. Monetary policy impulses have been relatively ineffectively transmitted by commercial banks, mainly because of specific features of the Polish banking system, including: the excess liquidity problem, the ownership structure, characteristics of banks’ balance sheets, and links between banks and borrowers making banks unwilling to cut their credit supply significantly (see e.g. Marszatek 2009, Kokoszczyński 2004).

The monetary policy did not change significantly since the global financial crisis. The NBP still focused on price stability, conducting inflation targeting strategy (but with more attention paid to financial stability) and influencing short term interest rates. As it was presented in Section 16, the Polish central bank has been trying to manage liquidity of banks by offering them some additional forms of refinancing and investing potential surpluses. Such policy, combined with other actions, turned to be effective: no bank bankrupted and overall stability was protected.
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THE ABSTRACT OF THE PROJECT IS:

The research programme will integrate diverse levels, methods and disciplinary traditions with the aim of developing a comprehensive policy agenda for changing the role of the financial system to help achieve a future which is sustainable in environmental, social and economic terms. The programme involves an integrated and balanced consortium involving partners from 14 countries that has unsurpassed experience of deploying diverse perspectives both within economics and across disciplines inclusive of economics. The programme is distinctively pluralistic, and aims to forge alliances across the social sciences, so as to understand how finance can better serve economic, social and environmental needs. The central issues addressed are the ways in which the growth and performance of economies in the last 30 years have been dependent on the characteristics of the processes of financialisation; how has financialisation impacted on the achievement of specific economic, social, and environmental objectives?; the nature of the relationship between financialisation and the sustainability of the financial system, economic development and the environment?; the lessons to be drawn from the crisis about the nature and impacts of financialisation? ; what are the requisites of a financial system able to support a process of sustainable development, broadly conceived?’
This project is funded by the European Union under the 7th Research Framework programme | theme SSH | Grant Agreement nr 266800

THE PARTNERS IN THE CONSORTIUM ARE:

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<td>UK</td>
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<td>2</td>
<td>University of Siena</td>
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