

**I. INAUGURAL LECTURE FOR OPENING THE ACADEMIC YEAR  
2014/2015**

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**THE POLISH BANKING SECTOR IN THE PROCESS  
OF TRANSFORMATION OF THE POLISH ECONOMY**

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**1. INTRODUCTION**

In the economy as in politics, not many significant events occur suddenly or accidentally. That was the case with the sort of “preparation” for the changes in the political and economic system in Poland which lasted for many years. These changes were pursued not only by the opposition, but also by a part of the elite associated with the system in power dominated by the Polish United Workers' Party (Pol. Polska Zjednoczona Partia Robotnicza, PZPR).

After the Solidarity uprising, supported by the authority of Pope John Paul II, who clearly expected a peaceful course of transformation, and after the painful experience of martial law, the search for ways to break the resultant deadlock became a necessity. After the introduction of “glasnost” by Mikhail Gorbachev, the chances of peaceful transformation significantly increased, and the process of preparation for change gained considerable momentum. This process was accompanied by a deep distrust justified on the grounds of historical experience.

Finally, the will to reach agreement and turn a new page in the history of Poland, Europe and the world won. In Poland, efforts to implement reforms made since 1983 by Professor Władysław Baka, began to take on a clearer shape only after a few years of struggle.

The changes involved, inter alia, issues such as establishing the independence of the National Bank of Poland (NBP), the separation of PKO BP, making Pekao S.A. and Bank Handlowy self-reliant, and then separating a group of nine regional banks from the NBP. This was reinforced by new regulations that included the banking law and the act on the NBP which was

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\* President of The Polish Banks Association (ZBP)

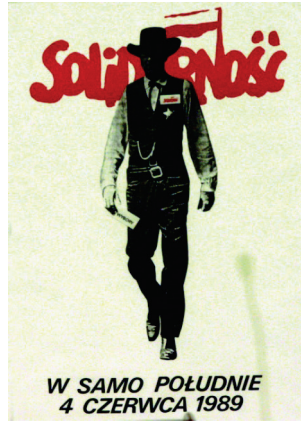
enacted in 1989. Poland's banks again became members of international financial community. The government, headed by Professor Zbigniew Messner, started working on the laws on entrepreneurship, and prices were gradually deregulated. This work was even accelerated, and various new solutions were implemented when the next government headed by Mieczysław F. Rakowski came into power.

Important changes in the area of civil liberties and justice occurred subsequently since 1980:

- In 1980 the Supreme Administrative Court was established.
- In the mid-eighties, compulsory job placement was abolished.
- In 1986 the Constitutional Tribunal was established.
- The Ombudsman's post was first established in January 1988.
- In 1988 arrangements were made on the freedom of association of private persons and economic entities as well as on the organisation of assemblies.
- In the same year, the socially sensitive issue relating to the free access of Poles to passports and the right to freely travel outside the country's borders were agreed upon.

These examples formed a pretty solid basis for building the foundations of trust between the representatives of the democratic opposition and the ruling group. Both sides understood that Poland needed some changes, and that none of these sides was able to bring about these changes separately because of internal and international constraints. They also understood that in order to carry out reforms, social support and trust are indispensable.





The Polish Round Table Talks, then the partially free elections of 4 June 1989, and finally the appointment of Tadeusz Mazowiecki as Prime Minister – which took place thanks to the initiative of Solidarity and the attitude adopted by the PSL (Polish People's Party) and the SD (Alliance of Democrats) – significantly accelerated the process of social, political and economic reforms in Poland.

Polish society was not only eager for change, but obviously also for a rapid improvement in the standard of living. It was ready to make sacrifices, but it needed social guarantees and safety, which were mainly provided by the Solidarity trade union, but also by a number of institutions and people associated with the widely perceived existing ruling group.

The administrative apparatus was, to a significant extent, prepared for the introduced changes and acted loyally. The Catholic Church played an essential role throughout the process of transformation. So did the academics and graduates of the Polish universities.

After a period of considerable uncertainty, some new perspectives on cooperation with the countries of Western Europe and the USA that were opening up, began to play a stabilizing role. This was particularly important when the foundations of the existing cooperation under the Council for Mutual Economic Assistance and the Warsaw Pact were disassembled.

More countries of the former Soviet bloc followed the Polish path of change. Opening up the opportunity to reunite Germany, thanks to the events which started in Poland, formed a completely new chapter of the cooperation between Poland and the Federal Republic of Germany, laying foundations for the accession of Poland to Western political, economic and military structures.

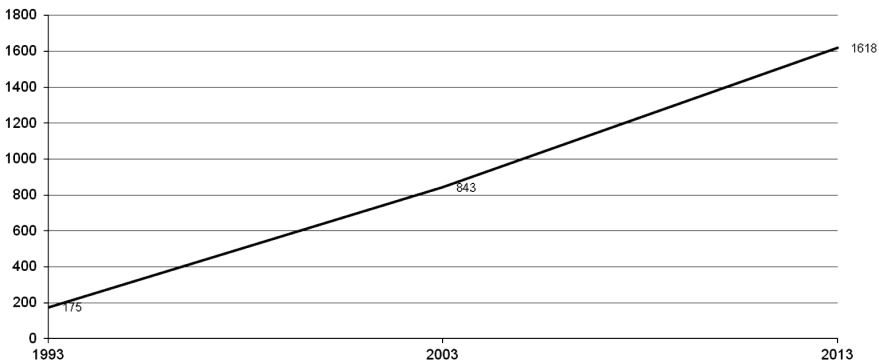
The package of economic laws developed by a team headed by Deputy Prime Minister Leszek Balcerowicz, approved by the government, also

changed the sphere of ownership and social relations. The gradual commercialization and privatization, often preceded by the restructuring processes forced by economic considerations, were implemented in a period of high inflation and changes in credit relations. This was often the cause of serious social tensions and protests against the increasing difficulties in managing the newly emerging reality.

Profound changes were also introduced into the Polish legal system. The adoption of the so-called Small Constitution, the laws on political parties, local government and finally, in 1997 by popular referendum, the new Constitution of the Republic of Poland, completed the process of the fundamental changes. In the same year a new Banking Law and the Act on the NBP were passed. As a result, the Monetary Policy Council (Rada Polityki Pieniężnej, RPP) came into being and the autonomy of the NBP was guaranteed.

Since 1998 the joint Commission for Banking Supervision (KNB) has been in existence. These decisions gave a particular reason for satisfaction to the Polish banking community because the Polish Bank Association (ZBP) put forward the proposal to constitutionally guarantee the autonomy of the NBP, establish the RPP and the KNB already in April 1994. At that time the proposal was hard to accept, but then it proved to be right. Also some laws adopted earlier turned out to be very important for the stable development of the Polish banking sector:

- in 1993, the Act on the Restructuring and Commercialization of State-Owned Enterprises and Banks,
- in 1994, the Act on the Restructuring of the Cooperative Banks and Bank Gospodarki Żywnościowej (BGŻ),
- in 1994, the Act on the Bank Guarantee Fund.

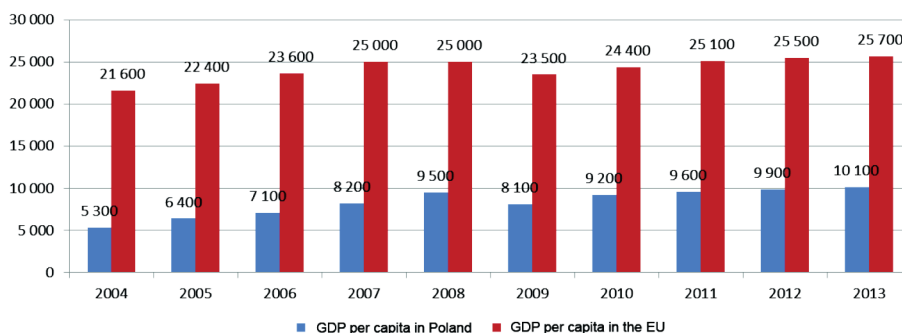




The process of the joint development of the economy and the Polish banks has continued uninterrupted, and it can be considered a big success of Poles, Polish companies and successive governments as well as the regulators and supervisors.

1) From 1993 to 2013, **GDP** in Poland increased nearly tenfold to reach the level of PLN 1,618 billion at the end of 2013.

Polish families benefited from the GDP growth especially in the period from 2004 to 2013, that is after Polish accession to the European Union. At the end of 2003, GDP per capita in Poland was €5,300, whereas in the EU it was €21,600. Ten years later these figures stood at €10,100 for Poland and €25,700 for the EU.

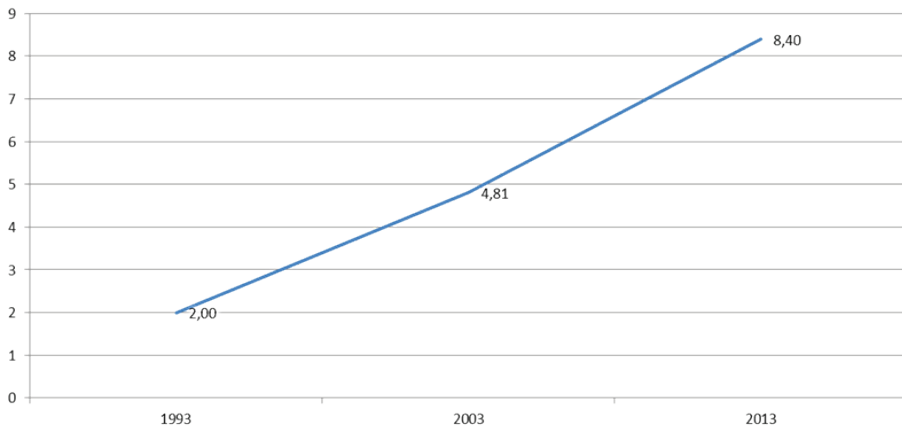


These good results were the consequence of steady growth in labour productivity, the high level of foreign direct investment and the significant increase in the innovativeness of the economy. Although the innovativeness was to a considerable extent imitative, its crucial importance for the economic development should not be downplayed.

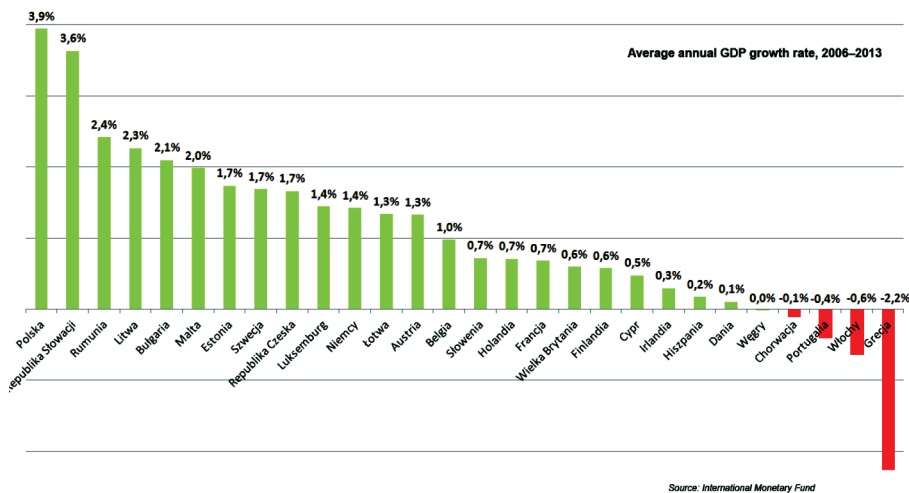
Even faster growth was recorded in this period by the Polish banking sector's own funds, which increased the ability to finance the development of the economy from private sources. At the end of 1993, the ratio of these funds to GDP accounted for 2.0% to reach the level of 8.4% of GDP after twenty years. Additionally, it is important to note that more than 90% of these funds are of the first category. Therefore they constitute a solid guarantee of the stability for the banks and the security of customer deposits.



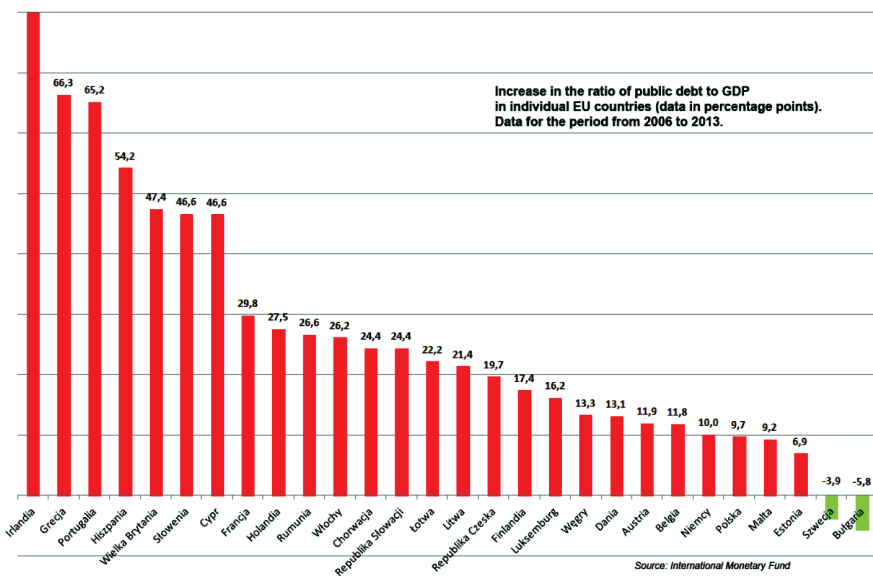
The average annual **GDP growth rate** looks even more interesting in the period from 2006 to 2013. In the case of Poland the rate was 3.9% and was the highest in the European Union. Slovakia, with a growth rate of 3.6%, was the second economy to have exceeded 3% in this period. In the remaining countries the rate of growth ranged from minus 2.2% in Greece to 2.4% in Romania.



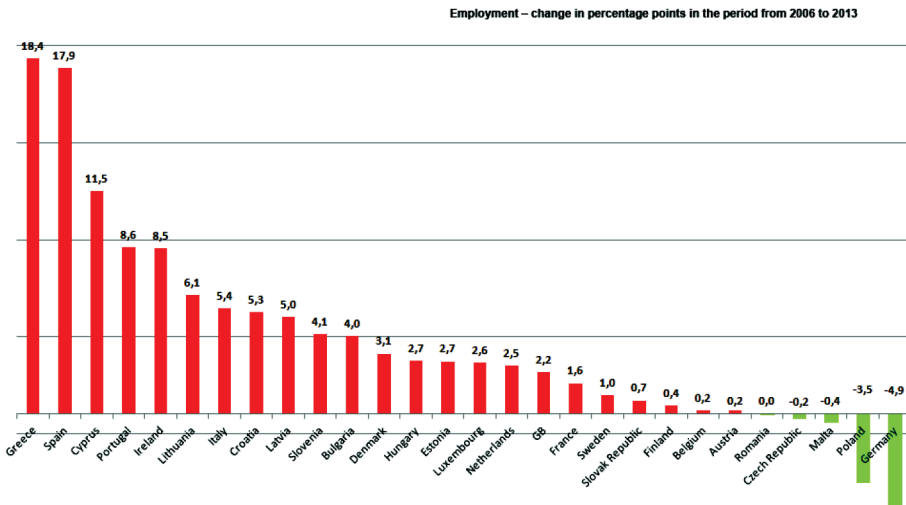
Difficult period: 2006-2013



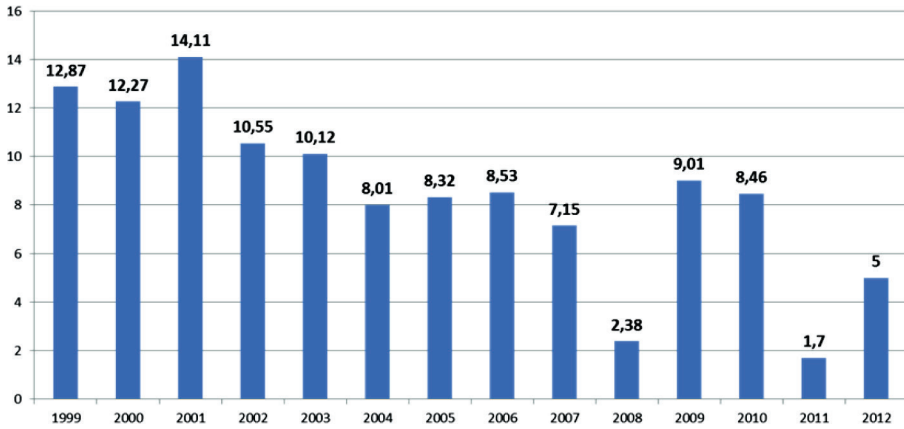
It is worth noting that in the period from 2006 to 2013 the ratio of public debt to GDP in Poland increased by 9.7 percentage points. At the same time in 24 other member states of the EU, public debt increased from 10 percentage points (Germany) to 80 (Ireland). Sweden and Bulgaria were the only countries that recorded a decline in public debt – by 3.9 and 5.8 percentage points, respectively.



A particularly important and socially sensitive issue is the unemployment rate, which decreased between 2006 and 2013 in only four EU countries, including Poland, where it fell by 3.5 percentage points. At the same time in 23 EU countries the increase in the unemployment rate ranged from 0.2 in Austria to 18.4 percentage points in Greece.



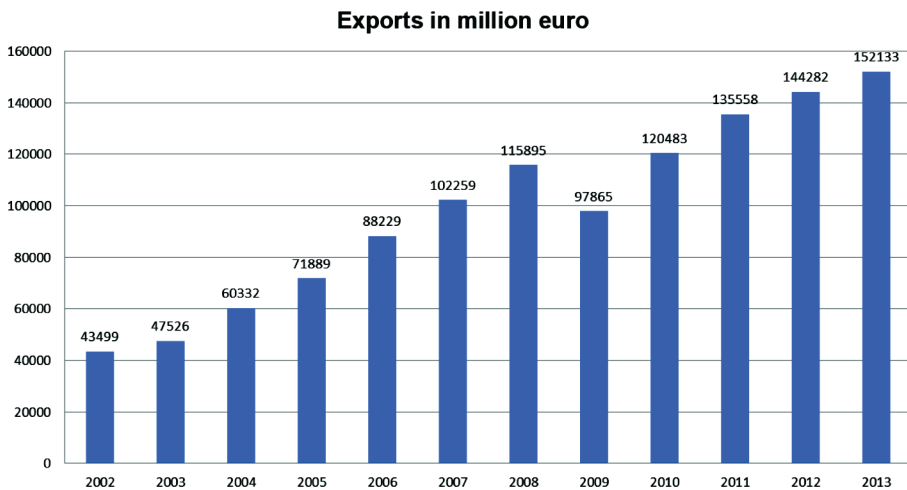
The **savings rate** in Poland is one of the lowest throughout the European Union. This is true both for the level of voluntary and compulsory savings. Many years of a backwardness in the process of building private financial resources, the relatively high propensity to consume and the lack of stable systems promoting long-term savings for housing, pension, health and educational purposes are the main reasons for this situation. It was further deepened by governmental interference in the system of saving for retirement purposes through the reform of the open pension funds (OFE).



In the area of building the propensity to save, strategic state intervention is indispensable. Otherwise the Polish economy will be threatened with a lower ability to finance the long-term development of the economy on the basis of its own resources.

## EXPORTS

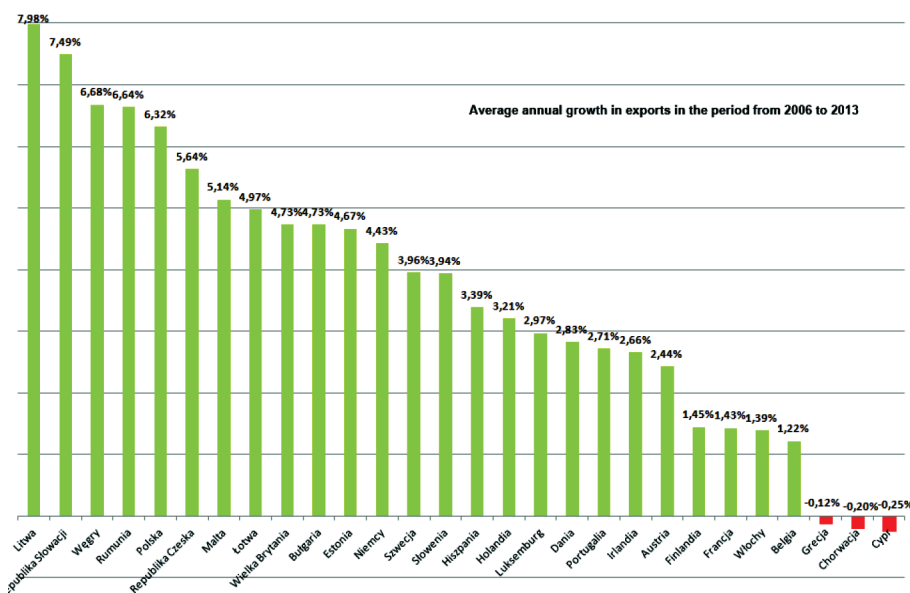
The export of products manufactured in our country became an important factor in maintaining the high rate of GDP growth. The main export markets include EU countries such as Germany, Italy, France and the UK.



Many Polish firms became regular partners of the exporting companies which have invested in Poland over the last twenty five years, or established stable cooperative relationships as a result of the significant increase in the quality of products manufactured by the Polish companies, but at the same time by offering attractive costs of their production. It is worth mentioning here the substantial increase in medium and highly processed technical products. These groups of products include cars, office equipment, car parts and hardware.

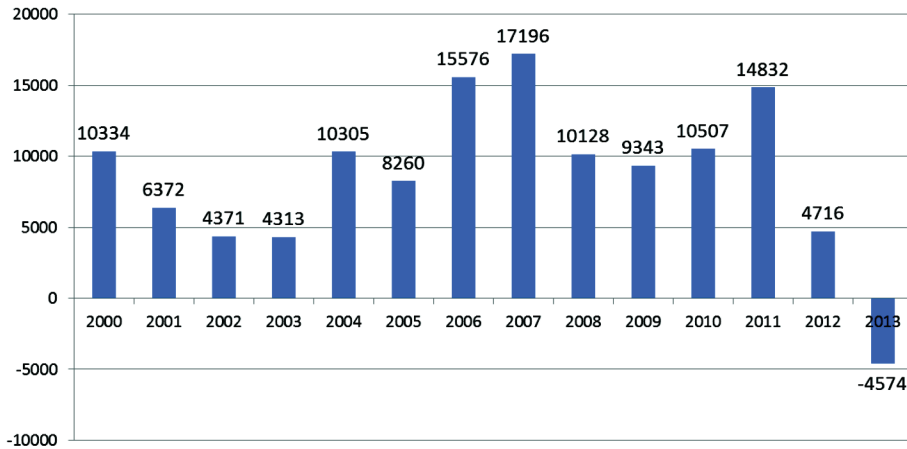
Particular success was achieved by the Polish food processing companies. Agriculture became a good example of the success of the Polish economic transformation because for a number of years it has recorded a significant surplus in the trade balance.

Overall, between 2006 and 2013, the average annual increase in Polish exports amounted to 6.32% and only four countries in the EU performed better.

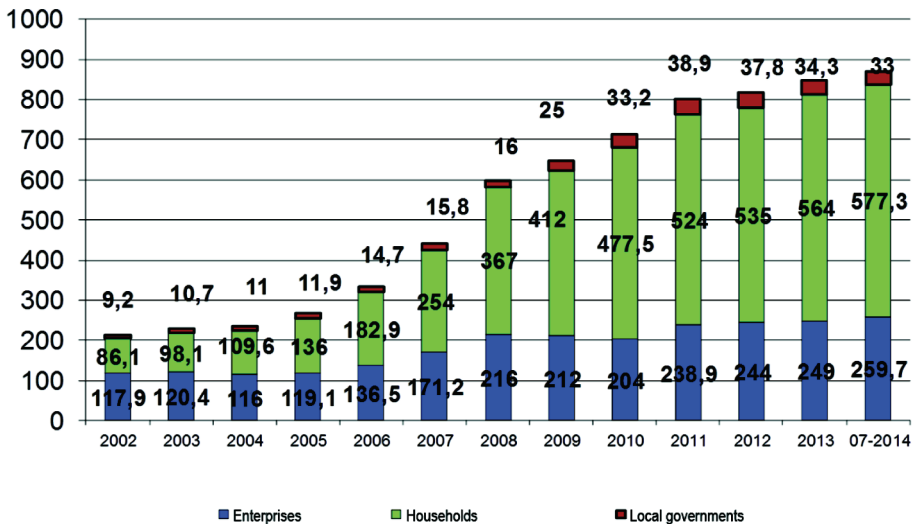


Direct investment played a significant role in the process of the modernization of the Polish economy. Although some experts point out that too many of them were implemented in the area of services (e.g. financial services, trade), the fact is that more than 60% of Polish exports is generated by companies with foreign capital. After 2006, Polish companies themselves

became a major foreign investor in the region. In total, the foreign investment of our companies exceeded USD 60 billion at the end of 2012. The vast majority of them were located in EU countries, but also the investment in the BRIC countries is worthy of note.

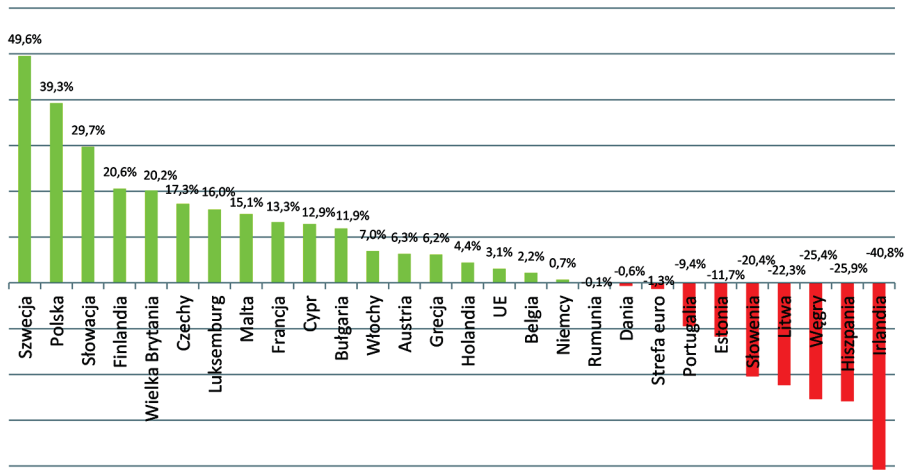


**LENDING ACTIVITY OF BANKS IN THE PERIOD  
FROM JANUARY 2008 TO MARCH 2014**

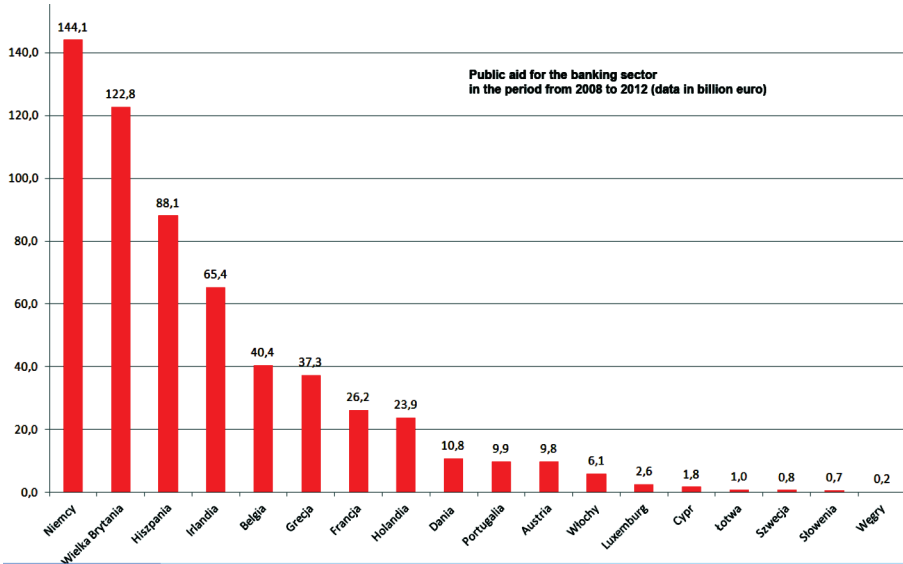




From among all the EU countries, between 2008 and 2015, Poland recorded the second largest percentage increase in loans, which accounted for 39.3%.

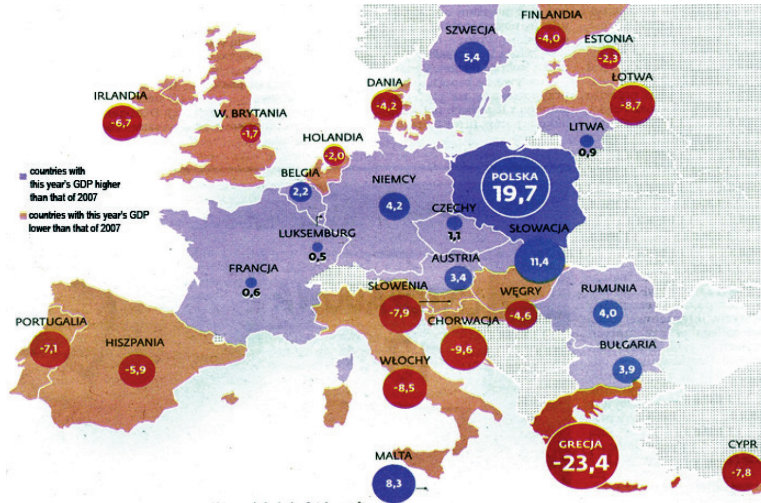


In the same period as many as nine EU countries recorded a decline in the granted loans, which undoubtedly contributed to a significant decrease in GDP growth and to the long-term recession. At this point it is worth noting that in eighteen EU countries it was necessary to provide a multi-billion public aid package for rescuing the domestic banks. In the case of Germany, the amount of this aid was over €144 billion, and in the case of the UK this amount exceeded €122 billion. In any case, it was not the only form of aid as it should not be forgotten that the ECB has several times increased cheaply the liquidity of the euro area banks.



### The Polish banking sector did not have to use such help

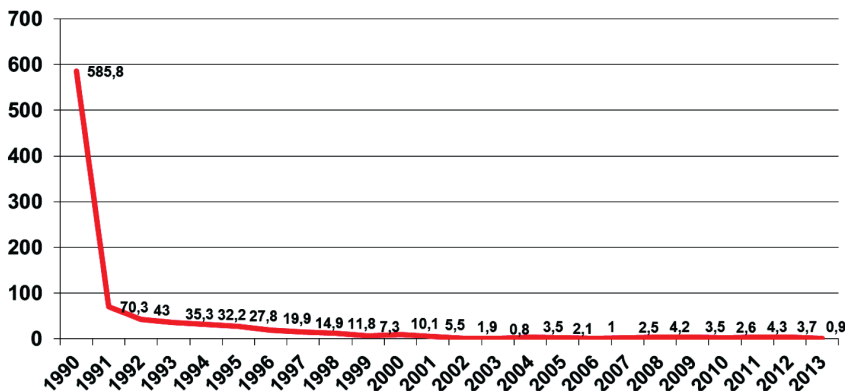
Undoubtedly the success of the Polish economy during the transformation period was underpinned by a number of factors. These factors include a number of wise political decisions (change of the political system as a result of the Round Table Talks, accession to the Council of Europe, OECD and, last but not the least, the adoption of a new constitution and accession to the European Union) and many good economic decisions such as the commercialization and privatization of companies as well as the implementation of numerous programmes of private and public investments. The Polish banking sector, which was still making its way, participated in the implementation of many economic programmes. This sector has learned from the experience of the past and now we can surely claim that it is well-managed, carefully supervised and has responsible investors.



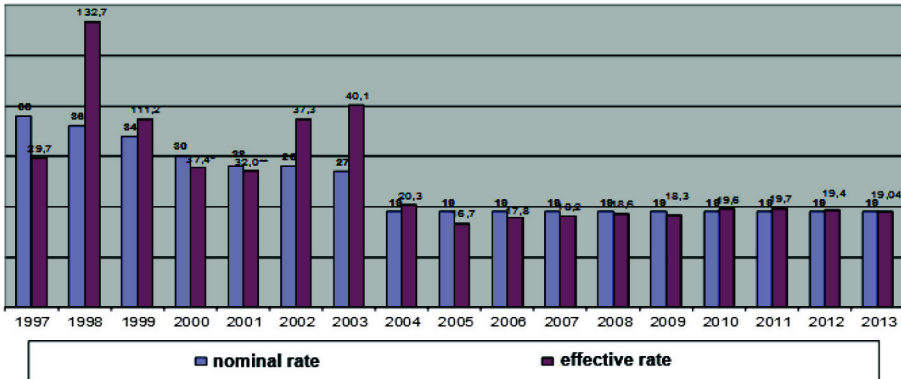
One can say with great certainty that the success of the Polish economy during the last decade is a result of good economic policy, stability, the efficient work of the banking sector, and the good use of the funds made available by the EU, but first and foremost, the entrepreneurial activity of the citizens.

### Some more history - banks in the process of disinflation

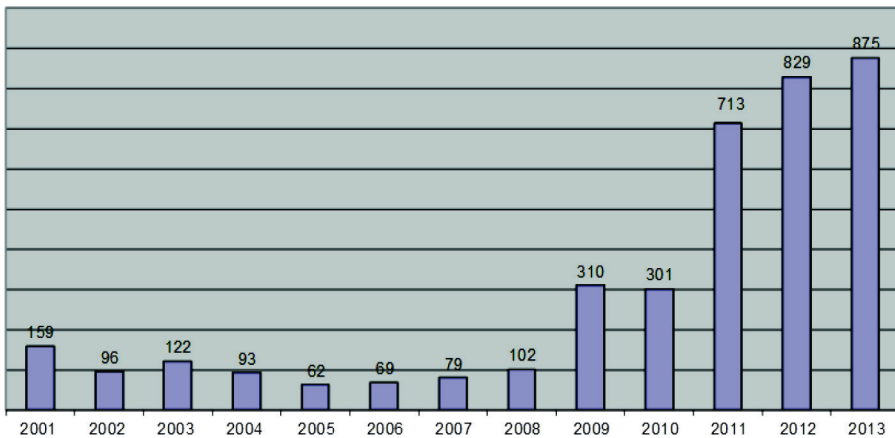
The first decade of the Polish transformation coincided with a period of hyperinflation, and then very high inflation. Thus, it is understandable that the customers of banks and banks themselves had to pay a high price for the process of disinflation in the economy.



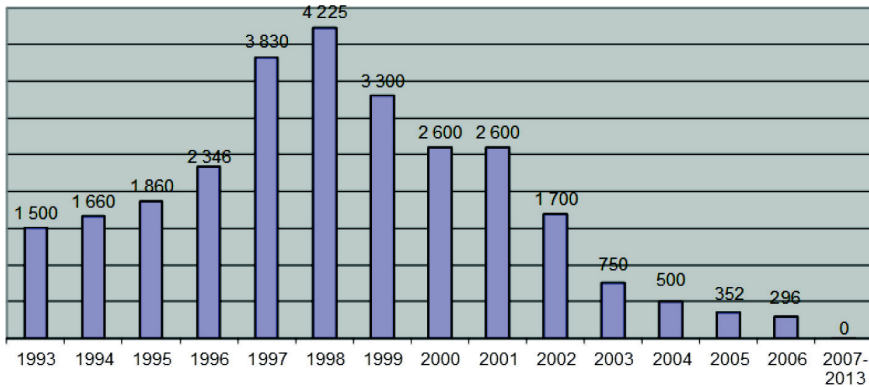
This price included reduced interest revenue from savings deposited in the banks and the higher interest rate of loans. The mechanism of placing a burden on banks and their customers operated through the obligation of maintaining high and interest-free (from the perspective of the banks' income) reserve requirements at the NBP and by allowing only a very small part of the specific reserves for non-performing loans as a tax deductible cost. In some years the effective income tax paid by banks exceeded 100%.



At the same time, since 1995 banks have been obliged to collect funds for the Bank Guarantee Fund which was nothing else but another tax, yet a good and stabilizing one for the banking sector, as it turned out after some years.

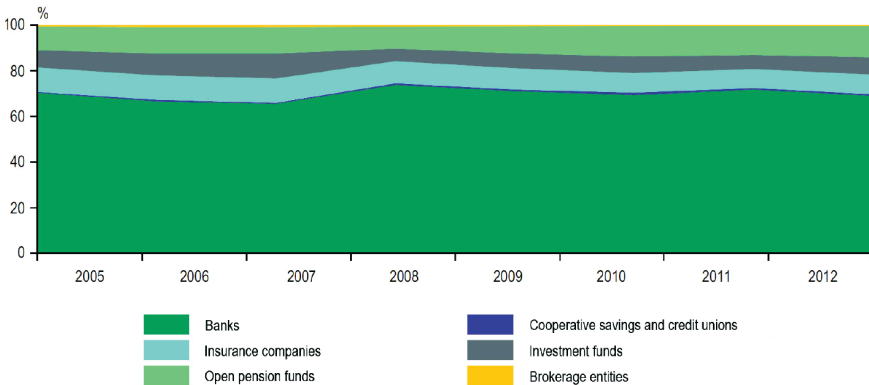


It is worth recalling in the ongoing debate on the possible modifications of the instruments of financial policy, that in the period from 1994 to 1997 it was the interest on reserve requirements that was used to finance the establishment and operation of the Agency for Restructuring and Modernization of Agriculture, and in the period from 2004 to 2008 a part of these funds was used to finance the establishment of the EU Guarantee Fund. Having achieved a very good performance in the last ten years, the Polish banking sector has become the largest payer of income tax.

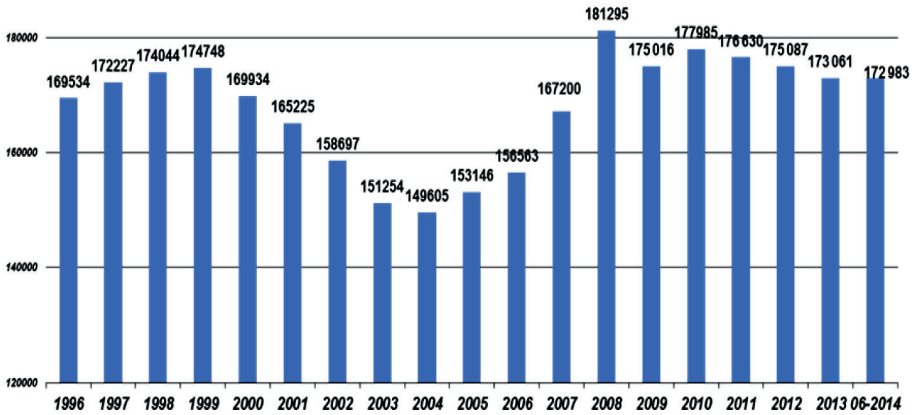


**The special role of banks among Polish financial institutions**

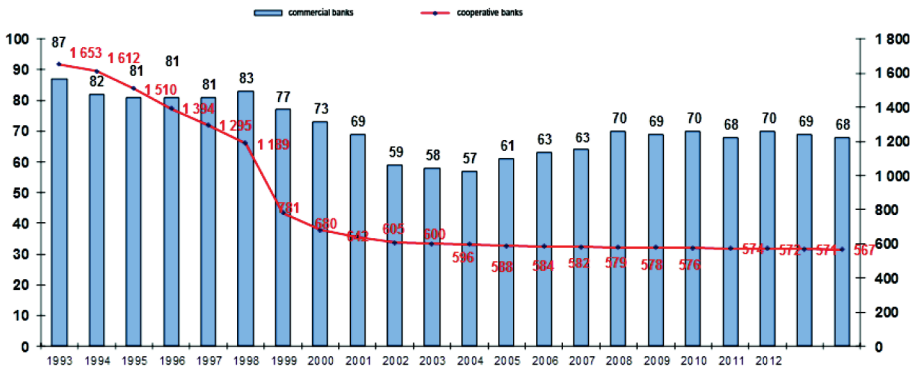
As in most EU countries, in terms of assets the Polish financial market is dominated by the banking sector. Banks play a leading role in the development not only of the capital market, but also the leasing and factoring markets. A significant proportion of insurance products in the Polish market are managed through banks.

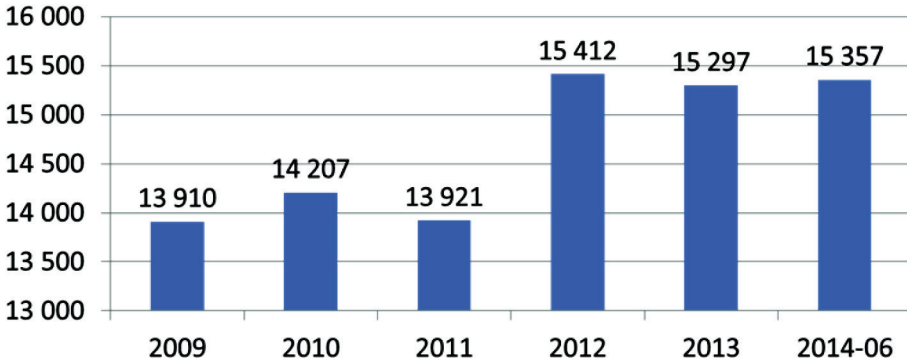


Polish banks employ well-educated and continually developing staff. Over the last twenty five years the number of employees ranged from 129 to 185 thousand. It has to be added that a big part of the banking business is subject to outsourcing, which means that another 30 thousand people approximately work in this sector.



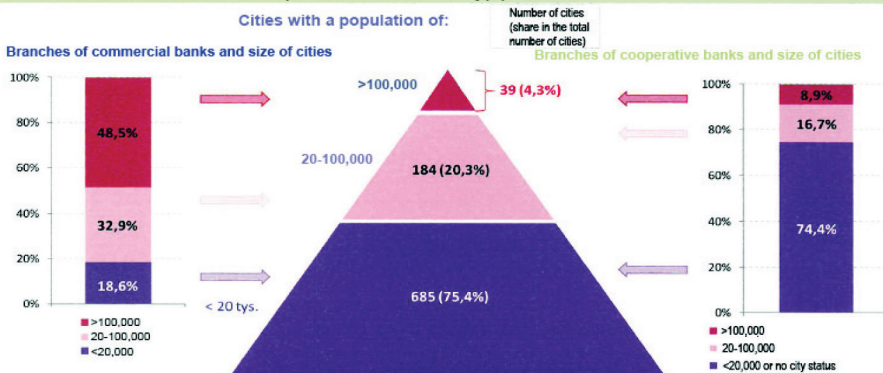
Although the scope and method of the operation of the banks and their branches have changed, their number has remained fairly stable in the last few years, with over 15,300 bank branches and more than 640 banks having domestic and foreign banking licences.





It is worth noting that only 18.6% of the commercial banks branches are located in towns with a population of less than 20,000 people. In contrast, more than 74% of the cooperative banks branches operate in exactly such towns. However, one cooperative bank branch is very often designated for several towns. Difficulties in accessing typical banking services are very often accompanied by poor access to such services through telecommunication due to a weak network and educational shortcomings of the customers. Given the fact that despite their 6-8% market share, the cooperative banks serve approximately 14.5% of SMEs, employ around 32,000 people and operate through the network of about 4,500 branches. Hence their strategic role in providing financial services to rural areas should be recognized.

#### Distribution of branches of commercial and cooperative banks in towns/cities by population



\*Own elaboration on the basis of search engines used for finding bank branches on the websites: [bankier.pl](http://bankier.pl), [lista.e-sieci.pl](http://lista.e-sieci.pl) and [sgb.pl](http://sgb.pl), and data on cities in the Demographic Yearbook 2013. Data covers approx. 73% of branches of commercial banks and approx. 78% of branches of cooperative banks.

**Commercial banks: nearly 50% of branches located in 39 large cities (>100,000 inhabitants)**

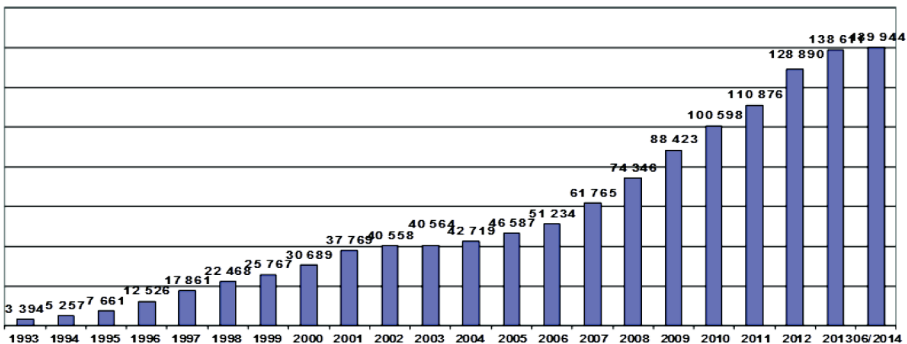
**Cooperative banks: nearly 75% of branches located in towns without city status and in small cities (<20,000 inhabitants)**



Banks with domestic capital played a very important and stabilizing role during the economic downturn between 2008 and 2013. First of all, they reduced lending to economic entities only slightly, and in many cases they took over the financing of entities for which banks with foreign capital could no longer provide loans. This issue requires more extensive research in the context of the idea of the Banking Union and the implementation of the economic policy in the countries that belong to it.

According to the methodology of the OECD, since 2008 the share of domestic capital in the Polish sector has increased by 19 percentage points and reached the level of 44%. During the same period, the share of assets managed by the banks with domestic capital increased by 29.5% to the level of 39%. Thus the banks in Poland have partially come back to the Polish owners. However, one should point out the responsible behaviour of the foreign investors in the Polish banking sector. This was represented in the constant reinvestment of the majority of profits and in the provision of resources to increase the liquidity of bank subsidiaries when there was a need for them, which made them achieve good results and let them become a showcase in many banking groups.

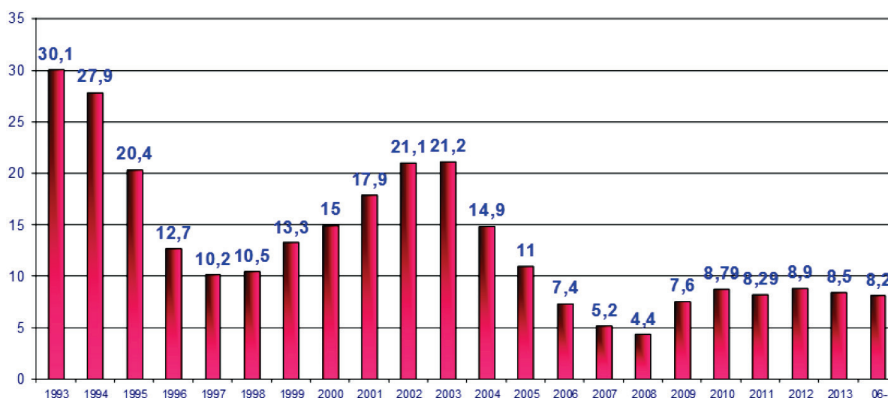
The well-coordinated and efficient actions taken by the regulatory and supervisory authorities in this period also have to be emphasized. As a result of the actions taken jointly with the banks, any possible adverse consequences of currency mismatches have been avoided in several banks, but also the level of security of the entire sector has been increased.



After 25 years of the transformation and building of the Polish banking system it can now be said that the Polish sector is:

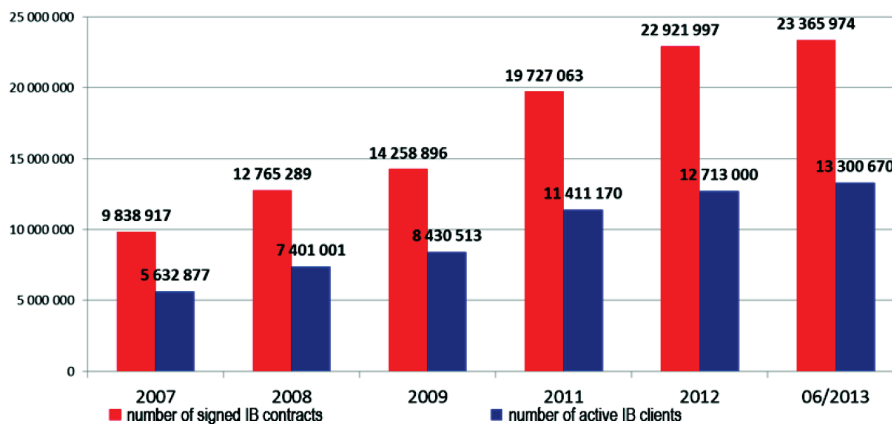
### 1) Stable, which is evidenced by:

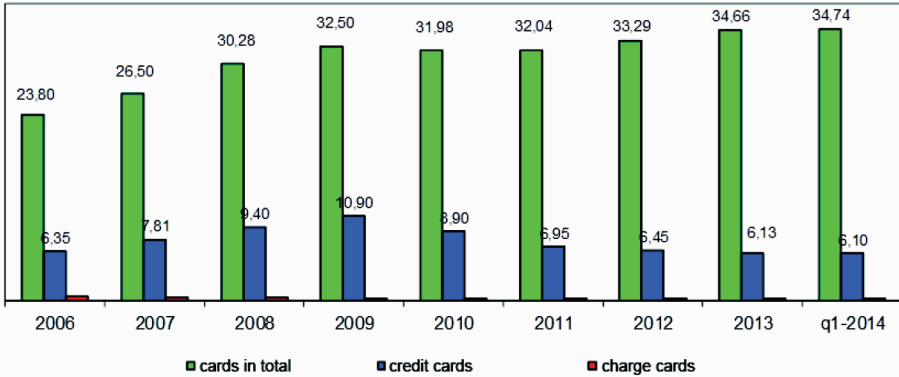
- the constantly growing level of own funds, which is sufficiently high for the size and nature of the conducted business;
- the high level of capital adequacy ratio;
- the high quality of the loan portfolio;
- the ex-ante funds collected at the Bank Guarantee Fund.



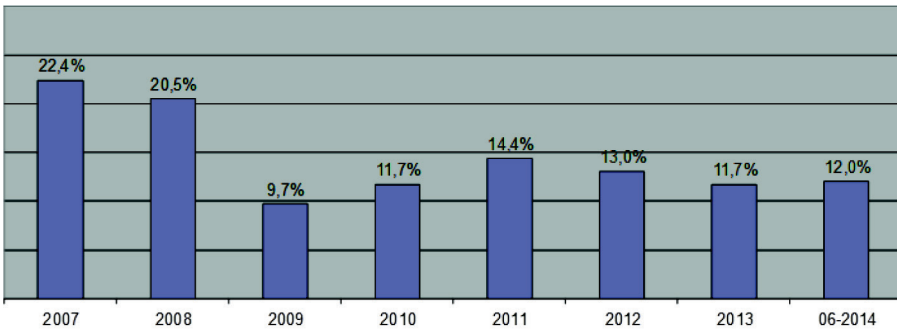
### 2) Modern, which is evidenced by:

- the wide range of traditional banking services;
- the modern payment and settlement system;
- the IT systems in all banks that are modern and proper for the profile of the conducted business;



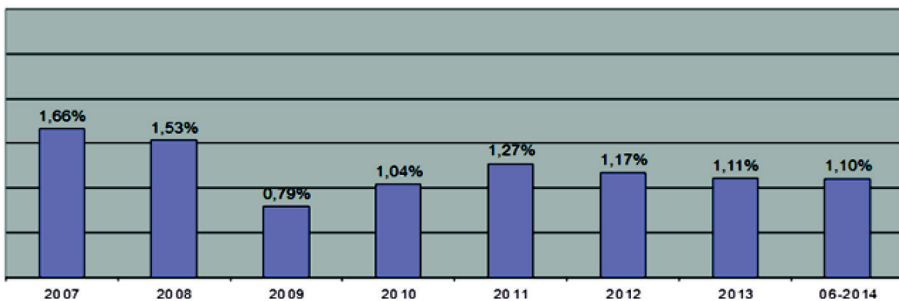


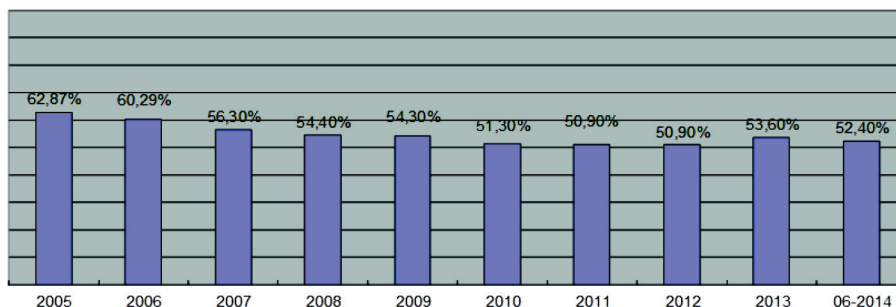
- the modern system of economic information;
- access to over 23 million private bank accounts via the Internet;
- access to over 2 million accounts of the SMEs via the Internet;
- the nearly 35 million modern and perfectly secure payment cards issued.



**3) Effective**, which is evidenced by:

- the high return on assets compared to other EU countries;





- the high return on capital compared to other countries;
- the satisfactory level of the C/I ratio;
- the increasing level of the use of banking services which exceeded 80% in 2013.

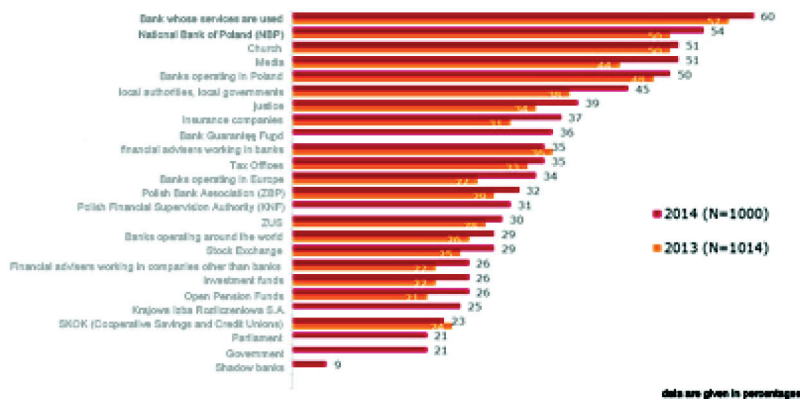
#### 4) Trustworthy, which is evidenced by:

- the systematic rise in savings;

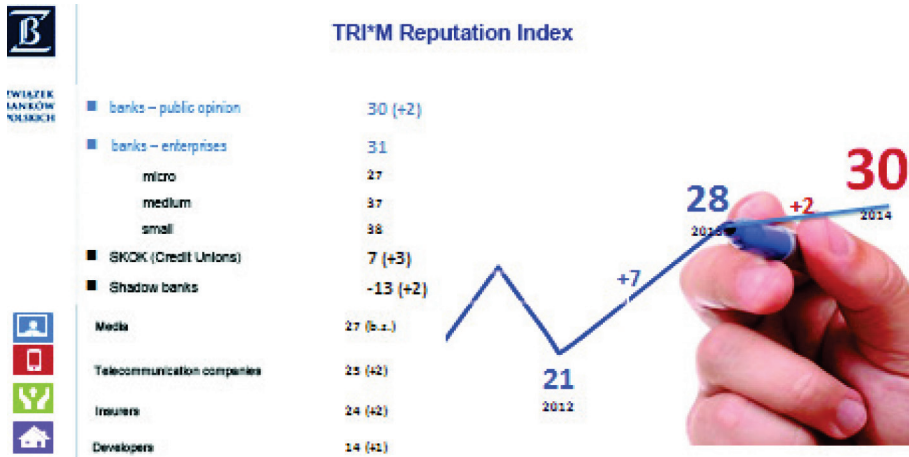


ZWIĄZEK  
BANKÓW  
POLSKICH

#### Trust in institutions – public opinion



- the results of the survey on trust in banks and the sector;
- the increasing reputation indices of the sector.



### 5) Backed by a solid infrastructure:

During the last 25 years the Polish banking sector has built stable entities of banking infrastructure, which mainly include:

- 1) the banking settlement system: KIR, e-service, Firstdata, PSP;
- 2) the system of economic information: BR in ZBP, MIG DZ, BIK S.A., BIG S.A., ZORO, SWOZ;
- 3) the system of bank staff training, the qualification standards and the schools of banking;
- 4) the system for the development of the inter-bank market WIBOR and WIBID indices.

Banks made a major contribution to the development of the modern Polish telecommunication and electronic economy and to a number of technological standards that were introduced. On the initiative of the ZBP and together with the National Bank of Poland, the banks founded the Banking Telecommunications Company Telbank, now Exatel.

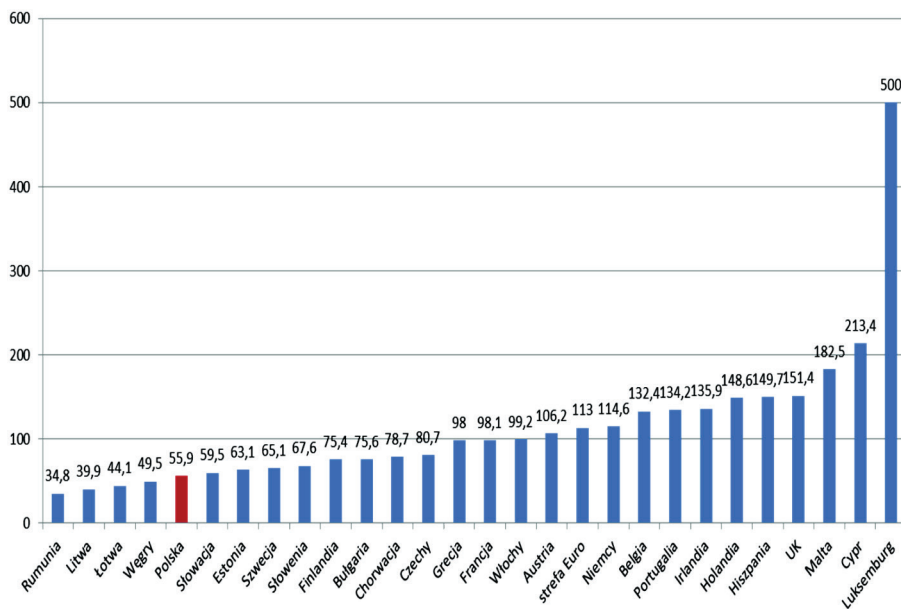
Polish banks played and still play a key role in the development of the Polish capital market. GPW, KDPW, KDPW\_CCP, BondSpot grew thanks to their active involvement. All the leading Polish banks are listed on the Warsaw Stock Exchange, and capital market services are mainly offered by the bank's brokerage offices and directly by the banks.

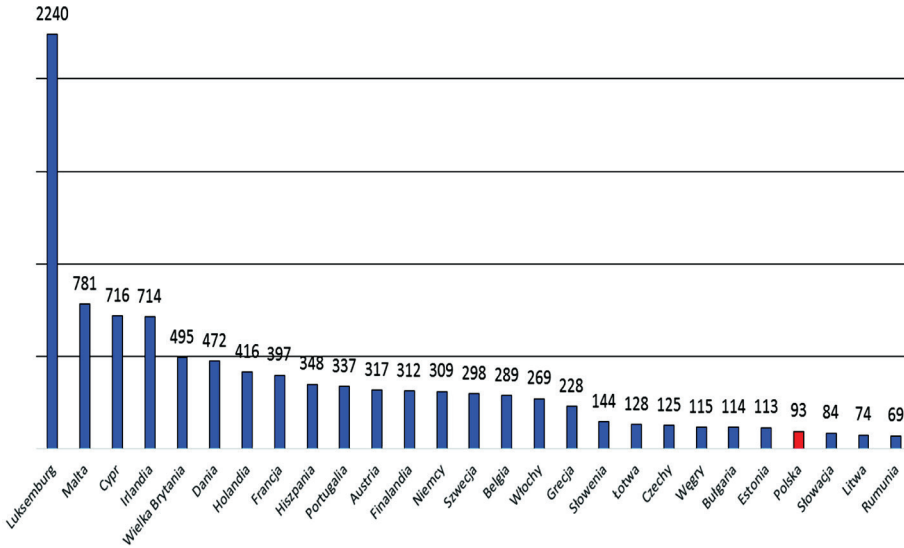
### Remarkable achievements but still a lot to be done

Despite the enormous progress that has been made over the past three decades, the Polish banking sector is still affected by important limitations of the possibilities of financing the economic development. They arise from the consequences of many turbulent historical events which took place during the last hundred years in this part of Europe. As a consequence of those events, the process of building the material capital of citizens and companies was interrupted repeatedly. Human capital was also tragically depleted several times.

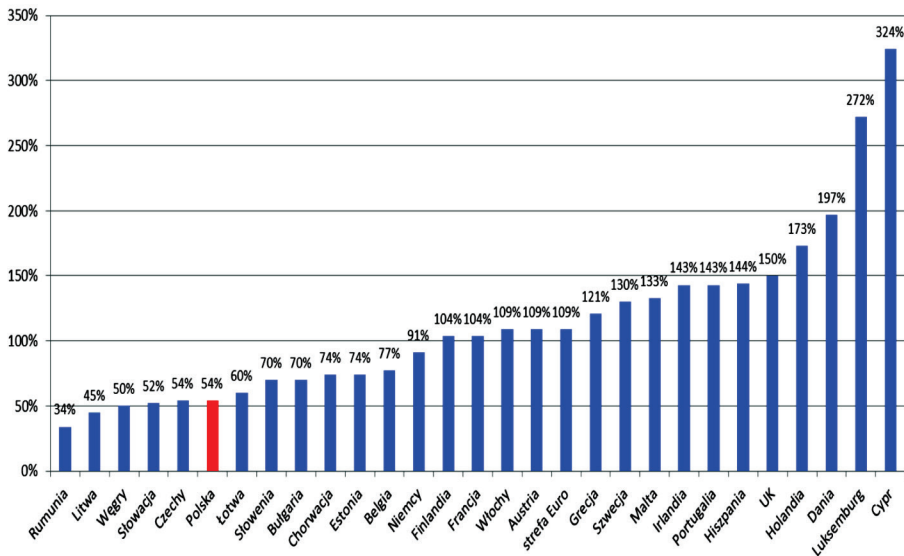
The low capability of the Polish banks to finance the development of the country is manifested by:

- the low rate of savings, including the level of bank deposits;
- the low ratio of the bank's equity to GDP;



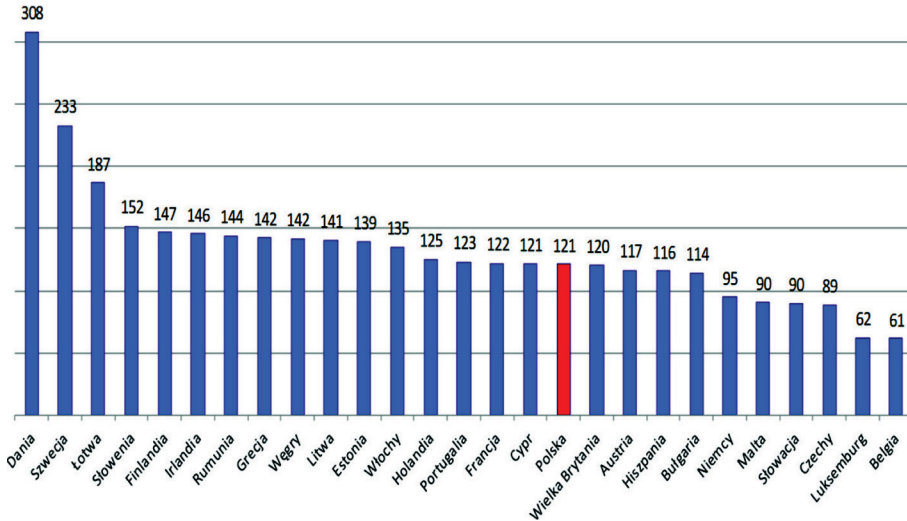


- the low level of assets, including the loans-to-GDP ratio;



- the still small number of citizens using banking services;





- the significant level of lending with the use of foreign funding and the associated currency risk and external economic shocks.

One has to remember that bank loans still play a crucial role in the financing of the economic development in Poland. In the light of the experience from the recent economic crisis, the problem of how to finance the development takes on a strategic importance and requires intense regulatory actions, and in the banks – the work on new business models and organizational efforts.

### **Opportunities, challenges and threats:**

Poland is a country of great *opportunities* and considerable development potential, with more than 1.8 million companies, 700 thousand agricultural holdings which are active in the market and millions of citizens eager for success. The geographical location of Poland, the natural resources and the well-educated workforce lay a solid foundation for the economic success of Poland.

Our presence in the European Union also opens up a great opportunity. An improvement in the economic situation of the euro area countries may ensure that the Polish accession to this club is another important incentive to the accelerated development of the country. This will mean an increase in the investment credibility of Poland, reduced transaction costs, reduced debt servicing costs and increased interest in foreign investment in Poland.

The *challenge* faced by the Polish economy is to maintain continuous labour productivity growth, establish close cooperation between Polish entrepreneurs and the world of science. The necessity is to build a long-term propensity to make pro-development savings for housing, pension, health, and education purposes among the citizens. Poland needs further growth in productive foreign direct investment and further expansion of the Polish companies in terms of investment and exports.

The method of financing the development of companies should undergo a significant evolutionary change. Financing with the use of debt instruments should become more and more widespread. Issues of bonds and mortgage bonds, as well as the possibility of the securitization of good assets on a larger scale should be conducive to the mobilization of financing and re-financing. In addition, the banking sector will be continuously mobilized to raise own funds, maintain a high level of liquidity and to further build the deposit protection funds and the orderly liquidation funds. In cooperative banking, an institutional protection scheme will have to be developed and the business models of the majority of the cooperative banks and the two associating banks will have to be modified.

Some *threats* are also clearly visible on the way to the further development of the Polish banking sector. They include, in particular, the lack of understanding of the role that the banks and other financial institutions play in the social market economy. The lack of understanding of the role of banking entails ignoring the needs of working out a long-term strategy for the development of the sector, as well as the poor-quality and unstable regulations that reduce the legal certainty of business transactions instead of resolving concerns. The lack of understanding of the role of financial institutions in the market economy also means the lack of initiatives by the state aimed at the active development of the propensity not only to save, but also to invest and innovate. As a result, for many years it has been difficult to build a stable system of warranties and guarantees for SMEs in Poland, and solid state guarantees for larger production projects have become rare.

From time to time, one can see initiatives imposing a special burden on the Polish banks in the form of additional levies or taxes, which would mean the deactivation of the banking sector. Many Polish politicians mindlessly attempt to imitate their colleagues from other countries, forgetting that their economies are over-financed, that the taxpayers there have incurred the enormous costs of the recapitalization of banks, whereas in Poland such events have not taken place, and Poland is still a country with a low level of banking penetration.

## SUMMARY

Over the course of the transformation period, the Polish banking sector underwent a rapid and multi-directional development. Solidly serving the customers, banks were simultaneously building their economic potential and took care of their own stability and the security of deposits. There is no stable country without stable banks, just as there is no stable banking system in an unstable country.

The Polish banking sector was and is strictly regulated and closely supervised, even with some symptoms of overregulation. The sector is safe, effective and modern though there are still some serious shortcomings, errors and regulatory delays, which reduce the possibility of providing a quality service to the customers of the banking sector.

Despite the enormous progress which has been made in the development of the sector, banks have a relatively low capability to finance the development of the Polish economy. It is thus necessary to formulate a long-term strategy for the development of Polish banking and the surrounding institutions.

Poland is a country of golden economic opportunities, and the Polish banking system offers similar opportunities. The Polish economy and the banking sector are faced with a number of challenges. Both the Polish economy and the banking sector are not free from threats. The important thing is to counteract the threats, meet the challenges, and seize the opportunities.

After the experience of the last twenty-five years, we can be optimistic about the future. A lot of work is still ahead of us and it is important to know where we are headed.