Creditreform Sovereign Rating

Creditreform Rating
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Rating Object	Rating Information			
REPUBLIC OF POLAND	Assigned Ratings/Outlook: **A /stable**		Type: Monitoring, unsolicited	
Long-term sovereign rating Foreign currency senior unsecured long-term debt Local currency senior unsecured long-term debt	Initial Rating Publication Date: Rating Renewal: Rating Methodologies:		31-03-2017 01-03-2019 "Sovereign Ratings"	

Rating Action

Neuss, 01 March 2019

Creditreform Rating has affirmed the unsolicited long-term sovereign rating of "A" for the Republic of Poland. Creditreform Rating has also affirmed Poland's unsolicited ratings for foreign and local currency senior unsecured long-term debt of "A". The outlook is stable.

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Key Rating Drivers

1. Expectation of moderating but still strong economic growth in 2019/20, underpinned by robust consumption and investment activity; in the medium term, sectoral shift towards higher-value activities should drive further income convergence with the EU
2. Fiscal balance surprised on the upside in 2018 but deficit can be expected to widen again in view of an increasingly pro-cyclical fiscal policy stance; moderate general government debt set to decline further, driven by high nominal GDP growth; elevated FX share in public debt balanced against favorable financing conditions and a stable investor base
3. Sovereign continues to be characterized by generally high quality of its institutional set-up, but key governance indicators have weakened since 2015; tensions with European institutions over rule of law are likely to persist, although government rolled back some elements of controversial judicial reforms
4. Despite highly negative net international investment position, external risks appear limited, given that FDI accounts for the bulk of external liabilities and a broadly balanced current account

Reasons for the Rating Decision

Our assessment of the Republic of Poland's high creditworthiness is reflected in the economy's ongoing convergence with the European Union's income levels on the back of resilient and inclusive economic growth.

The Polish economy has been growing without interruption since 1992; thus the country exhibits one of the longest, unbroken growth streaks among developed economies. In our view, its large domestic market and attractive conditions for FDI have been conducive to Poland's economic success. Buttressed by a favorable business environment and low labor costs, FDI-inflows into the Polish economy have averaged at 3.5% of GDP per year

since the country's EU accession in 2004. Drawing on Eurostat data, hourly labor costs in the manufacturing sector stood at EUR 8.40 in 2017, some 30% of the EU-28 level. At the same time, the country scores comparatively high in international rankings on the quality of its business environment. The World Bank's 2019 Doing Business report ranks Poland 33rd out of 190 economies (17/34 OECD high-income), with only the Baltics faring better among CEE-peers (LT: rank 14; EE: 16; LV: 19). Apart from the effective insolvency framework (rank 25), dealing with construction permits (rank 40) and property registration (rank 41) continue to stand out as Poland's main competitive strengths.

Sustained and balanced GDP growth combined with the implementation of comprehensive social policy measures (see below) has also helped to lower income inequality in the aftermath of Poland's EU accession. Between 2005 and 2017, the Gini coefficient of disposable income fell by 6.4 p.p. – the most significant decrease observed in any EU-28 country. This development should have continued in 2018 in view of growing social benefit expenses and rapidly expanding economic output.

The Polish economy continued to thrive last year. After an already strong 2017 (+4.8%), real GDP growth edged up to 5.1% in 2018 according to preliminary estimates of the National Statistical Office. Thus, Poland experienced the highest growth rate since 2007 (+7.0%) and remained among the fastest growing economies in the EU-28. Last year's economic expansion was entirely driven by strengthening domestic demand. Private consumption, which has been a cornerstone of Poland's macroeconomic performance in recent years, contributed the bulk to the increase in total output (2.6 p.p.). On the back of further improving labor market conditions, rising real wages and social benefits, consumer spending expanded by 4.5% (2017: +4.9%).

Moreover, 2018 witnessed a pick-up in investment activity, with growth in gross fixed capital formation almost doubling from 3.9 to 7.3%.The latest increase in investment was largely driven by higher capital spending by the government sector. Local governments scaled up their investment activities in the run-up to last year's local elections, and EU fund absorption gained further momentum. As illustrated by EU data on ESIF implementation progress, financial resources spent on investment projects rose from 13.7 (2017) to EUR 26.8bn up to Q4-18 (as of 27 February). As a result, public investment rose by 28.5% in nominal terms in the first nine months of the year, on the heels of a 22.9% increase in 2017. On the other hand, private sector investment growth remained relatively tepid, despite the economy's strong momentum. Having almost stagnated in 2017 (+1.2%), capital expenditures of Polish enterprises recorded a growth rate of 4.1% y-o-y in the first nine months of 2018. An EIB investment survey indicates that a shortage of skilled staff and an uncertain regulatory outlook may have prevented a stronger recovery of private investment. As in 2017, net exports made no contribution to GDP growth. Vividly growing domestic demand pushed up import volumes, resulting in a neutral contribution of net external trade in 2018. Balance of payments data reveals that y-o-y growth in imports (+9.6%) slightly outpaced exports between January and November 2018. In nominal terms, the total volume of exports expanded by 7.5% (Jan-Nov-17: 12.3%). This was mainly a result of slowing external demand for Polish goods. While service exports con-

tinued on its 2017 growth trajectory (+12.6%), annual growth in export of goods almost halved from 12.1 to 6.2%.

Thanks to vigorous economic growth, income convergence towards the EU-28 level further progressed in 2018. According to IMF estimates, GDP per capita stood at USD 31,647 (in PPP terms), equivalent to 73.4% of the EU-28 level last year (2017: 71.7%); however, we note that Poland's per capita income remains below the median of A-rated peers (USD 35,962). In the medium term, we anticipate the income gap to narrow further, driven by GDP growth about twice as high as in the EU-28. Having said this, the government's target to broadly eliminate the income gap by 2030 appears rather ambitious given the cyclical position of the economy and the pace of income convergence observed in the past.

Authorities are aware that moving-up the value chain is a prerequisite for sustained income convergence in the coming years. Although the Polish economy can be characterized as diversified and competitive, economic output is still concentrated in lower productivity services such as trade, transport and accommodation, which contributed one fifth (22.2%) to GDP alone in 2017. At the same time, the share of high value-added services remained relatively low. At the latest count, ICT and professional services made up for only 3.7 and 7.3% of GDP respectively, which compares low to the EU-28 as a whole (4.5 and 9.9% of GVA). Nevertheless, Poland is in the process of transforming into a modern service economy. Between 2013 and 2017, gross value added of ICT and professional services and grew by 39.1% 28.0 respectively, outpacing the overall increase in gross value added (+15.5%) by a wide margin. In the medium term, the implementation of the government's "Strategy for Responsible Development", adopted in February 2017, could help to accelerate the shift towards knowledge-intensive services. The strategy proposes to promote innovation and digitization, as well as an increase in high-tech manufacturing exports.

Going forward, GDP growth should taper off, prospectively falling back to 3.5 and 3.1% in 2019 and 2020, respectively. Given our expectation that economic growth in Poland's key trading partners (Germany, Czechia, and the United Kingdom) has peaked, export dynamics are likely to slow down over the coming two years. Weaker exports should be matched by decelerating imports due to less vibrant domestic demand. To be sure, we expect both consumption and investment to experience robust growth in the near term. Regarding investment, activities should increasingly shift from the public to the private sector. Although the inflow of EU funds into the Polish economy will continue over the next two years, we expect fund utilization to normalize after the extraordinarily strong absorption seen in 2018, curbing growth in public investment. By contrast, business investment in machinery and transport equipment should strengthen in light of favorable financing conditions and high capacity utilization. Spare capacity in the manufacturing sector remains tight, pointing to an increasing need for a build-up of additional production capacities. At the beginning of 2019, capacity utilization is still running significantly above its long-term average (Q1-19: 81.6% vs. 1992-2018 avg. 73.8%) and remains close to its all-time high marked in Q2-18 (83.4%). Meanwhile, the ease of zoning requirements passed in Jul-18, and the ongoing implementation of the government's rent-to-own hous-

ing scheme (“Home Plus”) should bode well for residential construction. A record-high number of building permits granted last year also points to strong construction investment in 2019. The number of permitted dwellings increased for the fifth consecutive year in 2018 (257,100), reaching the highest number in 19 years.

Sustained growth in headline investment should coincide with robust consumer spending. Underpinned by upbeat consumer sentiment, private consumption is set to remain the main driver of GDP growth. Although the European Commission’s Economic Sentiment Index somewhat weakened in the second half of 2018, falling from 109.1 (Jul-18) to 101.3 points (Jan-19), consumer sentiment is still consistent with solid growth in private consumption. In general, household spending should be supported by enduring employment growth and a further rise in disposable incomes. Alongside a minimum wage hike, which entered into effect at the beginning of the year, sustained nominal wage growth in the private sector should bolster consumers’ purchasing power. Nevertheless, real wages are expected to grow less dynamically than seen in 2018 in view of gradually increasing price pressures. After CPI inflation came in at a moderate 1.6% in 2018, inflation should slightly increase this year (2019e: 2.3%), dampening further gains in households’ purchasing power. In addition, households have only limited room to expand consumption by drawing down on their savings. In the year up to Q3-18, the household savings rate fell from an already low 1.5 to 0.7%. As a result, we expect growth in consumer spending to soften somewhat in 2019/20.

In general, we assess Poland’s medium-term growth prospects will remain favorable. Still, some downside risks to the economy’s growth outlook have to be pointed out. Most importantly, Poland is facing a sharp decline in its working-age population. While negative net migration has significantly slowed from -108,739 (2011) to -28,139 persons (2016), population ageing is expected to put pressure on labor supply going forward. According to the EU 2018 Ageing Report, Polish working-age population is forecasted to experience one of the steepest declines in Europe over 2016-30, falling by 6.1 p.p. In view of a declining working-age population, investment-driven productivity gains are crucial to sustain the catching-up process in terms of per capita income. However, private sector investment activity remains muted, partly mirroring regulatory uncertainties and limited public consultation in the legislative process in recent years. In 2017, Poland’s private investment-to-GDP ratio was the lowest among CEEs (14.0%) and the third lowest in the EU-28 (17.3%). Lifting private investment will become even more important in the event of a significant cut of Poland’s cohesion fund allocations in the EU’s 2021-27 budget cycle. As highlighted by a European Commission proposal presented in May-18, Poland could see a 23% drop in its fund allocations compared with the 2014-20 funding period.

To tackle these issues, boosting labor participation and capital accumulation appears essential. Regarding the latter, we note that the government is pushing ahead with reforms to improve business conditions and stimulate corporate investment by granting tax benefits. Last year, a comprehensive set of laws known as the “Constitution for Business” entered into force (Apr-18), which aims to reduce the administrative burden for entrepreneurs. The new legislation also aims at reducing regulatory uncertainty by the introduction of a new principle according to which public authorities are obliged to interpret unclear

provisions in favor of entrepreneurs. In June, the “Constitution for Business” was complemented by the adoption of a new investment bill. The bill extends the benefits of the country's special economic zones to the entire country by offering tax incentives to investors for the period of 10-15 years.

By contrast, recent government policies should have a neutral effect on labor supply at best. While the introduction of additional pension and family benefits since 2015 has undoubtedly reduced income inequality, there is a risk that the lowering of the statutory retirement age, as well as the “500+” child benefit scheme, reduce incentives to work for the elderly and women. In this context it has to be emphasized that Poland’s labor participation rate (15-64y) of 70.3% in Q3-18 already compares unfavorably with the EU as a whole (73.8%) and is some 10 p.p. lower than in the best-performing member states such as the Netherlands (80.4%) and Sweden (83.0%). We acknowledge that participation rates of the elderly and female population have not deteriorated yet. Nevertheless, labor participation of these groups should be monitored closely in order to assess the eventual impact of the implemented welfare policies.

With regard to 2018, the labor market situation continued to improve. Unemployment fell from 4.9 (2017) to 3.8%, reaching its lowest level since 1997. Thus, Poland’s unemployment rate also remained among the lowest in the EU-28 (avg. 8.3%). Meanwhile, employment growth continued, but showed signs of a slowdown. Employment growth, which had averaged at 1.3% in 2014-17, moderated to only 0.4% (Q3-18, s.a.) at the latest count. As evidenced by hard and soft data, slowing employment is rather a result of pronounced labor shortages than of weakening labor demand. EU Commission survey data points to an increasingly tight labor market. As of Q1-19, the share of respondent NFCs from the industry (40.9%) citing staffing issues to be a restricting factor to the production process was the second highest in the EU-28. Supply-side constraints are also indicated by accelerating wage dynamics. After average monthly gross wages and salaries had risen by 6.1% in 2017, wage growth accelerated to 7.1% last year. We believe that wage growth would have been even stronger without the continued inflow of foreign workers – in particular from the Ukraine. As revealed by social security insurance (ZUS) data, the number of insured Ukrainians has continued to increase rapidly in 2018. Up from 308,000 in 2017, the number of Ukrainians registered with the ZUS surged to 426,000 in Q3-18. Thus, the number of working immigrants from the Ukraine has almost quintupled within three years (2015: 91,000). In order to address labor shortages, Poland adopted new immigration rules in Jan-18, making it easier to engage seasonal workers from outside of the EU in agriculture, tourism, and accommodation. As Poland faces increasing competition for Ukrainian workers as of Jan-19, when Germany's easing of labor market requirements for non-EU citizens commenced, the Polish government plans to further facilitate the process for obtaining work permits, as well as extending their duration.

Despite strong wage growth in 2017/18, there are no signs of a deterioration in cost competitiveness yet. From a cross-country perspective, Poland’s unit labor costs (ULC) evolution in 2018 still compares favorably to its main trading partners. As of Q3-18, nominal ULC in the Polish economy was almost flat (+0.5%) y-o-y; at the same time, ULCs in France, Germany, and the Czech Republic increased by 1.3, 3.1 and 7.1%, respectively.

Furthermore, export performance does not warrant immediate concerns about cost competitiveness. The country's global export market share has been steadily on the rise in recent years, increasing by 28.6% in 2012-17.

Our credit assessment also factors in the sovereign's sustainable public finances mirrored by moderate debt levels, favorable financing conditions, and a buoyant fiscal performance in recent years. We note that the sovereign's budgetary position continued to strengthen in 2018, as the fiscal deficit should have narrowed from 1.4 (2017) to 0.6% of GDP last year. Our expectation is underpinned by quarterly budgetary data, according to which the government accounts reported a surplus of PLN 4.9bn up to the third quarter of 2018 (Q1-Q3 2017: PLN -9.2bn). Fiscal consolidation was primarily driven by briskly growing revenues. Growth in government revenues gained momentum in the first nine months, exceeding the previous year's level by 8.1%. Taxes on income, wealth, and social security contributions were boosted by rising wages and employment, and expanded by 14.3 and 8.4% y-o-y, respectively. In addition, the implementation of new tax compliance measures translated into higher VAT receipts (+8.8%). Among others, Poland introduced a VAT split-payment regime last year (Jul-18), and an obligation for all companies to file a Standard Audit File for Tax (SAF-T) electronically.

On the expenditure side of the budget, public investment and social benefits recorded high y-o-y growth rates, contributing the bulk (75%) to the overall increase in spending. Mirroring an accelerating implementation of EU co-funded investment projects, spending on public investment in the first nine months came in 28.5% higher than in the previous year. At the same time, spending on social benefits edged up by 6.6%, partly reflecting the impact of the 2017 pension reform. In the first half of 2018 the number of persons receiving pension benefits increased sharply by 267,400.

This year, procyclical fiscal policies are set to become even more expansionary. We expect the headline deficit to widen to 1.8% of GDP, as the recently adopted state budget 2019 envisages fast growing expenditures. While public investment should lose some momentum, higher spending on public servant wages and the continuing implementation of the government's key welfare projects will keep expenditure pressure high – in particular, the government plans to expand its support for families in 2019. The flagship "Family 500+" child benefit scheme introduced in 2016, which costs about 1.1% of 2017 GDP per year, will be supplemented by additional financial benefits for schoolchildren. Under the "Good Start" program, families will receive PLN 300 per year for each child to cover education-related expenses. Starting from Mar-19, Poland will pay out a new minimum pension applying to mothers of four or more children. According to Ministry of Finance estimates, costs for maternal pensions will total at about PLN 0.8bn per year.

Turning to the revenue side of the budget, we expect favorable dynamics to carry over into 2019. Nevertheless, we anticipate growth in tax receipts and social security contributions to moderate somewhat, mirroring slowing job creation and softening economic activity. Moreover, the introduction of a reduced 9% CIT rate for small businesses and lower excise taxes on electricity will curb the expansion of state revenues going forward. To mitigate the impact of tax relief and additional spending on the state budget, Polish authorities launched a new set of tax compliance measures. Among others, changes to the

withholding tax, stricter information requirements on tax planning, and efficiency gains in the revenue administration should yield additional revenues.

We think there are some downside risks related to the uncertainty of further tax compliance gains and intensifying spending pressure in the run up to this year's parliamentary elections. Our expectation is underpinned by recently revealed plans for a pre-election fiscal stimulus package, which goes beyond the measures introduced with the 2019 budget. The implementation of tax exemptions for young workers, extra payments for pensioners and higher transport investment could add up to PLN 40bn, thereby putting compliance with the deficit target at risk. Regarding tax collection, we acknowledge that Poland has made significant strides in recent years, with the VAT gap narrowing from 23.9 to 14.0% in 2015-17. In view of this sharp decline within such a short period, further improvements could prove increasingly difficult.

The sovereign's debt-to-GDP ratio, which totaled at 50.6% of GDP in 2017, should have dropped below the 50%-mark last year, and we expect deleveraging to continue gradually in 2019/20. Although the government's debt burden is moderate by European standards, the composition of the debt stock points to an elevated exposure to FX risks, as a comparatively large share of treasury debt is denominated in foreign currencies. In Dec18, foreign currency debt, which is dominated by EUR and USD borrowing, accounted for 29.3% of the state's total debt stock, down from 30.6% in Dec-17 (Dec-16: 34.4%). Refinancing risks are, however, mitigated by a stable foreign investor base (end of 2018: central banks and public institutions: 29.3%; investment funds: 23.1%) and favorable refinancing conditions. After having trended sideways for most of the year, 10y government bond yields started to decline in the final quarter of 2018, falling from 3.3 (Oct) to 2.8% (Jan-19). Recent monetary policy decisions should help to keep bond yields low for the foreseeable future. At its February meeting, the NBP's Monetary Policy Council decided to maintain its accommodative monetary policy stance. Reflecting softer growth and inflation projections, market expectations signal that a first interest rate hike should occur not before 2021. According to NBP governor Glapinski, monetary tightening may start even later. In January Glapinski stated that the reference rate could remain at its current record-low of 1.5% into 2022.

Turning to financial market policies, we note that governmental efforts aim to strengthen the domestic financial market and reduce dependence on foreign capital and financial institutions. Currently, authorities are elaborating a new capital market strategy in order to ease capital market access of NFCs and improve transparency standards. Together with the recently-introduced occupational pension scheme (PKS), the implementation of the strategy should boost domestic savings and deepen local capital markets.

Poland's moderately-sized banking sector (assets-to-GDP: 89.9% of GDP in Q3-18) is in good shape. As measured by EBA data, banks have sufficient capital buffers, as the CET 1 ratio stood at 16.3% in Q3-18 broadly unchanged from 16.5% a year before and slightly above the EU average (avg. 14.7%). Concurrently, improving asset quality is reflected by a further fall in the NPL ratio, which posted at 5.3% after standing at 6.0% in Q3-17. Financial stability risks associated with excessive credit growth appear largely contained. Loans outstanding to NFCs and households exhibited growth rates in the 5-6% range in

the second half of 2018. Hence, the expansion in total credit remained broadly aligned with nominal GDP growth; however, some attention should be paid to the trajectory of consumer loans, which have continued to grow dynamically (7-9%) throughout 2018. Although there are no signs of a weakening credit quality of consumer loans at this stage, this lending segment has carried disproportionately high impairment risks in the past.

Notwithstanding our belief that the financial sector harbors limited contingent liability risks at the moment, we note that the state and banks have become more intertwined since the current government entered office in 2015. The state holds controlling stakes in eight out of thirteen domestic commercial banks, including PKO Bank Polski and Bank Pekao, the country's largest banks by assets. Following the introduction of a 0.44% special tax on bank assets (excluding government bonds), banks' exposure to government securities has risen. Since the end of 2015 the share of Polish treasury debt in total bank assets has edged up from 11.5 to 14.7% (Nov-18). Against the background of already close links between banks and the state, we have some reservations as regards the recent changes to the financial supervisory framework. Looking forward, the legislative amendment passed in Nov-18, which provides the state with a blocking majority on the board of the Financial Supervision Authority (KNF), may potentially entail conflicts of interest and thus hamper effective financial sector supervision.

Our institutional assessment balances Poland's economic and political integration in the European Union, prudent monetary policies, and generally high levels of government effectiveness, against concerns related to a weakening of judicial independence.

The sovereign benefits from EU membership, involving the adoption of common stand-ards and rules, trade integration and, most importantly, significant financial support via EU funds. Being eligible to draw up to EUR 86.1bn of EU funding during the 2014-20 funding period, Poland is the largest beneficiary of ESI funds in absolute terms. Apart from that, Polish citizens make extensively use from the free movement for persons in the EU, which allows them to take up work in member states with higher wage levels. In 2017 about 2.5mn Polish citizens lived abroad, most of them in Germany, Ireland and the UK.

Although Poland features a generally high institutional quality, the country scores below average on all of the World Bank's World Governance Indicators (WGI) as compared with its A-rated peers. Notably, we observe a marked deterioration in 2015-17 regarding the quality of the legal framework and the freedom of expression. In the World Banks's latest assessment, Poland ranks 56th and 67th out of 209 countries on the WGI sub-indices voice & accountability and rule of law, down from rank 38 and 49 in 2015. We believe that Poland's slippage on these indicators may at least partly explained by an increasing gov-ernmental influence on the media, the judiciary and the banking sector. While there are no apparent signs for an erosion in investor confidence, a continuation of these rather interventionist policies may weaken the country's attractiveness for FDI in the longer run. This appears in particular important given our belief that sustained foreign capital inflows are needed to foster income convergence in the years ahead.

At the current junction, we see no signs of a fundamental change in administration's agenda even though it has recently revised parts of its controversial judicial reform. In

Sep-18, the European Commission (EC) decided to take Poland to the European Court of Justice (ECJ) over judicial reforms which the EU says could threaten the independence of the Polish judiciary. The ECJ finally ordered Poland to suspend the law on the lowering of retirement age of Supreme Court judges. The law had forced some judges to retire immediately, effectively enabling PiS to select their replacements. Nevertheless, we believe that tensions with the EU are here to stay. The EC still advances with the Article 7 procedure against Poland, as there are several other contentious pieces of legislation. Laws enabling the government to name the next chief of the Supreme Court and to choose the members of the National Judiciary Council (KRS), which appoints judges, are still in force. Taking into consideration that the ruling PiS party emerged stronger from the 2018 local elections and also leads the polls for the next parliamentary elections (Oct-19), further policy reversals appear rather unlikely. Notwithstanding our expectation that an imposition of EU sanctions is not likely in the near term, the Article 7 process could play an important role when EU members begin their negotiations on the EU's 2021-27 budget cycle. The European Parliament as well as some EU members have pushed to make access to future EU funding conditional on respecting democratic values such as the rule of law and judicial independence.

Risks related to Poland's external position are broadly balanced. After Poland had run a small current account surplus in 2017 (0.2% of GDP) for the first time since it entered the European Union, the current account weakened somewhat more recently. In the year up to September, Poland's current account balance slipped to -0.5% of GDP mainly due to a deteriorating trade in goods balance. In particular, rapid growth in EU co-funded government investment boosted imports last year. As a result, the trade in goods balance turned negative again, falling from 0.3 (2017) to -0.7% of GDP in Q3-18. Turning to trade in services, latest quarterly data suggests that positive developments have continued in 2018. In Q3-18 the trade in services surplus ticked up to 4.3% GDP (2017: 3.8% GDP).

Looking ahead, we expect the current account to post moderate deficits of around -1.0% of GDP, as strong wage growth and sustained ESI absorption should continue to stimulate imports. As with most other transition economies, Poland is an international net debtor, indicated by a comparatively large and negative net international investment position (NIIP), which came in at -59.3% of GDP in Q3-18 (2017: -61.0% of GDP). Although this implies elevated external vulnerabilities, we believe that risks associated with a high level of externally held liabilities are somewhat mitigated by the composition of the NIIP. As NBP data reveals, foreign direct investment accounted for almost half (46.0%) of external liabilities in Q3-18. Moreover, last year's increase in reserve assets has further enhanced the sovereign's capability to service its external debt in the event of adverse economic conditions. Between July and October, the NBP took advantage of declining gold prices and added 826,000 ounces to its gold reserves – equivalent to Poland's biggest purchase since 1998, and one the largest additions by a European Union member since then.

Rating Outlook and Sensitivity

Our outlook on the long-term sovereign rating is stable, as we assume that the risk situation underlying the key factors affecting sovereign credit risk – including macroeconomic performance, institutional structure, fiscal sustainability, and foreign exposure – is likely to remain fundamentally unchanged over the next twelve months.

We could raise our sovereign rating if medium-term growth turns out to be substantially higher than in our baseline scenario, resulting in accelerating income convergence towards EU-28 levels. Upward pressure on the rating could also arise if public finances improve on a sustainable basis, thus resulting in a steeper-than-anticipated downward trend of general government debt, or if reforms lead to a significant improvement in institutional quality.

A negative rating action could be prompted if, contrary to our belief, significant fiscal slippages were observed, leading to a reversal in the sovereign's debt-to-GDP ratio in the years beyond 2018. More generally, we could also consider a downgrade if key governance indicators continue to deteriorate as a result of additional institutional reforms, raising concerns about the independence of the judiciary. Weakening the country's institutional framework could eventually lead to an erosion of international investor confidence as well as to a lower allocation of ESI funds in the EU's next multiannual budget.

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Ratings*

Long-term sovereign rating	A /stable
Foreign currency senior unsecured long-term debt	A /stable
Local currency senior unsecured long-term debt	A /stable

*) Unsolicited

Economic Data

	2013	2014	2015	2016	2017	2018e	2019e
Real GDP growth	1.4	3.3	3.8	3.1	4.8	5.1	3.5
GDP per capita (PPP, USD)	24,119	25,413	26,680	27,801	29,642	31,647	33,472
Inflation rate, y-o-y change	0.9	0.0	-0.9	-0.6	2.0	1.6	2.3
Default history (years since default)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Life expectancy at birth (years)	77.1	77.8	77.5	78.0	n.a.	n.a.	n.a.
Fiscal balance/GDP	-4.1	-3.7	-2.7	-2.2	-1.4	-0.6	-1.8
Current account balance/GDP	-1.3	-2.1	-0.6	-0.5	0.2	n.a.	n.a.
External debt/GDP	69.8	72.7	71.8	76.4	66.9	n.a.	n.a.

Source: International Monetary Fund, Eurostat, NBP, own estimates

Appendix

Rating History

Event	Publication Date	Rating /Outlook
Initial Rating	31.03.2017	A /stable
Monitoring	02.03.2018	A /stable
Monitoring	01.03.2019	A /stable

Regulatory Requirements

In 2011 Creditreform Rating AG (CRAG) was registered within the European Union according to EU Regulation 1060/2009 (CRA-Regulation). Based on the registration Creditreform Rating AG is allowed to issue credit ratings within the EU and is bound to comply with the provisions of the CRA-Regulation.

This sovereign rating is an unsolicited credit rating. The Polish Ministry of Finance (MoF) participated in the credit rating process as the authorities commented on a draft version of this report. Thus, the report represents an updated version, which was augmented in response to the factual remarks of MoF. The rating outcome as well as the related outlook remained unchanged.

The rating was conducted on the basis of CRAG´s “Sovereign Ratings” methodology in conjunction with its basic document “Rating Criteria and Definitions”. CRAG ensures that methodologies, models and key rating assumptions for determining sovereign credit ratings are properly maintained, up-to-date, and subject to a comprehensive review on a periodic basis. A complete description of CRAG´s rating methodologies and basic document “Rating Criteria and Definitions” is published on the following internet page: www.creditreform-rating.de/en/regulatory-requirements/.

To prepare this credit rating, CRAG has used following substantially material sources: International Monetary Fund, World Bank, Organization for Economic Co-operation and Development, Eurostat, European Commission, European Banking Authority, World Economic Forum, Central Bank of Poland, Republic of Poland - Ministry of Finance, Statistics Poland.

A Rating Committee was called consisting of highly qualified analysts of CRAG. The quality and extent of information available on the rated entity was considered satisfactory. The analysts and committee members declared that the rules of the Code of Conduct were complied with. No conflicts of interest were identified during the rating process that might influence the analyses and judgements of the rating analysts involved or any other natural person whose services are placed at the disposal or under the control of Creditreform Rating AG and who are directly involved in credit

rating activities or approving credit ratings and rating outlooks. The analysts presented the results of the quantitative and qualitative analyses and provided the Committee with a recommendation for the rating decision. After the discussion of the relevant quantitative and qualitative risk factors, the Rating Committee arrived at a unanimous rating decision. The weighting of all risk factors is described in CRAG´s “Sovereign Ratings” methodology. The main arguments that were raised in the discussion are summarized in the “Reasons for the Rating Decision”.

As regards the rating outlook, the time horizon is provided during which a change in the credit rating is expected. This information is available within the credit rating report. There are no other attributes and limitations of the credit rating or rating outlook other than displayed on the CRAG website. In case of providing ancillary services to the rated entity, CRAG will disclose all ancillary services in the credit rating report.

The date at which the credit rating was released for distribution for the first time and when it was last updated, including any rating outlooks, is indicated clearly and prominently in the rating report; the first release is indicated as “initial rating”; other updates are indicated as an “update”, “upgrade or downgrade”, “not rated”, “affirmed”, “selective default” or “default”.

In accordance to Article 11 (2) EU-Regulation (EC) No 1060/2009 registered or certified credit rating agency shall make available in a central repository established by ESMA information on its historical performance data, including the ratings transition frequency, and information about credit ratings issued in the past and on their changes. Requested data are available on the ESMA website: https://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml.

An explanatory statement of the meaning of each rating category and the definition of default are available in the credit rating methodologies disclosed on the website.

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