Quarterly 4/2000 (7)

POLISH ECONOMIC OUTLOOK

TRENDS • ANALYSES • FORECASTS

Summary

3Q00 saw a slight deterioration in the Poland's economic situation in comparison to the previous quarter. External imbalances (measured by the current account deficit) improved, whereas the domestic environment worsened - both inflation and unemployment rates edged up.

According to our estimates, GDP rose 4.2% yoy and domestic demand 2.4% yoy. Dampened import growth (due to a slowdown in domestic demand) coupled with strong exports resulted in a decrease in the current account deficit. The annual cumulative deficit dropped from 8.3% of GDP in 1Q00 to 7.2% in 3Q00.

Among favourable developments we can point out the continued improvement in economic efficiency reflected in a decline in labour unit costs as well as in the double-digit growth of labour productivity in industry that has been recorded since the second half of 1999.

High unemployment and the upsurge in inflation proved the most worrying developments in 3Q00. In our view, supply-side factors driving inflation have ceased to operate, and a tight monetary and budgetary economic policy may lower inflation significantly in the short term. We forecast that the end-2001 NBP inflation target (i.e. 6-8%) will be reached as early as in March 2001 and the CPI will stay below 6% at end-2001. The average annual increase in prices will amount to 7.3% in 2001 and 5.8% in 2002.

We forecast the economy to stay on a relatively fast track. In the years 2000-2002 GDP may grow at 4.8%, 5.5% and 5.8%, respectively. This will be possible due to the continued robust performance of Polish exports, despite the tight monetary policy suppressing domestic demand.

In our view, it will not be possible to lower the official unemployment rate considerably in the next two years notwithstanding relatively fast GDP growth. The increased inflow of baby-boomers to the labour market, coupled with weaker labour demand (mainly due to restructuring), will lead to stabilisation of the unemployment rate at around 14%.

The years 2001-2002 will see the weakening of the zloty appreciation trend and an improvement in the deficit in the current account. The latter will reach 5.8% and 5.2% of GDP in 2001 and 2002, respectively. The future inflow of foreign capital will cover the current account deficit with a safe margin and foreign currencies reserves may rise.

The Center for Social and Economic Research - Foundation (CASE) presents its seventh issue of Polish Economic Outlook (PEO) prepared by CASE economists.

In this issue, we analyse the economic situation in Poland in 3Q00. We present the key short and long-term threats as well as the most recent economic outlook. For the first time forecast, a for 2002 is included.

All estimates and forecasts are derived from data available until end-October 2000. One should note that various data for previous years are updated in line with changes in official statistics.

We kindly remind our readers that the PEO is available in hard copy as well as in PDF file format - both in English and Polish.

For information about subscription please contact Ms Anna Grom at the CASE-Advisors Ltd. (pgtop@case.com.pl) or check the web site (www.case-doradcy.com.pl).

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POLISH ECONOMIC OUTLOOK
TRENDS • ANALYSES • FORECASTS

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Mirosław Gronicki

Editorial Assistant
Łukasz Rawdanowicz

Author
Mirosław Gronicki

Co-Authors
Rafał Antczak – monetary and exchange rate policies
Piotr Bujak – statistical analysis
Mariusz Jarmużek – econometric and statistical analysis, prices, and interest rates
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CeDeWu Graphic Design (ANB Studio),
Agnieszka Natalia Bury

Publisher

CASE – Center for Social and Economic Research Foundation
Sienkiewicza 12, 00-944 Warsaw, Poland
tel.: (4822) 622 66 27, 828 61 33, fax (4822) 828 60 69
e-mail: case@case.com.pl, www: case.com.pl

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Distributor PG TOP
CASE Advisers Ltd.
ul. Sienkiewicza 12, 00-944 Warszawa
tel./fax (48 22) 525 41 12
e-mail: doradcy@case.com.pl

Center for Social and Economic Research

Assessment of the economic situation in 3Q00

Poland's economic situation in 3Q00 was comparable with that of 2Q00. While the current account of the balance of payments relatively improved, domestic stability has deteriorated, which has manifested itself, among other things, in the following:

- **an increase in the registered unemployment rate (14.0% end-September)**
- **an increase in the CPI, up from 10.0% in 2Q00 to 10.8% in 3Q00**
- **a drop in average real wages and salaries and real average social benefits**
- **a low general household propensity to save**
- **a high level of nominal and real interest rates**
- **a decreased level of growth in industrial output**
- **a drop in construction output.**

Among transpired positive trends, we can distinguish the following:

- **a strong growth in exports to the EU and CIS countries**
- **a relative stabilisation of the current account**
- **a marked growth in labour productivity (over 12%) with a drop in unit labour costs**
- **a reduction in the government budget deficit, compared to 1999.**

Tighter monetary policy

After Poland experienced another bout of inflation in July 2000, the Monetary Policy Council (MPC) raised basic interest rates on August 30, 2000. The considerable weakening of domestic demand and an unchanged fiscal policy – compared to the previous quarter – has necessitated further tightening of the monetary policy. According to the MPC, the hike in interest rates was aimed at curbing inflationary expectations, assuming the occurrence of second-wave inflation stimuli triggered by a sharp increase of food and oil prices.

The increasingly tightening of monetary policy destabilises the existing balance between the actual fiscal policy (perceived as moderately restrictive) and the correspondingly restrictive monetary policy.

The weakening of domestic demand

There has been a marked slowdown in domestic growth of demand, as in the previous three quarters. We estimate that while GDP rose by 4.2% yoy in 3Q00, domestic demand increased by a mere 2.4%. It should be noted at this point that our estimate is based on incomplete foreign trade data. If foreign trade deficit improved more than currently estimated, then the growth in domestic demand might be even lower.

Nonetheless, domestic demand growth has been lower than GDP growth for the last four quarters. The slowdown in domestic demand growth results primarily from the aforementioned tighter economic policy and considerably weaker real income growth. We are of the opinion that forming a coherent and restrictive economic policy is imperative to further reduction of the high current account deficit.

Industrial and construction output

The weakening of domestic demand was the key factor responsible for slowing industrial output growth. It fell from 9.6% yoy in 2Q00 to 6.6% yoy. Nevertheless, positive trends in basic productivity parameters of the economy have still been recorded. Labour productivity is on the increase (over 12%) while unit labour costs are down. In addition, import costs from EU countries are lower because of the weak euro. However, the weak European currency, along with high crude oil prices, has reduced Polish exporters' profits. We believe that efficiency gains are currently stronger, that making it possible to improve the financial situation of enterprises.

Weak investment demand, rising construction sector costs (until 3Q00 growth in construction output prices was higher than the manufacturing sector's PPI), and the previously discussed tight monetary policy led to a drop in construction sector output. According to the CSO, output in 'large building companies' fell in 3Q00 by 3.0% yoy.

An increase in inflation

Inflationary pressures increased again in 3Q00. The CPI rose by 10.8% yoy and the PPI by 8.5%.

The reasons behind the hike in prices lie primarily on the supply-side: the supply of grains and processed food was down, fuel prices worldwide went up and electricity prices continued to rise. On the demand side, money supply, consumer credit, and wages and salaries remained under control.

The zloty's exchange rate

The zloty remained relatively strong continuing the trend from the last two quarters. We estimate nominal depreciation to be at 2%. However, according to JP Morgan, the effective real exchange rate was almost 8% higher in September than in May of this year. Largely, this stems from a considerable nominal euro's depreciation against the dollar (by about 5% from end-May to end-September) and a high share of total Polish foreign trade with the euro area.

At the same time, high volatility in exchange rate fluctuations was due to very low transaction volumes in the inter-bank market despite the floating of the exchange rate.

Money supply and demand

In 2000, the NBP expanded the range of instruments of the monetary policy (sterilisation account, conversion of the State Treasury's securities). This along with a tight monetary policy, budget deficit realization, and the lack of considerable inflows of short-term and long-term capital in 3Q00; led to a drop in reserve money supply by 3.2% compared to year end-1999.

The reduction of reserve money supply, given the stable money multiplier, gave rise to growth in M2 of 14% in 3Q00 yoy (and 6.7% since the beginning of 2000). Given the decreasing net budget debt (as a result of selling the State Treasury's liabilities from the NBP's portfolio) the private sector's increased use of credit was the key factor in M2 money supply growth.

An improvement in the trade and current account deficits

Polish exports have been improving since the end of 1999. According to preliminary data, exports (on the payment basis) reached US$7.2 billion in 3Q00, which is more than in the previous quarter and in 3Q99. Growth in export volume, according to our estimates, decreased slightly to about 18.1% compared to last quarter. In 3Q00, a further slowdown in imports occurred due to weak domestic demand.

Because of the improvement in exports and weaker growth in imports, there has been a relative stabilisation of the trade and current account deficits, which reached US$2.3 billion, according to preliminary estimates. The improved current account deficit was also due to the rescheduling of interest payments on the Polish government's debt from September to October.

Higher unemployment

Demand for labour continues to decrease. In 3Q00, according to the CSO, employment in the private sector fell by 2.2% yoy, in manufacturing alone by about 5.5%. Despite the seasonal increase in labour demand in the services sector, there was an upswing in the unemployment rate from 13.6% in June to 14.0% in September 2000. For the sake of comparison, the unemployment rate stood at 12.1% in September 1999. We envisage that the unemployment rate according to the LFS (Labour Force Survey) followed the same pattern. In 2Q00, the unemployment rate stood at 16.3% and we estimate that in 3Q00 it could be with a range of 16.1−16.4%.

A drop in real household income growth

For the first time since 4Q93, average real wages and salaries in the enterprise sector dropped by 0.5% yoy. Consequently, aggregate real wages and salaries of those employed in this sector decreased (it concerns over 5.1 million people, i.e. over 31% of the total workforce). In addition, social support benefits fell by 5% in real terms.

Household propensity to save remained low compared to 1999. Low savings were not enough to offset weak growth in real incomes, and consequently household consumption decreased.

Reduction in the general government budget deficit

As in the previous quarter, 3Q00 turned out to be favourable for the budget. Higher-than-expected inflation relatively increased tax revenues. Moreover, ZUS increased revenues by improving tax collection effectiveness, and by benefiting from faster economic growth. Fixing growth of social benefits at a relatively low level has made it possible to contain expenditure growth. As of the end of 3Q00, government expenditures reached 90.8% of the planned budget for 2000.

To sum up, in 3Q00 negative trends shifted from external imbalances to internal imbalances. The relative improvement of the current account deficit (although still significant) has occurred due to a big jump in exports offset by negligible import growth. To compensate, Poland's economy experienced a sharp increase in unemployment, a slowdown in industrial production, a drop in construction output, and a hike in inflation.

Determinants of Poland's economic development

We have not changed the assumptions of our forecast concerning the domestic environment since the release of the last issue (PEO 3/2000). However, the first signs of a slowdown in the US and an improvement in the economies of Russia and other CIS countries have made us revise our external assumptions.

In this issue, for the first time, we present our forecast for 2002.

Trends in the world economy, 2000–2002[1]

- **Global growth on a slower track**
- **High oil prices a threat to economic growth and price stability**
- **Continued sizeable depreciation of the euro**

The global economic situation remains stable, but a number of downside risks are beginning to emerge. According to the forecasters' consensus, growth is expected to slow down next year. The US will remain the engine of the world economy, but with a growth rate lower than in 2000. Growth in the euro-zone in the optimistic scenario will level off, but there are some reasons to expect a slowdown. The Japanese economy should pick up steam. On the other hand, emerging Asia will experience slightly less robust growth rates in 2001 than this year.

The slowdown in world economic growth in 2001, in particular in industrial production, will bring a reduction in the volume of imports. The biggest decline will be observed for Asian emerging economies (after the impressive results of the year 2000), whereas the fall in import volumes in developed economies will be less pronounced.

Current risks to global growth lie mainly in uncomfortably high oil prices. If prices are maintained at such a high level (i.e., above 30 dollars per barrel), then they may have a negative impact on growth via weakened consumer confidence and falling corporate profits. High oil prices will also add to inflation. If the non-inflationary environment is endangered, then the ensuing monetary tightening will additionally suppress economic growth.

Economic growth

Prior to discussing recent developments in the world economy, we would like to draw attention to an international comparison of GDP growth rates. Following Deutsche Bundesbank (*Monthly Report*, August 2000)

[1] Economic forecasts presented in this chapter constitute a consensus of leading forecasting centres (IMF, OECD, DIW, commercial investment banks, etc.).

and JP Morgan (*World Financial Markets*, October 2000), we focus on the use of hedonic pricing method in the national accounts. This method makes it possible to take into account a change in quality of a given good. For instance, if the price of a PC has not changed since last year, but its parameters have (faster processor, larger hard disk, etc.), then the traditional national accounts system do not record any change in the output volume. This is not the case with *hedonic* pricing, as the change in quality will be reflected in the increased volume and the reduced price. As a consequence of introducing this method in the US, the prices of information and communications technology (ICT) goods were deflated to a larger extent that the prices in countries that did not employ the method (e.g., in Germany). As a result of using this method, both the measure of real output growth of ICT goods and the measure of their contribution to GDP growth were higher than would have otherwise been the case.

The above effect of using *hedonic* pricing in the US is to some extent mitigated by chain weighting (i.e. changes in volumes and prices are related to the base of a previous year). For instance, in the EU the constant base approach is employed. Given the rapidly changing markets, especially in the case of ICT goods, the *hedonic* pricing approach coupled with the constant base system would result in even more robust real GDP growth (JP Morgan, p. 14).

Moreover, some changes in the definition of investment in the US have been introduced. They concern, for example, purchases of computer software. Such purchases are treated as investment, not as expenditure (according to standard national accounting principles they are counted as intermediate consumption). Apparently, this leads to higher measured economic growth, given that American firms spend significant amounts of money on software. Similar changes are to be introduced in Japan. Re-estimating investment in ICT goods over the period 1997–1998 may reduce the measured Japanese decline in 1998 from 1.9% to 0.7% (*The Economist*, September 21–27).

United States

The preliminary US GDP data showed a significant deceleration in growth in 3Q00. The annualised growth rate dropped from 5.6% in 2Q00 to a mere 2.7%. Government spending and residential investment were the main drags on growth. Surprisingly, the growth of personal consumption expenditures accelerated to 4.5% in 3Q00 from 3.1% in 2Q00. This means that high oil prices and less impressive wealth effects due to lower equity prices have not weakened consumer confidence

Table 1. GDP in selected countries, 1997–2002 (% change yoy)

	1997	1998	1999	*2000f*	*2001f*	*2002f*
Global	4.1	2.6	3.4	*4.7*	*3.9*	*3.5*
OECD	3.4	2.7	3.0	*3.9*	*3.1*	*3.0*
USA	4.4	4.4	4.2	*5.3*	*3.3*	*2.7*
Canada	4.4	3.3	4.5	*4.8*	*3.5*	*2.5*
Japan	1.6	-2.5	0.2	*2.0*	*2.3*	*2.5*
European Union	2.6	2.7	2.4	*3.4*	*3.3*	*3.4*
Germany	1.4	2.1	1.6	*3.0*	*3.3*	*3.5*
France	2.0	3.2	2.9	*3.4*	*3.7*	*4.0*
Italy	1.8	1.5	1.4	*2.7*	*3.0*	*3.3*
United Kingdom	3.5	2.6	2.1	*3.1*	*2.8*	*2.3*
Russia	0.9	-4.9	3.2	*7.2*	*6.0*	*5.0*
China	8.8	7.8	7.1	*8.0*	*7.0*	*7.0*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: f – forecasts.

yet. However, this was only possible due to the negative personal saving rate. Labour markets remained tight and wage increases became a widespread fact. The average unemployment rate in 3Q00 remained at the level of 2Q00 – 4% – but in September the rate fell to 3.9%.

A further weakening of growth will depend on the extent of the potential monetary tightening, the recent drop in equity prices, and the effects of high oil prices on corporate profits and consumer confidence.

European Union

Growth in the euro-zone is expected to slow down slightly in the second half of 2000 as compared to the first half of the year. High oil prices are partly behind the slowdown. However, growth should start to accelerate in 2Q01 due to fiscal easing, a competitive currency, and creation of new jobs. Despite the weak euro the surplus in merchandise trade has been declining. This is mainly due to high oil prices that boosted import payments. The labour market remains tight. The unemployment rate levelled off at 9% in July and August (the lowest rate in many years).

Economic growth in Germany, which cooled off in 3Q00, is expected to follow the European pattern. All business surveys send worrying messages. The Ifo indicator fell from 99.1 in July to 98.0 in September. All components were down, signifying a deterioration in the current situation, business climate and business expectations. Nevertheless, the September level of the Ifo is consistent with the 4% growth of industrial production. A tax reform, planned to bring a cut in the tax burden of around 2% of GDP, is expected to cause a rebound in growth next year.

France, on the other hand, continues to perform very well with solid economic growth, falling unemployment, and restrained price pressures. The country is also following the European trend of fiscal easing. The new fiscal plan will be implemented in 2001–2003. Households will gain most from the reform. As a result, consumer consumption is expected to increase. It is noteworthy that this fiscal easing is occurring at a time when France is already running a budget deficit.

Italy remains the euro-zone laggard, though its performance in the first half of 2000 was satisfactory. The gap in growth as compared to the European average is not expected to close in the near term.

In the UK the economic growth slowed in 3Q00. According to preliminary figures, GDP rose 0.7% qoq against 0.9% in 2Q00. The service sector is slowing down as well. The labour market remains tight, with the unemployment rate falling to 5.3% in August. The recent high oil prices help the country, given the fact that the UK is an net oil exporter.

CIS

The Russian economy continues to be on the mend. GDP growth stood at 7.5% yoy in the first half of 2000. The positive sign is that fixed investment for January–June was up 17%. Faster growth contributed to a boost in real disposable income, which grew almost 9% during first 7 months of 2000. High oil prices are, no doubt, a big help for Russia. Thanks to them, the first half of the year saw a trade surplus of US$29 billion (oil comprises a significant share of total Russian exports).

The budget draft, with a balanced budget for 2001, has been passed in the Duma. Despite the restrictive fiscal policy being pursued, the budget's impact on the economy is expected to be stimulatory. We would like to stress that the prospects of the Russian economy hinge heavily on the successful and fast introduction of reforms. Debt restructuring is also of key importance. So far, only deals with the London Club have been reached, but no progress has been observed in talks with the Paris Club.

CEFTA

The Hungarian economy continues to gain on strong external demand originated in the EU. Due to the export boost, GDP rose 5.9% yoy in the first half of 2000. These conditions are expected to last through year-end, and GDP growth in 2000 may reach almost 6.0%. High food and energy prices (the former due to this year's drought) caused a hike in inflation in 3Q00 (9.1% in June and 10.3% in September). In 2001, however, the inflationary pressures should ease and favourable economic conditions continue to hold.

The Czech Republic's economy is still on the mend, although GDP growth declined in 2Q00 to 1.9% yoy, after 4.9% growth in 1Q00. A strong export boost has weakened considerably and imports have accelerated. Unemployment, while on the decline, still persists at a high level. Excessively lax budgetary policy constitutes the main threat to next year's GDP growth. An excessive government stimulus to the economy may cause it to overheat, increasing inflationary pressure and leading in turn to higher interest rates and a lower long-term growth path.

Asia

In general, Asian economies continue to perform well. Due to the weakening of external demand (especially in the US and Europe), the fast pace of economic growth of recent quarters is to slow down. While net exports have been declining, a resurgence of private consumption has occurred. While these economies seem to be on a fast track, structural weaknesses in the corporate and financial sectors have not been fully overcome.

China experienced healthy growth of 8.2% during the first three quarters of 2000. The source of economic stimulus has shifted somewhat from exports to government spending. The greatest concern is with consumer spending, which remains weak. Nevertheless, most international organisations remain upbeat about the prospects for the economy's development this and next year.

Japan's GDP grew by 1.0% yoy as well as qoq in 2Q00. Public spending was the main driving force. This was the effect of the economic stimulus package introduced early this year. Another fiscal stimulus package was approved recently, which will take effect in the next 6 months. Consumption is gaining momentum in the wake of rising incomes, employment, and consumer confidence. Consequently, more robust rates of growth are expected in the second half of the year and in 2001.

Latin America

The overall economic situation in the region is satisfactory, though growth across countries is very uneven. The biggest economies in the region continue to be on a fast track. Strong domestic sales and foreign demand are fuelling economic recovery in Brazil and Mexico. The picture is not so rosy for Argentina, Colombia, and Peru. Venezuela gained from high oil prices, but its situation after spending the windfall will be uncertain.

Oil prices

In 3Q00 oil prices were on the rise, hovering around 28–36 USD per barrel. This was primarily due to a decline in oil reserves in the US (the US account for roughly 20% of global oil consumption). In addition, lower global oil reserves and failure of OPEC's oil production increase to match demand drove prices up to 36 dollars per barrel. Even Saudi Arabia's increase in oil production (by 500,000 barrels in July–August) and OPEC members' increase by 800,000 barrels in September were not of much help in ameliorating this situation. This was due to the fact that in September OPEC had already provided roughly 750,000 barrels more than the official declarations. Only the US intervention (consisting of the sale of 30 million tonnes of oil) calmed the market. It should be stressed that in 3Q00 OPEC has refrained from using the intervention mechanism of increasing production conventionally applied in the event of prices remaining outside the range of 22–28 dollars for 20 consecutive days.

We expect prices to fall below 28 dollars per barrel in 2001 due to the forecasted slowdown in economic growth and increase in oil production. If OPEC sticks to its intervention mechanism, then the price may fall to 30 dollars as soon as in 4Q00. The increased tanker traffic that has been observed since the end of August may be proof of an increase in OPEC oil output. However, higher demand due to the winter season in the northern hemisphere may delay the price decline until the end of 1Q01. Moreover, if the riots in the Middle East escalate and OPEC does not comply with its intervention mechanism, then a scenario of a 50-dollar price is possible.

Inflation

The global inflation outlook is becoming less optimistic, primarily due to persistently high oil prices. As they decline early next year, inflationary pressures in oil-importing countries should ease. Tight labour markets in developed economies will force wage increases. If the latter are not compensated with high enough growth in labour productivity, core inflation will edge up. In European emerging markets after a lull this year, disinflation should be continued in 2001.

In September the CPI in the US rose by 0.5% mom, yielding an annual rate of 3.5%. The monthly increase was the biggest one since June. The prices of energy (up 3.8% mom) were the main reasons behind the rise. The index of all items less food and energy rose 0.3% mom (i.e. only by 0.1 percentage point more than in previous months). So the annual rate of core inflation amounted to 2.6%.

Table 2. GDP deflator in selected countries, 1997–2002 (% change yoy)

	1997	1998	1999	*2000f*	*2001f*	*2002f*
OECD	1.7	1.4	1.0	*1.2*	*1.6*	*1.7*
USA	1.9	1.3	1.5	*2.2*	*2.5*	*2.8*
Canada	1.0	-0.6	1.6	*3.2*	*2.1*	*2.3*
Japan	0.3	0.3	-0.9	*-1.8*	*-0.5*	*0.1*
European Union	1.9	2.0	1.5	*1.4*	*1.7*	*1.4*
Germany	0.8	1.1	0.9	*0.8*	*1.4*	*1.0*
France	1.4	0.9	0.3	*0.6*	*1.0*	*1.0*
Italy	2.4	2.7	1.5	*1.7*	*2.0*	*1.4*
United Kingdom	2.9	3.0	2.5	*2.2*	*2.5*	*2.1*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: f – forecasts.

Table 3. CPI in selected countries, 1997–2002 (% change yoy)

	1997	1998	1999	*2000f*	*2001f*	*2002f*
OECD	2.0	1.1	1.4	*2.0*	*1.7*	*1.8*
USA	2.3	1.6	2.2	*3.4*	*2.4*	*2.8*
Canada	1.4	1.0	1.7	*2.6*	*2.1*	*2.0*
Japan	1.7	0.6	-0.3	*-0.6*	*-0.2*	*-0.2*
European Union	1.8	1.4	1.3	*2.0*	*1.9*	*1.8*
Germany	1.5	0.6	0.7	*1.8*	*1.5*	*1.4*
France	1.3	0.7	0.6	*1.6*	*1.4*	*1.2*
Italy	1.7	1.7	1.7	*2.5*	*1.9*	*1.8*
United Kingdom	2.8	2.7	2.3	*2.2*	*2.6*	*2.8*
Russia	14.7	27.7	85.9	*20.0*	*16.0*	*12.0*
China	2.8	-0.8	-1.4	*0.5*	*1.0*	*1.5*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: f – forecasts.

Table 4. Long-term interest rates in selected countries, 1997–2002 (%)

	1997	1998	1999	*2000f*	*2001f*	*2002f*
USA	6.3	5.3	5.7	*6.8*	*6.7*	*6.0*
Canada	6.1	5.3	5.5	*6.3*	*6.5*	*6.0*
Japan	2.3	1.5	1.8	*1.8*	*2.0*	*2.3*
Euro area	5.7	4.7	4.6	*5.5*	*6.0*	*5.5*
United Kingdom	7.0	5.5	5.0	*5.3*	*5.7*	*5.5*
LIBOR (US$/year)	5.9	4.8	5.4	*6.5*	*6.6*	*5.6*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: f – forecast.

Inflation in the euro-zone fell from 2.4% in July to 2.3% in August, but in September rose significantly to 2.8%. However, core inflation has not risen sharply so far (1.3% in August and 1.4% in September). The main drivers behind the rise are high oil prices and a weak euro. Lower oil prices forecasted next year (as early as 1Q01) and a relative appreciation of the euro should ease inflationary pressures. However, there is a risk that next year wage demands will drive core inflation up.

Interest rates

Due to the risk of rising inflation, primarily due to oil price developments and their second-round effects, interest rates hikes may take place. However, as core inflation is expected to rise no earlier than at the beginning of the next year, no immediate changes in monetary policies are foreseen. Besides, central banks may be concerned with the dampening effect of higher interest rates on growth in the face of the expected cyclical slowdown.

The ECB's last interest rate hike (by 25 base points) was on October 5. This made for a total increase of 225 base points since November 1999. The last decision was motivated by a threat to price stability stemming from high oil prices and the weak euro. If these factors continue to exert their negative effects and M3 growth exceeds the reference level, then further interest rate hikes may come before the end of the year. This is made more likely by the fact that, in the ECB's opinion, the current monetary policy is still conducive to economic growth and not overly restrictive. However, if this is not the case, then the next changes in interest rates should be expected in the first half of next year.

There has not been any change in the Fed's monetary policy since May 16, and one should not expect interest rates to be raised before year-end. Rates have been left on hold as a result of the cool-down of the economy and the continuing relative stability of core inflation. However, if price pressures mount next year, further tightening is possible.

The MPC of the Bank of England has continued its neutral monetary policy for 8 months. During its meetings in 3Q00 and in October it did not raise interest rates. The rates are expected not to be changed until year-end, as growth is slowing and prices fairly stable (especially as the average wages and salaries index has recorded only a minor rise).

Exchange rates

The euro has been gradually losing ground in nominal as well as real effective terms in 3Q00. It has depreciated against both the dollar and the yen. The rate of the euro

Table 5. The volume of imports in selected countries, 1997–2002 (% change yoy)

	1997	1998	1999	*2000f*	*2001f*	*2002f*
Global	9.8	4.3	5.1	*10.3*	*8.0*	*7.5*
OECD	10.9	7.6	8.3	*11.7*	*8.9*	*7.6*
USA	13.7	11.9	10.7	*13.2*	*9.0*	*8.0*
Canada	15.1	6.1	9.4	*13.0*	*8.5*	*7.0*
Japan	0.5	-7.6	5.3	*11.0*	*7.0*	*8.0*
European Union	9.2	9.3	6.2	*11.4*	*9.2*	*7.3*
Germany	8.3	8.5	7.1	*10.4*	*9.0*	*8.0*
France	6.8	11.2	4.4	*13.0*	*9.0*	*7.5*
Italy	10.2	9.1	3.3	*8.0*	*9.0*	*8.0*
United Kingdom	9.2	8.8	7.6	*8.0*	*5.0*	*3.0*
Russia	11.0	-16.0	-20.0	*8.0*	*13.0*	*12.0*
China	12.0	-3.8	8.0	*21.0*	*12.0*	*11.0*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: f – forecasts.

against the dollar fell from a level of around 0.95 at the beginning of July to 0.848 at the end of September. The very low rate of the euro forced the ECB and monetary authorities of the US, the UK, and Japan to undertake a concerted intervention in the exchange markets at this time. As a result the euro rose to 0.88 and stabilised around this level the following week. However, it declined thereafter, reaching a lifetime low of 0.833 against the dollar at the end of October.

Most investment banks have become pessimistic about the recovery of the euro next year, and the exchange rate against the dollar is forecasted to remain below 1.00 euro per dollar at the end of 2001. In our forecast, we assume the average euro-to-dollar rate for 2001 to stay at 0.9.

Forecast assumptions – domestic determinants

In the present forecast, we assume that a restrictive economic policy will continue until year-end as well as in 2001–2002. However, 2001 will see a combination of a tighter monetary policy and a considerably looser fiscal policy.

We also assume that improvements in economic efficiency, mainly reflected in a considerable reduction in unit labour costs and the adjustment of Polish enterprises to the pattern of demand in EU countries, will cause the strong export boost experienced since the end of 1999 to persist until the first half of 2001. We also expect that the dynamics of Polish exports to Russia and the Ukraine will significantly increase. Moreover, if the EU's economy performs very well in 2002, then the period of Polish export prosperity may extend even further.

We hope that the downside political risks (possible problems with passing the budget and appointing a new NBP president) will not interfere with the conduct of rational economic policy. Our forecast is based on three assumptions underlying economic policy:

(i) The MPC will leave main interest rates unchanged until 1Q01;
(ii) Fiscal policy will be aimed at reducing the public sector deficit, in particular the deficit in the central government budget and that of ZUS (the state insurance company); in addition, we assume that the government will pursue a policy of restricting to the maximum possible degree the financing of the deficit by the domestic financial system;
(iii) We expect that full liberalisation of capital flows according to the agreement with the OECD will be implemented at the beginning of the second half of 2001.

In 2001, we assume that the fiscal policy will be slightly less restrictive, and the stance of monetary policy will remain broadly unchanged (this implies continued high real interest rates). In 2002 and 2003 we further assume a gradual loosening of both fiscal and monetary policies.

We make the following special assumptions for years 2001–2002:

1. The cost of compulsory debt servicing to the Paris Club and the London Club, as well as indebtedness of the private sector, will amount to US$2.2 billion in 2001 and US$2.3 billion in 2002.
2. The labour force will grow by 0.4 and 0.5% in the respective years.
3. The growth in the number of old-age pensioners and recipients of disability allowances will be 0.7 and 0.5%, respectively.
4. Transfers from the EU will amount to US$0.9 billion in 2000 and US$1.2 billion in 2001.
5. Foreign direct investment (according to the balance of payments accounting) will reach US$7.8 billion and US$7.2 billion in the respective years.

Table 6. Dollar exchange rate vs. the euro and the yen, 1997–2002

	1997	1998	1999	*2000f*	*2001f*	*2002f*
Euro		1.11	1.07	*0.92*	*0.90*	*1.03*
Yen	121.0	130.9	113.9	*107*	*101*	*102*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: 1. f – forecasts.
2. Annual averages.

6. We assume that "large scale" privatisation will accelerate and will be completed in 2002, with proceeds amounting to 18 billion zlotys in 2001 and 8 billion zlotys in 2002.
7. The price indexation of social benefits will be maintained and thus nominal average social benefits will increase 8% and 6.5%; in addition, compensations for higher inflation in 2000 of 5 billion zlotys will be paid out in 2001.
8. In 2001, personal income taxes rates will fall by 4 percentage points, whereas corporate income taxes will remain at their 2000 level and the VAT base will be extended (by 2003 the VAT system will be similar to the EU's).
9. Employment in the public sector will be stable; the increase in employment will range from 0 to 0.3%. We assume an employment decline in the education and health care sectors, accompanied by an increase in the broad administrative sector.
10. We assume that the 2001 harvest will be at the average 1997–2000 level and, in 2002, at the average 1998–2001 level.

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Analysis of the economic situation and outlook for 2000-2002

Domestic demand

- **Low growth of domestic demand in 2000**
- **Stronger consumer and investment demand in 2001– 2002**
- **Loosening of monetary and fiscal policy after 2001**

We estimate that GDP rose by 4.2% yoy in 3Q00. Domestic demand, as in the previous three quarters, rose at a slower rate than GDP, increasing by 2.4%. Detailed data concerning the growth rates of basic components of aggregate demand are included in Table 7.

Such a large dampening of domestic demand growth results from the tightening of economic policy in comparison with last year. On the one hand, both monetary policy instruments (high nominal and real interest rates) and fiscal instruments (a lower public sector deficit than in 1999) have been employed in implementing a more restrictive policy. On the other hand, higher-than-expected inflation led to a decrease in the real income of those households whose nominal incomes are indexed using an official inflation index (in PEO 1/2000 we forecasted that the annual inflation rate would reach 9.2%, while the Ministry of Finance's official forecast was for a 5.7% increase).

The weakening of growth in real household incomes led to a slowdown in household consumption growth similar to that recorded in the first half of the year (a mere 2.4% yoy increase). Moreover, lower growth in real incomes was not compensated by a decrease in household savings.

It is quite likely, moreover, that household consumption growth has been overestimated. If the current estimates related to an improvement in the foreign trade balance according to the national accounts turn out to be too pessimistic, then estimates of household consumption growth will have to be adjusted downward. This is exactly what happened in 2Q00, when we assessed consumption growth at 3.9% and the CSO recorded an actual increase of 2.6%.

As in 1999 and the first half of 2000, growth in fixed investment continued to be low. We estimate that it rose by 3.6%. Growth in fixed investment in machinery, equipment and transport facilities was slightly higher. However, growth in outlays on construction was very low.

A considerable reduction in budget expenditure growth over the last two years led to low growth of public consumption. This trend continued in 3Q00, and public consumption growth, according to our estimates, stood at 1%. This was one of the factors reducing the rate of growth of total domestic demand.

The unexpected inflation of July and the related further weakening of domestic demand led to a considerable slowdown in economic growth, resulting in the downward revision of expected GDP increase in 2000 (from 5.4% forecasted in PEO 3/2000 to 4.8% now) and in 2001 (from 6.1% to 5.5% respectively). We envisage a slight acceleration of economic growth to 5.8% in 2002.

In our opinion, high nominal and real interest rates and fiscal tightening in 4Q00 will contain growth in domestic demand. We expect domestic demand growth to reach 3.4% in 2000. However, it might increase in 2001–2002 up to 5.1% and 5.7% respectively in the wake of a loosening of monetary and fiscal policies and higher growth in real household incomes. Nevertheless, it will still grow slower than GDP.

Table 7. Components of aggregate demand, 1998–2002 (% change yoy)

		GDP	Domestic demand	Household consumption	Public consumption	Investment in fixed assets	Exports	Imports
1998	1Q-4Q	4.8	6.4	4.8	1.6	14.2	14.3	18.5
1999	1Q-4Q	4.1	4.8	5.1	1.1	6.9	-1.5	1.4
forecast								
2000	*1Q-4Q*	*4.8*	*3.4*	*3.2*	*1.0*	*4.2*	*11.6*	*5.7*
2001	*1Q-4Q*	*5.5*	*5.1*	*4.7*	*1.2*	*9.6*	*12.3*	*10.0*
2002	*1Q-4Q*	*5.8*	*5.7*	*4.8*	*1.6*	*10.6*	*9.8*	*9.0*
1998	1Q	6.5	7.3	6.3	2.2	17.3	18.8	20.2
	2Q	5.3	5.7	4.1	1.6	14.6	24.7	23.0
	3Q	4.9	6.1	4.4	1.5	14.2	18.9	20.6
	4Q	3.0	6.6	4.6	1.1	12.9	-1.9	11.6
1999	1Q	1.6	3.3	4.4	1.1	6.1	-8.9	-2.8
	2Q	3.1	4.5	4.9	1.0	6.8	-3.5	2.0
	3Q	5.0	5.5	5.4	1.2	7.0	2.9	4.5
	4Q	6.2	5.6	5.6	1.1	7.3	3.8	2.0
2000	1Qe1	6.0	5.1	4.6	1.0	5.5	5.0	2.3
	2Qe1	5.2	3.3	2.6	0.9	2.9	10.8	3.5
	3Qe2	4.2	2.4	2.4	1.0	3.6	15.6	7.4
forecast								
2000	*4Q*	*4.1*	*3.2*	*3.2*	*1.0*	*4.7*	*14.1*	*8.9*
2001	*1Q*	*5.1*	*4.2*	*4.4*	*1.2*	*7.0*	*14.0*	*9.3*
	2Q	*5.4*	*5.0*	*5.8*	*1.2*	*9.2*	*12.5*	*10.1*
	3Q	*5.7*	*5.3*	*4.6*	*1.2*	*10.1*	*12.0*	*9.7*
	4Q	*5.8*	*6.0*	*4.1*	*1.2*	*10.5*	*11.0*	*10.8*
2002	*1Q*	*5.8*	*5.6*	*5.3*	*1.6*	*11.0*	*11.0*	*9.6*
	2Q	*5.7*	*5.4*	*4.5*	*1.6*	*11.4*	*9.2*	*8.0*
	3Q	*5.8*	*5.6*	*4.7*	*1.6*	*10.7*	*8.8*	*8.0*
	4Q	*5.8*	*6.1*	*4.6*	*1.6*	*10.0*	*10.2*	*10.3*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecasts – CASE.

Notes: 1. Data and estimates at annual average prices of a previous year.

2. Forecasts at average 1999 prices.

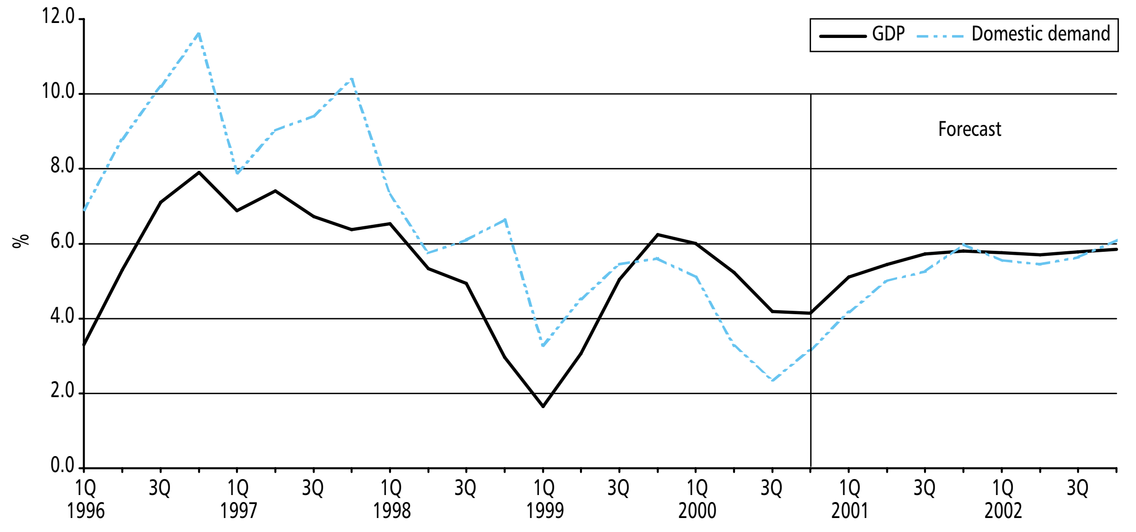
3. Domestic demand is defined as the sum consumption of households, and non-commercial institutions, public consumption and investment. This table does not provide separate indicators for the consumption of non-commercial institutions.

4. Data are not seasonally adjusted.

In 4Q00 growth of consumption demand may be slightly higher than in the previous quarter. The possible boost of demand will be due to expected lower inflation (given stable growth in nominal wages and salaries, purchasing power of household might increase). We estimate a 3.2% increase in household consumption in 2000 (i.e., 1.9 percentage points less than in 1999).

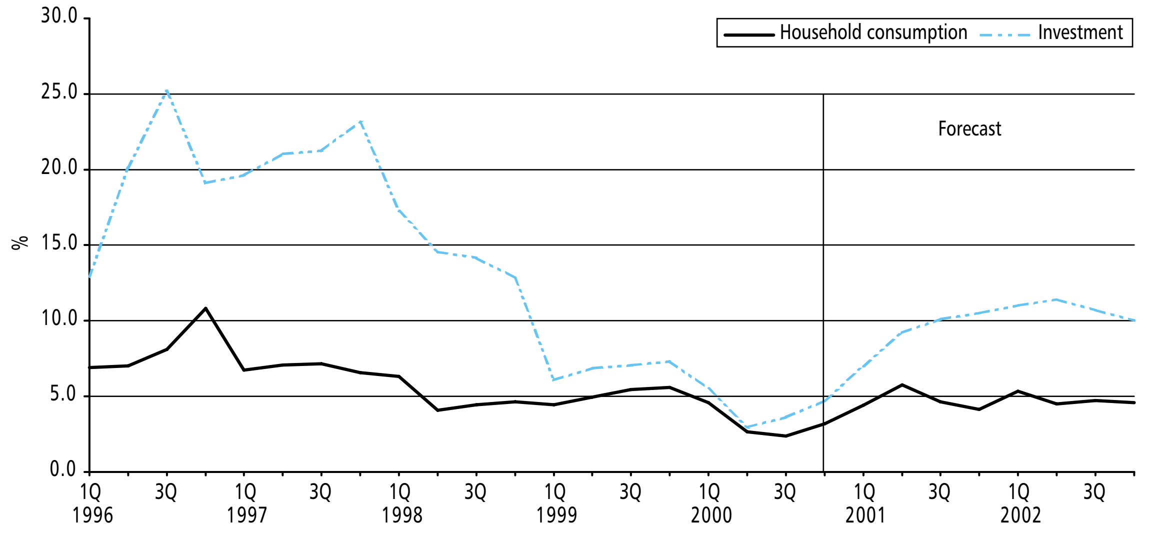
We estimate that domestic demand in 2001 will grow faster than in 2000 as a result of the compensation for pensioners, higher wages and salaries for public sector employees and Germany's compensation for forced labour during World War II. If, in addition, inflation turns out to be lower than we forecast, then one can expect a considerable acceleration in growth of real household incomes.

Figure 1. GDP and domestic demand, 1996–2002 (% change yoy)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

Figure 2. Household consumption and investment, 1996–2002 (% change yoy)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

We forecast a higher real increase in household incomes in the years 2001–2002, and a slightly higher propensity to save than in 2000 (see Table 9). We predict household consumption growth of 4.7% and 4.8%, respectively.

The expected improvement in efficiency of enterprises, the continued high level of foreign investment, the expected increase in enterprise savings, and lower growth in the prices of imported machinery and equipment (as long as the euro remains weak) should spur the growth of fixed investment.

Consequently, we forecast a gradual recovery of fixed investment outlays, which will rise from an expected 4.2% in 2000 to 9.6% in 2001 and 10.6% in 2002.

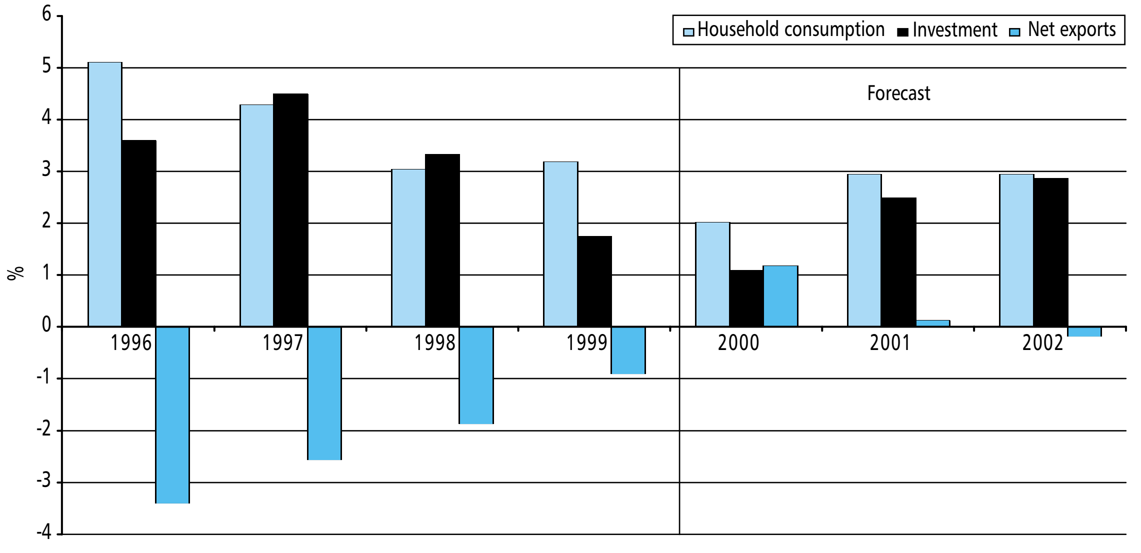
In the years 2001–2002 we do not forecast an acceleration of public consumption growth. The budgetary

Table 8. Contributions to GDP growth, 1998–2002 (%)

	GDP	Household consumption	Public consumption	Investment in fixed assets	Stock-building	Net exports	Exports	Imports
1997 1Q-4Q	6.8	4.3	0.6	4.5	0.1	-2.6	3.0	-5.5
1998 1Q-4Q	4.8	3.0	0.3	3.3	0.1	-1.9	3.7	-5.5
1999 1Q-4Q	4.1	3.2	0.2	1.7	-0.1	-0.9	-0.4	-0.5
forecast								
2000 1Q-4Q	*4.8*	*2.0*	*0.2*	*1.1*	*0.4*	*1.2*	*3.0*	*1.9*
2001 1Q-4Q	*5.5*	*2.9*	*0.2*	*2.5*	*-0.2*	*0.1*	*3.4*	*3.3*
2002 1Q-4Q	*5.8*	*3.0*	*0.2*	*2.9*	*-0.1*	*-0.2*	*2.9*	*3.1*

Source: CSO (GDP) and CASE (other data).
Notes: 1. Contributions to GDP growth were calculated using the following formula:
*(annual increase in X / annual increase in GDP) * rate of growth of X.*
2. GDP growth and the sum of contributions to GDP may not add up due to approximations.

Figure 3. Contributions to GDP growth, 1996–2002 (%)



Source: CSO and CASE.
Note: CASE forecast starting from the year 2000.

policy and the limited manoeuvre to increase relative government spending will be a major constraint (see section on budget).

We expect that a strong pro-export stimulus will continue to hold until the second half of 2001. At the same time, a considerable strengthening of import demand for Polish goods in the CIS countries, especially in Russia and Ukraine, is very likely.

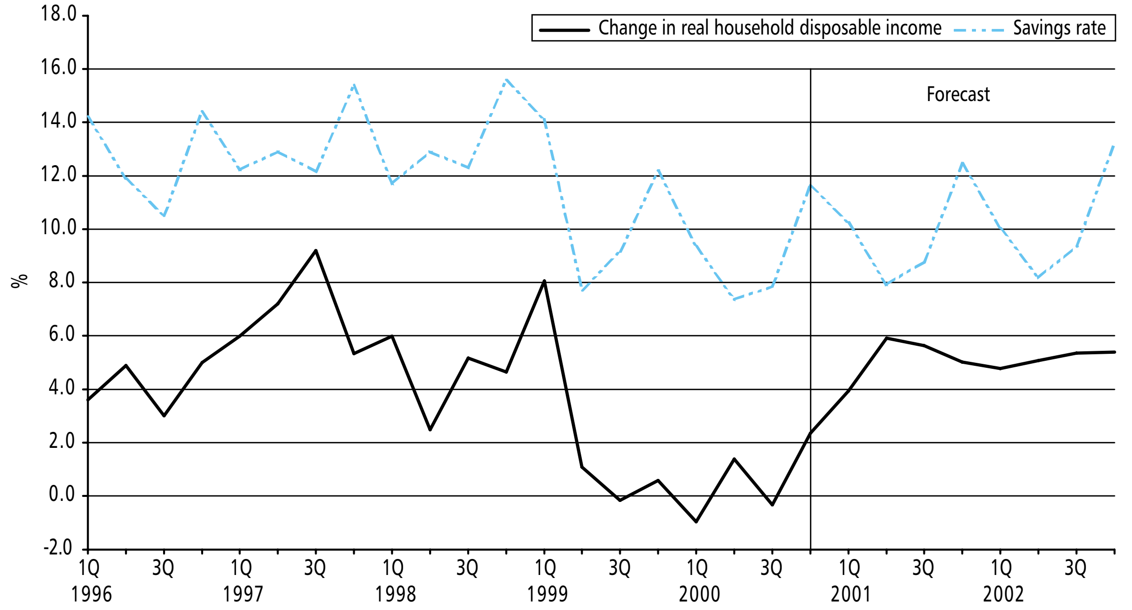
The expected and historic influence of individual components of aggregate demand on an increase in GDP is included in Table 8. In 2000 we envisage a temporary decline in the contribution of household consumption to GDP growth as a result of the expected weakening of consumer demand. However, in the years 2001–2002 we expect it to increase again to about 3% (i.e., the level of 1998–1999). It should be emphasised that during this period the contribution of consumption

Table 9. Household disposable income, 1998–2002

		Disposable income	Wages and salaries	Social benefits	Savings rate	Real disposable income
		% change	% change	% change	%	% change
1998	1Q-4Q	17.0	17.3	15.3	13.2	4.7
1999	1Q-4Q	9.7	10.7	9.1	10.8	2.3
forecast						
2000	*1Q-4Q*	*10.8*	*12.5*	*7.8*	*9.1*	*0.6*
2001	*1Q-4Q*	*12.6*	*11.1*	*8.9*	*9.9*	*5.1*
2002	*1Q-4Q*	*11.3*	*10.5*	*8.0*	*10.2*	*5.2*
1998	1Q	20.7	20.9	17.0	11.7	6.0
	2Q	15.9	17.9	15.4	12.9	2.5
	3Q	16.9	15.5	14.1	12.3	5.2
	4Q	14.3	15.0	14.9	15.6	4.6
1999	1Q	14.8	9.1	10.9	14.1	8.1
	2Q	7.5	10.4	7.3	7.7	1.1
	3Q	7.0	11.4	9.5	9.2	-0.2
	4Q	9.8	11.8	8.7	12.2	0.6
2000	1Q	9.2	13.3	10.4	9.3	-1.0
	2Q	11.5	13.1	8.7	7.4	1.4
	3Q	10.4	11.8	5.8	7.9	-0.3
forecast						
2000	*4Q*	*12.0*	*11.9*	*6.3*	*11.6*	*2.4*
2001	*1Q*	*12.5*	*12.0*	*8.0*	*10.2*	*3.9*
	2Q	*14.0*	*11.1*	*9.0*	*7.9*	*5.9*
	3Q	*12.5*	*11.1*	*9.6*	*8.8*	*5.6*
	4Q	*11.6*	*10.1*	*9.0*	*12.5*	*5.0*
2002	*1Q*	*11.1*	*11.0*	*8.0*	*10.0*	*4.8*
	2Q	*11.2*	*11.0*	*8.0*	*8.2*	*5.1*
	3Q	*11.6*	*10.3*	*8.0*	*9.4*	*5.4*
	4Q	*11.3*	*9.5*	*8.0*	*13.2*	*5.4*

Source: Annual data – CSO, quarterly data and forecast – CASE.
Notes: 1. % change yoy.
2. The savings rate is shown as a percentage of nominal disposable income.

Figure 4. Change in real household disposable income and savings rate, 1996–2002 (%)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

to GDP growth will, on the average, be much lower than in 1995–1997.

We forecast that in 2000 the investment contribution to GDP growth will be at its lowest level since 1993. Its increase is possible over the next two years, but, as in the case of household consumption, it will be on average much lower than in 1995–1997.

In 2000, the contribution of net exports might reach 1.2%, which would be the best result since 1995. However, as early as 2001–2002, we envisage a neutral impact on economic growth (i.e., contribution close to zero). It should be emphasised that the export contribution might increase considerably and may, on the average, be higher than in 1996–1998.

Value-Added

- **The weakening of growth in industrial output**
- **Decline in construction output**
- **Market services stabilise economic growth**
- **Expected faster growth in value-added in 2001–2002**

The weakening of economic growth manifested itself also by a considerable decline in growth of value-added. This resulted from a decline in agricultural output (poor crops and a decline in livestock), reduced growth in construction output due to the weakening of investment demand, and weak growth in industrial production due to weak consumer demand. We estimate that the value-added in non-agricultural sections (excluding agriculture, forestry, hunting, and fishing) was 3.8% higher than in 3Q99.

As in the previous quarters, higher-than-expected value-added growth was recorded in industry, telecommunication and trade sectors. Lower value-added growth occurred in construction and non-market services, among others. The estimates are presented in Table 10.

Output in enterprises employing more than 9 people increased by 6.6% yoy (see Table 11). Manufacturing was much weaker than in the previous quarter (the rate of growth dropped from 10.4% to 6.3%). There was a slight rise in mining output (by 1.8%). Energy, gas and water output increased as much as 14.9%. Value-added growth was also considerably lower than in the two previous quarters despite an upswing in exports.

As in the previous quarter, there has been a drop in construction output. This resulted from decreased demand for construction investment. We estimate that the other components of construction output did not compensate for the drop in construction output, and, as a result, value-added in the construction sector fell by 1.8% (while it rose by 0.8% in 2Q00).

Value-added in market services continues to stabilise economic growth. We estimate that it was slightly

Table 10. GDP and value-added in major sectors of the economy, 1998–2002 (% change yoy)

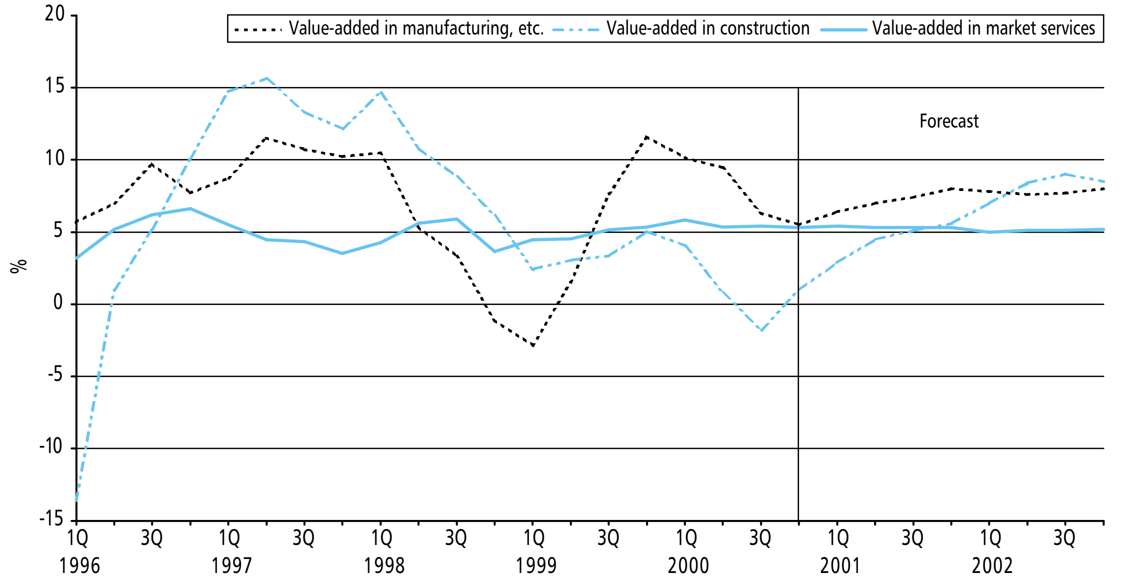
		GDP		Value-added				
				total	manufacturing, mining, water and gas supply	construction	market services	non-market services
		zloty billion	%	%	%	%	%	%
1998	1Q-4Q	554	4.8	4.7	4.3	9.3	4.8	2.3
1999e1	1Q-4Q	617	4.1	3.9	4.6	3.7	4.9	1.0
forecast								
2000	*1Q-4Q*	*703*	*4.8*	*4.6*	*7.7*	*0.7*	*5.5*	*1.0*
2001	*1Q-4Q*	*794*	*5.5*	*5.3*	*7.2*	*4.8*	*5.3*	*1.6*
2002	*1Q-4Q*	*890*	*5.8*	*5.6*	*7.8*	*8.4*	*5.1*	*1.8*
1998	1Q	124	6.5	6.4	10.5	14.6	4.3	3.7
	2Q	133	5.3	5.2	5.3	10.8	5.6	0.2
	3Q	140	4.9	4.8	3.3	8.8	5.9	1.4
	4Q	156	3.0	2.9	-1.1	6.1	3.6	3.1
1999e1	1Q	135	1.6	1.4	-2.8	2.4	4.4	1.0
	2Q	147	3.1	2.8	1.5	3.1	4.5	1.1
	3Q	156	5.0	4.8	7.6	3.4	5.1	0.8
	4Q	179	6.2	6.0	11.6	5.0	5.3	1.1
2000	1Qe1	154	6.0	5.8	10.1	4.0	5.8	1.0
	2Qe1	168	5.2	5.0	9.4	0.8	5.3	0.9
	3Qe2	178	4.2	3.8	6.3	-1.8	5.4	1.0
forecast								
2000	*4Q*	*203*	*4.1*	*3.9*	*5.5*	*1.0*	*5.3*	*1.1*
2001	*1Q*	*175*	*5.1*	*4.7*	*6.4*	*2.9*	*5.4*	*1.3*
	2Q	*190*	*5.4*	*5.2*	*7.0*	*4.5*	*5.3*	*1.5*
	3Q	*200*	*5.7*	*5.6*	*7.4*	*5.1*	*5.3*	*1.7*
	4Q	*228*	*5.8*	*5.7*	*8.0*	*5.6*	*5.3*	*2.0*
2002	*1Q*	*197*	*5.8*	*5.5*	*7.8*	*7.0*	*5.0*	*2.0*
	2Q	*213*	*5.7*	*5.6*	*7.6*	*8.4*	*5.1*	*1.8*
	3Q	*224*	*5.8*	*5.7*	*7.7*	*9.0*	*5.1*	*1.6*
	4Q	*255*	*5.8*	*5.7*	*8.0*	*8.5*	*5.2*	*1.6*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecasts – CASE.
Notes: 1. Data and estimates at annual average prices of a previous year.
2. Forecasts at average 1999 prices.
3. Data are not seasonally adjusted.

higher than in the previous quarter and reached 5.4% yoy. However, in our opinion the increase in value-added in non-market services stood at 1.0% yoy.

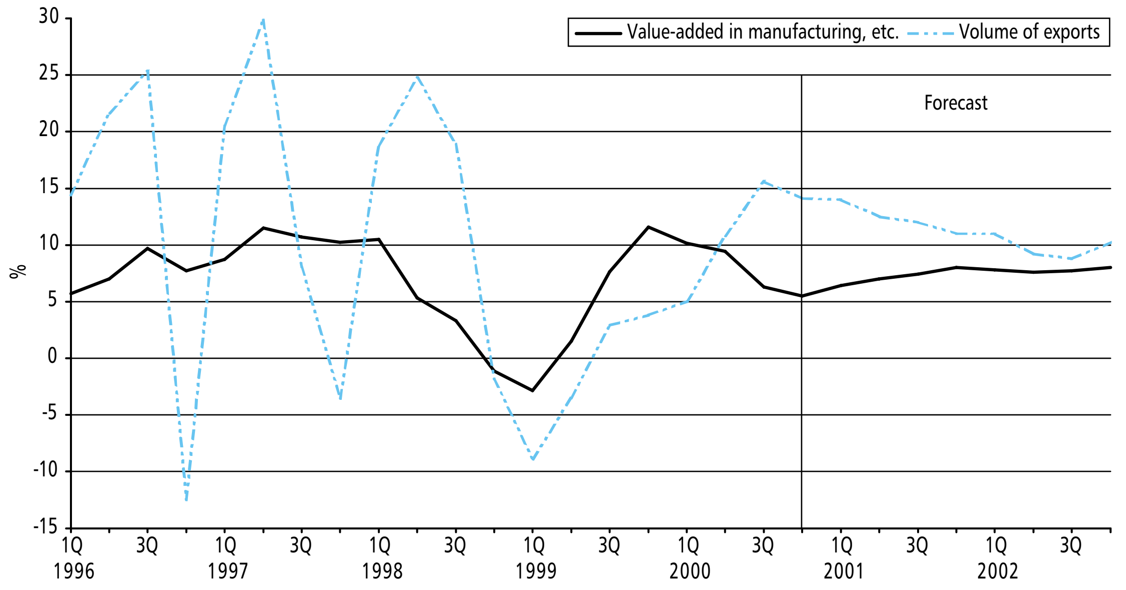
We forecast that in 2000 total value-added will increase by 4.6%, and in 2001 and 2002 by 5.3% and 5.6%, respectively. In our opinion, until the second half of

Figure 5. Value-added in major sectors of the economy, 1996–2002 (% change yoy)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

Figure 6. Value-added in manufacturing and volume of exports, 1996–2002 (% change yoy)



Source: CSO and CASE.
Note: 1. CASE forecast starting from 4Q00.
2. Volume of exports is presented according to the definition of national accounts and based on the latest CSO estimates.

2001, external demand will be most important for growth, while in subsequent quarters the effects of domestic demand will dominate.

Faster growth in value-added over the next two years will be possible due to expected faster growth in industry value-added (in 2001 and 2002 it may increase by 7.2% and 7.8% respectively) and the construction sector (4.8% and 8.4% respectively).

In addition, we forecast a stabilisation of growth in value-added in market services at the average level of

Table 11. Selected short-term indicators of the Polish economy, 1998–2002 (% change yoy)

		Output		Transport		Corporate sector	
		manufacturing, mining, water and gas supply	construction	freight	passengers	average employment	real gross wages
1998	1Q-4Q	4.6	11.4	-3.4	-2.9	1.5	3.7
1999	1Q-4Q	4.6	3.8	-2.2	-3.0	-1.2	3.0
forecast							
2000	*1Q-4Q*	*7.8*	*1.6*	*-1.0*	*-2.2*	*-3.1*	*2.0*
2001	*1Q-4Q*	*7.3*	*5.8*	*0.8*	*-1.2*	*-0.8*	*4.3*
2002	*1Q-4Q*	*7.9*	*9.4*	*1.0*	*-0.5*	*0.3*	*4.4*
1998	1Q	10.9	24.0	-5.8	0.3	1.9	4.4
	2Q	6.0	10.2	-4.6	-0.2	1.7	3.3
	3Q	3.9	13.2	1.6	0.5	1.0	3.6
	4Q	-0.8	4.5	-5.8	-0.6	1.6	3.7
1999	1Q	-3.1	0.6	-2.7	-6.0	-0.4	2.5
	2Q	1.2	4.0	-7.6	-7.1	-1.2	3.8
	3Q	7.4	3.2	-8.5	-6.1	-1.3	3.8
	4Q	11.7	6.4	-4.0	-5.7	-1.8	1.8
2000	1Q	10.7	4.8	-2.5	-3.9	-3.6	4.6
	2Q	9.6	-1.4	-1.1	-1.5	-3.4	2.5
	3Qe2	6.6	-3.0	-4.6	-2.0	-2.9	-0.5
forecast							
2000	*4Q*	*5.6*	*-1.0*	*-4.0*	*-1.5*	*-2.4*	*1.5*
2001	*1Q*	*6.6*	*3.6*	*-2.8*	*-1.1*	*-1.6*	*3.5*
	2Q	*7.1*	*5.5*	*-1.6*	*-1.0*	*-1.2*	*3.8*
	3Q	*7.5*	*6.3*	*-1.0*	*-0.7*	*-0.6*	*4.9*
	4Q	*8.1*	*6.9*	*-0.8*	*-0.6*	*0.0*	*5.0*
2002	*1Q*	*8.0*	*7.7*	*-0.3*	*-0.5*	*-0.1*	*4.7*
	2Q	*7.7*	*9.4*	*-0.1*	*-0.5*	*0.2*	*4.4*
	3Q	*7.8*	*10.2*	*0.4*	*-0.5*	*0.5*	*4.3*
	4Q	*8.1*	*9.8*	*0.5*	*-0.4*	*0.7*	*4.2*

Source: Data and estimates (e1) – CSO; estimates (e2) with an exception of output and real gross wages, and forecasts – CASE.
Notes: 1. Data on construction and assembly and transportation calculated from the monthly data.
2. Changes calculated from data published in Monthly Statistical Bulletin (CSO).
3. Annual data on average employment relate only to enterprises classified as "large enterprises" (e.g. in manufacturing-those with more than five employees until end-1999 and those with more than 9 thereafter).

1997–1999. Telecommunication, trade and hotels will continue to develop at the present fast pace, while transport and services related to real estate and companies will be somewhat slower.

We forecast low growth in value-added in non-market services in 2001. Not until 2002 can one expect faster growth (about 2% yearly) on a par with that reached in 1998.

Labour market

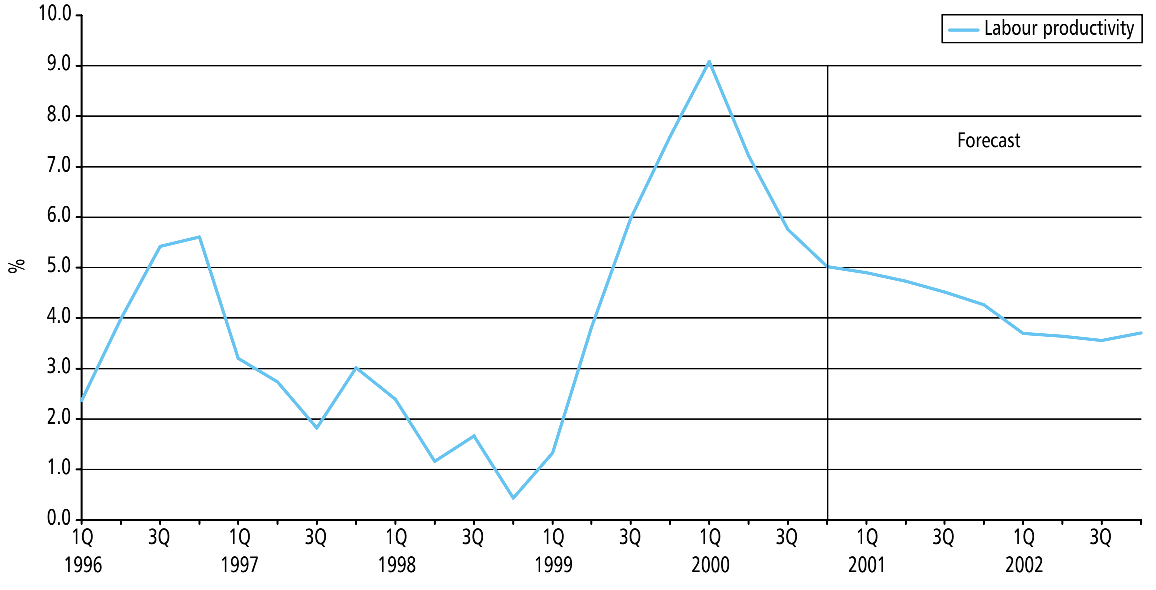
- **An increase in the unemployment rate to 14%**
- **No prospects for an improvement in the labour market for the next two years**
- **More flexible labour market – the key component of a more effective programme to combat unemployment**

Unemployment

In 3Q00 the situation in the labour market deteriorated as compared to the previous quarter. At the end of September there were 2,528.8 thousand people registered as unemployed, i.e., 91.4 thousand more than at the end of the previous quarter and 351 thousand more yoy. These figures are by no means indicative of a further deterioration in the labour market as compared to the previous year. Since 1Q00 the annual growth rate of unemployment has been on the decline. As late as January there were 430.8 thousand more unemployed than in January 1999; already by March, however, the figure had dropped to 362.2 thousand. Unfortunately, beginning in 2Q00, the growth in unemployment began to stabilise at a level of the analogous months of 1999. This implies a more or less stable rate of growth (350 – 370 thousand people) in the number of the unemployed in 12-month periods. Clearly, it also means that unemployment in Poland is on the rise. It might be something of a consolation that unemployment is not rising every month, as was the case throughout the whole of last year. If this trend continues until the end of this year, the unemployment rate may reach 14.4% by the end of December.

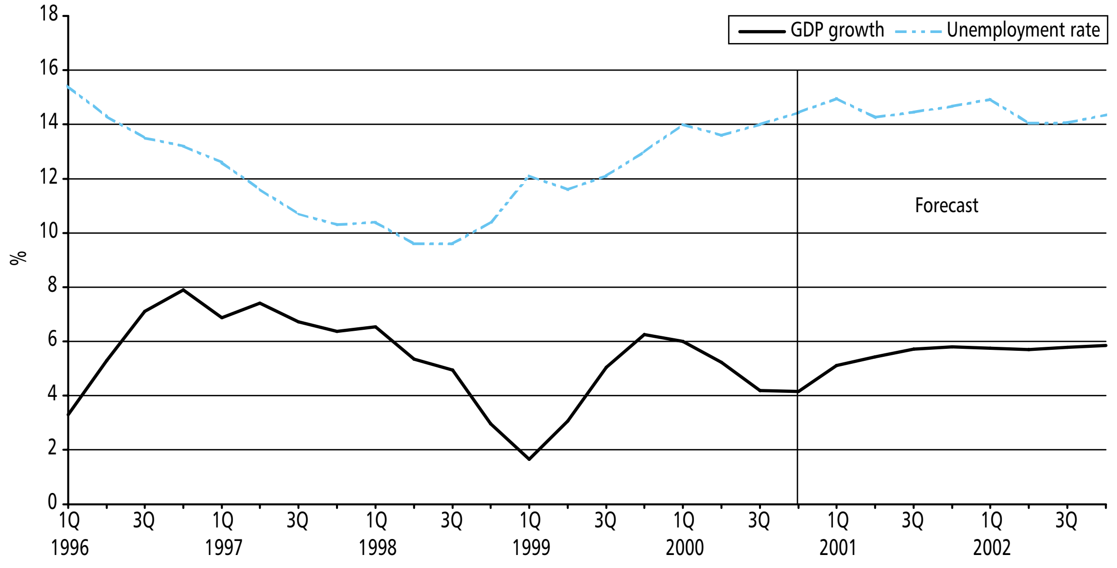
A drop in labour demand – and, consequently, an increase in the number of the unemployed – result belatedly from the economic slowdown of 1998–1999 triggered by the Russian crisis. In addition, the labour market problems have been aggravated by a situation characteristic of all countries with structural unemployment.

Figure 7. Labour productivity in non-agricultural sectors of the economy, 1996–2002 (% change yoy)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

Figure 8. GDP growth and unemployment rate, 1996–2002 (%)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

Within the next two years the situation in the labour market will gradually stabilise, although a considerable improvement should not be expected. We forecast that the unemployment rate will stay above 14.0%. Weak labour demand will result from the continued restructuring processes in industry and the continued rapid growth in labour productivity (although the latter will not grow as fast as in the last few quarters). Moreover, the influx of baby-boomers will have a negative impact on the labour market. Increased employment in the service sector will not suffice to stabilise employment in the whole economy. In this case it is necessary to take all-round measures to make the labour market more flexible. Among other measures, the Labour Code should be adapted to the new conditions on the labour market, the minimum wage should be differentiated by region, the range of training for the unemployed should be expanded, etc.

Employment in the enterprise sector

The unemployment in the enterprise sector fell by 25,000 people over the last quarter and 152,000 over the last year, i.e., 0.5% and 2.8% respectively.

The biggest drop in employment has traditionally occurred in sectors undergoing restructuring, i.e., hard coal mining, where 7,000 jobs were lost over the last quarter and 27,000 over the whole year (representing 3.6% and 12.8% drops, respectively). The steel industry lost 7,000 jobs within the last quarter (a 7% fall), and 20,000 people were laid off over the whole year (a 17.6% drop).

An increase in employment in market services was not enough to offset the losses due to redundancy in restructured industry, and a change in this respect is unlikely unless more radical steps are taken to make the labour market more flexible and lower labour costs, primarily in small businesses.

Reducing the working week or making the employment relationship more flexible – a short description based on the cases of France and Holland

The EU countries have been struggling with structural unemployment for many years. It is those countries that have most often developed strategies designed to reduce the scale of failures in structural adjustment. Both short-term and long-term measures have been developed. One example of such short-term measures is the reduction in the working week which is currently being introduced in France and which has recently been advocated in Poland. Long-term measures, on the other hand, are as a rule neither as simple nor as easy to push through politically, and entail taking a whole range of actions. Holland is a country which has employed this strategy.

In February 1998 the French parliament voted to reduce the official working week from 39 to 35 hours beginning in 2000. According to the government, this would increase the number of jobs by 700,000. The reduction of the working week was not the only measure introduced by the new law. The authorities also created an incentive scheme encouraging employers to introduce a 35-hour working week, including lower social pay-

Table 12. Components of the labour market, 1998–2002

		Employment		Registered unemployment	Unemployment rate
		thousand	% change	thousand	%
1998	1Q-4Q	15800	2.3	1831	10.4
1999	1Q-4Q	15710	-0.6	2350	13.0
forecast					
2000	*1Q-4Q*	*15508*	*-1.3*	*2627*	*14.4*
2001	*1Q-4Q*	*15546*	*0.2*	*2687*	*14.7*
2002	*1Q-4Q*	*15721*	*1.1*	*2648*	*14.3*
1998	1Q	15506	3.0	1846	10.4
	2Q	15819	2.9	1688	9.6
	3Q	15921	2.1	1677	9.6
	4Q	15953	1.4	1831	10.4
1999	1Q	15513	0.0	2170	12.1
	2Q	15726	-0.6	2074	11.6
	3Q	15808	-0.7	2178	12.1
	4Q	15792	-1.0	2350	13.0
2000	1Q	15185	-2.1	2532	14.0
	2Q	15524	-1.3	2437	13.6
	3Q	15638	-1.1	2529	14.0
forecast					
2000	*4Q*	*15685*	*-0.7*	*2627*	*14.4*
2001	*1Q*	*15155*	*-0.2*	*2722*	*15.0*
	2Q	*15548*	*0.2*	*2573*	*14.3*
	3Q	*15698*	*0.4*	*2629*	*14.5*
	4Q	*15785*	*0.6*	*2687*	*14.7*
2002	*1Q*	*15291*	*0.9*	*2735*	*14.9*
	2Q	*15719*	*1.1*	*2552*	*14.0*
	3Q	*15902*	*1.3*	*2575*	*14.1*
	4Q	*15974*	*1.2*	*2648*	*14.3*

Source: Annual and quarterly data with an exception of employment data – CSO; quarterly employment data and forecasts – CASE.

ments and taxes. Additionally, firms which both reduce the average employee's working time and hire new employees are entitled to extra financial relief, for example, a subsidy for employing new people and complete exemption from social payments for new employees for a period of 5 years.

This incentive scheme not only made it profitable to adopt the shorter working week but (most importantly) made it profitable to employ new workers. Moreover (as a result of a strong pressure from employers' organisations), it was possible to count the 35-hour week on a yearly basis. This allowed employers to keep the old 39-hour week and increase the length of vacations.

Although an improvement in the labour market has been observed following the introduction of the new regulations, there are doubts as to their actual effectiveness. It seems that the drop in unemployment in France was due not only to the changes in French law, but also to a decreasing trend in unemployment all over Europe. Second, the question remains whether the decline in France's unemployment was due more to the reduction in the working week or more to the accompanying system of incentives to employ new workers. Third, the unemployment rate in France remains one of the highest in Europe, and it does not look as if it will come any nearer to the British rate in the foreseeable future.

A slightly different model of reforms aimed at reducing unemployment has been adopted in Holland. It combines some elements of the liberal model used in, for instance, the Great Britain and the US, and the social model adopted, for example, in Germany and France.

The Dutch strategy, while using some elements of the Anglo-Saxon model, preserves at the same time the continental social protection of labour. First, the Dutch consolidated state finances and rationalised social expenditures. Second, a social consensus was reached which made it possible to maintain a relatively slow growth in real wages and salaries. Third, part-time work was popularised, and so-called 'flexible employment' – i.e., work without a permanent contract and fixed hours – has become common. However, all this is taking place in the context of continuing strong protection of the 'permanent' employment relationship, with a strong relation between average pay and the minimum wage, as well as high unemployment and social security benefits.

In the Dutch case, the continental model was preserved. However, regulations were introduced that enabled the interested parties (employers and employees) to dodge financial burdens and difficulties related to the model. In addition, some costs of the labour protection system were lowered, for example, by an artificial reduction in the inflexibility of wages and salaries. This made it possible to significantly reduce the unemployment rate, which reached 2.5% in August 2000. For the sake of comparison, in the mid-'80s the unemployment rate in Holland was roughly equal to the EU average, at around 11%–12%. Preserving the social protection system entails certain costs. One of the main costs is a relatively high percentage of the permanently unemployed in the total number of the jobless and the frequency of so-called flexible employment.

If we were to speculate on the feasibility of introducing the aforementioned models in Poland, then in the case of the French one, it seems too early to draw conclusions concerning the effectiveness of the reduced working week. First, the time in which the regulation has been in force is too short for sound inferences. Second, it is impossible to isolate other effects stemming from the introduction of employment incentives as well as from the exceptionally favourable external circumstances. At first glance, the Dutch model seems an attractive one. One should bear in mind, however, that the flexible forms of employment common in that country appear to be compatible with a 'dense' labour market, characterised by a wide choice of employers and a high percentage of highly qualified persons in the workforce. In Poland such markets appear only locally, in large urban centres. It seems that in Poland, a 'classical' flexible employment relationship is the only available means for bringing about real growth in employment and, consequently, a drop in unemployment.

Inflation

- **Inflationary pressures increased in 3Q00**
- **The continuation of disinflation process as early as in 4Q00**

Inflationary pressures increased again in 3Q00. The Consumer Price Index (CPI) rose by 10.8% yoy and Producer Price Index (PPI) – 8.5%. However, it should be emphasised that inflation (measured in terms of the CPI and the PPI) started to subside already in August. Whilst in July the CPI was 11.6% higher yoy, the September reading was 10.3%. The PPI followed suit and it fell from 9.0% in July to 8.3% in September.

The reasons behind the price increase at the beginning of 3Q00 are mainly supply-driven: supply of grains and processed food was down, the global fuel prices were up; prices of electricity continued to rise. On the demand side, money supply, consumer credits as well as wages and salaries remained under control.

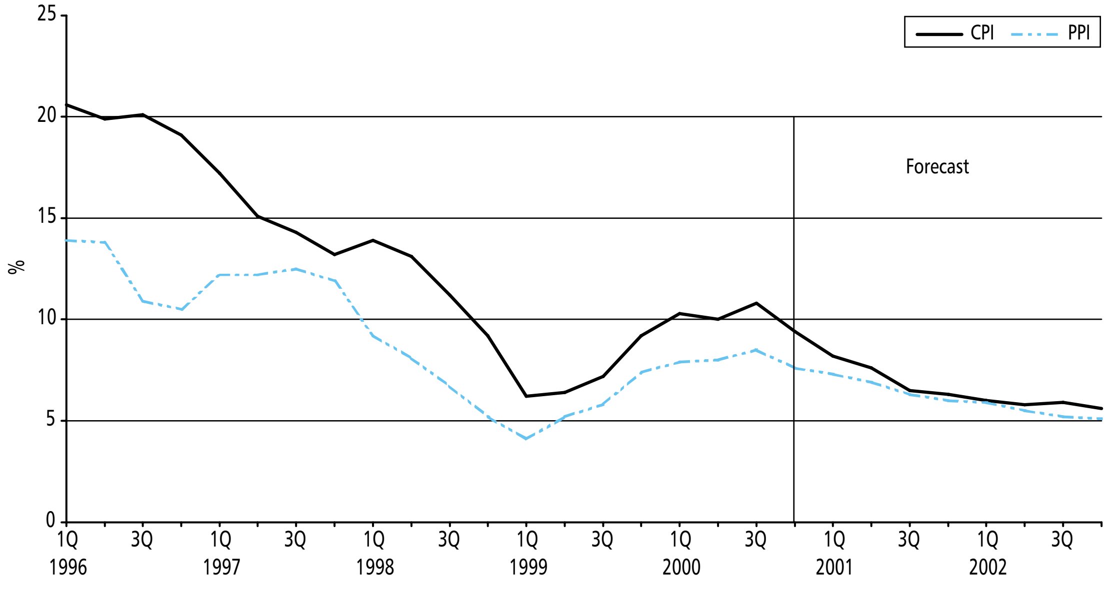
The acceleration of CPI in 3Q00 was caused primarily by increases in food prices. They were up by 12.7% yoy, driven mainly by a considerable increase in the price of bread and grain products. The latter occurred as a result of the aforementioned decrease in their supply, delayed interventions of the Agriculture Agency (*Agencja Rynku Rolnego*), and high customs duty on grains introduced last year. This protectionism indirectly led to a reduction in the number of swine and livestock which in turn caused the prices of meat to go up.

In 3Q00 annual growth in the prices of non-food products decreased. They were up by 9.3% in 3Q00, whereas in 2Q00 they stood at 10.4%. Weak consumer demand and the substitution effect (higher growth in food prices reduced additionally demand for durables) were mainly behind lower growth in prices. As in 2Q00, there was a marked upsurge in fuel prices in the domestic market as a result of a rise in global fuel prices in September, following a temporary stabilisation in the two previous months.

The prices of services rose by 11.4% yoy in 3Q00 as compared to 10.1% in 2Q00. Higher growth was due to a different calendar of electricity and gas price increases. In previous years, power stations were allowed to raise prices usually within one month. This year, however, the rise was extended for a few months as a result of prolonged negotiations with the newly established Energy Agency (*Urząd Regulacji Energetyki)*. First power stations raised prices in May and the last in September. Consequently, the whole process took much longer and distorted usual price dynamics.

In 3Q00, PPI continued to rise reaching 8.5% yoy. This rise resulted from the timing of electricity and gas price increases, and a September increase in base fuel prices by 6%. The relative strengthening of the currency basket

Figure 9. CPI and PPI, 1996–2002 (% change yoy)



Source: CSO and CASE.
Note: CASE forecast starting from 4Q00.

between June and August and weaker domestic demand have acted as stabilising factors. The latter manifested itself in a drop in new orders for the industry and an increase in stocks of finished goods.

We envisage a gradual slowdown in monthly growth rates of food prices in the next three months. This will result from the predicted decline in the growth of prices of bread, grain products, and meat. Due to high grain and fuel prices, profitability of cattle-breeding will be low next year and this will be reflected in the limited number of swine and livestock. This, in turn, may prevent a quick stabilisation of meat prices. We forecast healthier crops between 2001–2002 and increased flexibility of interventions on the part of the Agriculture Agency. In addition, we expect a gradual increase in the popularity of swine-breeding among farmers, which might help to ease the so-called hog cycle.

Table 13. Basic price indicators, 1998–2002 (% change yoy)

		Price indices				Currency basket	GDP deflator
		CPI	PPI	exports	imports		
1998	1Q-4Q	11.8	7.3	6.8	2.4	6.1	11.7
1999	1Q-4Q	7.3	5.6	8.1	7.2	10.3	7.1
forecast							
2000	*1Q-4Q*	*10.1*	*8.0*	*4.6*	*6.4*	*2.1*	*8.7*
2001	*1Q-4Q*	*7.2*	*6.6*	*5.9*	*5.1*	*4.7*	*7.0*
2002	*1Q-4Q*	*5.8*	*5.4*	*6.2*	*5.2*	*4.2*	*5.9*
1998	1Q	13.9	9.2	10.4	9.9	13.1	11.9
	2Q	13.1	8.1	8.1	3.2	6.7	12.1
	3Q	11.2	6.7	6.0	-0.1	3.9	12.0
	4Q	9.2	5.2	3.9	-1.4	1.6	11.4
1999	1Q	6.2	4.1	8.0	2.7	9.0	7.2
	2Q	6.4	5.2	7.0	7.3	12.5	7.2
	3Q	7.2	5.8	4.7	6.6	7.7	5.9
	4Q	9.2	7.4	11.8	11.3	11.5	7.8
2000	1Q	10.3	7.9	1.1	6.6	1.9	7.8
	2Q	10.0	8.0	3.5	7.4	3.2	8.3
	3Q	10.8	8.5	6.6	7.0	2.1	9.5
forecast							
2000	*4Q*	*9.4*	*7.6*	*7.0*	*4.6*	*1.3*	*9.0*
2001	*1Q*	*8.2*	*7.3*	*5.8*	*5.1*	*5.4*	*8.2*
	2Q	*7.6*	*6.9*	*4.5*	*4.4*	*4.3*	*7.4*
	3Q	*6.5*	*6.3*	*5.5*	*5.3*	*5.2*	*6.7*
	4Q	*6.3*	*6.0*	*6.2*	*5.2*	*4.2*	*6.1*
2002	*1Q*	*6.0*	*5.9*	*6.7*	*5.7*	*4.7*	*6.4*
	2Q	*5.8*	*5.5*	*6.3*	*5.3*	*4.3*	*6.1*
	3Q	*5.9*	*5.2*	*6.0*	*5.0*	*4.0*	*5.8*
	4Q	*5.6*	*5.1*	*6.0*	*5.0*	*4.0*	*5.5*

Source: Annual data – CSO; currency basket – NBP; GDP deflator, estimates (e) with an exception of CPI, PPI and the currency basket, and forecasts – CASE.
Note: Currency basket over 1996–1998 consists: 55% of US$ and 45% of DM, and from 1999: euro – 55% and US$ – 45%.

Figure 10. Export and import price indices and nominal change in the currency basket, 1996–2002 (% change yoy)

Source: CSO and CASE.
Notes: 1. CASE forecast starting from 4Q00.
2. Currency basket over 1996–1998 consists: 55% of US$ and 45% of DM, and from 1999: euro – 55% and US$ – 45%.

We forecast a deceleration in the growth of non-food prices in 2001. This will stem from tight monetary policy and a further gradual slowdown in the growth of wages and salaries. It also seems that the crude oil prices in the world markets should be increasingly lower, that will stabilise prices in the domestic market.

We expect the prices of services to stabilise in 4Q00. In 1Q01 we expect a rise in the quasi-administered prices, while in 2Q01 a rise in the price of electricity and gas is expected. In our view, the scale of the latter will not exceed the inflation level by more than 2–3 percentage points. The price of gas, imported mainly from Russia, is difficult to predict. If it turns out that the prices are subject to re-negotiation, as Poland's suppliers insist on, then we may expect an inflationary boost. In 2002 we project growth in the quasi-administered prices of 2–3 percentage points higher than the CPI rate.

We expect a continued downward trend of the PPI growth mainly on the back of weak domestic demand and increased economic efficiency. We also expect crude oil prices to fall in the world markets. Consequently, one of the main drivers of the PPI would be eliminated.

Exchange rate

- **Relative appreciation of the zloty compared to 1999**
- **The euro loses against the dollar**
- **Weaker real appreciation of the zloty in 2001–2002**

Another quarter (third in a row) witnessed a relative appreciation of the zloty and considerable daily volatility of the nominal exchange rate. The latter was mainly as a result of releases of monthly data on the current account deficit, the daily exchange rate of the euro against the dollar, and the changing opinions on the possible realisation of the budget deficit planned in 2001. Moreover, the currency market still remains very shallow with daily turnover below US$1 billion.

An expected reduction in the current account deficit to below 7% of the GDP by the end of the year nevertheless calmed the currency market. Nonetheless, the market sentiment was shifting along with changing monthly results of the balance of payments. It does not look, however, as if any external events worse than those from the first three quarters were to take place until the

Core inflation

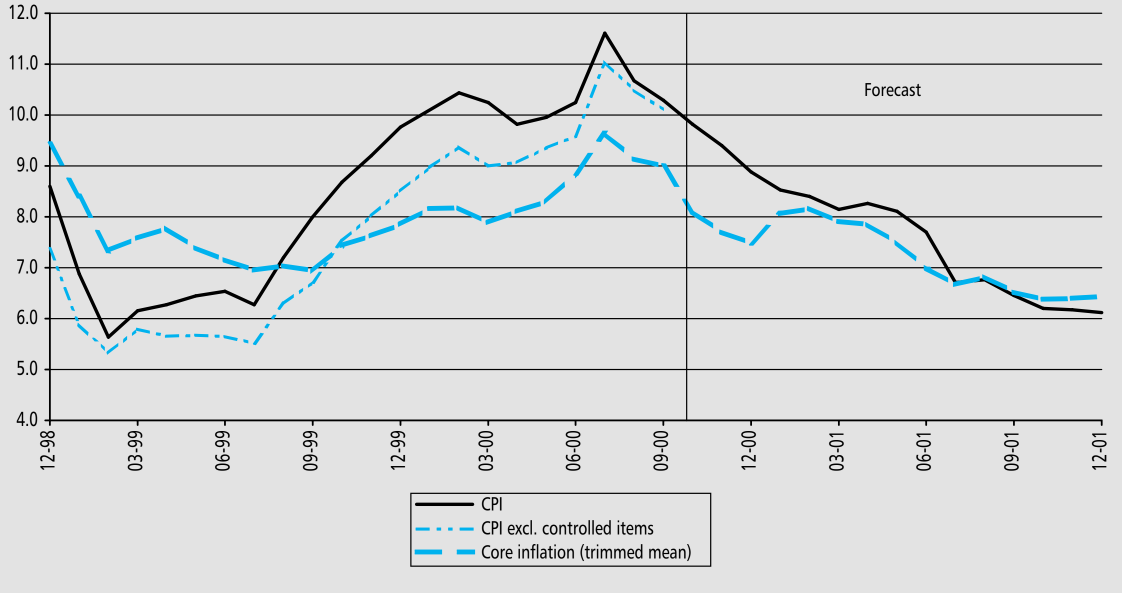
The 12-month dynamics of core inflation reached their peak in July and began to show a falling trend since August. This trend is likely to be sustained until the end of 2001 with the exception of 1Q01 when a slight increase and stabilization of the dynamics is predicted. The figure below shows the behavior of the Consumer Price Index (CPI) along with two alternative measures of inflation: the core inflation (trimmed mean) and the CPI calculated with exclusion of the administratively controlled goods and services that is quoted by the NBP (author's calculations).

In July all indices reached their highest values in several years and entered the long-run falling path. The core inflation index has exhibited consistently lower dynamics than the CPI for over a year now. The immediate cause of this situation has been the presence of temporary shocks of supply nature that have come to dominate the inflation process resulting in disproportionally big price hikes in a few sectors. Although many of these shocks are gradually disappearing, their impact is still reflected in the distance between the core index and the CPI. Main factors behind higher CPI dynamics in the past months have originated in the food sector. Compared with September 1999 prices of flour and bread were higher in September 2000 by almost 30%, eggs by 36% and sugar by 65%. Additionally, the impact of the increases in the energy sector is still transmitted to the CPI. Although recent months brought a relative stabilization in this sector, the 12-month dynamics of gasoline and liquid gas prices is still among the highest in the overall index and amounts to 26% and 47% respectively.

The distance between the standard CPI and the CPI calculated without the influence of administratively controlled prices has narrowed markedly. This distance, albeit still positive, has currently reached the lowest level in years, which points to the weakening of the dominant role that controlled prices have played in the inflation processes throughout the 1990s.

We predict that most of the effects of supply shocks that were behind higher CPI dynamics during the past 12 months will recede and gradually disappear in the near future. As a consequence, we forecast a fall in core inflation in 4Q00. The dynamics of the core index is likely to pick up slightly in the very beginning of the next year, then stabilize around 8% in 1Q01 to reenter the falling trend right after and follow it until the end of 2001. We predict that the values of CPI and the core index will coincide in 3Q01 and consequently core inflation will exhibit higher dynamics than CPI.

Core inflation, 1998–2001

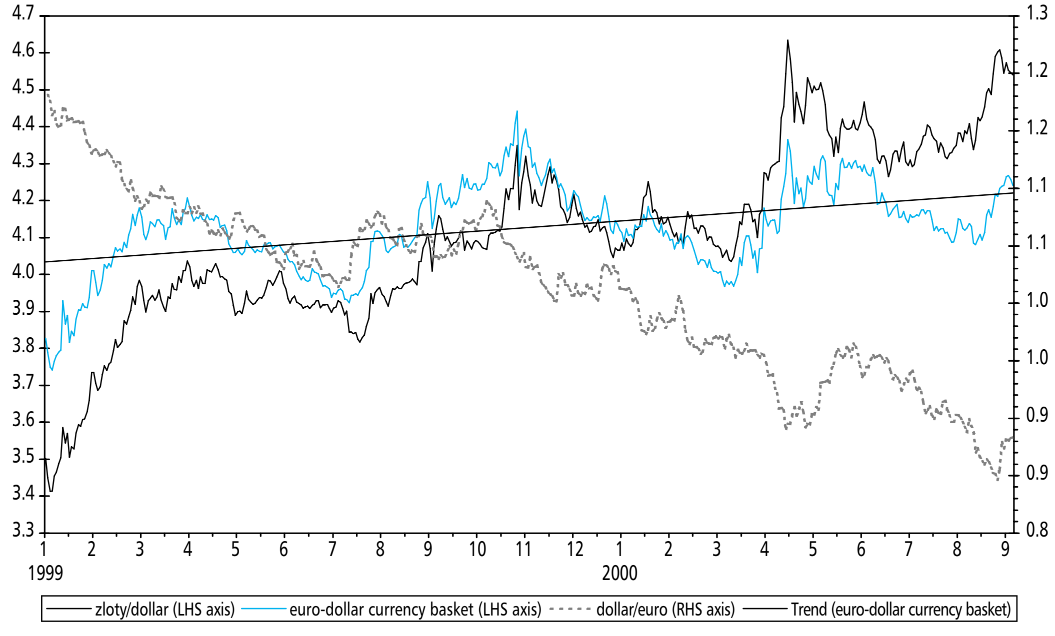


Source: CSO and CASE.

end of this year. They comprised primarily a sharp upsurge in the price of crude oil and the depreciation of the euro against the dollar from 1.02 to 0.85 between January and September 20 (i.e. by 18.4%).

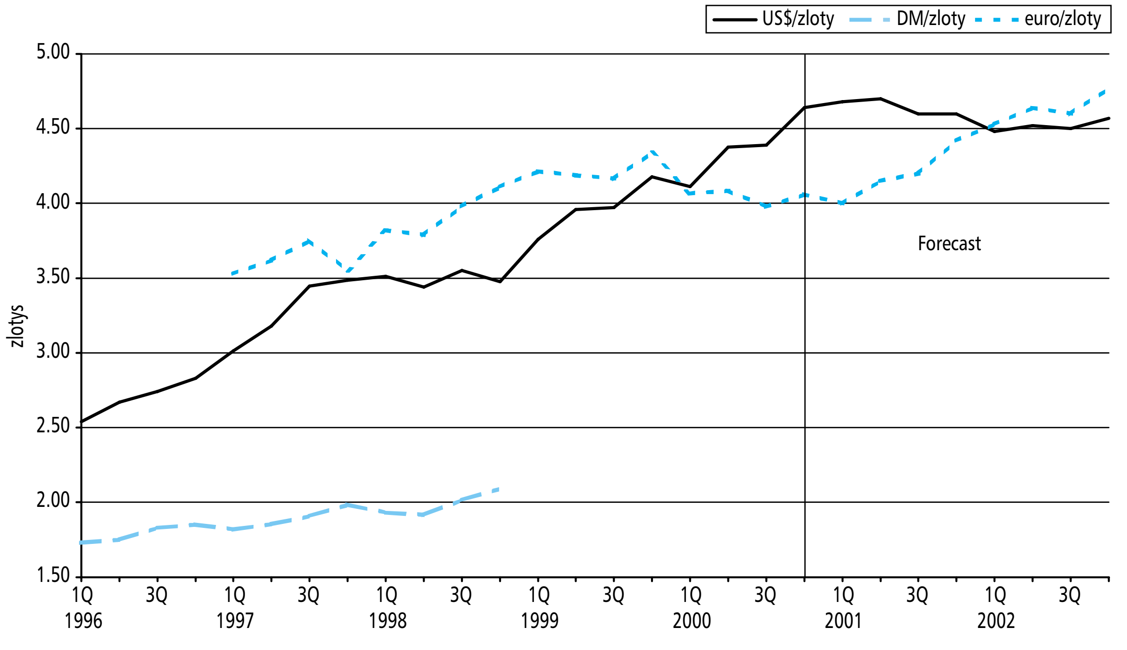
The draft budget for 2001 was released in mid-July. The introduction of a concept of economic deficit (see fiscal policy) and news on the scale of fixed budgetary expenditure along with their rescheduled realisation

Figure 11. Average exchange rates of the zloty against the dollar and the euro-dollar currency basket, 1999–2000



Source: NBP.

Figure 12. Basic exchange rates, 1996–2002 (in zlotys)



Source: NBP and CASE.
Note: CASE forecast starting from 4Q00.

within the 2001 budget triggered a wave of contradictory analyses, although the currency market reacted positively. Sticking to the original provisions as to the scale of the budget deficit in the budget bill for the parliament due November 15 will send a clear signal to the markets. Given the improved deficit in the current account and lower inflation, the budget deficit remains the only uncertain factor influencing the way foreign investors perceive the Polish economy.

Another factor disturbing the proper functioning of the exchange rate market is its 'dollarisation' in the face of the dominant positions of London banks. This is in sharp contrast to the big share (roughly of 50%) of trans-

Table 14. Basic exchange rates, 1998–2002 (in zlotys)

		US$	DM	ECU/Euro	Real effective exchange rate
1998	1Q-4Q	3.49	1.99	3.92	151.3
1999	1Q-4Q	3.97	2.16	4.23	147.2
forecast					
2000	*1Q-4Q*	*4.38*	*2.07*	*4.05*	
2001	*1Q-4Q*	*4.65*	*2.14*	*4.19*	
2002	*1Q-4Q*	*4.52*	*2.37*	*4.64*	
1998	1Q	3.51	1.93	3.82	151.7
	2Q	3.44	1.92	3.79	153.8
	3Q	3.55	2.02	3.98	150.2
	4Q	3.48	2.09	4.11	147.4
1999	1Q	3.76	2.15	4.22	144.5
	2Q	3.96	2.14	4.19	147.4
	3Q	3.97	2.13	4.17	150.1
	4Q	4.18	2.22	4.34	146.7
2000	1Q	4.11	2.08	4.07	158.1
	2Q	4.38	2.09	4.08	159.2
	3Q	4.39	2.03	3.98	167.0
forecast					
2000	*4Q*	*4.64*	*2.08*	*4.06*	
2001	*1Q*	*4.68*	*2.05*	*4.00*	
	2Q	*4.70*	*2.12*	*4.15*	
	3Q	*4.60*	*2.15*	*4.20*	
	4Q	*4.60*	*2.26*	*4.42*	
2002	*1Q*	*4.48*	*2.32*	*4.53*	
	2Q	*4.52*	*2.37*	*4.64*	
	3Q	*4.50*	*2.35*	*4.60*	
	4Q	*4.57*	*2.44*	*4.77*	

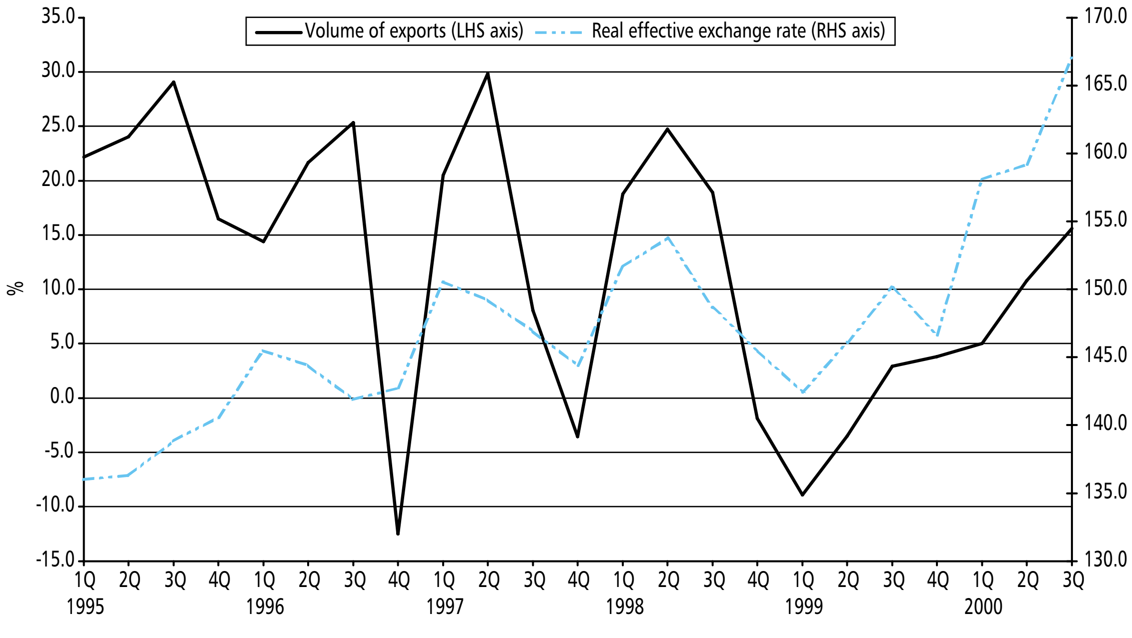
Source: NBP, real effective exchange rate – JP Morgan, forecast – CASE.
Notes: 1. Average exchange rates.
2. Real effective exchange rate, 1990 average = 100.
3. Until end-1998 - the ECU and then the euro.

actions denominated in the euro in total Polish foreign trade. With strong volatility of the euro-dollar exchange rate, such a market structure leads to the strengthening of domestic signals (both positive and negative) and in turn increases the zloty-dollar exchange rate volatility. The latter, for historical reasons (dollarisation of the economy under socialism), is of prime importance for the public evaluation of Poland's macroeconomic stance. This apparent contradiction will not be resolved until the zloty is officially fixed to the euro. This can happen in the event of Poland's entry into the ERM II after 2003 or of the euroisation, i.e. a unilateral adoption of the euro.

From January 1, 1999 to September 30, 2000 the euro-dollar exchange rate depreciated by over 25% in nominal terms and by over 14% within three quarters of 2000 alone. At the same time, the zloty exchange rate against the dollar depreciated by over 31% and 10%, respectively and the zloty exchange rate against the euro appreciated by 1.8% and over 4%, respectively. The euro-dollar basket, in our view, is the most relevant indicator of the zloty's nominal depreciation/ appreciation. The zloty exchange rate against the currency basket depreciated by 12% between 1999 and 2000 and by 2.4% only this year. In nominal terms, zloty's exchange rate against the currency basket remains stable, yielding real annual appreciation of the zloty of roughly 7%. The stable zloty exchange rate against the currency basket enables in practice a very effective hedging against the risks of changes in cross exchange rates of the euro and the dollar and their impact on the zloty exchange rate.

As a result of the euro-dollar exchange rate volatility in September, the zloty depreciated against the dollar reaching the quarterly maximum of 4.61 on September 21 (the lifetime low of the euro against the dollar was recorded on September 20). The euro-dollar exchange rate – after eliminating budget policy uncertainties and sustained positive macroeconomic trends – will remain the key factor affecting the zloty exchange rate against the dollar. In view of possible considerable volatility of the euro-dollar exchange rate, one might also expect an increased volatility of the zloty-dollar exchange rate. This volatility will not be mitigated by the expected inflows of short-term foreign capital after passing the budget bill in the Parliament at the beginning of next year.

Figure 13. The volume of exports and real effective exchange rate, 1995–2000



Source: CSO and JP Morgan.
Notes: 1. Real effective exchange rate (right-hand scale), 1990 average = 100.
2. The volume of exports – according to the national accounts' definition.

Foreign trade

- **Weaker import growth**
- **Good performance of exports**
- **Terms of trade still at an unfavourable level**

A considerable slowdown in domestic demand in 2Q00 and 3Q00 – due to tight economic policy and a drop in the growth of real household incomes (which directly dampens imports of consumer goods and, indirectly, imports of commodities via weaker demand for domestic production) – caused a drop in import demand. Consequently, we estimate the rate of growth of import volume (according to customs data) fell from 13.5% in 2Q00 to 3.6% yoy in 3Q00. According to preliminary NBP's estimates, imports stood at US$10.5 billion yielding a slight annual increase (US$0.4 billion) as well as in comparison to the previous quarter (US$0.66 billion).

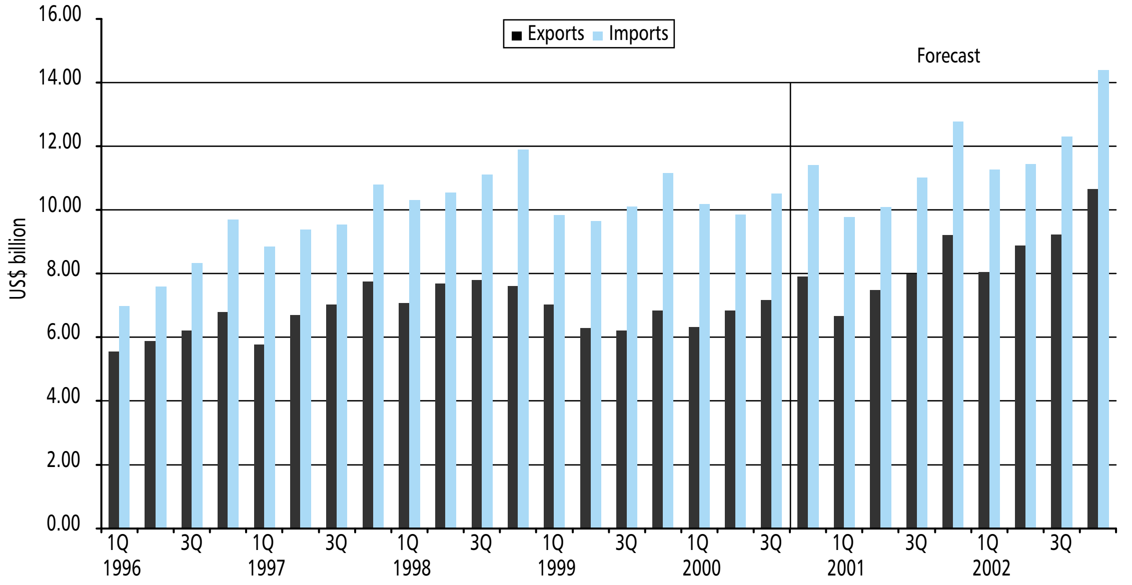
For 2001–2002 we forecast an increase in import growth as a result of acceleration in domestic demand

Table 15. Exports, imports and net exports, 1998–2002 (US$ billion)

		Exports			Imports			Net exports		
		NBP	CSO	National accounts	NBP	CSO	National accounts	NBP	CSO	National accounts
1998	1Q-4Q	30.12	28.23	44.62	43.84	47.05	52.92	-13.72	-18.83	-8.30
1999	1Q-4Q	26.35	27.41	40.75	40.73	45.91	50.84	-14.38	-18.50	-10.08
forecast										
2000	*1Q-4Q*	*28.24*	*31.49*	*41.61*	*41.93*	*49.43*	*51.07*	*-13.69*	*-17.95*	*-9.45*
2001	*1Q-4Q*	*31.35*	*34.91*	*46.24*	*43.67*	*52.43*	*55.31*	*-12.32*	*-17.51*	*-9.07*
2002	*1Q-4Q*	*36.82*	*41.04*	*54.29*	*49.39*	*60.03*	*63.95*	*-12.57*	*-18.99*	*-9.67*
1998	1Q	7.06	7.02	10.82	10.30	11.09	12.59	-3.24	-4.06	-1.77
	2Q	7.67	7.04	11.31	10.55	11.70	13.16	-2.88	-4.65	-1.85
	3Q	7.80	6.89	11.13	11.10	12.00	13.09	-3.30	-5.10	-1.96
	4Q	7.60	7.27	11.35	11.90	12.28	14.09	-4.31	-5.00	-2.73
1999	1Q	7.01	6.62	9.79	9.83	10.26	12.32	-2.82	-3.64	-2.53
	2Q	6.28	6.51	9.56	9.64	11.13	12.42	-3.36	-4.62	-2.86
	3Q	6.21	6.75	10.48	10.10	11.54	12.63	-3.89	-4.79	-2.15
	4Q	6.84	7.53	10.92	11.15	12.99	13.47	-4.31	-5.46	-2.54
2000	1Q	6.32	7.55	8.89	10.17	11.77	11.98	-3.85	-4.22	-3.09
	2Q	6.84	7.51	9.57	9.85	12.28	12.02	-3.01	-4.77	-2.45
	3Qe	7.18	7.82	11.38	10.51	12.00	13.10	-3.33	-4.18	-1.73
forecast										
2000	*4Q*	*7.90*	*8.60*	*11.78*	*11.40*	*13.38*	*13.97*	*-3.50*	*-4.78*	*-2.19*
2001	*1Q*	*6.65*	*7.94*	*9.35*	*9.78*	*11.54*	*11.99*	*-3.12*	*-3.60*	*-2.64*
	2Q	*7.49*	*8.23*	*10.48*	*10.09*	*12.84*	*12.82*	*-2.61*	*-4.61*	*-2.34*
	3Q	*7.99*	*8.71*	*12.67*	*11.01*	*12.81*	*14.27*	*-3.02*	*-4.10*	*-1.60*
	4Q	*9.22*	*10.03*	*13.74*	*12.79*	*15.24*	*16.24*	*-3.57*	*-5.21*	*-2.49*
2002	*1Q*	*8.05*	*9.62*	*11.32*	*11.27*	*13.49*	*14.15*	*-3.22*	*-3.87*	*-2.83*
	2Q	*8.86*	*9.74*	*12.41*	*11.43*	*14.73*	*14.86*	*-2.56*	*-4.98*	*-2.44*
	3Q	*9.25*	*10.09*	*14.67*	*12.30*	*14.47*	*16.29*	*-3.04*	*-4.39*	*-1.62*
	4Q	*10.65*	*11.60*	*15.88*	*14.40*	*17.34*	*18.66*	*-3.74*	*-5.74*	*-2.77*

Source: NBP, CSO, estimates (e) and forecasts – CASE.
Note: National accounts – according to the CSO definition (merchandise trade plus the value of transport, construction and communication services, net processing turnover, printing services and others).

Figure 14. Exports and imports, 1996–2002 (US$ billion)



Source: NBP and CASE.
Note: CASE forecast starting from 4Q00.

and faster growth in real household incomes. The growth will stabilise at 10% annually (according to the national accounts' nomenclature), and will be twice as fast as last year, but markedly slower than in the period 1995–1998.

There has been a sustained improvement in Polish exports initiated at end-1999. The NBP estimates exports at US$7.2 billion on the payment basis, i.e. more than in the previous quarter (by US$0.96 billion) and in 3Q99 (by US$ 0.34 billion). In 3Q00 the annual rate of growth in export volume (according to customs data) declined to 18.2%, while it stood at 21.6% in 2Q00. This deterioration is partially attributable to a low base effect in 2Q00.

The first half of 2000 marked similar growth rates of export volume to the EU and Central European countries- 21.1% and 21.3%, respectively. After eight months, exports to Russia and the Ukraine are outside the top ten main Polish export markets (the two countries occupy 11th and 12th place in the ranking).

In the baseline scenario we forecast a gradual increase in export growth. This, as we predicted, will be feasible due to economic boost in EU after 2001 and an improved economic situation in Russia and Ukraine. In addition, we expect a change in the product structure of Polish manufacturing towards goods of higher value-added as well as increased competitiveness of Polish producers.

As we predicted, the terms of trade in 2Q00 were roughly on the same level as in 1Q00 and stood at 96.2. This value stemmed from a still low growth in export prices denominated in zlotys (3.5% yoy) and sustained growth in import prices (7.6%). Import prices are still to a large extent determined by high crude oil prices. They also rose as a result of the weaker zloty against the dollar in 2Q00. In 3Q00 the terms of trade could slightly deteriorate (on the back of increased import prices due to another increase in global crude oil prices and decreased export prices denominated in zlotys due to the euro's depreciation). However, 4Q00 will see an improvement although the terms of trade will stay below 100. This unfavourable development will continue to lower Poland's purchasing power in foreign trade.

Balance of Payments

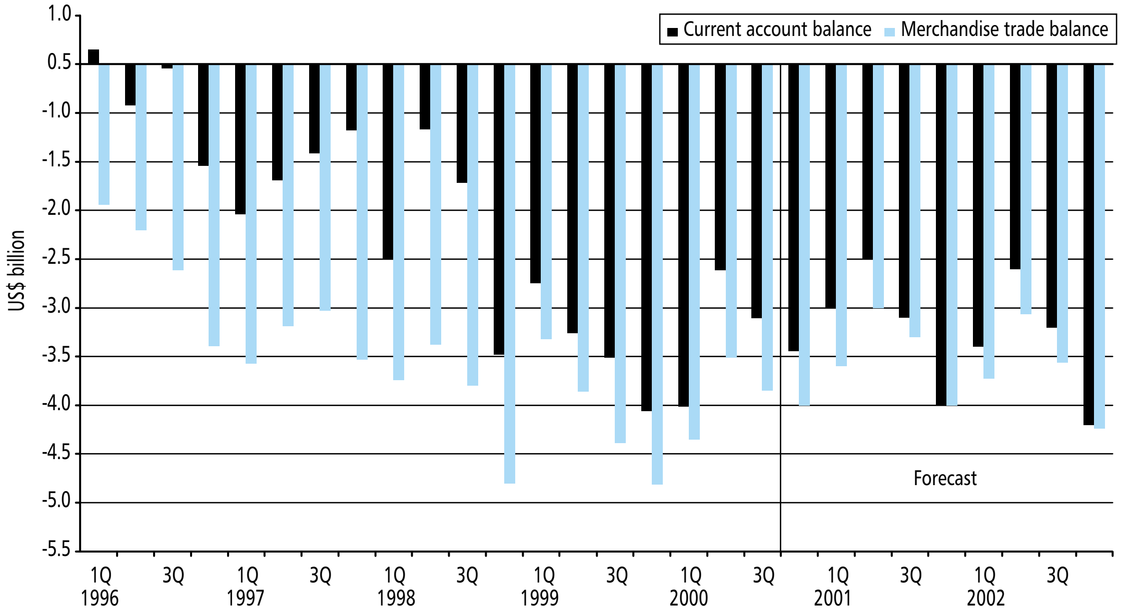
- **Good current account**
- **Outflows of portfolio capital**
- **Lower FDI inflows**

Table 16. Components of the balance payments, 1998–2002 (US$ billion)

	Balance on					Net direct investment	Net portfolio investment	Net credits beyond 1 year	Change in foreign currency reserves	Foreign currency reserves
	current account	% of GDP	merchandise trade	unclassified current transactions	capital and financial account					
1998 1Q-4Q	-6.86	-4.33	-13.72	6.00	11.67	4.97	1.33	1.75	6.71	27.38
1999 1Q-4Q	-11.57	-7.44	-14.38	3.64	8.25	6.35	1.45	2.07	0.16	25.49
forecast										
2000 1Q-4Q	-11.02	-6.87	-13.69	3.87	8.84	8.17	2.08	0.49	0.45	26.68
2001 1Q-4Q	-9.90	-5.79	-12.32	4.35	11.40	7.80	1.10	2.10	1.50	28.18
2002 1Q-4Q	-10.20	-5.18	-12.57	4.10	11.20	7.20	1.00	2.70	1.00	29.18
1998 1Q	-2.00	-5.67	-3.24	1.16	3.24	1.00	0.21	0.21	2.58	23.06
2Q	-0.67	-1.71	-2.88	1.72	2.19	1.26	0.36	0.44	1.99	25.26
3Q	-1.22	-3.08	-3.30	1.87	3.54	1.68	-0.86	0.13	1.81	27.08
4Q	-2.98	-6.62	-4.31	1.25	2.70	1.02	1.61	0.97	0.23	27.38
1999 1Q	-2.24	-6.26	-2.82	0.80	1.85	1.13	-0.29	-0.11	0.85	26.60
2Q	-2.76	-7.41	-3.36	0.79	1.29	1.04	0.03	0.60	-0.64	25.85
3Q	-3.01	-7.67	-3.89	1.15	2.06	2.47	-0.09	1.01	-0.23	26.03
4Q	-3.56	-8.30	-4.31	0.90	3.05	1.71	1.80	0.57	0.18	25.49
2000 1Q	-3.52	-9.39	-3.85	0.73	2.08	1.55	2.44	-0.02	-0.57	25.59
2Q	-2.11	-5.51	-3.01	1.06	1.16	1.12	0.24	0.04	-0.26	25.34
3Q	-2.26	-5.58	-3.33	1.08	1.20	0.90	-0.11	0.17	0.01	25.42
forecast										
2000 4Q	*-3.14*	*-7.16*	*-3.50*	*1.00*	*4.40*	*4.60*	*-0.50*	*0.30*	*1.26*	*26.68*
2001 1Q	*-2.80*	*-7.48*	*-3.12*	*0.80*	*2.60*	*1.60*	*-0.10*	*0.50*	*-0.20*	*26.48*
2Q	*-1.80*	*-4.45*	*-2.61*	*1.00*	*2.20*	*1.70*	*0.20*	*0.70*	*0.40*	*26.88*
3Q	*-2.00*	*-4.59*	*-3.02*	*1.40*	*2.60*	*2.00*	*0.40*	*0.50*	*0.60*	*27.48*
4Q	*-3.30*	*-6.65*	*-3.57*	*1.15*	*4.00*	*2.50*	*0.60*	*0.40*	*0.70*	*28.18*
2002 1Q	*-2.90*	*-6.59*	*-3.22*	*0.80*	*3.00*	*1.50*	*0.50*	*0.60*	*0.10*	*28.28*
2Q	*-1.80*	*-3.82*	*-2.56*	*0.95*	*2.00*	*1.40*	*0.40*	*0.70*	*0.20*	*28.48*
3Q	*-2.10*	*-4.21*	*-3.04*	*1.30*	*2.50*	*1.90*	*0.10*	*0.70*	*0.40*	*28.88*
4Q	*-3.40*	*-6.09*	*-3.74*	*1.05*	*3.70*	*2.40*	*0.00*	*0.70*	*0.30*	*29.18*

Source: Data and estimates (e) – NBP; forecasts – CASE.
Note: 3Q00 data – preliminary.

Figure 15. Merchandise trade balance and current account balance, 1996–2002 (US$ billion)



Source: NBP and CASE.
Note: CASE forecast starting from 4Q00.

According to the NBP's preliminary data, the current account deficit stood at US$2.3 billion in 3Q00. This constitutes a slight deterioration as compared to the previous quarter, but is still a satisfactory result. The accumulated annual current account deficit reached 7.2% of GDP. This relative improvement in the current account deficit is largely attributable to a comparatively low merchandise trade deficit that amounted to US$3.3 billion (i.e. 0.3 billion more qoq and 0.5 billion less yoy).

In addition, the deficit in trade of services was lower qoq and yoy and stood at US$329 million. Thus, the deficit continues a downward trend since the beginning of the year.

The unclassified current transactions stayed on roughly the same level as in 2Q00 (US$1.1 billion), although in September they edged up to US$420 million – a record high for almost a year. This might be indicative of a gradual improvement in the unclassified current transactions.

It should be emphasised, however, that the relatively low deficit on the current account stems also from rescheduling interests payments on Poland's debts from September to October. The income deficit, and in turn the current account deficit, could have been larger by almost US$200 million. As a result, a deterioration in the balance of current account should be expected in October.

Tighter economic policy in the first three quarters of 2000 could continue to dampen domestic demand and, at the same time, demand for imported goods and services in 4Q00. Consequently, we expect a further improvement in the current account deficit recorded since 2Q00. The deficit will reach US$11.0 billion in the entire 2000, i.e. 6.9% of GDP (0.6 percentage points less than in 1999).

In the years to come, import growth will stabilise at a level higher than in 2000, that is roughly 10.0% (according to national accounts' nomenclature). This will result from higher real incomes and stronger domestic demand. At the same time, a strong export performance will stabilise the merchandise trade deficit at roughly US$10 billion in 2001–2002.

The improved current account balance will be also attributable to increased transfers, mainly from EU funds, as the date of Poland's entry to the Union draws closer.

In 3Q00 the net inflows of foreign direct investment were very small reaching a mere US$0.9 billion – a 3-year low. In part, this stems from delayed privatisation of Polish Telecom. As a consequence, one could expect higher inflows in 4Q00.

As early as 2001, aside from the end of privatisation of 'large enterprises', lower inflows of foreign direct investment are expected. Their further decrease will progress in 2002, while in subsequent years one could expect increased inflows of *greenfield* investment.

The net inflow of portfolio capital was negative in 3Q00. In August, there was a net outflow of capital of US$0.23 billion. Initially, the NBP estimated the outflow at over US$0.4 billion. The revision concerned, first of all, the debt instruments – Polish investments abroad were overestimated, as was the outflow of portfolio capital due to debt instruments. A raise in interest rates by 150 base points on August 31 did not spur a significant return of portfolio investment in September. As a result of the still high Polish portfolio investment abroad, the portfolio capital balance in September was negative again.

Large errors and omissions in 3Q00 may be due to undervaluation of capital inflows into Poland. The data on 3Q00 are likely to be revised in the coming months and the figures on the errors and omissions item will be corrected accordingly.

Gross reserve assets have been falling for a year. They reached US$25.4 billion at end-September – US$0.57 billion less than at end-June. Still this amount is enough to cover 7-month average imports. At end-2000 we forecast that the reserves will reach US$28.7 billion (also equivalent of 7-month imports). We expect sustained improvement in the balance of payments in the coming years.

Public finances

- **Increased deficit of public finances in 2000**
- **Delayed proceeds from privatisation**
- **Uncertainties surrounding the 2001 budget**

The realisation of the government budget in 2000

In the first three quarters, 69.5% of the planned budgetary revenues for the entire year were fulfilled (roughly as in the previous year). Revenues from indirect taxes were fulfilled to a smaller extent (67.7%), which can be attributed to weaker growth in consumer demand. Personal income tax revenues remain lower than expected (61.0%). As compared to the first half of the year, there was a rapid growth in corporate income tax revenues (80.2%) mainly due to a marked improvement in the financial standing of enterprises. Customs duty revenues continue to grow at a high rate (82.0%). The NBP did not transfer its proceeds in the last quarter. A somewhat higher level of budget realisation has been recorded on the expenditure side; in the first three quarters of 2000, 71.6% of the planned expenditure was fulfilled (a level comparable with last year's). The high fulfilment of domestic debt servicing (75.4%) – due to high interest rates – should be noted as opposed to foreign debt servicing (64.8%). Labour Fund (*Fundusz Pracy*) expenditure indicator remains high (84.1%), which means that the planned funds will run dry by the end of the year. The loans taken out by the Labour Office (*Urząd Pracy*) will only add to the general budget deficit in 2000 (probably by roughly 0.1% of GDP).

As a result, the government budget deficit reached 14 million zlotys, i.e. 90.8% of the planned budget deficit for 2000 after three quarters and grew by 3.2 billion zlotys in 3Q00. This means a relative deterioration in the government budget. In 3Q00, it was usually possible to maintain a balanced budget on the back of considerable seasonal fluctuations in expenditure (relatively lower in the summer). In 3Q00 foreign debt was brought down by 2.4 billion zlotys (according to budgetary plans it should drop yet this year by additional 1.0 billion zlotys). The state borrowing needs on domestic market increased due to a rise in compensation payments in 3Q00 (1.1 billion zlotys i.e. 78.6% of the plan). The deficit in three quarters was financed by means of privatisation proceeds (3.3 billion zlotys), issue of bonds (2.0 billion zlotys) and a rapid growth in the issue of T-bills (4.9 billion zlotys). A sharp upturn in domestic debt in the first three quarters is attributable to the realisation of only 37.6% of planned privatisation proceeds. This low rate of growth resulted from delayed sell-off of Polish Telecom shares. After this transaction was closed

Table 17. Selected items of the government budget, 1998–2002 (zlotys billion)

		Revenues		Expenditures	Central government balance	
		total	of which tax revenues		zlotych billion	% of GDP
1998	1Q-4Q	126.5	113.8	139.8	-13.3	-2.4
1999	1Q-4Q	125.9	112.7	138.5	-12.6	-2.0
forecast						
2000	*1Q-4Q*	*136.4*	*120.4*	*151.8*	*-15.4*	*-2.2*
2001	*1Q-4Q*	*159.0*	*141.7*	*172.9*	*-13.9*	*-1.8*
2002	*1Q-4Q*	*175.7*	*157.0*	*179.3*	*-3.7*	*-0.4*
1998	1Q	28.7	25.6	32.3	-3.5	-2.9
	2Q	29.3	26.3	35.1	-5.8	-4.4
	3Q	33.1	29.9	34.1	-1.1	-0.8
	4Q	35.5	32.1	38.3	-2.8	-1.8
1999	1Q	27.7	24.8	36.5	-8.7	-6.5
	2Q	28.8	25.2	31.4	-2.6	-1.8
	3Q	32.4	29.5	32.4	0.0	0.0
	4Q	36.9	33.1	38.2	-1.3	-0.7
2000	1Q	30.9	27.6	37.9	-6.9	-4.5
	2Q	33.2	27.5	37.1	-3.8	-2.3
	3Q	33.8	31.0	37.0	-3.2	-1.8
forecast						
2000	*4Q*	*38.5*	*34.4*	*39.9*	*-1.4*	*-0.7*
2001	*1Q*	*34.5*	*30.8*	*42.2*	*-7.8*	*-4.4*
	2Q	*38.4*	*32.1*	*43.0*	*-4.6*	*-2.4*
	3Q	*40.6*	*37.7*	*39.9*	*0.8*	*0.4*
	4Q	*45.5*	*41.1*	*47.8*	*-2.3*	*-1.0*
2002	*1Q*	*38.2*	*34.3*	*44.6*	*-6.4*	*-3.2*
	2Q	*42.3*	*35.6*	*44.3*	*-2.0*	*-0.9*
	3Q	*44.9*	*41.7*	*41.4*	*3.6*	*1.6*
	4Q	*50.2*	*45.4*	*49.0*	*1.2*	*0.5*

Source: Data – Ministry of Finance, forecasts – CASE.

in October the privatisation proceeds plan was exceeded by about 30% (6.1 billion zlotys). We may expect a rapid decrease in the number of bonds and T-bills, which are still in the hands of investors.

Underestimating the expenditure on pay rises for teachers by 1.2 billion zlotys cast a shadow on the budget realisation. The government financed a part of this gap by transferring 0.5 billion zlotys appropriated for other purposes and the remaining part will have to be cover by local authorities. Because of this the deficit in public finances will be by 0.7 billion zlotys higher, i.e. 0.1% of GDP.

Local authorities

Low personal income tax revenues in the first eight months of 2000 questioned the feasibility of meeting local authorities' budgets as the tax constitutes 30–35% of total local authorities' revenues. In this case, some decided to take out commercial credits. There is however no indication of any substantial change in the up-till-now very prudential financial policy of local authorities. Potentially, a deteriorating standing of Regional Health Funds could have a negative impact on local budgets. Financing part of teachers' salary increase by the local authorities is a separate

Table 18. Public sector balance, 1999–2001 (% of GDP)

	1999	2000 budget	2000 CASE	2001 budget draft
Government budget balance	**-2.0**	**-2.2**	**-2.2**	**-1.4**
Local governments balance	-0.2	-0.3	-0.4	-0.3
Funds balance	-1.0	-0.3	-0.4	-0.3
Regional Health Funds balance	-0.1	0.0	-0.1	0.0
General government balance	**-3.3**	**-2.8**	**-3.1**	**-1.7**
Compensations	-	-0.5	-0.5	-0.3
II pillar in the social insurance system	0.5	1.3	1.3	1.3
Expenditures financed by revenues from UMTS licences				-0.9
Total effect on domestic savings (i.e. economic deficit)	**-2.8**	**-2.0**	**-2.3**	**-1.6**

Source: CASE and the 2001 budget draft as of June 2000.

issue, as the money will be reimbursed from the government budget as late as in 2001.

Social Insurance Board (ZUS)

ZUS reforms are bringing positive results. Better payers' records and more effective collection policy enabled to reach a higher-than-expected collection rate (97.1% in the first half of 2000). As a result, contributions to Regional Health Funds and OFE (open pension funds) are transferred regularly and ZUS' commercial debt fell from 2.6 billion zlotys at the end of 1999 to 1.6 billion zlotys in mid-September (although it is subject to considerable fluctuations and it may yet significantly increase by the end of the year). ZUS took a new credit from the budget of 0.5 billion zlotys out of 2 billion zlotys' loan provisioned in the government budget for 2000, however, it did not use the total budget subsidy (in the first three quarters 71.9% of the planned amount for this year was transferred). It is very likely that the ZUS deficit will exceed slightly the planned 0.3% of GDP this year.

Regional Health Funds

The deteriorating standing of Regional Health Funds is more and more conspicuous. Financial problems result from higher-than-planned expenditure. ZUS' contributions to Regional Health Funds are higher than expected (by 0.5 billion zlotys in the first half of 2000 and probably 1 billion zlotys at the end of the year). Regional Health Funds used conservative revenue forecasts in their expenditure plans (financial balance requirement). The actual expenditure slipped out of control (not always through the fault of Regional Health Funds). This deals particularly with expenditure on medicines; while in 1999 3.5 billion zlotys was appropriated for this purpose, in the first half of 2000, the expenses reached as high as 2.2 billion zlotys. The Regional Health Fund of Mazowsze, for instance, spent on medicines over 60% more than planned for the whole year. Such rapid growth results from a growing number of free drug prescriptions (abuse in nearly in over half of the cases), the increased zloty exchange rate against the dollar affecting the prices of imported medicines, and problems with verifying health insurance of patients (which is connected with ZUS' faulty computer systems).

The budget for 2001

The prospects for tightening the budgetary policy, even to an extent proposed in the budget draft in July, are bleak. This is the result of the VAT vote, unfavourable for the government (a loss in income of 1.5 billion zlotys) and the revenues of mining gminas (a loss of 0.2 billion zlotys) as well as the failed attempt to prevent expenses related to the teachers' bill (*Karta Nauczycieli*), (a salary increase for teachers of 1.5 billion zlotys higher than earlier planned). Pension payments may be higher than planned in July provisions. However, over 60% of budget expenditure comprise fixed expenses, hence the room for manoeuvre is limited. The Ministry of Finance intends to economise on early-pension benefits (about 1 billion zlotys). There are doubts, however, if such attempts, very unpopular politically, will be successful. It is also quite likely that the government's new proposal concerning the VAT increase in the construction sector will be rejected. Its thus possible that the economic budget will grow in 2001 even by 4 billion zlotys, i.e. 0.5% of GDP (in the worst scenario) or the budget draft might not be proposed in the parliament by November 15.

Monetary policy

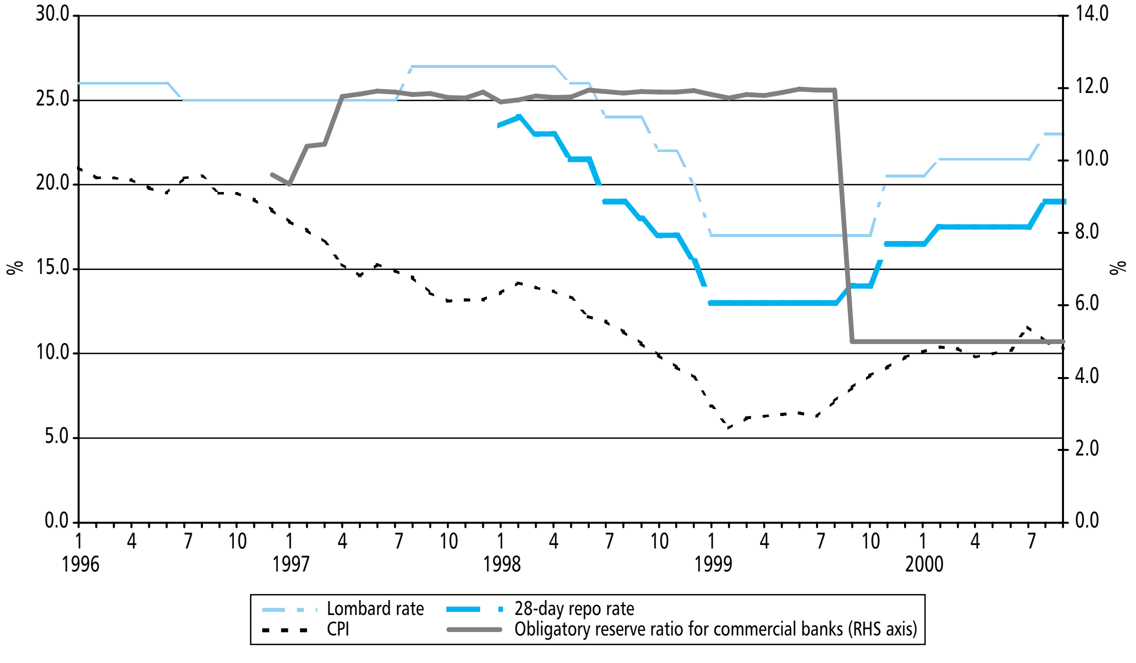
- **Tightening of monetary policy in 3Q00**
- **Setting inflation target at 6–8% in 2001**
- **The start of eliminating overliquidity in the banking system**

An increase in interest rates on August 30, 2000 by 150 base points was widely anticipated by the markets, as it expected an even higher tightening on the back of the CPI edging up to 11.6% in July. While analysing the MPC's decisions to raise interest rates this year, one has the impression that they came too late. The first increase in interest rates of 100 base points took place on February 23. Inflation decreased slightly in Mach and April. However, already in March core inflation started to climb (see page 29). In that case, the scenario of inflation remaining at a level of 10–11% until end-August should have appeared to the MPC as highly probable. When comparing inflation trends with the inflation target for 2000 (set optimistically at 5.4–6.8% yoy in December), the MPC should have decided to raise interest rates between April and May this year.

The increase in interest rates in August coincided with the release of the 2001 budget draft, which gave the impression that it was the NBP's immediate comment on the fiscal policy, whereas the above analysis testifies to a rather delayed reaction of the MPC. The hike in interest rates also forced the Ministry of Finance to re-estimate the expenses for domestic debt servicing in 2001 and higher inflation led to an increase in fixed expenses for the public sector (see public finances).

The NBP set the inflation target for 2001 at 6–8% (yoy in December). The target is consistent with the Ministry of Finance July budget draft for 2001 and it seems realistic and conducive to a proper policy-mix.

Figure 16. Monetary policy instruments, 1996–2000 (%)



Source: NBP and CASE.

However, it will be necessary to aim at the lower band of the inflation target in order to improve the credibility of the monetary policy (and reduce the costs of financing the budget deficit), especially as inflation after 1Q01 might be on that level. In that case the Ministry of Finance should plan expenses rigorously in 1Q01, which, as a rule, are the highest in all of the year, and the Ministry of Treasury could attempt to attain privatisation proceeds to finance the budget deficit at the beginning of the year and not at its end. The sterilisation of the privatisation proceeds via the monetary authorities' special account proved to be successful in eliminating the pressure on the zloty's appreciation. This, however, has not precluded problems with co-ordination, which we anticipated in PEO 3/1999 and 1/2000. The belated inflow of proceeds from the privatisation of Polish Telecom (in mid-October) forced the Ministry of Finance to take out short-term loans at higher interest rates (see reserve money and monetary policy instruments).

Towards the end of September, the NBP began to reduce, as announced in 1999, the overliquidity of the banking system via open-market operations using the Treasury's converted bonds from the NBP's portfolio instead of 28-day bills. The central bank is in possession of treasury securities worth 16.5 billion zlotys in nominal terms (market value stands at about 14 billion zlotys). The operation was launched despite the continued liquidity of the banking system at a level of 19–20 billion zlotys, i.e. significantly above the NBP's portfolio. According to the released auction timetable (every Thursday), the NBP intends to sell 1.2–1.5 billion zlotys' worth of treasury securities. This amount could mean that there are plans to sell the securities by the end of 2001. It is also possible that half of the NBP's securities will be sold and thus the NBP will attain the balance structure typical for European central banks. Until the beginning of October there wasn't much interest in NBP's auctions, which could be attributed to excessive yields demanded by investors (see reserve money and monetary policy instruments).

Further decisions on the conduct of the monetary policy will depend largely on inflation and budget deficit levels. In the baseline scenario we assume the economic deficit at 1.6% of GDP in 2001 and inflation below 8% in 1Q01. Thus, a reduction in interest rates by 100–200 base points is feasible only at the end of 1Q01. However,

Table 19. Components of the reserve money supply, 1998–2000 (cumulative % change)

		Reserve money (RM)	Net foreign assets (NFA)	Net domestic assets (NDA)	Net claims on government (NCG)	Claims on deposit money banks (CDMB)	Other items net (OIN)
1998	1Q	4.82	25.37	-7.00	-5.31	-1.69	-13.55
	2Q	17.54	36.32	-10.22	-8.74	-1.48	-8.56
	3Q	17.50	48.85	-4.39	-6.35	1.96	-26.94
	4Q	26.78	63.44	-0.90	2.95	-3.85	-35.75
1999	1Q	0.44	-0.78	-0.57	-0.50	-0.07	1.79
	2Q	10.20	14.07	1.54	2.10	-0.57	-5.42
	3Q	-13.94	6.15	-3.65	-2.79	-0.87	-16.45
	4Q	-1.57	18.50	-4.75	-3.71	-1.04	-15.34
2000	1Q	-14.44	1.03	-1.91	-1.57	-0.34	-13.56
	2Q	-1.83	-2.94	9.15	9.82	-0.67	-8.05
	3Q	-3.20	14.20	1.15	1.53	-0.38	-18.55

Source: The NBP Bulletin and authors' calculations.

Notes: 1. The shares of components of reserve money are calculated using the following formula: $\Delta RM/RM_{-1} = \Delta NFA/RM_{-1} + \Delta NCG/RM_{-1} + \Delta CDMB/RM_{-1} + \Delta OIN/RM_{-1}$, cumulative in the current year. Net foreign assets were re-estimated (valuation adjustment) using the average exchange rate of the currency basket for a given period to account for fluctuations in the exchange rate of the zloty.

2. Changes in comparison to the PEO 1/99 stem from the introduction of the currency basket into calculations instead of using zloty/dollar exchange rate.

much will depend on the new NBP president and his view on monetary policy. If he turns out a monetarist, then a tight monetary policy and reaching the lower band of the inflation target will be preferred. This would give hopes for inflation at 4% in 2003.

Reserve money and monetary policy instruments

In 2000 the NBP effectively increased the range of monetary policy instruments (sterilisation account, and conversion of Treasury securities). This, coupled with tight monetary policy, the realisation of budget deficit, and the lack of significant inflows of short-term and long-term capital in 3Q00, led to a drop in reserve money supply by 3.2% as compared to the end of 1999.

Due to postponing the payments for Polish Telecom, the Ministry of Finance borrowed on the market and the NBP sold on three occasions rare 1-day and 2-week securities in the last week of September. Despite revealed demand of 6.3 billion zlotys, only bills worth 4.8 billion were sold. But the maximum yield of 18.5% was accepted against the Ministry's expectations at 18.2%. Hence, the delay in the payment for Polish Telecom cost the Treasury about 34 billion zlotys.

This delayed privatisation coincided with the tender for NBP's bonds. During the first three auctions (September 19 and 27, and October 5) 618 million zlotys' worth of bonds were sold in nominal terms (485 million zlotys in real terms). During the first two auctions the NBP offered bonds with all possible maturity, but at the third one it only offered 2-year bonds. Their average yield stood at 18.6% and it was higher by 0.5–0.6 percentage points as compared to the market yield.

The banking system and broad money

The reduction in the reserve money supply facilitated the slowing of M2 growth to about 14% in 3Q00 (and 6.7% since the beginning of 2000). Given the decreasing net budget debt (also due to sell out of the Treasury's liabilities from the NBP's portfolio), the net claims on the private sector was the main driving force of M2 growth.

Table 20. Components of broad money, 1998–2000 (cumulative %)

		Broad money (M2)	Net foreign assets (NFA)	Net domestic assets (NDA)	Net claims on government (NCG)	Claims on private sector (CPS)	Other items net (OIN)
1998	1Q	2.25	3.76	0.85	-2.85	3.70	-2.36
	2Q	8.97	4.79	5.25	-2.60	7.86	-1.08
	3Q	15.35	4.33	13.76	0.86	12.90	-2.74
	4Q	25.12	9.72	20.60	3.42	17.18	-5.20
1999	1Q	4.30	-0.53	5.74	1.18	4.55	-0.91
	2Q	7.01	2.35	9.59	1.77	7.82	-4.93
	3Q	11.42	2.45	13.19	0.14	13.06	-4.23
	4Q	19.36	6.43	18.45	1.51	16.94	-5.53
2000	1Q	-0.58	1.94	-0.54	-3.62	3.08	-1.98
	2Q	8.11	1.11	8.14	-2.30	10.44	-1.13
	3Q	6.73	3.79	8.07	-2.58	10.65	-5.13

Source: The NBP Bulletin and authors' calculations.

Notes: 1. The share of broad money components are calculated using the following formula: $\Delta M2/M2_{-1} = \Delta NFA/M2_{-1} + \Delta NCG/M2_{-1} + \Delta CPS/M2_{-1} + \Delta OIN/M2_{-1}$, cumulative in the current year. Net foreign assets were re-estimated (valuation adjustment) using the average exchange rate of the currency basket for a give period to account for fluctuations of the exchange rate of the zloty.

2. Changes in comparison to the PEO 1/99 stem from the introduction of the currency basket into calculations instead of using zloty/dollar exchange rate.

Table 21. Calendar of the most important events in the monetary policy of the NBP over the period 4Q99–3Q00

Source	Date of the resolution	Events
J. NBP No. 20	November 17, 1999	NBP rediscount rate 19% Lombard rate 20.5% Refinancing rate 20.5/21.5% 28-day repo rate at least 16.5%
J. NBP No. 21	November 19, 1999	Interest rate on NBP current deposits 6.15%
J. NBP No. 26	December 22, 1999	Amendment to the law on reserves due to bank insurance, in force on March 30, 2000
J. NBP No. 1	February 23, 2000	NBP rediscount rate 20% Lombard rate 21.5% Refinancing rate 21.5/22.5% 28-day repo rate at least 17.5%
J. NBP No. 2	February 25, 2000	Interest rate on NBP current deposits 6.45%
J. NBP No. 6 and Monitor Polski No. 11/231 and 232	April 11, 2000	Abolition of crawling peg of the zloty and the permissible exchange rate fluctuation band
J. NBP No. 13	August 31, 2000	NBP rediscount rate 21.5% Lombard rate 23.0% Refinancing rate 23.0/24.0% 28-day repo rate at least 19.0%

Source: Official Journal of the NBP, various issues. Authors' compilation.

This means that a higher rate of growth in credits than in deposits is maintained. The zloty denominated banks' liabilities against individuals and total liabilities against the corporate sector rose in nominal terms at annualised rate of 18% and 14% in 3Q00, while corresponding credits grew 43% yoy and 18% yoy, respectively.

The increase in interest rates at the end of August by 150 base points did not cause a corresponding increase in commercial banks' interest rates. The money market discounted a 200-base-point rise already in August. Consequently, market interest rates were reduced in the aftermath of the NBP's decision. A significant supply of treasury securities on the market (prevailing since August) caused an increase in the average yield of 2-year bonds from below 18% to 18.6% at the beginning of October. The 1-year bonds' yield on the primary market rose from 17.7% in July to 18.3%–18.2% in August/September. The rates of 1-day loans were high and were hovering around 19–20%, which was the result of speculations in the expected event of a drain of zlotys due to Polish Telecom payments or the Ministry of Finance's need to borrow. The latter was the case. Temporary increases in interest rates attracted foreign investors who after backing out of the treasury bonds' in the primary market invested in the secondary market, especially in September.

In the next two years we forecast an increase in M2 growth in accordance with growth in nominal GDP. Changes in the structure of money supply and demand will follow a similar pattern. On the supply side, the importance of currency in circulation and currency deposits should be expected to diminish, whereas on the demand side, the general government debt will be increasingly less important, and the share of credits to the private sector will be relatively buoyant.

Stanisław Gomułka

Center for Social
and Economic Research

The outlook

The prospect of a slowdown? How strong? What causes, costs and benefits?

There appears to be a considerable tension, perhaps even confusion among both analysts and decision-makers about how to interpret the recent macroeconomic data for Poland and how to evaluate the current macroeconomic policy. The key concerns which dominated discussions in the second half of last year and the first half of this year, have been a large current account deficit and a sharp increase in the rate of inflation. The underlying deeper concern was that the policy response to the current account deficit has been inadequate and that, as a result, the risk of macroeconomic instability continued to increase. But now things are changing in several respects. Firstly, the tough monetary policy of the NBP is reducing sharply the growth of bank credit and the strength of domestic demand. Secondly, a sharp recovery of exports is beginning to reduce the current account deficit. Thirdly, a high and increasing rate of unemployment is beginning to restrain the growth of wages; this in turn has started to reduce the rate of inflation. However, there is a considerable uncertainty about the current fiscal policy, both the budget outcome this year and the proposed budget for 2001, as well as about the prospective fiscal policy of an SLD (or SLD-led) government which is expected to come to power next year.

The most important uncertainty in the second half of 2000 concerns the extent and the duration of the slowdown in industrial and GDP growth that started gently in the third quarter of this year, but which will almost certainly be more evident in the fourth quarter. The wrong policy mix of the last twelve months may cause this current slowdown to extend also into the first half of next year. There is a consensus around the view that the current macroeconomic conditions are not quite right, and are moreover deteriorating, for sustaining rapid growth and solid stability. But in response to the question: What is required to put the Polish economy back on track? very different answers are given. Indicative of the differences in concerns are some of the questions which foreign analysts have been recently asking this author: What can be expected from the 2001 budget? What kind of fiscal policy can be expected from the next Government? Does the current account deficit really matter? Is the domestic demand slowing too fast or just sufficiently? What policies other than high interest rates could/should be used in relation to the current account? Is the central bank doing a good job? Real interest rates are high – are they too high? What would make them go up/down?

The 'ideal' policy mix and departures from it

External shocks of the 1997–1998 years have complicated the macroeconomic management of the Polish economy, as they reduced for a while both exports and growth, and caused strong fluctuations in the rate of inflation. Nevertheless, the key medium-term objectives remained the same as before: higher savings, faster growth, lower unemployment and lower inflation. Liberalisation on capital account was expected to bring a convergence of Polish and external interest rates, which would mean lowering sharply real interest rates in Poland. The process of disinflation was to be helped by a more flexible labour market and a lower government deficit, possibly a budget surplus. Under the newly-adopted floating exchange rate regime, the current account deficit would be equal to the capital account surplus, but the latter would be of a moderate size on account of low interest rates. Implementation of this 'ideal' policy mix needed, thus, a close co-operation between the central bank (interest rates, exchange rate policy), the government (fiscal policy) and the parliament (new legislation with respect to the Labour Code, taxes, capital account transactions, and pensions).

In June 1999, the government approved the document The Strategy for Public Finances and Economic Development, Poland 2000–2010. Thereby it also announced the intention to adopt these components of the ideal policy-mix for which it and the current parliament are responsible. However, in practice the fiscal policy has continued to be lax, the Labour Code has remained unchanged, and the proposed tax reforms have been curtailed. One of the results was a large increase, much larger than in most other European countries, of both the inflation rate and the unemployment rate in the second half of last year and the first half of this year. The original inflation stimulus, in the form of higher energy and food prices, has been sustained and strengthened by higher wage inflation. These simultaneous and large increases of the wage inflation and unemployment rates are clear evidence that the labour market in Poland is still highly inflexible. At the same time some general government revenues have been reduced (social security contributions, profit and income taxes and border taxes), while some public (general government) expenditures have been increased (the cost of servicing public debt, infrastructure investments). There was also some weakening of the discipline in the tax collection. The result has been a failure on the part of the government to reduce significantly the budget deficit and to restructure public expenditures away from social transfers. This dual failure, with respect to public finances and the labour market reforms, has led the central bank to respond by raising interest rates to very high levels in both nominal and real terms, higher than would be the case under the ideal policy mix, and to adopting a higher, more 'realistic' inflation target of 6 to 8% for the end of year 2001.

The causes of the growth slowdown

The Polish economy has been affected adversely not only by these exceptionally high interest rates, but also by an exceptionally weak euro. Credit interest rates are now some 6 percentage points higher than in September 1999. Since the enterprise bank debt (net of enterprise deposits) equals about 15% of GDP, therefore the cost of servicing this debt increased by 0.9% of GDP. An even bigger dent on profits should have resulted from this year's appreciation of the zloty against the euro, by about 10% in nominal terms and by about 15% in real effective terms. Poland's exports to the euroland represent about 55% of total exports, that is about 10% of Poland's GDP. If the 15% appreciation were to be absorbed fully by lowering profits of Polish exporters, then these profits would fall by 1.5% of GDP. Given the weakening of domestic demand, Polish exporters must have been keen not to increase their euro prices, so they could increase sharply the volume of exports, which they apparently managed to achieve. However, lower profits and high interest rates have caused a sharp fall in the growth rate of investment. Deteriorating enterprise finances and a high unemployment are now beginning to have a moderating impact on wages. Since May of this year real wages in the enterprise sector are no longer increasing, while real wages in the government sector and real pensions are declining. This is good news for future inflation, but bad news for the current and short-term consumer demand. Moreover, a poor harvest has meant a fall in value-added in the agriculture.

The cumulative impact of all these developments should be a very considerable slowdown in economic growth in the fourth quarter of this year and, at the least, also in the first half of the next year.

The budget debate

A few months ago, the Ministry of Finance, then still under L. Balcerowicz, had an optimistic view of the probable fiscal outcome this year. However, later it became evident that the revenue side of the budget for 2000 is based in part on somewhat unrealistic assumptions. Moreover, the tax collection discipline has deteriorated. The result is that the deficit outcome this year, on the payment basis, is unlikely to be much better than assumed in the Budget 2000. The 2.8% of GDP consolidated deficit target for the year 2000 should be compared with the actual 3.3% in 1999. The actual outcome for 2000 that takes into account also arrears in the payments of budget units will be known probably only in March or April 2001. This outcome may turn out to be close to the outcome for 1999. The proposed consolidated fiscal deficit of 2.6% of GDP (using a measure that excludes the 0.9% of GDP revenues expected from the sale of UMTC mobile phone licences) for 2001 is based on assumptions that the GDP growth will be 5.2% this year and 5.3% next year. These assumptions are likely to prove overoptimistic, especially with respect to 2001. In the end the actual fiscal outcome for 2001 may therefore be not much different than the outcome for 2000.

The growth slowdown as a stabilisation factor

Given the prospect of little change in the fiscal stance, the MPC will be reluctant to reduce interest rates before the rate of inflation falls to a level within the target range of 6 to 8%. This tight monetary policy and a weak euro would therefore probably sustain the slowdown for at least the first half of next year. In the meantime, the rate of unemployment will continue to increase and the growth of nominal wages will continue to decline. Thus the conditions will be created to reduce both the rate of inflation and the current account deficit. This could and probably will be followed by several small reductions in interest rates. However, unless the slowdown becomes a near-recession, real interest rates are likely to remain high (though lower than now) during the next several years. A significant reduction in real interest rates may have to wait until the budget deficit is brought under a stricter control, or until Poland adopts the euro as the country's currency (whether unilaterally or by joining the EMU is of little significance).

The external environment and the budget

The external factors which are usually given attention to, are an apparently strong recovery in Russia (especially in terms of the current account, public finances and the dollar GDP), the possibility of a somewhat weaker growth in the European Union and a risk of still higher energy prices. Their combined impact on growth in Poland is however likely to be marginal. The euro should at some point start to recover, but the recovery is unlikely to be strong in 2001. Therefore the EU should continue to enjoy a respectable rate of growth. Indeed, the ECB is expecting the GDP growth of the euroland to increase from 2.5% this year to 3% next year and in 2002 (*FT*, 27.X.2000).

The outlook for Poland is, at present, also clouded by the considerable uncertainty concerning the date of entry to the EU. This uncertainty may well diminish in the course of next year. If we are to believe the Commission officials, the internal EU reforms will be adopted in time for the EU to be ready for enlargement by the year 2003. There is also evidence that Poland will be seen as ready to join the EU sometime in the period 2003–2005. Increased clarity on these dates should be perhaps the most significant positive external development next year.

The main risks for Poland

The very high current account deficit still poses a major short-term risk for the exchange rate, hence also for the inflation rate and the overall economic stability. The market participants know that Poland's short-term debt is manageable, but the current economic slowdown and political uncertainties could trigger a substantial fall in the inflow of foreign direct investments and a substantial out-flow in portfolio investments. Such developments would depress suddenly the surplus on capital account which is now financing the current account deficit. This in turn would trigger a substantial depreciation of the zloty.

Given these risks and uncertainties, the NBP must be prepared to intervene in the defence of the zloty at some point. Given the present level of reserves, such a defence should be successful. What is more important, the growth slowdown would automatically assist in bringing the trade deficit down. The concern with enhanced risk of a potential instability may also force the NBP to keep interest rates high for as long as it takes to bring the trade deficit down to a safe level.

A government can help to reduce this short-term risk of instability by continuing with its programme of accelerated privatisation. Unfortunately, before parliamentary elections are held this instrument is the only important one a minority government still posses. Stronger and appropriate legislative measures with respect to public finances, taxes and the labour code should be theoretically possible soon after the next year elections. However, in practice it may well take much time and a large increase in unemployment to persuade the next government and parliament to do what the present government and parliament have failed to do. There is unfortunately also a distinct possibility that Poland will follow Spain rather than Ireland of the years 1975–1995, and so the present practice of little change in vital areas of economic policy will continue for a prolonged period.

Stanisław Gomułka
London School of Economics

Early warning crisis indicator

For the second time, we present our early warning crisis indicator. We would like to stress that the indicator's values should be interpreted with caution, in light of other available information. This indicator is not an absolute and infallible tool used as a warning signal against crises. We are fully aware that the choice of variables and the system of weights and scoring may be subject to criticism. However, all indicators of this kind raise reservations. A detailed methodology of the indicator can be found on our web site (www.case.com.pl/pgtop/pgtopen.html).

3Q00 saw an increased risk of a currency crisis. The value of our indicator rose to 82 points. All components, excepting the current account deficit, have deteriorated.

In the real sector, a downward revision of the GDP forecast (by 0.6 percentage points) and a surge in the unemployment rate, which returned to its end-1Q00 level, were the main unfavourable developments. Moreover, we have revised the forecast government budget deficit upward.

Inflation and WIBOR components have deteriorated in the wake of the higher-than-expected inflation rate and the ensuing hike in interest rates. Credit expansion as a percentage of M2 went up as well.

The trend of appreciation of the real effective exchange rate of the zloty in relation to its 3-year average persisted. However, this phenomenon results primarily from the sizeable depreciation of the euro against the dollar, and hence it is determined externally.

Both short-term and total debt of Poland have increased, although not significantly.

The only favourable development was the improvement in the current account deficit. We lowered our forecast of the deficit in 2000 to 7.0% of GDP.

It should be noted that the difference in the indicator's value in 2Q00 (as compared to the previous issue of PEO) stems entirely from a change in the NBP's statistics on Polish debt. Due to the fact that it is not feasible to distinguish within merchandise credits between those with maturity of up to one year and those beyond one year, all merchandise credits were classified as short-term debt beginning from 1Q00. Consequently, the Poland's short-term debt in 1Q00 was increased by US$0.5 billion. As a result, our indicator edged up by 4 points from a level of 67 points.

Table. Early warning crisis indicator, 1999–2000

	3Q99	4Q99	1Q00	2Q00	3Q00
1. GDP forecast for 2000	6	5	5	5	6
2. Unemployment rate (end-quarter)	10	10	10	10	10
3. CPI forecast (end-2000)	10	10	6	10	10
4. Forecast of government budget deficit as % of GDP for 2000	0	0	10	0	10
5. Forecast of C.A. deficit as % of GDP for 2000	10	10	10	4	4
6. Real effective exchange rate	10	0	10	10	10
7. Credit expansion as % of M2 (end-quarter)	4	0	4	6	10
8. Polish short-term foreign debt as % of liquid reserves (end-quarter)	10	10	6	10	6
9.Total Polish foreign debt as % of GDP (end-quarter)	6	10	6	10	6
10. Real 3-month WIBOR (end-quarter)	0	10	4	6	10
Indicator	**66**	**65**	**71**	**71**	**82**

Source: CASE.

Threats and recommendations for economic policy

1. The low propensity to save and high interest rates encourage Polish entrepreneurs to take on foreign credits. Should the demand for short-term foreign loans increase excessively, the risk of a currency crisis will grow.

2. If the euro continues to stay at a very low level and the EU economy lose steam due to potential hikes in interest rates in 2001, then Polish export boom may reverse. In addition, in the case of strong demand stimulus due to a faster-than-expected disinflation coupled with a considerable increase in nominal wages and salaries, imports will surge. As a consequence, the current account deficit could dangerously deteriorate.

3. Unfavourable trends in global commodity prices may impede disinflation in Poland.

4. The government and the Parliament should do their best to minimise political risks. Failure to pass the budget and appoint a new NBP president before the end of this year may unsettle financial markets. Consequently, this may lead to interruption of FDI inflows and lower privatisation proceeds. A similar situation may occur on the event of postponing Poland's entry date to the EU beyond the date set by the Polish government - i.e., beyond 2003.

5. In face of unemployment reaching a socially and politically uncomfortable level, the creation of new jobs should be a top priority of Polish economic policy. We do not recommend artificial boosting of demand for labour, but rather an introduction of simple measures already tested in other countries aiming at increasing labour market flexibility. These include, among others, regional differentiation of minimal wages and salaries, providing retraining opportunities, and reform of the educational system. In addition, the employers' burden of labour costs that are not directly related to remuneration should be diminished.

6. Macroeconomic policy should continue to curb the current account deficit. This means cutting the public sector deficit. A further widening of the deficit on the current account in face of possible smaller FDI inflows increases the likelihood of a financial crisis.

7. The long-term economic policy should reduce income taxes. If this is done, it will possible to increase domestic savings (and investment) and boost demand for labour, leading to lower unemployment. At the same time, lower tax revenue will enforce greater fiscal discipline on the expenditure side.

Appendix

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Table A1. GDP at 1999 prices, 1996–2002 (% change yoy)

		GDP	Gross value-added					
			total	agriculture and forestry	manufacturing, mining, etc.	construction	market services	non-market services
1996	1Q-4Q	6.0	5.3	2.5	7.6	2.8	5.3	2.6
1997	1Q-4Q	6.8	6.4	1.0	10.3	13.6	4.4	2.9
1998	1Q-4Q	4.8	4.7	5.7	4.3	9.3	4.8	2.3
1999e1	1Q-4Q	4.1	3.9	-2.0	4.6	3.7	4.9	1.0
forecast								
2000	*1Q-4Q*	*4.8*	*4.6*	*-7.5*	*7.7*	*0.7*	*5.5*	*1.0*
2001	*1Q-4Q*	*5.5*	*5.3*	*5.1*	*7.2*	*4.8*	*5.3*	*1.6*
2002	*1Q-4Q*	*5.8*	*5.6*	*1.6*	*7.8*	*8.4*	*5.1*	*1.8*
1996	1Q	3.4	2.5	-2.0	6.1	-18.5	3.3	2.4
	2Q	5.4	4.4	2.2	6.9	-4.2	5.2	1.8
	3Q	7.2	6.5	2.7	9.8	5.0	6.1	2.9
	4Q	7.9	7.7	6.7	7.6	21.9	6.5	3.2
1997	1Q	6.9	6.4	-1.5	8.7	14.7	5.5	4.9
	2Q	7.4	6.7	1.7	11.5	15.6	4.5	1.3
	3Q	6.7	6.5	2.7	10.7	13.3	4.3	1.1
	4Q	6.4	6.2	0.3	10.2	12.2	3.5	3.8
1998	1Q	6.5	6.4	0.8	10.5	14.6	4.3	3.7
	2Q	5.3	5.2	4.3	5.3	10.8	5.6	0.2
	3Q	4.9	4.8	5.2	3.3	8.8	5.9	1.4
	4Q	3.0	2.9	12.8	-1.1	6.1	3.6	3.1
1999e1	1Q	1.6	1.4	-1.8	-2.8	2.4	4.4	1.0
	2Q	3.1	2.8	-2.7	1.5	3.1	4.5	1.1
	3Q	5.0	4.8	-1.8	7.6	3.4	5.1	0.8
	4Q	6.2	6.0	-1.4	11.6	5.0	5.3	1.1
2000	1Qe1	6.0	5.8	-7.0	10.1	4.0	5.8	1.0
	2Qe1	5.2	5.0	-7.8	9.4	0.8	5.3	0.9
	3Qe2	4.2	3.8	-8.0	6.3	-1.8	5.4	1.0
forecast								
2000	*4Q*	*4.1*	*3.9*	*-7.0*	*5.5*	*1.0*	*5.3*	*1.1*
2001	*1Q*	*5.1*	*4.7*	*-1.0*	*6.4*	*2.9*	*5.4*	*1.3*
	2Q	*5.4*	*5.2*	*4.0*	*7.0*	*4.5*	*5.3*	*1.5*
	3Q	*5.7*	*5.6*	*8.0*	*7.4*	*5.1*	*5.3*	*1.7*
	4Q	*5.8*	*5.7*	*7.2*	*8.0*	*5.6*	*5.3*	*2.0*
2002	*1Q*	*5.8*	*5.5*	*4.5*	*7.8*	*7.0*	*5.0*	*2.0*
	2Q	*5.7*	*5.6*	*1.6*	*7.6*	*8.4*	*5.1*	*1.8*
	3Q	*5.8*	*5.7*	*1.0*	*7.7*	*9.0*	*5.1*	*1.6*
	4Q	*5.8*	*5.7*	*0.5*	*8.0*	*8.5*	*5.2*	*1.6*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecast – CASE.
Notes: 1. Data not seasonally adjusted.
2. Data and estimates at annual average prices of a previous year.
3. Forecasts at average 1999 prices.

Table A2. Aggregate demand at current prices, 1996–2002 (billion zloty)

		GDP	Domestic demand	Consumption			Investment	Stock-building	Net exports
				total	households	public			
1996	1Q-4Q	387.83	393.86	309.04	241.90	67.14	80.39	4.43	-6.03
1997	1Q-4Q	472.35	492.72	376.72	296.65	80.07	110.85	5.15	-20.37
1998	1Q-4Q	553.56	582.57	437.56	346.94	90.62	139.20	5.80	-29.01
1999	1Q-4Q	617.04	657.04	489.77	390.88	98.89	161.68	5.59	-40.00
forecast									
2000	*1Q-4Q*	702.96	744.12	551.52	441.60	109.92	184.14	8.46	-41.16
2001	*1Q-4Q*	794.00	836.15	613.16	493.01	120.15	215.59	7.41	-42.15
2002	*1Q-4Q*	889.54	933.22	676.70	546.50	130.20	249.50	7.03	-43.68
1996	1Q	85.27	83.92	72.33	56.50	15.83	10.97	0.63	1.35
	2Q	92.88	94.38	77.71	60.41	17.30	15.95	0.72	-1.51
	3Q	98.48	100.81	78.85	61.82	17.03	20.93	1.03	-2.33
	4Q	111.20	114.75	80.15	63.18	16.97	32.54	2.05	-3.54
1997	1Q	103.78	105.63	89.24	70.19	19.05	15.48	0.92	-1.85
	2Q	112.98	117.58	93.26	73.81	19.45	23.29	1.03	-4.60
	3Q	119.15	123.78	95.69	76.22	19.47	27.13	0.96	-4.62
	4Q	136.43	145.73	98.54	76.43	22.10	44.96	2.24	-9.30
1998	1Q	123.70	129.90	107.22	85.24	21.97	21.54	1.14	-6.20
	2Q	133.37	139.73	109.05	85.56	23.49	29.37	1.31	-6.36
	3Q	140.01	146.96	112.32	88.98	23.35	33.30	1.33	-6.94
	4Q	156.48	165.98	108.96	87.15	21.81	54.99	2.02	-9.50
1999e1	1Q	134.78	144.28	119.59	95.16	24.43	24.60	0.09	-9.51
	2Q	147.33	158.66	123.35	97.50	25.85	34.10	1.22	-11.33
	3Q	155.72	164.26	123.54	98.65	24.89	38.78	1.94	-8.54
	4Q	179.21	189.84	123.29	99.57	23.73	64.20	2.35	-10.63
2000	1Qe1	153.97	166.67	137.23	109.72	27.51	27.81	1.62	-12.70
	2Qe1	167.91	178.62	137.80	109.15	28.65	38.03	2.79	-10.72
	3Qe2	177.65	185.24	138.16	110.51	27.65	45.15	1.94	-7.59
forecast									
2000	*4Q*	203.44	213.59	138.33	112.21	26.12	73.15	2.10	-10.15
2001	*1Q*	175.11	187.45	152.32	122.17	30.15	33.56	1.57	-12.34
	2Q	190.14	201.13	155.02	123.66	31.37	44.41	1.70	-10.99
	3Q	200.39	207.75	153.27	123.08	30.19	52.67	1.81	-7.35
	4Q	228.36	239.82	152.55	124.10	28.44	84.95	2.32	-11.46
2002	*1Q*	197.04	209.72	168.60	136.00	32.59	39.70	1.42	-12.68
	2Q	213.23	224.28	171.23	137.10	34.13	51.47	1.57	-11.05
	3Q	224.28	231.57	169.18	136.45	32.73	60.69	1.70	-7.29
	4Q	255.00	267.66	167.69	136.94	30.75	97.64	2.33	-12.66

Source: Data and estimates (e1) – CSO; estimates (e2) and forecast – CASE.
Note: Domestic demand is defined as the sum of consumption of households, public consumption, non-commercial institutions' consumption and investment. Consumption of non-commercial institutions is not separated in the table.

Table A3. Aggregate demand at 1999 prices, 1996–2002 (% change yoy)

		GDP	Domestic demand	Consumption			Investment	Exports	Imports
				total	households	public			
1996	1Q-4Q	6.0	9.7	7.2	8.7	2.1	19.7	12.0	28.0
1997	1Q-4Q	6.8	9.2	6.1	6.9	3.2	21.7	12.2	21.4
1998	1Q-4Q	4.8	6.4	4.2	4.8	1.6	14.2	14.3	18.5
1999e1	1Q-4Q	4.1	4.8	4.3	5.1	1.1	6.9	-1.5	1.4
forecast									
2000	*1Q-4Q*	*4.8*	*3.4*	*2.7*	*3.2*	*1.0*	*4.2*	*11.6*	*5.7*
2001	*1Q-4Q*	*5.5*	*5.1*	*4.0*	*4.7*	*1.2*	*9.6*	*12.3*	*10.0*
2002	*1Q-4Q*	*5.8*	*5.7*	*4.2*	*4.8*	*1.6*	*10.6*	*9.8*	*9.0*
1996	1Q	3.4	8.0	7.1	8.5	2.2	13.1	14.4	36.7
	2Q	5.4	6.7	3.4	6.5	-6.4	20.5	21.6	29.1
	3Q	7.2	10.6	6.7	8.3	1.2	26.8	25.3	42.2
	4Q	7.9	13.0	11.6	11.4	12.0	17.3	-12.5	7.9
1997	1Q	6.9	7.9	6.0	6.7	3.4	19.6	20.5	24.2
	2Q	7.4	9.0	6.3	7.1	3.5	21.0	29.9	36.1
	3Q	6.7	9.4	6.4	7.1	3.4	21.2	8.1	18.4
	4Q	6.4	10.4	5.7	6.6	2.4	23.2	-3.5	11.7
1998	1Q	6.5	7.3	5.4	6.3	2.2	17.3	18.8	20.2
	2Q	5.3	5.7	3.5	4.1	1.6	14.6	24.7	23.0
	3Q	4.9	6.1	3.8	4.4	1.5	14.2	18.9	20.6
	4Q	3.0	6.6	3.9	4.6	1.1	12.9	-1.9	11.6
1999e1	1Q	1.6	3.3	3.7	4.4	1.1	6.1	-8.9	-2.8
	2Q	3.1	4.5	4.1	4.9	1.0	6.8	-3.5	2.0
	3Q	5.0	5.5	4.6	5.4	1.2	7.0	2.9	4.5
	4Q	6.2	5.6	4.7	5.6	1.1	7.3	3.8	2.0
2000	1Qe1	6.0	5.1	3.9	4.6	1.0	5.5	5.0	2.3
	2Qe1	5.2	3.3	2.3	2.6	0.9	2.9	10.8	3.5
	3Qe2	4.2	2.4	2.1	2.4	1.0	3.6	15.6	7.4
forecast									
2000	*4Q*	*4.1*	*3.2*	*2.7*	*3.2*	*1.0*	*4.7*	*14.1*	*8.9*
2001	*1Q*	*5.1*	*4.2*	*3.8*	*4.4*	*1.2*	*7.0*	*14.0*	*9.3*
	2Q	*5.4*	*5.0*	*4.8*	*5.8*	*1.2*	*9.2*	*12.5*	*10.1*
	3Q	*5.7*	*5.3*	*4.0*	*4.6*	*1.2*	*10.1*	*12.0*	*9.7*
	4Q	*5.8*	*6.0*	*3.6*	*4.1*	*1.2*	*10.5*	*11.0*	*10.8*
2002	*1Q*	*5.8*	*5.6*	*4.6*	*5.3*	*1.6*	*11.0*	*11.0*	*9.6*
	2Q	*5.7*	*5.4*	*3.9*	*4.5*	*1.6*	*11.4*	*9.2*	*8.0*
	3Q	*5.8*	*5.6*	*4.1*	*4.7*	*1.6*	*10.7*	*8.8*	*8.0*
	4Q	*5.8*	*6.1*	*4.0*	*4.6*	*1.6*	*10.0*	*10.2*	*10.3*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecast – CASE.

Notes: 1. Domestic demand is defined as the sum of households' consumption, non-commercial institutions' consumption, public consumption and investment. Consumption of non-commercial institutions is not separated in the table.

2. Data are not seasonally adjusted.

3. Data and estimates at annual average prices of a previous year.

Table A4. Employment, 1996–2002 ('000)

		Total	Paid employment				Market services	Non-market services
			of which employment	agriculture and forestry	manufact-uring, mining, etc.	construction		
1996	1Q-4Q	15021	8548	4010	3730	843	4161	2277
1997	1Q-4Q	15439	8637	3985	3740	908	4489	2316
1998	1Q-4Q	15800	8752	3969	3701	961	4798	2371
1999	1Q-4Q	15710	8702	3931	3529	954	4892	2404
forecast								
2000	*1Q-4Q*	*15508*	*8100*	*3905*	*3340*	*940*	*4950*	*2373*
2001	*1Q-4Q*	*15546*	*8078*	*3905*	*3325*	*930*	*4965*	*2375*
2002	*1Q-4Q*	*15721*	*8059*	*3890*	*3313*	*898*	*5053*	*2428*
1996	1Q	14682	8487	4002	3714	737	3969	2260
	2Q	14932	8513	4001	3719	837	4120	2255
	3Q	15083	8522	4044	3730	879	4181	2249
	4Q	15386	8671	4038	3759	919	4326	2344
1997	1Q	15048	8567	3982	3753	788	4235	2290
	2Q	15374	8645	3980	3733	910	4441	2311
	3Q	15594	8675	4020	3735	952	4578	2309
	4Q	15739	8706	4006	3740	981	4656	2356
1998	1Q	15506	8717	3956	3717	864	4609	2360
	2Q	15819	8759	3953	3722	978	4804	2362
	3Q	15921	8714	3991	3676	1010	4901	2343
	4Q	15953	8817	3976	3688	992	4879	2418
1999	1Q	15513	8747	3900	3587	871	4725	2430
	2Q	15726	8717	3925	3543	973	4877	2408
	3Q	15808	8649	3960	3507	1001	4974	2366
	4Q	15792	8695	3940	3480	970	4992	2410
2000	1Q	15185	8139	3880	3350	840	4765	2350
	2Q	15524	8106	3890	3330	970	4944	2390
	3Q	15638	8045	3920	3330	980	5038	2370
forecast								
2000	*4Q*	*15685*	*8111*	*3930*	*3350*	*970*	*5055*	*2380*
2001	*1Q*	*15155*	*8052*	*3880*	*3290*	*800*	*4825*	*2360*
	2Q	*15548*	*8042*	*3880*	*3300*	*930*	*5018*	*2420*
	3Q	*15698*	*8014*	*3910*	*3320*	*940*	*5108*	*2420*
	4Q	*15785*	*8113*	*3910*	*3330*	*940*	*5165*	*2440*
2002	*1Q*	*15291*	*8068*	*3860*	*3300*	*780*	*4921*	*2430*
	2Q	*15719*	*8069*	*3860*	*3320*	*920*	*5139*	*2480*
	3Q	*15902*	*8048*	*3880*	*3330*	*940*	*5252*	*2500*
	4Q	*15974*	*8151*	*3880*	*3340*	*950*	*5284*	*2520*

Source: Annual data – CSO; quarterly data and forecasts – CASE.
Note: Employment is calculated according to the CSO's methodology.

Table A5. Unemployment, 1996–2002

		Registered unemployment		Unemployment LFS	
		('000)	%	('000)	%
1996	1Q-4Q	2360	13.2	1961	11.5
1997	1Q-4Q	1826	10.3	1737	10.2
1998	1Q-4Q	1831	10.4	1827	10.6
1999	1Q-4Q	2350	13.0	2880	16.7
forecast					
2000	*1Q-4Q*	*2627*	*14.4*		
2001	*1Q-4Q*	*2687*	*14.7*		
2002	*1Q-4Q*	*2648*	*14.3*		
1996	1Q	2726	15.4	2349	14
	2Q	2508	14.3	2103	12.4
	3Q	2341	13.5	2018	11.6
	4Q	2360	13.2	1961	11.5
1997	1Q	2236	12.6	2176	12.8
	2Q	2040	11.6	1927	11.3
	3Q	1854	10.7	1853	10.7
	4Q	1826	10.3	1737	10.2
1998	1Q	1846	10.4	1896	11.1
	2Q	1688	9.6	1753	10.2
	3Q	1677	9.6	1786	10.3
	4Q	1831	10.4	1827	10.6
1999	1Q	2170	12.1	2141	12.5
	2Q	2074	11.6	-	-
	3Q	2178	12.1	-	-
	4Q	2350	13.0	2641	15.3
2000	1Q	2532	14.0	2880	16.7
	2Q	2437	13.6	2825	16.3
	3Q	2529	14.0		
forecast					
2000	*4Q*	*2627*	*14.4*		
2001	*1Q*	*2722*	*15.0*		
	2Q	*2573*	*14.3*		
	3Q	*2629*	*14.5*		
	4Q	*2687*	*14.7*		
2002	*1Q*	*2735*	*14.9*		
	2Q	*2552*	*14.0*		
	3Q	*2575*	*14.1*		
	4Q	*2648*	*14.3*		

Source: Data – CSO; LSF estimates for 2Q99 and 3Q99, and forecasts – CASE.
Note: The CSO resumed publishing LFS (labour force survey) statistics in 4Q99.

Table A6. Selected price indices, 1998–2000 (% yoy)

		CPI	PPI		Export price index	Import price index
			Manufacturing, etc.	Construction		
1998	01	13.6	9.2	15.7	9.8	7.9
	02	14.2	9.1	15.7	10.0	11.0
	03	13.9	9.2	15.4	11.5	10.4
	04	13.7	8.4	14.6	8.4	4.4
	05	13.3	8.2	14.4	8.2	0.7
	06	12.2	7.7	14.1	7.8	4.4
	07	11.9	7.0	13.6	6.9	1.5
	08	11.3	6.6	13.0	4.4	–5.6
	09	10.6	6.4	12.4	7.0	3.3
	10	9.9	5.8	11.7	3.8	3.4
	11	9.2	5.1	11.1	3.2	–2.3
	12	8.6	4.8	10.6	4.7	–5.1
1999	01	6.9	3.9	9.9	2.8	-0.3
	02	5.6	3.7	9.4	9.6	1.5
	03	6.2	4.7	9.0	10.7	5.6
	04	6.3	5.0	8.6	9.9	9.0
	05	6.4	5.2	8.4	10.2	8.2
	06	6.5	5.2	8.1	1.1	4.8
	07	6.3	5.5	7.8	0.3	5.2
	08	7.2	5.9	7.8	7.2	10.3
	09	8.0	6.2	8.2	6.3	4.6
	10	8.7	6.8	8.3	11.0	7.4
	11	9.2	7.5	8.6	13.5	11.7
	12	9.8	8.1	8.9	10.8	15.1
2000	01	10.1	8.2	7.7	7.1	11.8
	02	10.4	8.1	7.5	1.4	7.4
	03	10.3	7.3	7.7	-3.6	2.3
	04	9.8	7.4	8.3	-2.4	3.5
	05	10.0	7.9	8.4	4.2	8.1
	06	10.2	8.9	8.8	8.8	10.6
	07	11.6	9.0	8.9	9.4	7.4
	08	10.7	8.4	8.7		
	09	10.3	8.3	8.2		

Source: CSO.

Table A7. Exchange rates, 1998–2000 (in zlotys)

		US$/zloty	DM/zloty	euro(ECU)/zloty
1998	01	3.5316	1.9461	3.8432
	02	3.5386	1.9505	3.8503
	03	3.4593	1.8941	3.7560
	04	3.4194	1.8827	3.7329
	05	3.4188	1.9246	3.7917
	06	3.4789	1.9420	3.8362
	07	3.4592	1.9226	3.8002
	08	3.5850	2.0046	3.9543
	09	3.6066	2.1211	4.1713
	10	3.4955	2.1353	4.2071
	11	3.4496	2.0514	4.0323
	12	3.4858	2.0884	4.0979
1999	01	3.5417	2.1007	4.1087
	02	3.7948	2.1727	4.2494
	03	3.9430	2.1927	4.2886
	04	4.0016	2.1905	4.2843
	05	3.9368	2.1387	4.1830
	06	3.9431	2.0947	4.0969
	07	3.8827	2.0537	4.0166
	08	3.9510	2.1447	4.1946
	09	4.0799	2.1925	4.2881
	10	4.1092	2.2513	4.4031
	11	4.2527	2.2484	4.3974
	12	4.1696	2.1577	4.2200
2000	01	4.1036	2.1274	4.1608
	02	4.1439	2.0886	4.0850
	03	4.0902	2.0200	3.9507
	04	4.2347	2.0469	4.0033
	05	4.4988	2.0839	4.0758
	06	4.3994	2.1341	4.1740
	07	4.3229	2.0801	4.0684
	08	4.3593	2.0189	3.9486
	09	4.4900	2.0018	3.9152

Source: NBP.
Notes: 1. Monthly average.
2. Until end-1998 the Ecu exchange rate, then the euro exchange rate.

Table A8. Foreign trade, 1998–2000 (US$ million)

		Exports		Imports		Net exports	
		CSO	NBP	CSO	NBP	CSO	NBP
1998	01	2156	2120	3172	3565	-1016	-1445
	02	2377	2265	3667	3078	-1290	-813
	03	2490	2671	4248	3657	-1758	-986
	04	2340	2468	3849	3496	-1509	-1028
	05	2300	2449	3886	3350	-1586	-901
	06	2401	2753	3959	3699	-1558	-946
	07	2393	2936	3929	3924	-1537	-988
	08	2168	2529	3552	3309	-1385	-780
	09	2332	2336	4516	3864	-2183	-1528
	10	2621	2533	4372	3908	-1750	-1375
	11	2369	2369	4098	3695	-1728	-1326
	12	2283	2693	3807	4297	-1524	-1604
1999	01	2027	2693	3147	4297	-1120	-1604
	02	2092	2119	3239	3331	-1147	-1212
	03	2452	2495	4034	3279	-1583	-784
	04	2167	2398	3633	3223	-1466	-825
	05	2237	2161	3700	3197	-1463	-1036
	06	2154	1999	3667	3020	-1514	-1021
	07	2119	2122	3761	3425	-1641	-1303
	08	2193	2092	3651	3429	-1458	-1337
	09	2438	2078	4093	3308	-1655	-1230
	10	2595	2044	4324	3363	-1729	-1319
	11	2511	2224	4373	3360	-1862	-1136
	12	2423	2151	4290	3557	-1866	-1406
2000	01	2278	2464	3519	4235	-1241	-1771
	02	2549	1922	3912	3380	-1363	-1458
	03	2725	2030	4338	3178	-1613	-1148
	04	2495	2371	3935	3613	-1441	-1242
	05	2427	2032	4268	3108	-1840	-1076
	06	2591	2407	4079	3301	-1487	-894
	07	2631	2397	4095	3438	-1464	-1041
	08	2327	2473	3713	3515	-1386	-1042
	09		2271		3595		-1324

Source: NBP and CSO.
Notes: 1. NBP data on payments basis, CSO's data on SAD basis.
2. NBP data on August and September – preliminary.

Table A9. Balance of payments, 1998–2000 (US$ million)

		Balance on						Gross foreign exchange reserves
		current account	merchandise trade	current transfers	unclassified current transactions	direct investment	portfolio investment	
1998	01	-963	-1443	102	374	477	-309	-97
	02	-278	-813	131	397	150	268	-2197
	03	-755	-986	120	392	277	253	-284
	04	-428	-1001	121	578	334	89	-848
	05	-200	-901	117	587	539	130	-492
	06	-8	-945	399	550	248	144	-650
	07	-102	-988	192	574	589	121	-1378
	08	183	-780	165	856	661	-643	-174
	09	-1296	-1528	163	438	496	-336	649
	10	-962	-1375	159	449	359	-73	228
	11	-830	-1326	149	363	201	723	-634
	12	-1187	-1604	124	437	638	963	178
1999	01	-894	-1212	101	320	291	-81	74
	02	-512	-784	102	242	317	-177	-83
	03	-833	-825	176	237	530	-46	-142
	04	-938	-1036	113	232	364	2	108
	05	-690	-1031	108	300	403	-251	64
	06	-1134	-1302	132	253	382	167	0
	07	-1055	-1322	138	301	297	70	-47
	08	-783	-1230	142	429	1393	228	-26
	09	-1147	-1309	137	423	788	-388	442
	10	-849	-1139	130	426	363	451	76
	11	-1178	-1561	148	299	789	809	-116
	12	-1640	-1706	161	174	681	306	-120
2000	01	-1207	-1458	113	286	763	298	25
	02	-962	-1148	113	225	361	571	664
	03	-1346	-1242	133	218	430	1573	-122
	04	-851	-1076	122	398	449	131	200
	05	-401	-894	162	324	310	20	-184
	06	-860	-1041	137	337	363	90	240
	07	-701	-1042	170	309	488	232	268
	08	-961	-1324	120	350	169	-234	-300
	09	-594	-965	126	420	239	-104	19

Source: NBP.
Note: August and September data – preliminary.

Table A10. Interest rates, 1998–2002

		Rediscount rate	Lombard rate	3-month WIBOR	28-day repo rate
1998	01	24.5	27.0	26.1	23.5
	02	24.5	27.0	25.2	24.0
	03	24.5	27.0	25.1	23.0
	04	24.5	27.0	24.5	23.0
	05	23.5	26.0	23.2	21.5
	06	23.5	26.0	22.1	21.5
	07	21.5	24.0	21.0	19.0
	08	21.5	24.0	19.8	19.0
	09	21.5	24.0	18.8	18.0
	10	20.0	22.0	17.9	17.0
	11	20.0	22.0	16.7	17.0
	12	18.3	20.0	15.9	15.5
1999	01	15.5	17.0	14.8	13.0
	02	15.5	17.0	13.2	13.0
	03	15.5	17.0	13.2	13.0
	04	15.5	17.0	13.2	13.0
	05	15.5	17.0	13.3	13.0
	06	15.5	17.0	13.3	13.0
	07	15.5	17.0	13.4	13.0
	08	15.5	17.0	13.7	13.0
	09	15.5	17.0	14.3	14.0
	10	15.5	17.0	16.6	14.0
	11	19.0	20.5	18.2	16.5
	12	19.0	20.5	19.3	16.5
2000	01	19.0	20.5	17.2	16.5
	02	20.0	21.5	17.8	17.5
	03	20.0	21.5	18.4	17.5
	04	20.0	21.5	18.3	17.5
	05	20.0	21.5	18.4	17.5
	06	20.0	21.5	18.5	17.5
	07	20.0	21.5	18.5	17.5
	08	21.5	23.0	19.1	19.0
	09	21.5	23.0	19.6	19.0
forecast					
	2000	–	*23.0*	*19.6*	–
	2001	–	*19.0*	*16.3*	–
	2002	–	*14.0*	*12.4*	–

Source: Data – NBP and forecast – CASE.
Notes: 1. End-month except for WIBOR – monthly average.
2. End-period forecast.

Table A11. Monetary indicators, 1998–2002 (billion zloty)

		M0	M2	Cash	Zloty deposits			Foreign currency deposits	Credits			Net liabilities of the budgetary sector
					total	individual	corporate		total	individual	corporate	
1998	1Q-4Q	53.6	220.8	30.2	156.9	109.6	47.3	33.6	138.5	23.9	114.6	61.3
1999	1Q-4Q	52.8	263.5	38.1	185.7	124.1	61.6	39.7	175.9	36.6	139.3	64.7
forecast												
2000	*1Q-4Q*	*52.0*	*295.6*	*34.0*	*215.4*	*152.0*	*63.4*	*46.2*	*217.9*	*49.0*	*168.9*	*59.0*
2001	*1Q-4Q*	*54.9*	*332.0*	*35.0*	*247.0*	*179.0*	*68.0*	*50.0*	*257.1*	*57.5*	*199.6*	*60.0*
2002	*1Q-4Q*	*57.8*	*371.8*	*34.4*	*284.9*	*208.7*	*76.2*	*52.6*	*300.5*	*67.4*	*233.1*	*62.4*
1998	1Q	44.4	180.4	27.3	123.3	88.9	34.4	29.8	114.7	18.6	96.1	50.3
	2Q	49.7	192.3	29.7	132.9	95.1	37.8	29.7	122.1	20.1	102.0	50.7
	3Q	49.7	203.5	30.3	142.3	101.8	40.5	30.9	131.0	21.9	109.0	56.8
	4Q	53.6	220.8	30.2	156.9	109.6	47.3	33.6	138.5	23.9	114.6	61.3
1999	1Q	53.9	230.3	32.0	161.2	116.5	44.6	37.1	148.6	25.3	123.3	63.9
	2Q	59.1	236.2	33.6	166.2	119.2	47.0	36.4	155.8	28.3	127.5	65.2
	3Q	46.2	246.0	34.2	173.3	122.4	51.0	38.5	167.4	32.4	135.0	61.6
	4Q	52.8	263.5	38.1	185.7	124.1	61.6	39.7	175.9	36.6	139.3	64.7
2000	1Q	45.2	262.0	33.0	186.9	134.8	52.1	42.2	184.0	38.5	145.6	55.1
	2Q	51.8	284.9	35.1	205.3	141.6	63.7	44.4	203.4	50.8	152.6	58.5
	3Q	51.1	281.2	34.7	201.7	145.3	56.4	44.8	208.0	45.6	162.4	57.9
forecast												
2000	*4Q*	*52.0*	*295.6*	*34.0*	*215.4*	*152.0*	*63.4*	*46.2*	*217.9*	*49.0*	*168.9*	*59.0*
2001	*1Q*	*51.6*	*299.0*	*35.0*	*217.0*	*160.0*	*57.0*	*47.0*	*225.1*	*50.0*	*175.1*	*52.0*
	2Q	*53.0*	*309.9*	*35.0*	*227.0*	*167.0*	*60.0*	*47.9*	*233.3*	*52.7*	*180.6*	*56.0*
	3Q	*54.1*	*316.8*	*35.3*	*233.0*	*171.0*	*62.0*	*48.5*	*249.0*	*54.6*	*194.4*	*55.0*
	4Q	*54.9*	*332.0*	*35.0*	*247.0*	*179.0*	*68.0*	*50.0*	*257.1*	*57.5*	*199.6*	*60.0*
2002	*1Q*	*54.5*	*336.2*	*35.0*	*251.4*	*187.6*	*63.8*	*49.7*	*263.3*	*58.4*	*204.9*	*53.0*
	2Q	*55.8*	*346.9*	*34.4*	*262.2*	*195.0*	*67.2*	*50.3*	*273.1*	*62.0*	*211.1*	*57.5*
	3Q	*56.9*	*354.5*	*34.7*	*268.7*	*199.3*	*69.4*	*51.0*	*290.9*	*64.4*	*226.5*	*56.7*
	4Q	*57.8*	*371.8*	*34.4*	*284.9*	*208.7*	*76.2*	*52.6*	*300.5*	*67.4*	*233.1*	*62.4*

Source: Data – NBP and forecast – CASE.