CEC

GOVERNMENT RELATIONS

CEC IN DEPTH
THE MORAWIECKI PLAN

Contents

Introduction

Poland's new government has an ambitious economic plan. Deputy Prime Minister and Development Minister Mateusz Morawiecki, who leads Poland's economic growth strategy, argues that the country's recent progress was the result of structural factors rather than past governments' liberal policies. He furthermore believes that Poland could soon fall into a middle income trap. While the country's economy continues to prosper, citizens have not enjoyed the full benefits of such developments, Morawiecki argues, citing increasing disparities between GDP and real wage growth (see Chart 1). In order to combat this, the Development Ministry has put forward a 'Plan for Responsible Growth' (also known as the Morawiecki Plan). [1] Partially modelled after France

1. The basic slides outlining the Plan are available in English on: http://www.mr.gov.pl/media/14873/Responsible_Development_Plan.pdf and in Polish on http://www.mr.gov.pl/media/14840/Plan_na_rzecz_Odpowiedzialnego_Rozwoju_prezentacja.pdf

and South Korea's development schemes, it hopes to boost Poland's growth over the next 25 years, focusing on innovation, investments, and a new wave of industrialisation. The Plan's initial drafts received some criticism for being too vague on details, but they are better understood as an initial mission statement. The Ministry of Development intends to conduct wider consultations with businesses and industry groups on the scheme, before enshrining it in legislation.[2] A strategic blueprint, through which the Plan will be implemented, is expected to be announced in July and accepted by the legislature this autumn. Responses to the Plan have been mixed so far, with most economists agreeing with its diagnoses but remaining divided as to its solutions. It is certainly a deeply ambitious programme and will need to not only make an economic impact but also transform mindsets within businesses and public institutions alike in order to succeed.

The Plan is still in its infancy, more details will be revealed in the coming months

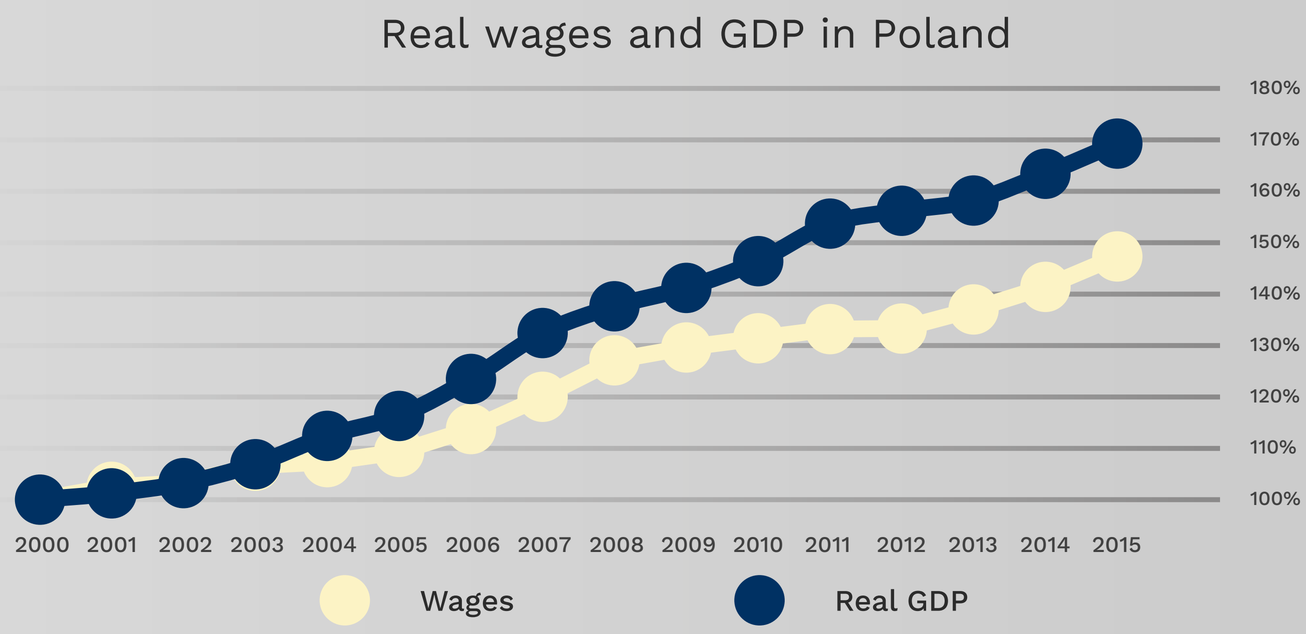


Chart 1. Real wages and GDP in Poland expressed as percentages of 2000 values. Morawiecki has pointed to such disparities when arguing that Poland's citizens have not enjoyed the benefits of their country's economic growth as much as they could have.

Morawiecki has identified some of Poland's economic problems and devised a series of solutions, which will form a key part of his department's development strategy. They are presented overleaf, along with a series of economic and legislative goals that the Ministry hopes to accomplish through implementing its new Development Plan.

2. http://www.pb.pl/4428843,62853,rozpoczely-sie-regionalne-konsultacje-planu-morawieckiego

Morawiecki's Diagnoses and Plans: A Brief Overview

The Morawiecki Plan analyses Poland's economic problems and offers a series of solutions, outlined below

Problems

A potential middle income trap

The competitive wages that have driven Poland's recent growth are rising, and the country's economy risks a significant slowdown. This is a common diagnosis, echoed by firms such as Deloitte, and publications such as the Economist. Morawiecki furthermore points that real wages in Poland have grown at a far slower pace than GDP has.

Too much growth is driven by foreign investors

Morawiecki argues that foreign firms frequently repatriate their profits, failing to invest them in Poland, and that the Polish government and companies are excessively indebted to foreign entities.

Insufficient innovation

Too little of the Poland's GDP goes towards investment, research and development, and domestic firms have not innovated as much as their Western counterparts have. While Poland has a strong small and medium-sized business sector, it has few prominent large businesses, and an underdeveloped startup and venture capital scene.

Demographic problems

Poland's working age population is shrinking rapidly. This will lead to labour force shortages as well as problems with employment and pension payments. There is also a dearth of vocational training and significant regional inequalities.

Weak public sector institutions

Poland could be losing anywhere from 45 to 95 billion PLN annually due to ineffective tax collection and tax avoidance. Morawiecki furthermore argues that businesses are encumbered by excessive bureaucracy, spending too much time on paperwork and accountancy.

Solutions

Reindustrialisation

Also known as neo-industrialisation, this programme marks a qualitative shift, as Poland's government must start promoting the growth of businesses in which the country can gain a competitive advantage, including biotechnology, drones, transport, and cybersecurity. This will be accompanied by a parallel development of economic clusters, which the government could back through grants, tax cuts, and an open attitude towards foreign investors.

Support for Polish exporters

The government plans to create new international offices that specialise in economic diplomacy, especially in markets that Polish companies are rarely present in, such as the Middle East, Africa and the Americas.

Innovative companies

Poland must create the conditions necessary for innovative firms to grow and expand, including through new legal and tax codes, tax cuts for businesses that invest in innovation, and greater cooperation between science, public research, and industry.

Demographic solutions

The 500+ programme as well as further schemes, such as childcare and school reforms, and programs to aid young children and pregnant women, which will be implemented by 2017. This will be combined with a greater focus on vocational training. The Development Ministry furthermore hopes to lower regional inequality and boost the development of Eastern Poland.

Better governance and administration

A centralised public procurement system could save around 5-12% of total costs. The state would no longer have to purchase the cheapest product, either, but could back small and medium enterprises and innovative businesses. The Morawiecki Plan also emphasises the cost and time savings of e-government, and hopes to simplify tax and judicial systems, improving the ease of doing business in Poland.

The Development Ministry's Goals and Targets

The Ministry of Development hopes to accomplish the following economic and legislative goals through implementing the Morawiecki Plan

	Poland's per GDP capita as percentage of EU average	Poles at risk of poverty
2030	100%	14,9%
2020	79%	15,5%
2015	70%	16,2%

	2015	2020
Investments as percentage of GDP	18%	25%
R&D as percentage of GDP	0,8%	2%

By **2020:**

Research and Development expenditures will rise to **2%** of GDP

Investments will rise to over **25%** of GDP

They currently stand at:

0,8%

19%

The Constitution for Business

A set of simplified business regulations

will become **law** in **2016**

Financing the Plan

Morawiecki hopes to raise over a trillion PLN for the new economic plan. Many of those funds have been used to finance in-country investments in the past. The Ministry of Development does, however, aim to create a single, long-term spending strategy that would direct the money more effectively into specific growth targets. Sources of finance include:

How the Morawiecki Plan will be financed

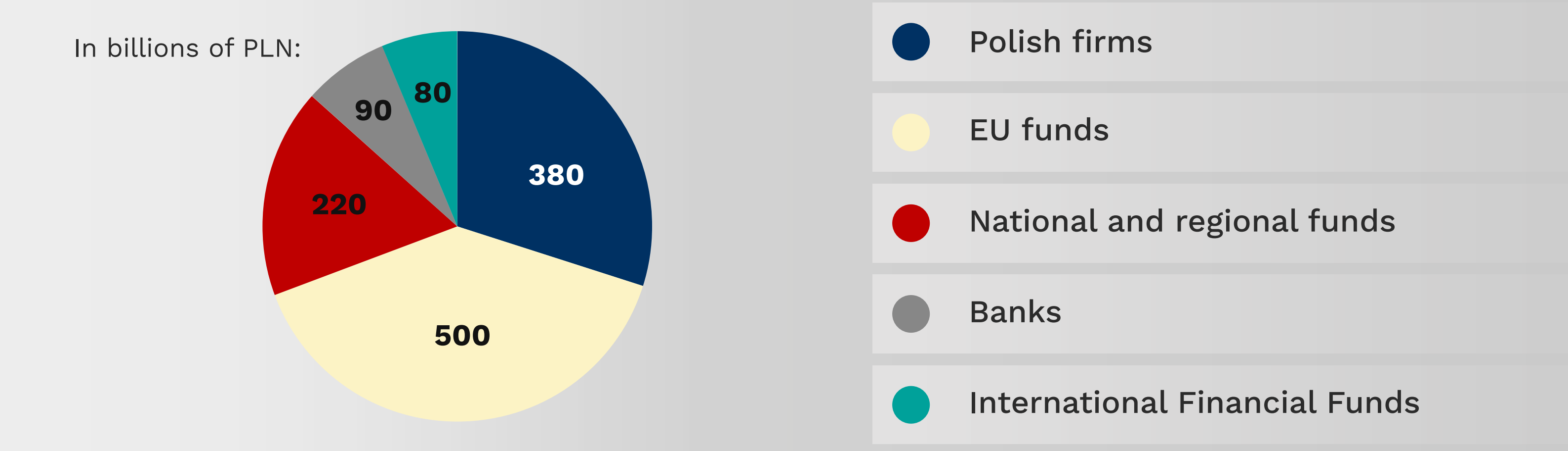


Chart 2. The chart above estimates the maximum amount of money that the Polish government hopes to get out of each of the sources above.

Polish firms must invest more of their revenues, Morawiecki argues

Polish firms, both state-owned and private ones (up to 380 billion PLN) – According to Morawiecki, many companies based in Poland transform their revenues into board and shareholder profits, without investing them into further growth. He hopes to encourage them to invest through several mechanisms, including greater state support for research and development, tax benefits, and simplified business regulations. Still, former Minister of Finance Mirosław Gronicki points out that the Development Ministry has failed to explain how it will address or reduce the risks that all investments bear. [3] Economist Jan Czekaj furthermore points out that companies' profits often go towards servicing debt and loans, and that Morawiecki's estimates of firms' investable income are therefore vastly overestimated. [4]

3. https://www.rp.pl/Dane-gospodarcze/302169815-Plan-przyspieszenia-rozwoju.html?template=restricted
4. http://www.rp.pl/Opinie/302239830-Plan-Morawieckiego-nie-spelnia-oczekiwan.html

EU funding (around 480-500 billion PLN) – Poland already receives significant EU funding, but the Ministry of Development hopes to restructure its spending and redirect some of those funds through a new, unified financial institution (more on which below). Past Polish governments also benefited from immense structural development funds, yet the Ministry of Development is working under the assumption that such finances will be spent more effectively under the new Plan. Morawiecki's team has not yet presented a detailed blueprint of how this could happen, though the Ministry plans to unify several institutions responsible for growth and investment (more below), which could also contribute to a more consistent strategy for spending EU funds. Some of the EU's financial support is furthermore contingent on national wealth; states whose per capita GDP falls below 75% of the EU average receive the biggest share of growth funds. [5] According to predictions presented by Morawiecki, Poland's per capita GDP could rise to 79% of the EU average by 2020, and it remains to be seen how the country receives and uses EU funding beyond that point.

Morawiecki hopes to restructure, better target EU funding

National and regional funding (up to 220 billion PLN) – Around half of this funding will come from the newly established Polish Development Fund, which will come about as a merger of existing institutions that manage public investment (more below) in Poland's economy. The other half will come from a variety of national sources.

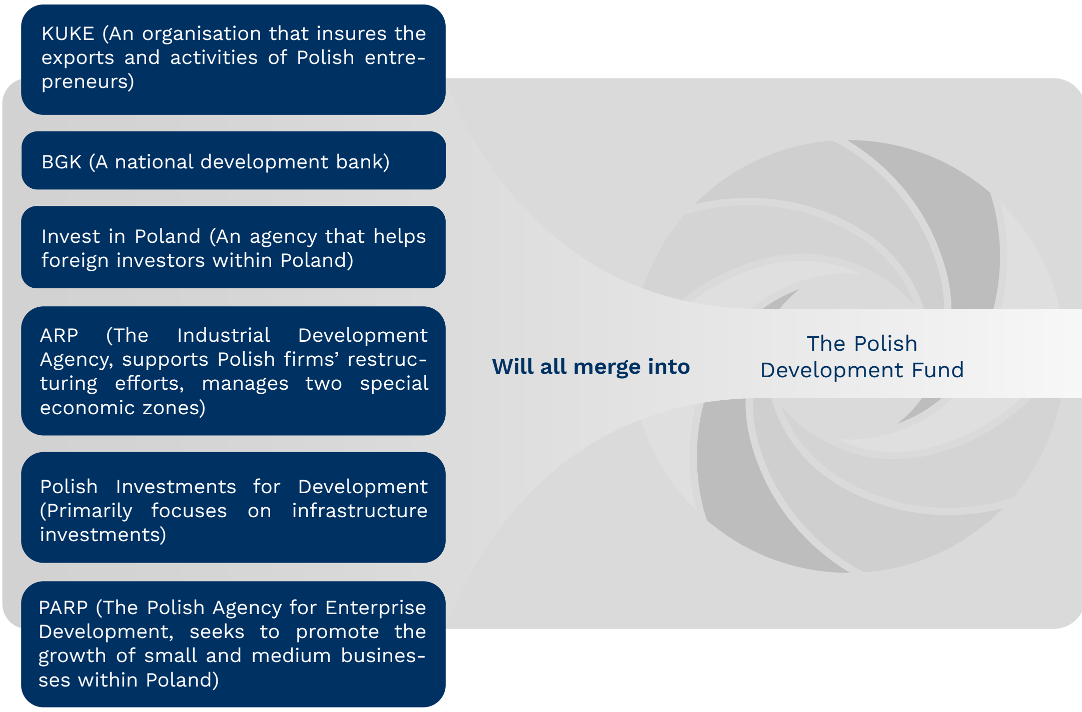
Other sources, iincluding banks, will give up to 90 billion PLN of funding. The Plan will also invest the funds of international financial institutions, such as the European Bank for Reconstruction and Development, the European Investment Bank, the European Fund for Strategic Investments, the World Bank, and the Asian Investment Bank, which are estimated to total around 50-80 billion PLN.

5. http://www.europarl.europa.eu/atyourservice/en/displayFtu.html?ftuId=FTU_5.1.2.html

The Polish Development Fund – a new, merged financial institution

Morawiecki hopes to merge Polish growth institutions into one

Currently, Poland's development and investment strategy is managed by many different entities, including bodies responsible for development financing, industrial development, and export. Morawiecki, however, plans to unite all those departments, whose investment-focused competencies and portfolios frequently overlap, [6] into a single unit, arguing that this would allow the Polish state to pursue a targeted development strategy. This scheme is still at its draft stages, and it remains to be seen whether institutions such as PARP (The Polish Agency for Enterprise Development) end up becoming part of the Polish Development Fund as well.



The plan to merge financial institutions has nonetheless encountered some criticism. Economist Jan Czekaj argues that the various bodies that Morawiecki seeks to unite have divergent purposes and goals, and that a single umbrella entity that would embrace all of them would be virtually 'unmanageable'. [7] Furthermore, integrating development bank BGK into the Polish Development Fund has proven difficult. Its portfolio does not involve investment support alone; the bank is also

6. http://www.wprost.pl/ar/532171/Zeby-konie-szly-w-jedna-strone/

7. http://www.rp.pl/Opinie/302239830-Plan-Morawieckiego-nie-spelnia-oczekiwan.html

responsible for issues such as currency trading and controls. [8] According to a new law, BGK's board will be filled by five members appointed by the Development Ministry, two by the Finance Ministry, and one each by the Energy and Treasury Ministries. This allows Morawiecki's team to assume significant control over BGK while some of its financial portfolio still remains under the Finance Minister's mandate. [9]

But integrating some, including BGK, has proven problematic

Selected issue areas

Innovation, research, and development

Salaries in Poland are on the rise, and the country is losing the competitive edge it once had as a provider of lower cost but effective labour. Morawiecki hopes to alleviate that by inviting foreign firms that can shore up domestic research and development and create long-term technical jobs in the country, rather than companies that merely operate manufacturing facilities in Poland. The government furthermore hopes to transform scientific and research institutions, but has not yet announced any thorough plans on the shape of such reforms. Deputy Prime Minister and Minister of Science and Higher Education Jarosław Gowin has emphasised that scientific research and discoveries must not stay in the realm of academia alone but need to have a greater economic impact. For that purpose, his Ministry will spend over 8 billion PLN on research in 2016 alone, [10] with the money going primarily into small and medium enterprises.

The government plans to introduce a new law on innovation in mid-2016, which will grant tax relief for research and development, in line with the Morawiecki Plan. [11] Consultations will also open for wider

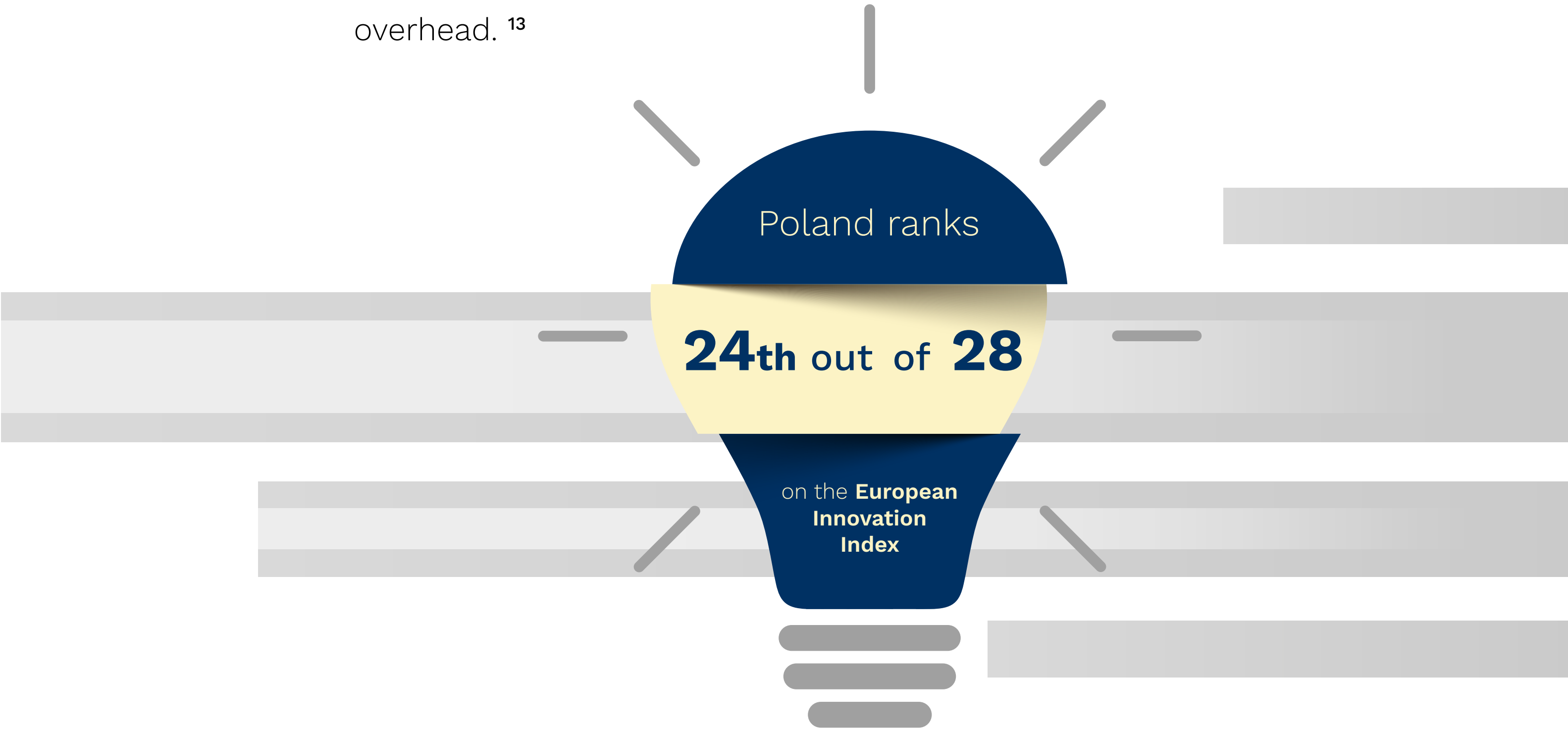
Tax cuts could also encourage private R&D spending

8. http://gospodarka.dziennik.pl/news/artykuly/513423,banku-gospodarstwa-krajowego-morawiecki-szalamacha-plan-morawieckiego.html
9. http://pulsbiznesu.pb.pl/foto/4427377,78937,160389,167398
10. http://www.forbes.pl/jaroslaw-gowin-do-2016-roku-ponad-16-mld-euro-trafi-na-innowacje,artykuly,201778,1,1.html#
11. http://wyborcza.pl/1,91446,19798053,zmiany-w-projekcie-malej-ustawy-o-innowacyjnosci-korzystne.html?disableRedirects=true

pro-innovation legislation, to be passed in 2017. The government has furthermore announced plans to establish a new form of legal entity which will reduce the bureaucratic load on startups and other small businesses, while visa reforms which would make it easier for Poland to attract migrants who could bring in innovative product and business ideas.

Polish research institutes could also see an overhaul

Deputy Minister of Development Jadwiga Emilewicz also proposed a merger of state-led research and development institutes. Drawing on the example of the German Fraunhofer Institute (where around 70% of financing comes from private grants, with the rest coming from public funds), [12] she argues that a smaller number of strong research institutions would boost effectiveness and lower administrative overhead. [13]



Morawiecki's assessments and solutions are largely correct and tax incentives for research and development, a policy that was also promoted by the past government, are likely to boost innovation expenditures. Still, the Plan does not effectively differentiate between small and large firms; while the former form the bedrock of Poland's economy, it is the latter that often innovate the most. A more subtle strategy that differentiates between the needs of small and large

12. http://www.fraunhofer.de/en/about-fraunhofer/profile/facts-and-figures/finances.html

13. http://pulsinnowacji.pb.pl/4423785,16966,urzednicy-obiecuja-raj-na-ziemi-dla-start-upow

institutions is needed, and could emerge in the next months following wider consultations. Finally, the government's plans to commercialise more research point in the right direction but could be difficult to implement. They will require not just a change of mindset within universities themselves but also new industrial clusters and incubators, which could offer funding and business opportunities.

Startups

While seed funds function well within Poland, effective venture capital is lacking, frequently forcing local startups to seek funding abroad. The Start In Poland programme attempts to tackle this trend. The scheme is inspired by existing corporate venture capital efforts and will allow existing state-owned corporations to back startups by giving them capital, sharing business expertise, and by offering an early market for their products. The project would similarly set up a network in which startups could demonstrate their ideas, and businesses could communicate their needs, signalling what software and hardware solutions they might require. Successful startups could receive further financing or be completely bought by the companies they design products for. The project would be financed by a structure known as FIZAN, which is expected to operate a portfolio of 100-150 million PLN in 2016.

Poland lacks effective venture capital

Government plans cooperation between state-owned firms and startups

As Polish daily Dziennik Gazeta Prawna reports, people such as Eliza Kruczkowska, chair of the Startup Poland Foundation, as well as wider startup environments, have reacted positively to Morawiecki's new plans. [14] The Ministry is willing to cooperate with and gather the opinions of startups, meeting with founders and investors. [15] At the same time, however, a single top-down initiative is not enough. Effective startup growth requires a wider change in mindset among businesses, the civil service and administration, and it remains to be seen whether the broad remit of the Morawiecki Plan is sufficient to achieve it.

14, 15. http://biznes.gazetaprawna.pl/artykuly/923679,plan-morawieckiego-panstwo-to-nie-start-up.html

Foreign investors

Morawiecki hopes to invite new and innovative foreign investors

Morawiecki's new economic plan focuses on growing Poland's production and research facilities but is in no way hostile to foreign investors; if anything, it encourages them. At the same time, however, the plan marks a qualitative shift towards backing foreign investment that will lead to a greater added value in Poland. Instead of non-technical manufacturing bases or call centres, the Ministry of Development wants to encourage foreign firms to invest in technical production, research, and innovation.

Several means will be used to achieve such a shift, including the new pro-innovation laws mentioned above. The Ministry of Development furthermore plans to encourage scientists and researchers who have emigrated from Poland to return to the country. Finally, the government is working on expanding its export and promotion efforts, and is likely to set up new trade and investment units outside of the EU, which could not just promote Polish products abroad but could also serve as a forum for dialogue with foreign investors.

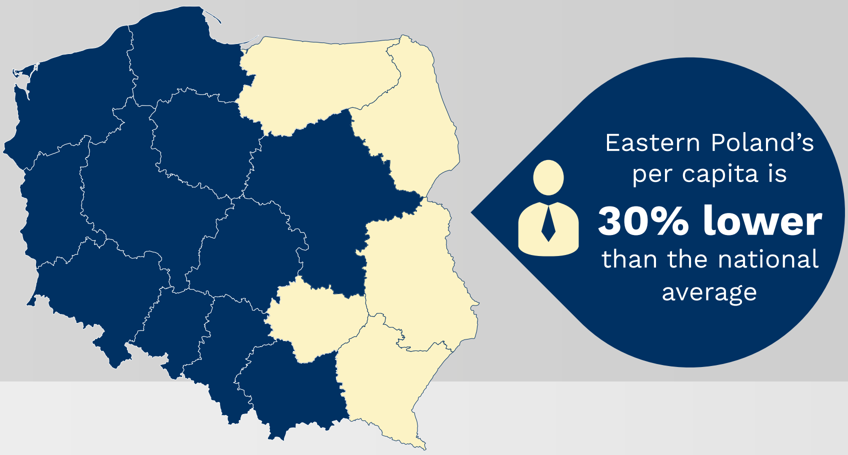
Initial investor reactions to Morawiecki's Plan have been positive, with HSBC economist Agata Urbańska-Giner [16] arguing that it introduces a welcome air of predictability, and that investors are pleased with its focus on long-term stability. At the same time, however, the plan has not been published in its entirety yet. The government is expected to open a wider set of consultations with businesses in the coming months, and large parts of the Morawiecki Plan could be enshrined in law by the end of 2016.

New Constitution for Business

Morawiecki argues that excessive legislation, bureaucracy, and paperwork put far too great of a burden on Polish businesses. In order to address this, he proposes a set of rules known as the "constitution for business". The rules will be encoded in law, rather than consisting of voluntary regulations, and are expected to introduce a set of long-term, predictable laws, as businesses have frequently complained of an uncertain legislative future. [17] Morawiecki hopes to open up wide consultations with small, medium, and large businesses and integrate their suggestions into the business constitution. He hinted that the document could be published within the next few months, by the end of the year at the latest.

16. http://www.pb.pl/4423989,10688,urbanska-giner-z-hsbc-plan-morawieckiego-ws.-finansow-uspokoil-inwestorow
17. http://www.polskieradio.pl/42/273/Artykul/1584599,Bez-Polski-lokalnej-plan-Morawieckiego-sie-nie-uda

Local and regional development



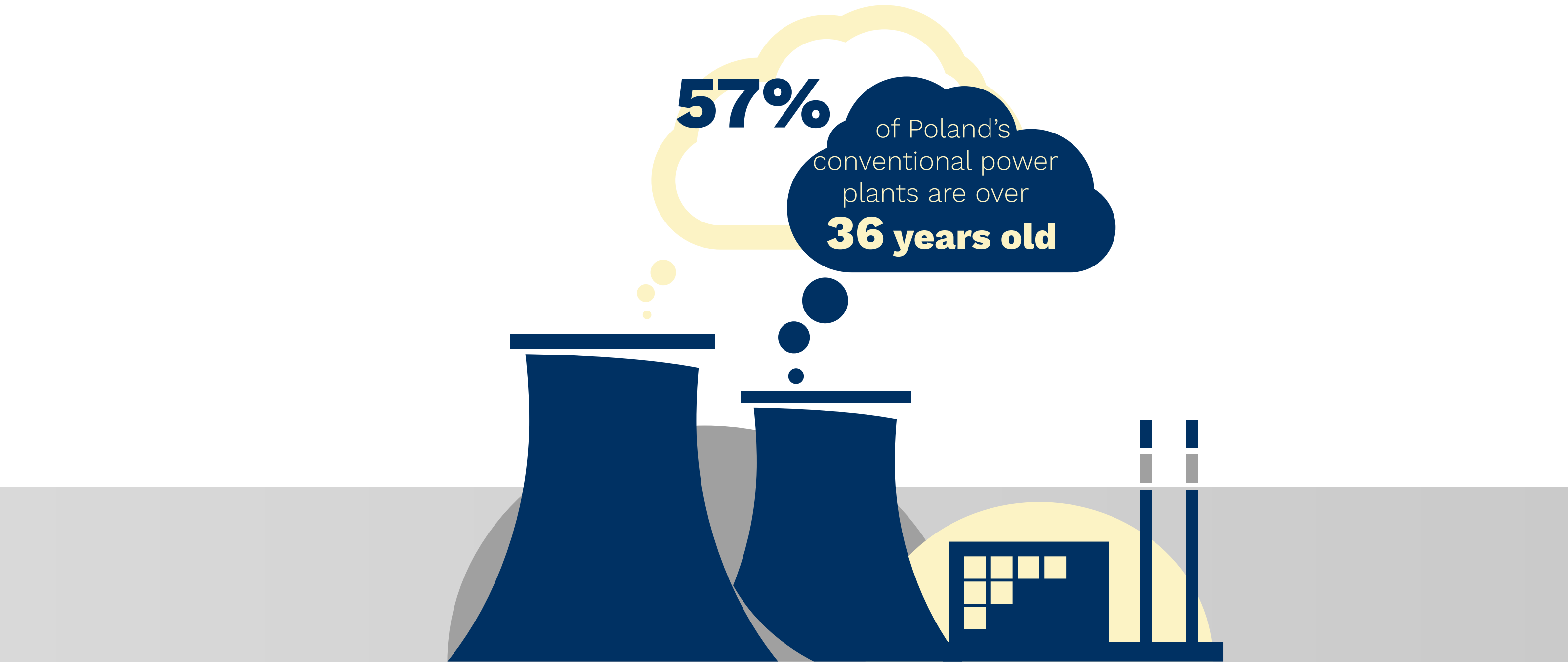
During the initial presentation for the Plan, Morawiecki pointed out that Poland's economic development has been heavily skewed towards certain cities and industrial centres. Other regions, particularly in East Poland, have failed to enjoy the fruits of the country's recent economic growth as much as some areas have. The differences do not manifest themselves in GDP per capita alone; East Poland's infrastructure is also less developed than that in the centre and west of the country. Morawiecki has announced a set of new initiatives that are expected to combat this discrepancy, including new railway lines. More EU funds are expected to be allocated to Poland's Eastern regions, including through a scheme known as Program Operacyjny Polska Wschodnia (The Operational Programme for Eastern Poland), [18] which supports several Eastern regions, including Podkarpacie (Subcarpathia). Institutions such as kindergartens in poorer regions could similarly help tackle the causes of structural poverty. Finally, several large-scale industrial clusters will be located in the East, including ones which focus on clean coal technologies and organic food.

Poland's economy suffers from regional imbalances

18. https://www.polskawschodnia.gov.pl/

Energy

Poland's energy sector faces several problems, including ageing infrastructure, with the blackouts and electricity shortages of August 2015 starkly highlighting the sector's vulnerabilities. The Morawiecki Plan acknowledges those issues and pledges to tackle them through several mechanisms, including a diversification of energy sources and an expansion of energy infrastructure, such as storage technologies and international interconnectors. The Plan will furthermore promote the development of household energy sources and small-scale generation, while backing low-carbon and renewable sources, with a particular focus on geothermal energy.



Yet, while the goals outlined above are feasible and ambitious, the Ministry of Development has given little more information on how the Morawiecki Plan will affect Poland's energy sector. This criticism has been echoed by many business representatives, including leaders of the Polish Chamber of Commerce. [19] They point out that Morawiecki's plan will fail without a strong emphasis on stable and reliably priced energy supplies, necessary for industrial development. [20] The Ministry of Development has not given any details on funding or precise targets

Too few details on energy reforms so far

19. http://energetyka.wnp.pl/herbert-gabrys-kig-energetyczna-czesc-planu-morawieckiego-wymaga-uszczegolowienia,267854_1_0_0.html

20. http://energetyka.wnp.pl/plan-morawieckiego-stawia-na-energetyke-niskoemisyjna-i-odnawialna,267571_1_0_0.html

for the energy sector yet, though Morawiecki has called on energy firms to increase their investment expenditures.

Morawiecki has criticised the EU's approach towards climate policy, characterising it as economic geopolitics in disguise that allows countries with developed or developing renewables industries, such as France and Germany, to increase their competitive advantage. While Western Europe's economic growth was built on carbon emissions, he argues, Poland is not allowed to do the same and must keep its industrialisation within strict, externally prescribed, limits. Finally, he points out that current climate limits focus on reducing domestic emissions alone and do not tackle the issue of purchasing carbon-intensive products from others, putting Poland's industry at an even greater disadvantage. This view is largely consistent with the perspective of the ruling PiS party, which has been calling for a renegotiation of the EU's Climate Pact. [21]

Morawiecki critical of EU's approach to climate

Analysis and Conclusions

Economics matters...

Morawiecki's diagnoses are largely correct. Poland is struggling to find new sources of economic growth, ranks low in innovation indices, has one of the lowest birth rates in Europe, and faces significant regional inequality. To a large extent, though, assessments of Morawiecki's solutions will depend on political and economic orientations; classical liberals are unlikely to appreciate his focus on national industries or state-driven growth. As economist Jan Czekaj furthermore points out, PiS's economic policies aim to boost wages, investment, and growth all at once, something he characterises as a contradiction. [22] Morawiecki has, however, explained that those three goals are sequential, rather than simultaneous; first comes investment, which then boosts growth, which eventually leads to higher wages.

Morawiecki's diagnoses are correct ...

21. http://energetyka.defence24.pl/269898,rzad-pis-zamierza-renegocjowac-pakiet-klimatyczny
22. http://www.rp.pl/Opinie/302239830-Plan-Morawieckiego-nie-spelnia-oczekiwan.html#ap-1

One of the biggest limitations of the Morawiecki Plan lies in its funding sources and estimates, and the government had not yet presented any details of how it could encourage firms to invest large parts of their profits. Morawiecki's assessments of companies' savings and investment potential are also likely to be overestimates, as firms frequently spend their revenues on servicing debt rather than shareholder profits, several economists have argued. Still, the Plan is only in its initial stage, and its blueprints are expected to be refined over the coming months. It is therefore too soon to either praise or condemn it. Early business reactions have furthermore been largely positive, suggesting that investors are optimistic about the Development Ministry's Plan and its abilities to fulfil it.

... but finding the funds for his plan could prove difficult

... as does culture

Culture eats strategy for breakfast. Those words, frequently attributed to management expert Peter Drucker, apply to public institutions just as much as private ones. No matter how well structured or economically sound Morawiecki's Plan is, it will fail if it does not lead to a shift in culture and mindset among investors and state bodies alike. In an interview, Morawiecki explained that a 2011 economic plan put forward by the past government faltered because it was implemented by a small group that lacked political support and capital, even among their own party ranks. While the Ministry of Development enjoys much bigger political backing than the founders of the 2011 plan did, it still faces several organisational obstacles.

Changing mindsets will prove challenging, both in private and public institutions

The biggest challenge will be to persuade private firms to buy into the government's strategy, with Jacek Adamski, advisor to business association Konfederacja Lewiatan rightly pointing out that Morawiecki still needs to earn the trust of local and foreign investors alike. [23] The Development Minister plans to tour the country in the next months, meeting business representatives both to reassure them of the feasibility of the Ministry's Plans and to gain their feedback for upcoming legislation, such as the Constitution for Business.

23. https://www.rp.pl/Dane-gospodarcze/302169815-Plan-przyspieszenia-rozwoju.html?template=restricted

The second necessary cultural shift, within government ministries themselves, should be easier. Morawiecki enjoys significant support within the ruling party and his Ministry plays a powerful economic role. Yet Morawiecki's Plan will also require the cooperation of the education sector and the civil service, both of which will need a significant cultural overhaul to become more business-orientated. Morawiecki himself stated in a recent interview that PiS's recent civil service reforms aim to transform the institution into a more professional and driven one that follows the government's political priorities, but it remains to be seen how effective such a shift will be. Finally, many of the Plan's goals, such as infrastructure and business clusters, will be realised locally and their success will therefore heavily depend on the effectiveness of individual local governments.

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