POLAND
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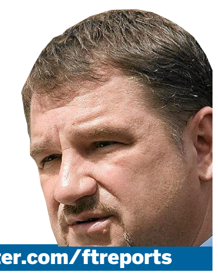

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A buoyant future hangs in the balance

Prospects for growth are good but the need for prudence and reforms remain, writes **Jan Cienski**

Poland dodged the recession bullet last year through a combination of skill and luck, and the hope is that both of those qualities still remain in force as the country grapples with serious fiscal imbalances that will put the largely unrealised reformist promises of the government to the test.

Last year's good economic news – the country eked out a 1.7 increase in gross domestic product – will be followed by even better news this year, with growth of 3.5 per cent as the economy gains speed thanks to continuing buoyancy in domestic demand and to Germany's economic revival, which is pulling in large amounts of Polish exports.

"We didn't get hit by the crisis, and now we are on a very fast path of development," says Jan Kulczyk, Poland's wealthiest man, who has ambitious plans for Poland after being largely absent for several years and is hoping to buy state-owned Enea, the country's third largest power generator, in an attempt to build a private utility company.

Poland's exceptional performance is drawing attention from investors. When the treasury ministry was book building for the initial public offering of the Warsaw Stock Exchange, institutional investors snapped up the offering in only 10 hours. Large private equity funds are keeping an eye on big potential deals, like the impending $5bn sale of Polkomtel, a mobile telephone operator.

"There is enormous enthusiasm for Polish debt, both denominated in zlotys and in euros or dollars," says Dominik Radziwill, the deputy finance minister, who notes that rates for Polish 10-year bonds are below those of troubled eurozone countries such as Portugal, Ireland and Italy.

Donald Tusk, PM, right, at Warsaw Stock Exchange with Aleksander Grad, treasury minister, centre, and Ludwik Sobolewski, WSE head Reuters

In the first eight months of this year, Poland saw financial inflows of €24bn, the same level as in 2008, the peak of the boom. But there is a big difference. Two years ago much of the money pouring into Poland was used to buy real estate or set up factories, while now 70 per cent of it is portfolio investment, which can be withdrawn in a hurry.

That underscores the fragility of Poland's current situation.

Jacek Rostowski, the finance minister, insists that public debt will not reach 55 per cent of gross domestic product, a legal threshold that, if crossed, forces the government to undertake painful spending cuts. The debt ratio is likely to hover very close to that number – without crossing over – thanks to some massaging of statistics, but the slightest turbulence in currency markets or investor sentiment could cause insuperable problems.

Donald Tusk, the prime minister, is resisting calls from some of the country's most prominent economists, including Leszek Balcerowicz, the architect of the 1990 reforms that launched Poland's market economy, to undertake radical steps to bring the budget back into balance. The deficit this year is expected to reach 7.9 per cent, although the government says it will fall next year and drop to 3 per cent by 2013.

However, the steps taken so far are fairly cautious, including a temporary increase in the VAT rate, a fairly porous public sector wage freeze and a spending rule that limits increases in discretionary expenditures to 1 per cent above inflation.

That is too unambitious for many economists. "There is a risk of complacency on the fiscal side," says Christian Keller with Barclays Capital. "Poland overall looks very robust, in a region that suffered significantly from the global crisis, but if inertia prevails in making the necessary fiscal adjustment, that could backfire."

However, the government has made it clear it is not interested taking more radical steps.

"I cannot agree that the Tusk government operates on the basis of expediency," says Jan Krzysztof Bielecki, a former prime minister who is one of Mr Tusk's closest advisers. "This government operates on the basis of principles, but also on the fundamental assumption that Poland does not need a new round of shock therapy."

Although Mr Tusk was elected in 2007 on a programme of reform and economic freedom, including slashing away at the red tape that throttles Polish businesses, he has been very cautious in governing. Several initiatives aimed at reducing the level of bureaucracy have

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Poland

Critics call for fiscal restraint as debt grows

Economy

The government's spending reforms must address looming challenges, writes **Neil Buckley**

Poland looks set to follow its achievement of avoiding recession in 2009 by reporting the second-fastest growth in the European Union this year, beaten only by Slovakia. But economists are warning that even it could do with a dose of the austerity measures being adopted by some EU counterparts.

The centre-right Civic Platform-led coalition was credited with a sure-footed response to the financial crisis, though last year's 1.7 per cent economic growth resulted, in part, from good fortune.

The previous Law and Justice party government had cut taxes and social security payments before the crisis began. A conservative banking sector and strict regulation meant Poland had not seen the bubble in foreign-currency lending that left its neighbours vulnerable when crisis hit. It had just embarked, too, on a multi-year investment fuelled by EU funds.

But alarms are being raised over public finances. The budget deficit reached 7.1 per cent of gross domestic product last year – from 1.9 per cent in 2007 – and the government predicts a 7.9 per cent deficit this year.

General government debt is now perched close to a legal ceiling of 55 per cent of GDP. If it breaches that level, the government is obliged to reduce the deficit in the budget for the following year. With about one-third of debt held in foreign currencies, any weakening of the zloty exchange rate could tip it over the line.

Both figures seem low compared with western European counterparts. The deficit compares with this year's forecast EU average of 7.2 per cent, and is well below Greece, Ireland, Spain or the UK. The debt remains substantially below the EU average of 80 per cent of GDP. But among Poland's central European neighbours, only Hungary, on 78 per cent, is higher.

"We are poor compared with developed west European states and we can't afford this stock of debt," says Krzysztof Rybinski, a former deputy central bank governor who is leading criticisms by a group of liberal economists.

Their biggest concern is that Poland's government – unlike Europe's high-deficit states – has done little to curb spending. They argue the deficit, rather than being caused mostly by last year's slowdown, is largely structural. Public sector employment has risen by 100,000 since 2005.

There are concerns that the government's plans to cut the deficit to 3 per cent by 2013 rely on Poland growing itself out of trouble. The finance ministry predicts a realistic 3.5 per cent growth rate this year and next, but a very optimistic 4.8 per cent in 2012.

More broadly, critics say Poland should shift away from poorly-targeted social

Anti-austerity protesters march to the prime minister's office in Warsaw AFP/Getty

spending, including myriad benefit payments, towards carefully planned measures to address looming challenges. These include an ageing population and the need to nurture a more high-tech economy.

The government could previously blame slow

> One effect of the bulging deficit is to push back the likelihood of Polish euro membership any time soon

progress in reforms on the possibility that they would be vetoed by the Law and Justice president Lech Kaczynski. Since his death in April's Smolensk air crash, and the election of Civic Platform's Bronislaw Komorowski as president, that problem has gone.

Some analysts accuse the government of excessive caution ahead of parliamentary elections next autumn.

"The government hasn't understood the severity of the fiscal situation," says Jacek Adamski, director of the economics department at Lewiatan, the employers' body. "It is better to start changing fiscal policy now than wait until the result of the elections."

The government rebuffs the criticisms. Jan Bielecki, a former prime minister and now economic adviser to premier Donald Tusk, says the government wants to "run the country much longer than one year".

He says three factors are inflating the deficit. First, Poland has introduced private pension funds as an alternative to its pay-as-you-go state scheme. That is a more viable long-term model, but the government has to make up for revenue shortfall in the public system in the short term.

Mr Bielecki says that swells Poland's deficit by about 2.4 percentage points, but the EU will not change its rules to take account of the effect of such reforms. The country calculates that with such a change, its public debt would be 35 per cent of GDP in 2014.

Second, municipalities have borrowed heavily to co-finance improvement projects enabled by EU funds. Mr Bielecki says municipal borrowing comes to 1.2 per cent of GDP, a figure that is added to public debt.

Third, the government has spent about 1 percentage point of GDP in this year's budget on long-overdue, partially EU-funded motorway construction.

He insists the structural deficit is smaller than critics claim, and that spending measures and benefits they are targeting are less costly than they make out.

He suggests Civic Platform will be ready to push through reforms, assuming it leads the government after next year's election.

It may be forced into spending reforms before then. Poland's constitutional court last month ruled unconstitutional a system under which the state covers all farmers' health insurance contributions regardless of income. It gave the government 15 months to change it.

One effect of the bulging deficit is to push back the likelihood of Polish euro membership any time soon. Polls show popular support for joining the single currency has fallen slightly since the financial crisis.

But many economists and business leaders want the country to join by mid-decade, giving a further boost to foreign investment. "If you are a big company from France or Germany, you like being in Poland," says Ryszard Petru, former chief economist at Poland's Bre Bank. "But you will still be more cautious than investing in the eurozone."

Brussels aid transforms infrastructure

EU funds

The €67bn is being used to close the gap with wealthier member states, writes **Jan Cienski**

A couple of years ago, when Magdalena Jaworska, deputy head of the Polish government's road building agency, would travel around the country, her driver would turn down his CB radio so she would not have to listen to the streams of invective from drivers enraged at the lack of highways.

Nowadays, her driver no longer bothers, as Europe's largest infrastructure project – the effort at last to equip Poland with a decent highway network – starts to bear fruit.

Ms Jaworska's increasingly quiet drives are in large measure a result of the enormous amounts of European Union money pouring into the country during the 2007-2013 budget cycle – €67bn ($94bn) in structural funds, intended to close the gap with wealthier member states, of which about €10bn is going for road construction. And that does not include billions more spent on farmers and other EU programmes.

"Without the funds, almost nothing would be happening," says Ms Jaworska, noting that about two-thirds of the money used by her agency comes from Brussels.

It is not just roads that are benefiting from the EU. In Jaslo, a town in the south-east of the country, not far from the border with Ukraine, Stanislaw Slawniak thanks Brussels for helping to build a modern sewage and water treatment system for a group of localities lying along the fast-running Wislok River. The programme cost €49m, of which 84 per cent came from the EU.

"Some localities had no sewerage systems at all, and dumped waste straight into the river," he says. "Without these funds the project would have been impossible – some of these localities are very poor."

Maria Kurowska, the mayor of Jaslo, runs through a list of projects co-financed by the EU: setting up a new economic zone, putting up CCTV cameras, insulating public buildings, education programmes, computerising local government offices, new buses, and modernising the crisis response system. In all, about 24m zlotys ($8.5m) in funding for a town whose total annual budget comes to 130m zlotys.

"Without EU funds none of this would have happened," she says.

The activity in Jaslo is replicated across Poland, and the effect on the economy has been enormous. Elzbieta Bienkowska, the minister of regional development, whose ministry controls most EU structural fund spending, says about half of Poland's 1.7 per cent economic growth last year was due to EU money.

"It is impossible to overstate the impact of these funds," she says. "No country has ever received so much money in one go."

The government has become better at filling in complicated paperwork required by Brussels. There were hiccups immediately after joining the EU, mainly because state laws were not yet harmonised with EU requirements, which meant that organisations following Polish laws ended up violating Brussels-mandated regulations. But those issues are now mostly resolved.

There were initial fears that the combination of the state's fearsome bureaucracy with the national character of seat-of-the-pants making-do would jeopardise the country's ability to take advantage of the available money. But Poland has turned out to be very good at squeezing every last cent out of the EU. Ms Bienkowska says the country is on track to exhaust all of the money in this budget cycle.

However, the flow of funds is causing problems for Jacek Rostowski, finance minister, as he attempts to rein in the country's growing deficit and public debt.

'Without [EU] funds, almost nothing would be happening' – Magdalena Jaworska

That is because every EU project must have a local co-payment of at least 15 per cent, and often more.

Local governments go into debt in order to fund the projects. "It would be unwise for local governments not to apply for projects where they get back 85 per cent of the cost," notes Ms Bienkowska.

Municipal borrowing comes to about 1.2 per cent of GDP, which is added to the public debt, pushing it closer to 55 per cent of GDP threshold beyond which the government is forced to undertake spending cuts.

In addition, Mr Rostowski also faces problems because of the timing of the financial flows from Brussels. Next year, the gap between money spent and reimbursements from Brussels will be 19bn zlotys. The situation gets better in 2012, when the funding gap is only 9bn zlotys. By 2013, when more projects are completed and refunded, the pendulum will swing in the opposite direction, benefiting the budget.

Despite the accounting problems, most Poles see EU funds as a way of catching up with west European living standards.

"We would still have to do these projects, but over 20 or 25 years, not five," says Ms Bienkowska.

Moving with the times Factory relocation, relocation, relocation forms basis for business model

Economic dislocation is the driving force of business, and for Poland's Pol-Inowex it is also a very good way to make a living.

That is because the company has specialised in tearing down and moving factories that have been driven out of business, relocated to cheaper countries or been made obsolete by better technology. The business gives Pol-Inowex a good view of the economic trends transforming the European Union, particularly after the admission of Poland and other low-cost central European countries in 2004 and 2007.

Bartosz Swiderek, the son of the company's founder, Jerzy Swiderek, and Pol-Inowex's vice-president, says that about three-quarters of his work consists of shipping factories from west to east as owners seek to take advantage of cheaper labour. And by west to east, he means not just from western Europe to central Europe, but also from Europe to Turkey, Iran and the Indian subcontinent.

"We sometimes transfer everything, leaving only the concrete walls," he says.

Paradoxically, the economic crisis, which shut factories across the continent, has not been a particularly lucrative period. Banks are warier about providing the financing to pay for relocations, and cash-strapped companies try to use surplus workers to undertake the tricky job themselves.

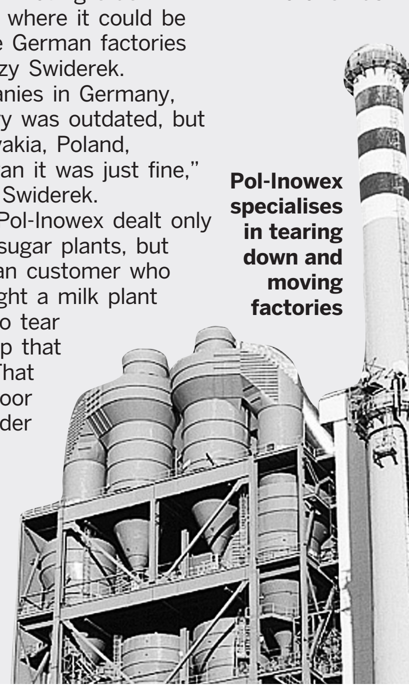
"Before 2008 we had a lot of factories closing because of the movement of technology and because factories were in good locations in the heart of cities where the real estate they were sitting on was worth a lot of money," says Mr Swiderek. "Now we are dealing with factories that have run into financial trouble."

Pol-Inowex got its start in 1988, producing parts for sugar beet plants in Poland and East Germany. Those factories did not have the hard currency to buy expensive parts in the west and so turned to lower-cost local manufacturers. After German unification, the East German sugar plants were all taken over by West German companies, which used much more modern equipment. That created a business opportunity in moving that equipment to where it could be used, and the German factories turned to Jerzy Swiderek.

"For companies in Germany, this machinery was outdated, but in Czechoslovakia, Poland, Hungary or Iran it was just fine," says Bartosz Swiderek.

Until 1995 Pol-Inowex dealt only in relocating sugar plants, but then an Iranian customer who had also bought a milk plant asked them to tear down and ship that factory too. That opened the door to a much wider range of business.

Sugar factory moves now account for less than a fifth of the work done by Mr Swiderek and his 100 workers.



Pol-Inowex specialises in tearing down and moving factories

Recent projects include shipping a cement factory from Berlin, where it was no longer needed after the end of the construction boom that saw the German capital rebuilt, to Moscow, where it was needed for the Russian capital's grandiose revitalisation. Some of the parts were so large that they had to be moved by heavy transporters originally used to carry SS-20 missiles.

In Iceland, Pol-Inowex had to use most of the island nation's cranes to pack up cement silos and ship them to Russia's Kaliningrad province on the Baltic.

As countries become more developed, it becomes increasingly difficult to make easy generalisations about the direction of investment flow. Mr Swiderek recently supervised the move of a chemical plant from the Netherlands to Jaslo in south-eastern Poland, and is now looking after the move of part of that factory to Italy.

But no matter what the reason for the move, the job is often a tough one, as the company's crews can be berated by workers distraught at losing their work and seeing their traditional places of employment backed on to trucks or barges and shipped away.

"Our workers have to be resilient," says Mr Swiderek. "Sometimes we are given local helmets and uniforms and told not to speak Polish so that the local workers don't know what is going on."

Jan Cienski

Buoyant future hangs in the balance

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produced lacklustre results, and Poland now trails the rest of the region in the World Bank's Doing Business rankings.

But the government is not keen to rock the boat politically, pointing to parliamentary elections set for next year. That has been a familiar refrain – the previous barrier hindering a more activist approach was presidential elections, won this year by Bronislaw Komorowski, Mr Tusk's ally.

After next year's vote, there will be an unusual three-year lull with no elections, which theoretically opens the road for politically difficult reforms, but Mr Tusk's team has not shown much appetite for radical steps for a good reason – except for the fiscal imbalances, Poland is actually doing very well.

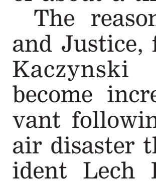
The country has become the EU's largest building site, thanks in large part to the €67bn in structural funds flowing into Poland during the 2007-2013 budget cycle. The signs of activity are visible everywhere, from the south-eastern border with Ukraine, site of the future A4 highway linking the region to Germany, to the outskirts of Warsaw, where a new bridge is being thrown across the Vistula River.

"Poland had a slowdown and not a recession because of European Union funds," says Elzbieta Bienkowska, the minister of regional development, the body responsible for administering much of the EU's structural funds programme.

The real estate market has stabilised after being rocked in late 2008 by the global crisis, and banks are again lending, although more cautiously than before. With unemployment at only 11.5 per cent, Polish consumers are continuing to spend.

That creates little domestic pressure for dramatic reforms. Coupled with that is Civic Platform's dominant political position. Opinion polls consistently show the party with the support of about half of the electorate, while the right-wing opposition Law and Justice party usually manages to garner the support of about a third of voters.

The reason is that Law and Justice, founded by the Kaczynski twins, has become increasingly irrelevant following the April 10 air disaster that killed President Lech Kaczynski and



'Poland had a slowdown and not a recession' –Elzbieta Bienkowska

95 others. Jaroslaw Kaczynski, the party leader, is obsessed with finding out what happened that foggy morning near Smolensk, Russia, and some of his more febrile supporters see a Russian plot to murder the president. When not hunting for the guilty in the air crash – although all evidence points to pilot error as the leading cause – the party has engaged in poisonous infighting.

The result is that, as Mr Tusk has quipped, "There is no one to lose against."

Poland's domestic well-being is mirrored abroad, where Warsaw has been forging an ever-closer alliance with Berlin – a relationship that Radoslaw Sikorski, the foreign minister, calls "the best in history".

Ties with Russia are much improved, although the bloody past continues to loom over the relationship, particularly Russia's reluctance to co-operate fully in investigating the 1940 murder of 20,000 Polish officers by the Soviet Union.

"Our history is a tough one. We would like a Polish-Russian reconciliation to match the Polish-German one," says Mr Sikorski.

Secure abroad and relatively content at home, Poland is in a sweet spot, as long as the external environment continues to be benign. "I don't think there is a need for dramatic change," says Mr Bielecki.

Long and winding road to a waiting market

The east

Jan Cienski on a region missing out on foreign investment because of poor access

Backwater: few foreigners look east of Warsaw to cities such as Lublin Bart Pro/Alamy

Forty minutes late for his interview, a frazzled Andrzej Kidyba rushes into his office in the eastern Polish city of Lublin and profusely apologises for being late – the 160km drive from Warsaw airport had taken him more than four hours.

"If an investor ever had to go through that hell, they would simply not come here," says the head of Lublin Development Foundation, an agency dedicated to trying to drum up investments in one of Poland's poorest regions.

Mr Kidyba's hellish drive is one of the reasons that very few foreign investors have bothered to make the trek east of Warsaw.

The vast majority of foreign factories have set up in the west of the country, close to Germany, Poland's largest export market, and decently connected to the rest of the continent by highways.

"There is a lack of a big investor in the region who can act as a magnet and pull in others," says Mr Kidyba.

Lena Kolarska-Bobinska, the local European MP, is shepherding about a dozen potential investors through Lublin, with 350,000 people, the region's largest city. They are all Poles – not one foreigner has come along to explore the area.

The problem is similar all along Poland's eastern border with Belarus and Ukraine. The region – known as the "eastern wall" in Polish – has historically been backward. It formed the forgotten fringes of the Russian and Austro-Hungarian empires, and was long ignored by the government in Warsaw. Today, the region has only about two-thirds of Poland's average per capita wealth, has higher unemployment, and has seen greater labour migration than the rest of the country.

Transport is one of the main reasons for the gap with the more advanced parts of the country. Sitting in her office in central Warsaw, Magdalena Jaworska, the deputy head of the government-run road building agency, glances up at a big wall map showing all the highways and slightly lower quality express roads being built around the country.

The west of the country is dense with black – showing completed roads – and red – showing roads under construction. But the east of the country is green and white – showing roads in planning stages where completion is in the far-distant future.

Very few road projects in eastern Poland meet the European Union's criteria for traffic and economic benefits, she admits, which is why little is being done except to build bypasses around larger towns to steer cars and lorries out of city streets.

The EU's structural funds, €67bn ($92bn) of which are flowing into Poland during the current 2007-2013 budget cycle, are supposed to help level out some of the differences, but that is not turning out to be the case.

The more developed regions in the centre and west file many more funding applications for innovation grants than those in the east, in large part because it is easier to economically justify such projects in wealthier parts of the country and because civil servants in richer regions are more experienced in dealing with Brussels.

> 'There is a lack of a big investor in the region who can act as a magnet and pull in others'

A smaller €2.7bn programme aimed specifically at eastern Poland has seen 114 projects approved so far, but the money is not enough to make up the gap between east and west.

The one part of eastern Poland that is seeing an increase in investor interest is the Podkarpackie region, in the south-east, where the A4 highway running across southern Poland from the Ukrainian to the German borders is under construction.

Elsewhere the movement is much smaller scale. Pol-Mot Warfama, an agricultural machinery producer with factories in western Poland, is setting up a new factory in Lublin in part of a car plant that used to belong to Daewoo before the Korean company ran into trouble in the early years of this decade and pulled out of Poland.

The idea is to assemble Chinese tractors and pick-up trucks.

"We have experience in the west of the country and we saw that it was more and more difficult to find qualified labour at reasonable prices there," says Karol Zarajczyk, the company's chief executive. He estimates that workers cost about a third less in Lublin than in western Poland.

With unemployment in Lublin at 11.9 per cent compared to 8.5 per cent in the region around Poznan, where one of Pol-Mot's factories is located, Jan Wielgus, the rumpled engineer in charge of the Lublin project, says he will have no difficulty finding the 70 qualified workers he expects to hire in the next few months.

"Look at that stack of applications from welders lying on my desk," he says, pointing.

The task for the region is to make big investors see that as well.

Na zdrowie, toast to the spirit of a nation

Vodka

Moves are afoot to change the downbeat image of 'little water', writes **Adam Easton**

Did those potatoes ripen on the south side of the hill? That is the kind of question few vodka drinkers ask but, if Tadeusz Dorda has his way, an alcohol best known for its get-drunk-quick properties could join the world's finest beverages.

In an 18th century wooden potato storage building, Mr Dorda extols the virtues of vodka.

"The rye vodka has a very strong smell like freshly baked bread … the potato vodka is very fragrant and full-bodied," he says. Chopin Vodka, which Mr Dorda makes and markets as a luxury potato vodka, on the other hand, has "a very fresh aroma, the texture is very creamy and rich".

Those adjectives may not be the first thing that comes to mind when sipping a glass of clear vodka.

During a tour of the distillery, which has been making vodka from potatoes harvested from the surrounding fields since 1896, the 59-year-old businessman says he is trying to change perceptions about a drink he feels is wrongly defined as "tasteless, colourless and odourless".

Chopin Vodka should be sipped and savoured like a fine cognac or malt whiskey, he says.

"It does vary in taste from year to year slightly. It does taste different depending on what time of the year the potatoes are harvested and those differences are quite sizeable to the developed palate. I think the time will come when the intelligent consumer will say, 'I want to know what I'm drinking'. He's saying that with wines and other products, he's not saying that with vodka yet," he adds.

Instead, the average Polish drinker is more likely to be taking a vodka bottle out of the freezer and knocking back a shot followed by a bite of a pickle – while many foreigners use vodka as a base for mixed drinks.

Poles have been producing the drink, whose name means "little water", since at least the 11th century, and the country still ranks as the fourth largest vodka consumer in the world. But vodka's dominant position has been toppled by beer and, as Poles grow more affluent and succumb to western tastes, they are increasingly drinking wine as well. "We know that Poland and vodka go together so why don't we present it in such a way that it is a plus and not a minus? In the minds of the Polish people vodka is a minus," Mr Dorda says in between sips at a glass at the small distillery in Krzesk, in eastern Poland.

Now a boutique product, the vodka was first produced to mark a beauty contest in 1993. Chopin Vodka retails at more than twice the price of better known rivals and sells around 100,000 cases a year worldwide.

Chopin is not the only luxury vodka. It competes with Belvedere, a vodka distilled from Dankowskie Gold rye and made by the Polmos Zyrardow distillery, owned by the US-based Millennium Imports, and Wyborowa Exquisite, another rye vodka packaged in a twisted square bottle made by the Pernod Ricard-owned Wyborowa distillery in Poznan, in western Poland.

Poland is about vodka: Tadeusz Dorda makes and markets Chopin, his luxury drink

Mr Dorda acknowledged that changing people's perceptions about vodka is tough. Single malts and cognacs can entice consumers with details of sherry oak casks or age. Vodka is not aged; it is distilled four times and can merely boast traditional ingredients.

The row in the European Parliament over what vodka can be made out of has not helped Mr Dorda's cause. Traditional producers in eastern Europe and Scandinavia wanted a definition that restricted vodka to a drink made from potatoes or rye. Instead, the EU decided it can be made out of products such as grapes and sold as vodka as long as it says so on the label.

Mr Dorda worries that if vodka's image is sullied by having to compete with unorthodox alcohols calling themselves vodka, it could end up hurting Poland's image.

"Vodka has a very low appreciation level and that's what we are trying to raise. Let people discover the culture that goes with it and in the process you discover Poland because Poland is about vodka," he adds.

Poland

Fast movers in a positive state of mind

Private equity

A record year is on the cards for a sector with an eye on rapid company development, writes **Jan Cienski**

In much of the US and western Europe, the popular imagination lumps private equity in with mustachio-twirling villains for using very high leverage to buy troubled companies, then slashing costs and jobs before selling on. But that is definitely not the view of the industry in Poland.

"In Poland private equity has been about financing development," says Monika Morali-Efinowicz, the managing director of Advent International's Warsaw office.

"Most transactions have been about giving fast-growing companies capital."

That has given the industry a very positive image – but one that may be about to change as Poland's economy matures and it becomes more difficult to find obvious market niches where companies can grow explosively.

Recent fast-growing investments include Zabka convenience shops, owned since 2007 by Penta, the Czech and Slovak investment firm. The investor helped Zabka expand into the Czech Republic, and financed a rapid expansion – the chain now has 2,300 shops, and plans to open about 250 locations a year. "They are a credible and financially sound investor, which allowed us to get financing on very favourable conditions which allowed us to speed up development and open new shops," says Jacek Roszyk, the company's CEO.

However, he admits that the market ceiling for his chain is about 7,000 locations. That means growth will probably slow in the future. Penta is preparing to exit its investment, possibly in early 2011.

That makes Zabka one of an increasing number of secondary offers on the Polish market. One of the heftiest is Aster City, one of Poland's largest cable operators, which is being sold for as much as $1bn by Mid-Europa Partners, which bought the company in 2005 for $488m.

Funds are also circling around Polkomtel, a mobile telephone operator owned by a group of Polish state-controlled companies and the UK's Vodafone Group, that is likely to come to market early next year for as much as $5bn

Transactions that big are enough to attract the attention of larger west European funds, which have not generally invested in setting up Polish operations, due in large part to the limited deal size, which tends to hover at an average of about €10m ($14m).

"There are people who still need to buy a leading company in Poland," says Tod Kersten of DC Advisory Partners, a corporate finance house, explaining that the positive Polish story as the only EU country to avoid recession last year has attracted the attention of outside funds.

The new deals will test the financial architecture of the industry.

Until now most transactions have been at fairly conservative levels of leverage – three or four times earnings before interest, tax, depreciation and amortisation, while levels twice that or more are common in western Europe.

The lower leverage is a result of the conservatism of local banks, as well as the fact that adding leverage to the turbulence inherent in fast-growing sectors makes for a very risky combination.

Funds will also be faced with new management challenges. Ataste of that came this year when Enterprise Investors, one of the biggest players in Poland, pulled out of Orbis, a well-known travel agency, resulting in a raft of bad publicity as news reports were filled with tales of stranded holidaymakers.

"It was a distressed asset, and no one in Poland or in the region specialises in that," says Jacek Siwicki, chairman of Enterprise Investors.

"It's a lot more pleasant to fund growth than to lay off people and to cut costs."

As big firms like Aster are sold on, local funds are hoping to capitalise on their knowledge and connections to scoop up the next wave of emerging companies as entrepreneurs who set up their businesses during the turbulent transition from socialism to a market economy two decades ago now look to cash out.

A Polish private equity executive was recently asking an entrepreneur why he was interested in selling. "Because my son is a moron," came the reply.

But, so far, despite any genetic shortcomings of the next generation, most business founders are willing to sell only minority stakes in their companies, an unattractive proposition for private equity funds, so entrepreneurs tend to list on the Warsaw Stock Exchange, the most liquid bourse in central Europe.

In spite of such difficulties, as 2010 draws to a close Poland's private equity industry is expected to produce a record year for investments – after a lacklustre 2009 – but the result is due to the unexpectedly large size of a few deals than to any wider revival in the sector.

Mr Siwicki says so far this year six big deals amount to about €800m, dwarfing the uninspiring €268m seen in crisis-ridden 2009, a decline from the €633m in 2008 – and that is without the possible Aster City sale. "We are expecting the best year ever in Polish private equity," he says.

Main attraction: Polkomtel, owner of Plus GSM, could be on the market next year for as much as $5bn Bloomberg

Settlers happy with new home

Case study
Samsung

Neil Buckley on a manufacturing move by the electronics group

In December last year, much of Europe was only starting to emerge from recession. But Samsung chose exactly that moment to press ahead with European expansion, becoming one of many multinationals in recent years to start manufacturing in Poland.

The South Korean electronics group agreed to buy the refrigerator and washing machine manufacturing facilities of Amica, a Polish appliance maker, in Wronki, a town in rural western Poland.

It was a rare acquisition for Samsung – and part of an ambitious strategy to repeat the success it has achieved in flat-screen TVs and mobile phones. From its current position as the sixth-biggest manufacturer of white goods in Poland, it aims to become number one in Europe in the coming years.

As well as its Wronki factory, Samsung has plants manufacturing televisions and home cinema products in Hungary and Slovakia. It is also not the only Korean manufacturer to choose Poland as a European production hub; rival LG built a factory for flat-screen TVs and consumer electronics in Wroclaw, south-west Poland, four years ago.

Samsung's investment in manufacturing in Poland last year built on long-standing experience in the country. It opened a sales and marketing operation in Warsaw in 1996 and followed that up in 2000 when it transferred its European research and development arm from Frankfurt to Warsaw.

"We knew that we could hire very well-educated engineers here in Poland, but it was very hard to hire those well-educated engineers in Germany," explains Choi Kyung-sik, president of Samsung's Polish business. "The German labour market is a little bit tighter currently."

The Polish capital, he adds, proved a particularly good place to find the kind of engineers Samsung needed, thanks in part to the strength of the University of Warsaw and Warsaw University of Technology.

Its sales and marketing office now employs 250 people. The R&D centre has more than 650 staff, focusing on developing software for mobile phones, "smart" internet-enabled TVs, and set-top boxes, and carrying out mobile phone testing.

When it came to finding a factory to help fulfil its strategic aim in white goods, it chose Poland in part for the same reason many other manufacturers have done – geography.

"This country is the centre of the whole of Europe, if you look at the map, so we can produce and then send products to all European countries very easily," says Mr Choi. The Polish plant is its seventh household appliance facility worldwide, adding to factories in South Korea, China, Thailand, Malaysia, India and Mexico.

Buying an existing factory rather than building one was something of a departure. But Mr Choi explains that the Amica Wronki factory met its requirements well.

"We also thought about having a factory near our TV factories, but if we'd built it from scratch it would take a bit of time. If we buy a business we can start production straight away,"

"We didn't need to have a big headache of hiring 1,500 people. Some 600 were already working in the Amica factory, and the other 900 were hired from regional plants. This area has many well-educated workers, so it will be no problem expanding our business. The government also helped with various types of benefits," he adds.


Praise: Choi Kyung-sik, head of Samsung's Polish operations

After a little modification of the plant, the first Samsung products came off the production line at Wronki last May.

Now Samsung is spending the same amount again, another $76m, to double the capacity of the factory by next year, so that it can produce about 2m fridges and washing machines annually by 2013. "We've had very good experience in making our business number one in other product groups, so we are quite sure we can achieve this goal," Mr Choi says.

Samsung's experience in Poland makes him confident about the country's future, too. "The Poles have a lot of potential, since they are eager to study very hard – it is the same as in Korea," he says. "They focus on developing for the future. There is very high potential to make this country grow."

Banks balk at proposed loan restrictions

Banking

They weathered the crisis but there are fears new rules will stifle growth, writes **Neil Buckley**

The Polish banking sector's conservative nature helped it weather the crisis without state support. Now its concern is the possibility of tighter regulation that it fears could be unfairly restrictive.

Much has changed since the first quarter of last year, when one bank chief warned of an approaching "tsunami". The zloty was tumbling against the euro, pressuring the balance sheets of banks that had been providing foreign currency loans and mortgages.

In fact the zloty stabilised, Poland's economy continued growing last year, and foreign parents – which control about 70 per cent of the sector – maintained support for their Polish subsidiaries.

Poland's banks were less vulnerable going into the crisis than those of some neighbours. The relatively underdeveloped banking sector had stuck to plain-vanilla business models, eschewing more sophisticated, risky products. Regulation by Poland's KNF or Financial Supervision Auth- ority was relatively firm.

Foreign currency lending had not reached the level of neighbouring countries – though it was growing fast when the crisis hit. Banks had also loosened their lending criteria too far on consumer loans.

Krzysztof Pietraszkiewicz, president of the Association of Polish Banks, says the crisis came at a "good moment. Two or three years later the situation would have been worse".

Banks did rein in lending last year, strengthening balance sheets and boosting interest rates to attract savings in a "deposit war".

Their relatively thick capital cushions enabled them to absorb losses on bad loans and remain in profit last year – though profits fell by a third from 2008, to 8.7bn zlotys ($3bn).

"The banking sector came through its difficulties well and has remained profitable, well-capitalised, and liquid," says Pawel Kusiak, head of commercial banking at HSBC Bank Polska.

Non-performing loans grew from 4.5 per cent of banks' portfolio at the end of 2008 to 7.6 per cent by the end of last year and 8 per cent by June this year. Mr Pietraszkiewicz says they may top 9 per cent by year-end, but will have peaked.

Zbigniew Jagiello, head of PKO Bank Polski, Poland's largest bank, says his bank has an NPL ratio of 7.4 per cent, with most bad loans coming from corporate and retail cash loans.

Banks have started to increase lending again. Mr Pietraszkiewicz says lending may be up more than 4 per cent this year, with higher growth in retail lending offset by a slower increase in corporate lending.

> 'We don't believe that regulations should be retrospective'
>
> **Krzysztof Pietraszkiewicz, Polish Banks' Association**

But banks are warning they should not be penalised for others' mistakes, and hit with regulation that could be disproportionate.

The KNF in August introduced stricter requirements on sales of foreign-currency loans. It has also proposed limiting foreign currency lending to 50 per cent of banks' loan books.

The regulator says effective restrictions are needed to avoid the sector becoming vulnerable in future.

But if the proposal is applied to existing loans, the banks' association says it would be onerous, particularly for some foreign banks that have made as much as 90 per cent of lending in foreign currencies.

Mr Pietraszkiewicz's association has proposed an alternative, agreed by the banking community, of limiting forex loans to 30 per cent of banks' new loan production, in a phased approach by mid-2012. The sector is meeting that now, he says, with 27 per cent of new credits in foreign currencies, largely euros.

"Our approach . . . would allow more time for banks to introduce a new strategy," he says. "We don't believe regulations should be retrospective."

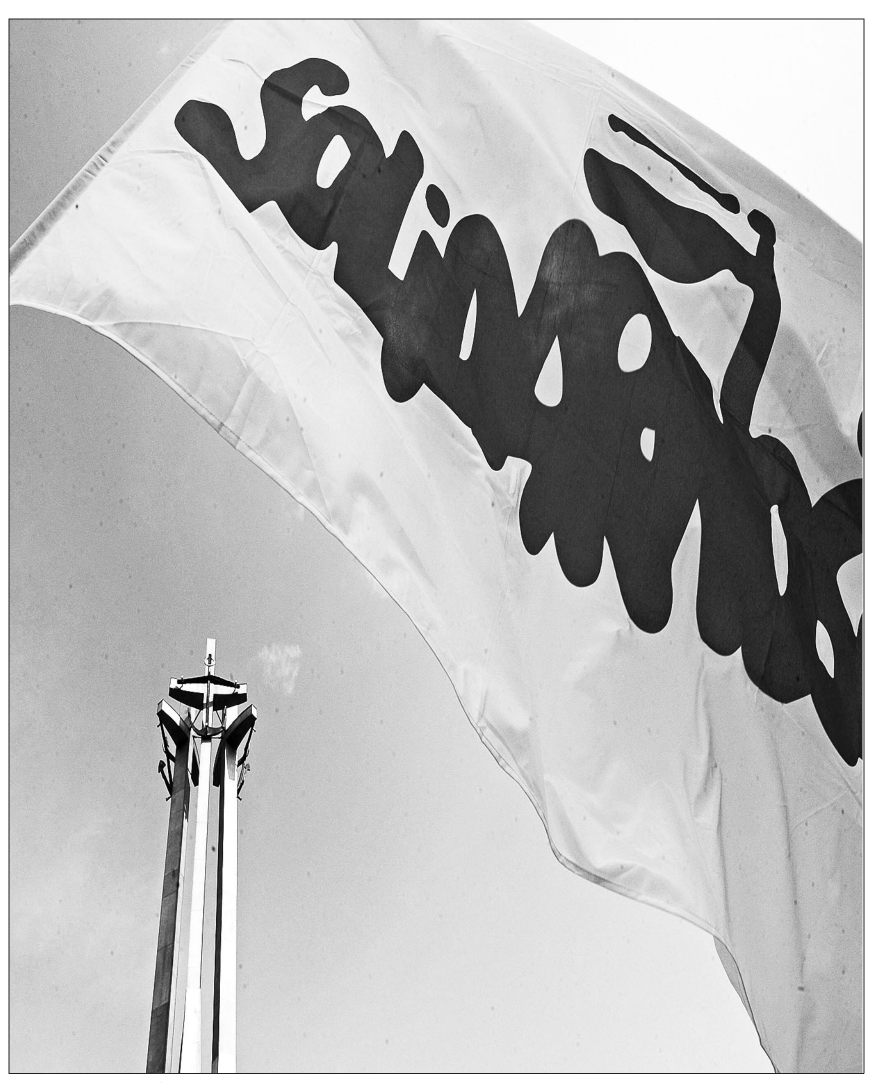
Of similar concern is talk from some opposition parties and prime minister Donald Tusk of a possible tax on banks,

Mr Pietraszkiewicz says that would impose an unfair burden on a sector already facing one of the highest effective tax rates in Europe.

Banking executives agree. "The government has very little justification for such a tax," says Stephane Hild, head of Société Générale in Warsaw. "It did not have to step in to help the sector."

The crisis also focused attention on the extent of foreign ownership. Though foreign parents supported Polish subsidiaries this time, concerns remain about what might happen if there was any recurrence.

Freedom fighters struggling to find a role in new world


When the red Solidarity slogan is unfurled, some of the old magic remains

Solidarity

It battled to free Poland from Communism but now its leaders and members face a different enemy, says **Jan Cienski**

Poland's freedom was won thanks in large part to Solidarity, and many leading members of both the government and the main opposition party cut their political teeth in the union 30 years ago.

Today Solidarity is a shadow of its former self as it and other large labour organisations struggle to stay relevant.

At its peak three decades ago, Solidarity had more than 10m members, but, at the time, it was much more than a simple union – it was a force for liberating society from communist oppression.

Now, 20 years after Poland's transformation into a market economy, Solidarity has only 700,000 members and has long since become a regular union, fighting regular battles.

Something of that old magic still remains, when banners carrying the familiar red Solidarity slogan are unfurled, and union leaders reminisce about when they were the country's leading political and social force.

But now the battle is not with communists, but with the market liberals in the Civic Platform party

Continued on Page 5

Shift from global ambition puts the accent on Europe

Foreign policy

Forging an alliance with the US has been sidelined in favour of a key European role, writes **Jan Cienski**

Polish special forces took part in the 2003 invasion of Iraq, and 2,600 Polish troops are fighting Taliban insurgents in the southern Afghan province of Ghazni, but the age of Poland's global foreign policy ambitions – tied to hopes of becoming one of America's crucial European allies – is fading.

Instead, Poland is recognising that its true strength lies in its increasing influence within the European Union, where, with 38m people, it is the sixth largest member.

Poland sees its fate as inextricably tied with the Union – from the millions of workers who moved to western Europe after Poland joined the EU in 2004, to the €67bn ($94bn) in EU structural funds that Poland will receive during the 2007-2013 budget cycle.

The current government achieved a head start by simply being different from its predecessors in the 2005-2007 right-wing Law and Justice party government, which had reignited historical tensions with Germany and Russia, and which viewed Brussels with suspicion, preferring to focus on ties with the US.

Since then Poland's growing economic weight, and the current government's calmer EU negotiating tactics, have strengthened Poland's position.

A crucial component of Poland's foreign policy is its ever closer ties with Germany, a relationship that Radoslaw Sikorski, the foreign minister, calls "the best in history". The animosities left from Germany's brutal wartime occupation of Poland are fading, and the two now see each other as increasingly reliable allies.

In a recent interview, Mr Sikorski makes a special point of underlining that Germany's trade relationship with Poland – exports worth €31bn in the first half of 2010 – is more important than its much higher-profile trade with Russia. German exports to Russia were worth only €26bn in the same period.

Poland's close links to Germany – helped by the apparently decent personal relationship between Angela Merkel, the chancellor, and Donald Tusk, Poland's German-speaking prime minister – have made the two countries a natural pair for pressing the EU's influence into the troubled ex-Soviet republics lying between Poland and Russia. The Polish and German foreign ministers travelled to Minsk this month to press Alexander Lukashenko, Belarus's authoritarian president, to break with precedent and hold free and fair presidential elections on December 19.

"With Germany, our first duty is to our immediate neighbourhood, and that is where we have the biggest impact," says Mr Sikorski, who also expresses dismay at the reluctance of other EU countries to make a clear offer of membership to countries such as Ukraine, which would strengthen pro-EU trends in that region.

'With Germany, our first duty is to our immediate neighbourhood' – Radoslaw Sikorski

The Eastern Partnership, a programme devised by Poland and Sweden and offered to six non-Russian republics in eastern Europe and the Caucasus, will be the main focus of Poland's EU presidency in the second half of next year.

For Poland, eastern Europe carries a similar historical weight to Latin America for Spain and North Africa for France and Italy – a region that carries echoes of old imperial glory. But, in the case of eastern Europe, these are countries that are potential future EU members, making the Union's approach to them of enormous importance.

Paradoxically, one of Poland's worst foreign relationships is with fellow-EU member Lithuania, its partner in the Renaissance-era state that controlled most of the region.

A $3.7bn investment by PKN Orlen, the state-controlled oil company, in Lithuania's Mazeikiu refinery has gone sour, and ties are bedevilled by irritants such as Lithuania's refusal to allow its Polish minority to write their names using Polish, not Lithuanian, script. However, the relationship with Russia has improved markedly, although Mr Sikorski is careful to call it "good but fragile".

Economic ties are also growing – with Poland taking Russian natural resources such as oil and gas, and the Russians buying Polish finished goods.

"We are a superpower in consumer products, car parts and furniture," quips Mr Sikorski.

The April 10 Smolensk air crash that killed President Lech Kaczynski and many senior officials put the newly improved relationship to a severe test.

The Russians have taken the lead in investigating the crash, but there have been tensions over the way the inquiry has gone. The government of Mr Tusk and his Civic Platform party has come under fire from Jaroslaw Kaczynski, the Law and Justice party leader and the dead president's twin brother, who sees Russian bad faith in the way the investigation has been conducted.

Mr Kaczynski's more febrile supporters suspect – on the basis of no evidence – that the crash was a Russian plot to kill Lech Kaczynski.

Those conspiracy theories have not derailed warmer ties with Russia, which is a key part of the Polish government's bid to play a leading role in central and eastern Europe.

That focus will grow as its more far-flung obligations such as Afghanistan – where Bronislaw Komorowski, the president, wants to end combat by 2012 and pull the troops out by 2014 – come to an end.

Coal-fired source of a looming dark age

Power

Adam Easton looks at the pressing challenge to find an alternative way of producing energy

Crisis generation; water vapour and smoke rise from a power station in Belchatow Bloomberg

Poland's ageing coal-dependent power industry is facing its biggest challenge in years – replacing obsolete plants while foreign investors are abandoning plans to build new capacity in the country.

Seventy per cent of the country's power plants and transmission lines are more than 30 years old and must soon be rebuilt at an estimated cost of €50bn.

Most of those plants are fuelled by heavily-polluting coal. Poland is the European Union's largest hard coal producer and around 95 per cent of the country's electricity is produced from both hard coal and lignite.

Polish and foreign generators have announced plans to build 26.4GW of capacity but much of this will never be built. Just two new units, with combined capacity of less than 1GW, have been connected to the national grid in the past three years. Difficulties in raising financing for new projects and the unclear cost of complying with future climate change regulations have led foreign investors in the Polish market to reconsider their plans. Vattenfall, the Scandinavian utility, has dropped two large coal-fired investments and is reviewing its presence in the country. Germany's RWE and CEZ of the Czech Republic have also dropped plans for new plants. Analysts say the cost of carbon alone already adds between 20-25 per cent to Polish wholesale electricity prices and after 2013, no one yet knows how much it will increase.

Krzysztof Rozen, head of corporate finance at KPMG Poland, reckons 60 per cent of the country's installed power generation capacity will be obsolete by 2016.

"There is a huge need to replace this and in Poland right now we don't have the investment in place to do it. On the other hand our capacity to import electricity from abroad is also limited, so a blackout, unless something dramatically changes in the next couple of years, is looming over Poland in five years' time," he says.

The global financial crisis helped Poland in its precarious position by cutting power demand by 4 per cent last year. In comparison, so far this year, electricity consumption has risen 4.6 per cent. Wladyslaw Mielczarski, a leading power sector expert from Lodz Technical University, says if annual gross domestic product continues to grow by a conservative 3 per cent for the next five years, Poland will suffer electricity shortages by 2017-18.

'If the government continues to do very little we will have some kind of catastrophe'

"If the government continues to do very little we will have some kind of catastrophe in the next five years," he says.

Mr Mielczarski says the government would probably have to introduce controlled rolling blackouts with industries forced to reduce production, as happened during supply crises in communist times. He said the government should offer investors incentives to build new plants, something that is possible under EU directives.

Foreign investors may be shying away from coal projects in Poland, but that is not the case with the country's four vertically-integrated state-controlled power companies. The largest, Polska Grupa Energetyczna (PGE), will soon connect a new lignite-fired unit at the giant Elektrownia Belchatow plant, which produces almost 20 per cent of the country's electricity. PGE is also tendering for new coal units at two of its other plants.

The Polish government recognises the country's plants cannot keep burning so much coal. The government's energy policy for the next 20 years plans to reduce dependency on the fuel by around 40 per cent, partly through the construction of the country's first two nuclear power plants.

"I think we have to change fuel and if we are pushed by the EU we will do it slowly, we cannot do it overnight. The only way we can significantly reduce our dependence on coal in the next 10 years is through gas," says Mr Mielczarski.

Poland produces its own natural gas but it relies on Russian imports for two-thirds of its needs, making gas, which is about 50 per cent cleaner than coal, much less politically acceptable as a fuel. The government has signed a gas deal with Russia to secure supplies until 2022 but it is also pinning its hopes on the country's – as yet unproven – reserves of shale gas.

Over the past three years oil majors such as ExxonMobil, ConocoPhillips and Chevron have bought shale gas exploration licences in Poland.

The investors are optimistic and Radoslaw Sikorski, the foreign minister, has even talked of Poland becoming a new Norway. But no one knows how much shale gas is under Polish soil or that it will prove commercially viable.

Growing into trouble...

Guest Column

KRZYSZTOF RYBINSKI

Poland was the only EU member to survive the crisis of 2009 without falling into recession. A thrilled Donald Tusk, prime minister, presented this achievement by showing a map of Europe with Poland as a green island floating on a red sea of European recession.

But the narrow escape – Poland's economy grew by 1.7 per cent last year – carries the seeds of serious future problems caused by Poland's high budget deficit – estimated at 7.9 per cent this year – and a rapidly rising public debt. Poland remains one of the fastest growing economies in Europe, with GDP growth expected to reach 3.5 per cent this year. Both government and National Bank of Poland forecasts call for growth above 4 per cent next year.

There are three major factors behind this solid growth. First, the structure of Poland's economy proved resilient to the crisis, with low leverage and a low reliance on external trade. Second, pure luck, as Poland reduced taxes just before the crisis. And third, and most worrying, an enormous Keynesian-style fiscal expansion.

This last factor comes as a surprise to many analysts, because 18 months ago the Polish government declared it would not bow to the International Monetary Fund's pressure to expand public spending. And while Germany and the US tried to revive demand with policies such as the cash-for-clunkers programme to boost car sales, Poland called for increased savings. In early 2009, the government even declared that it would reduce the public administration headcount by 10 per cent.

With time it became evident that not only had the savings trumpeted by the Tusk government failed to materialise, but public spending was expanding. According to government forecasts, the ratio of public spending to GDP from 2008 and 2011 will rise from 42 to 48 per cent. A big part of this growth is due to the massive increase in public infrastructure investment financed by the EU.

Added to that, promised cuts in public sector employment have not materialised; on the contrary a recent Polish statistical agency report showed that in the past 12 months the public administration headcount has increased by 7 per cent. There is one obvious question, is this expansion sustainable?

Professor Krzysztof Rybinski delivers a warning on the economy

The government's medium-term fiscal report predicts that public debt will rise between 2008 and 2013 by 330bn zlotys ($118bn), to which should be added 30bn zlotys of road infrastructure spending shifted from the budget to the National Road Fund. That means new debt comes to 21 per cent of GDP.

Poland has seen these kinds of numbers before, between 1970 and 1980. Then, Poland's communist leader, Edward Gierek, launched massive infrastructure and industrial investments financed by foreign borrowing.

During the 1970s, Polish public debt increased by 40 per cent of GDP (measured in 1980 terms). That means that during the six years of Mr Tusk's government, the growth in debt is similar to that seen under Mr Gierek.

Although, as roads and power plants built in the 1970s can attest, not all the money borrowed by Mr Gierek was wasted, the country was unable to repay its debt and went bankrupt.

The fate of Mr Gierek's leveraged modernisation leads to a question about how Mr Tusk's heavy borrowing will end. In order to reduce the risk of unpleasant fiscal turbulence, economists have called on the government to accelerate much needed structural reforms: rationalise social spending, end privileges for special groups such as farmers and miners, raise the retirement age from one of the lowest in the EU, and reduce the deficit.

But the government and Bronislaw Komorowski, the president, have responded to those calls by saying there is no need to engage in "romantic" reforms. Romantic or not, they are needed.

And markets are likely to test the government's willingness to reform immediately after the 2011 general elections.

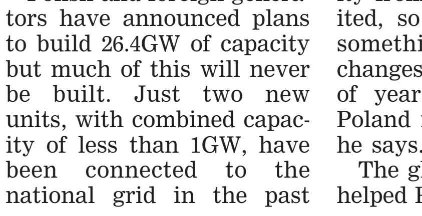
Prof Krzysztof Rybinski is rector of the University of Economics and Computer Science in Warsaw and a former deputy governor of National Bank of Poland.

Continued from Page 4

government of Donald Tusk, the prime minister and a Solidarity member in 1980.

"We don't want to be seen as a brake on the economy – we do see the problems of this crisis, but our government is using a liberal approach and they think everything will fix itself, and that's just not true," says Piotr Duda, the newly elected head of Solidarity.

Mr Duda, who was only 18 in 1980, is breaking with his predecessor Janusz Sniadek, who had despaired of Civic Platform and moved closer to the right-wing Law and Justice party founded by the Kaczynski twins, in effect turning the union into the military arm of the party.



'Our government is using a liberal approach and they think everything will fix itself, and that's just not true'

Piotr Duda

But Law and Justice is consumed with internal warfare and unlikely to take power in the near future, and the close association was beginning to hurt the union.

"We will not identify with political parties, but with their programmes," says Mr Duda.

For Mr Duda and his counterpart Jan Guz, leader of the left-wing All Poland Alliance of Trade Unions (OPZZ), which had its roots in the unions set up by the communists after Solidarity was banned in 1981, the fight is less about being a political force than ensuring that unions still have a role to play in today's Poland.

"Unions paid for the transformation. They destroyed the old system, but a lot of people are living in poverty and forgotten," says Mr Guz.

Union membership has plunged as Poland has turned into a vibrant market economy, and now only about 20 per cent of full-time workers belong.

For many Poles, unions are redolent of the heavy smokestack industries that were a feature of the communist past, and they are still best known for fighting for the privileges of industrial workers.

In the most notorious example, enraged miners wielding axe handles threatened to storm parliament in 2005, defending their right to early retirement and higher-than-average pensions.

At the Kompania Weglowa, the EU's largest coal company, 13 unions rub shoulders, with each union guaranteed a few jobs with salaries covered by the company.

Jacek Korski, the company's deputy chairman, says that last year Kompania Weglowa, which had a 2009 profit of only 25m zlotys ($9m), paid out 20m zlotys in such benefits. Even Mr Guz admits: "Pluralism is good, but these types of situations have also weakened the union movement."

That hurts unions when the government is talking about cutting public service jobs, freezing pay, and economists are advising the prime minister to increase the retirement age and slash benefits in order to bring the budget deficit under control.

Unions have threatened to go on strike, but so far the actual steps taken by the government have been quite careful, and Poles seem to have lost their once revolutionary temperament. "The French are at least fighting for their rights," says Mr Duda, admiringly.

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