

CESEE reunion with Europe



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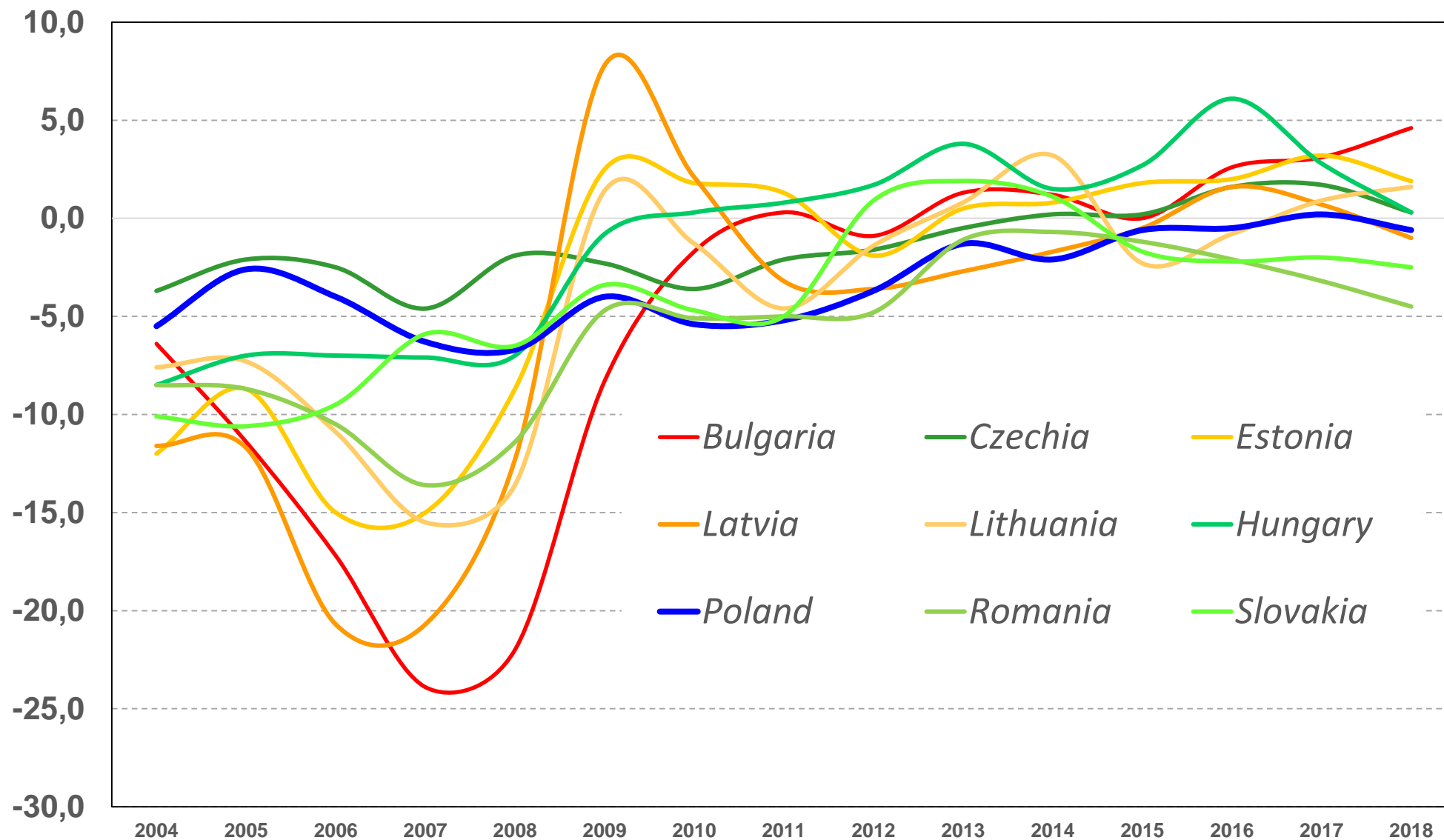
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1. Exchange rate policy

The choices of exchange rate regimes in the early 1990s

- Initial fixing of the zloty enabled Poland to overcome hyperinflation (600%)
- Its subsequent gradual floating facilitated adjustments in the BOP
- Currency boards were a rational choice for the Baltic states and Bulgaria, but exposed them to unsustainable lending booms

Current account balance (% of GDP)



The 1990s proved that interventions on FX markets can be effective

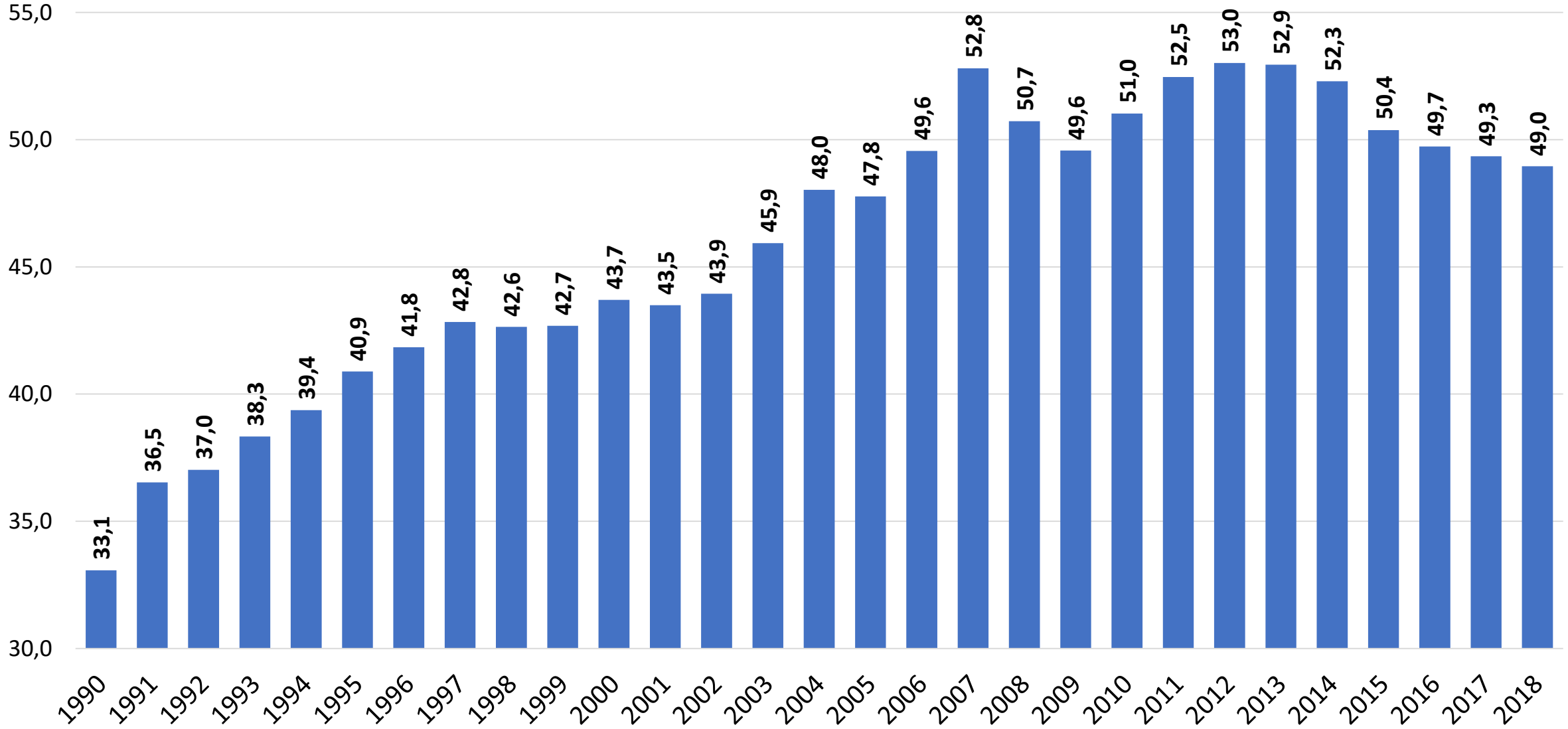
- Stabilizing speculation within the zloty's band in the mid-1990s
- Smoothing out the appreciation of the koruna in the early 2000s
- Successful defence of the forint's 15% band in 2003
- Keeping the koruna's ceiling of 2013-2017 with few interventions

2. What made stabilizing inflation in the 2000s easier than initially expected?

- Enhanced central banks' credibility due to successful disinflations of the 1990s
- CESEE countries' increasing export potential allowed them to use nominal appreciation as an inflation-stabilizing tool
- Global fall in inflation
- Participation in the European GVCs facilitated trade deficits reduction and exchange rates stabilization

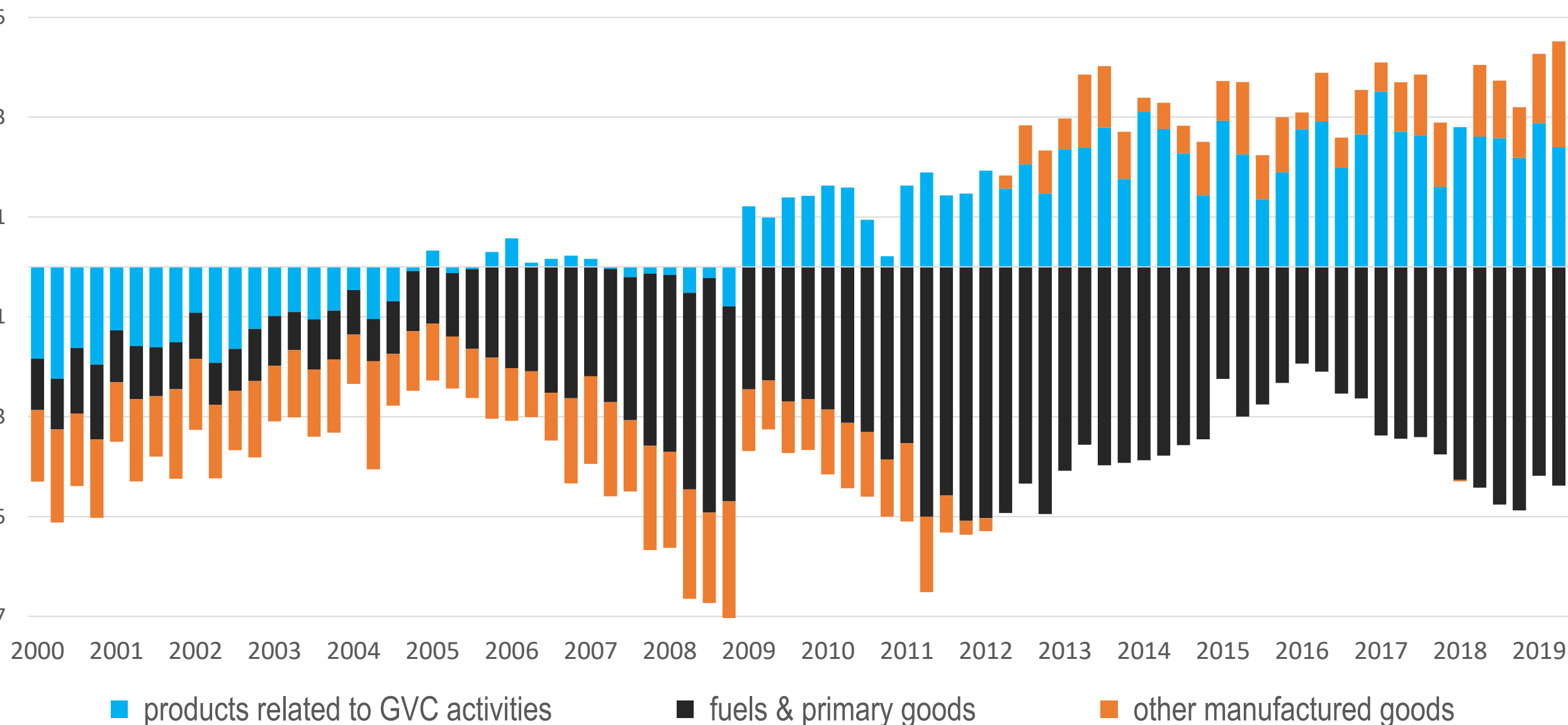
%

Global value chains (share in exports)



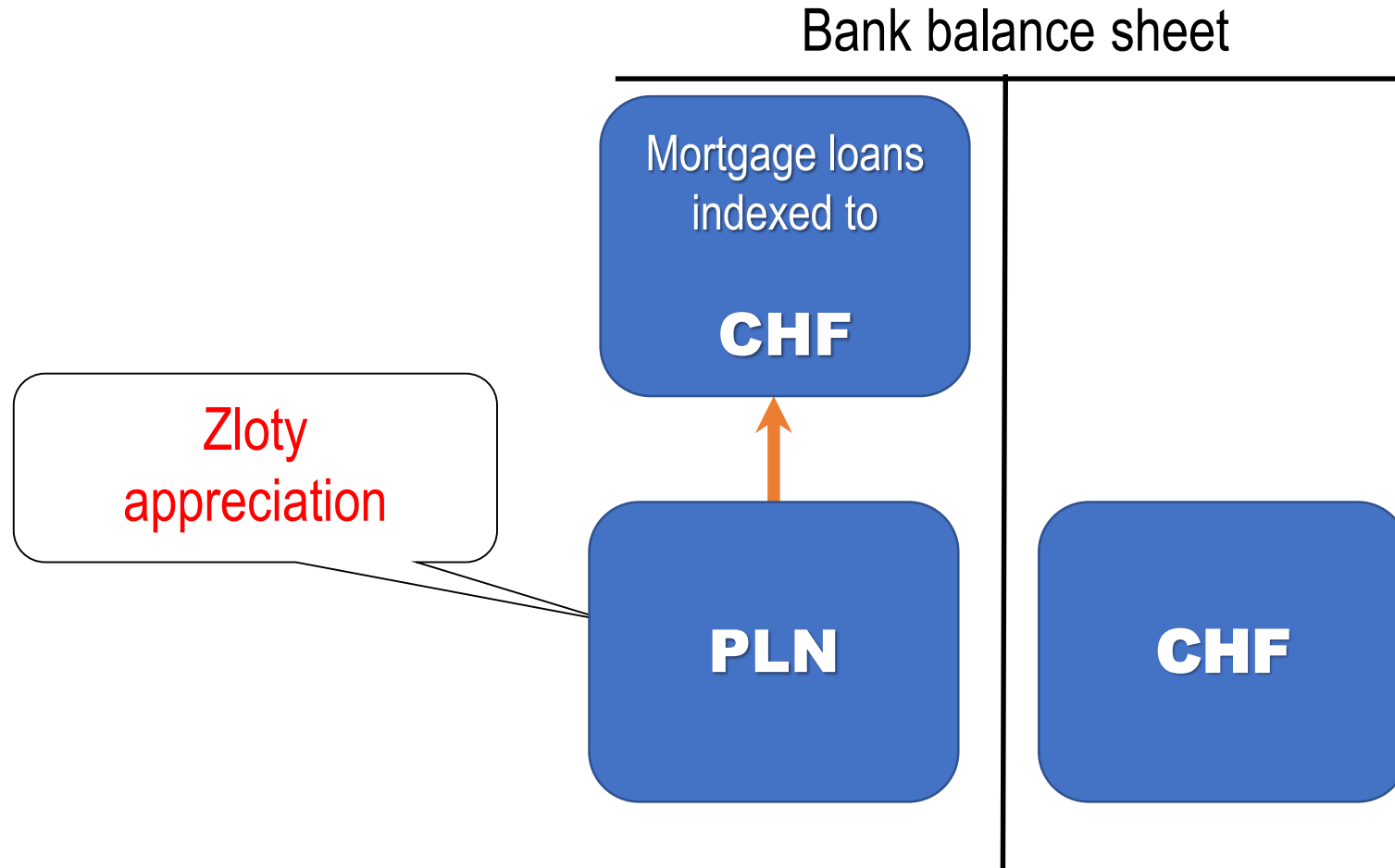
The GVC impact on Poland's trade balance

EUR bn



3. The 2007-2009 crisis: Why was there no exit strategy in Poland?

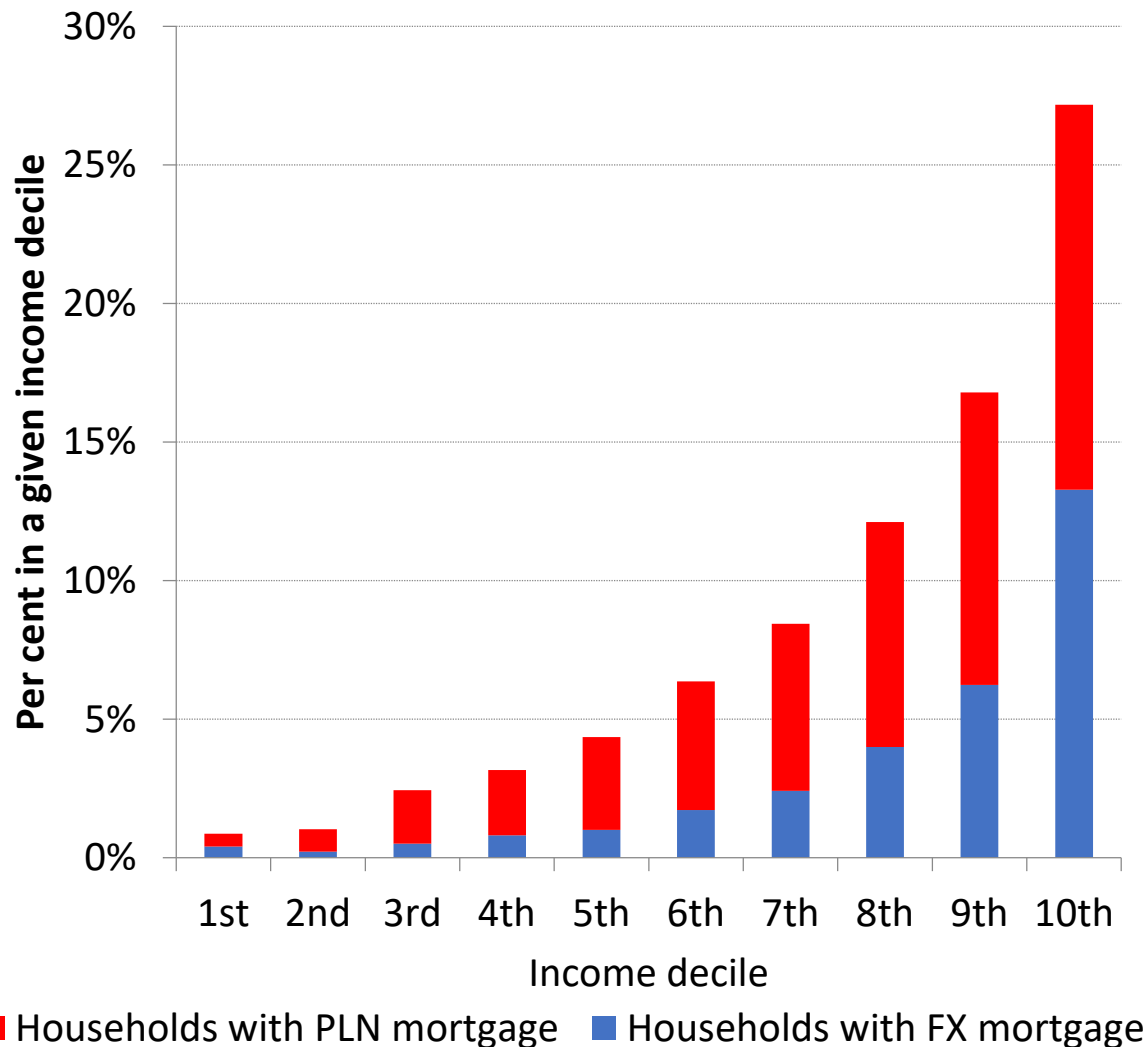
FX loans complicated monetary policy



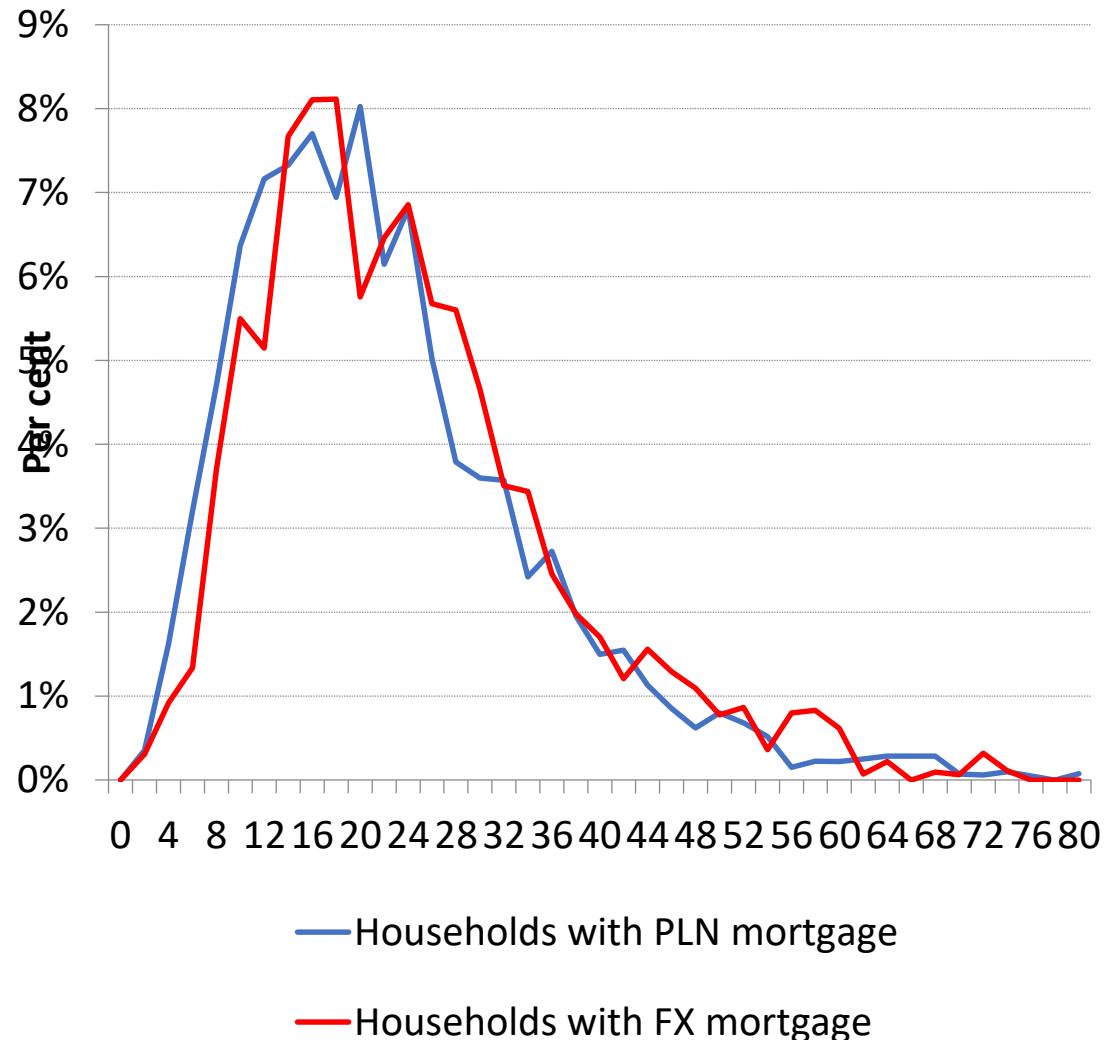
- Tightening LtV and DSTI ratios in 2006 directed FX loans mainly to more affluent borrowers
- The way in which the bad debts problem was solved in the early 1990s had long-term positive effects

FX loans were granted mostly to high-earners

Share of mortgage borrowers by income decile



Distribution of mortgage borrowers by DTI



Source: NBP calculations based on PHBS data

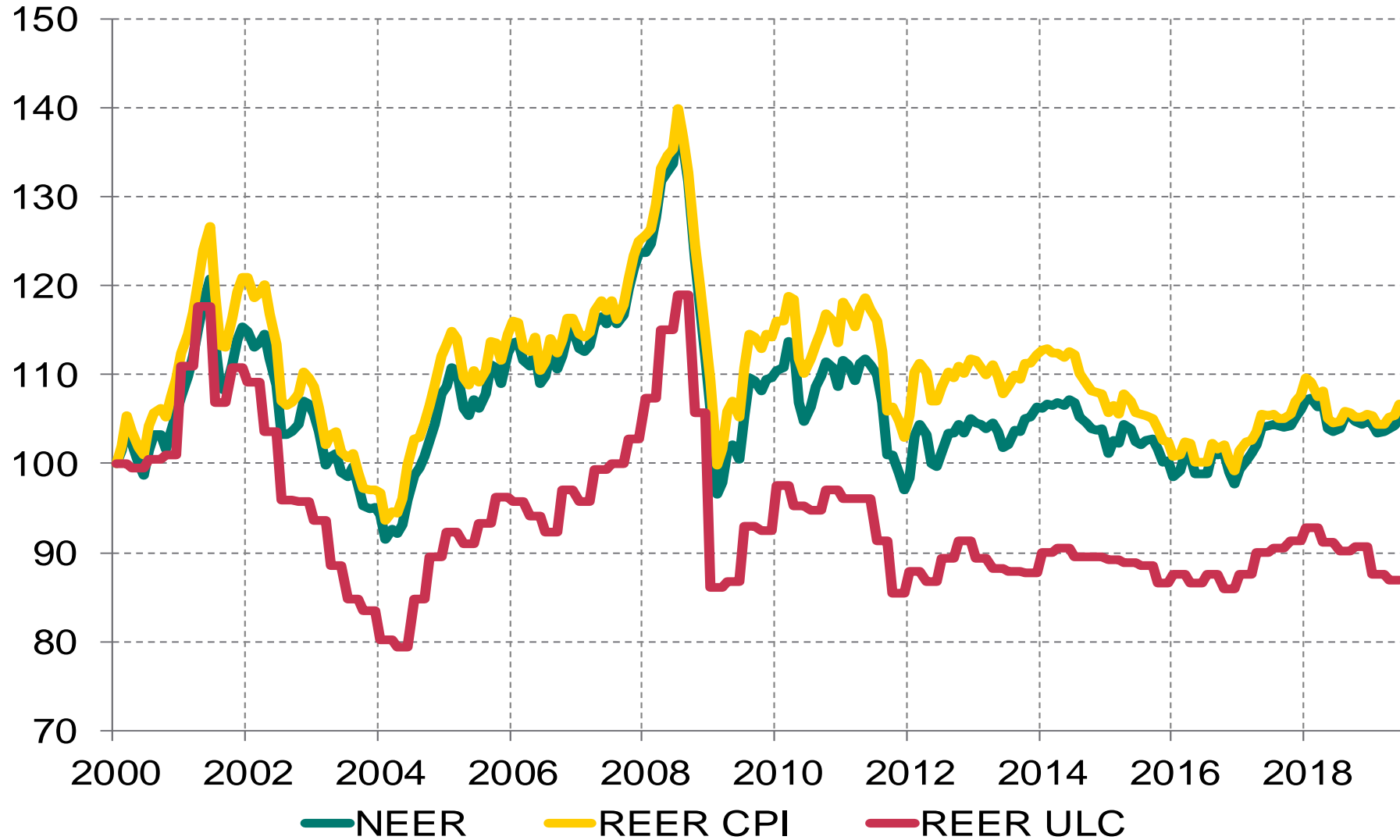
Source: NBP calculations based on PHBS data

4. The adoption of the euro

The 2007-2008 crisis made some new Member States cautious about the timing to join the Eurozone

- Floating of the zloty brought some positive results, such as reducing external imbalances and stabilizing the REER
- The small differences in economic developments in Slovakia and the Czech Republic reflect diminishing importance of exchange rate regimes

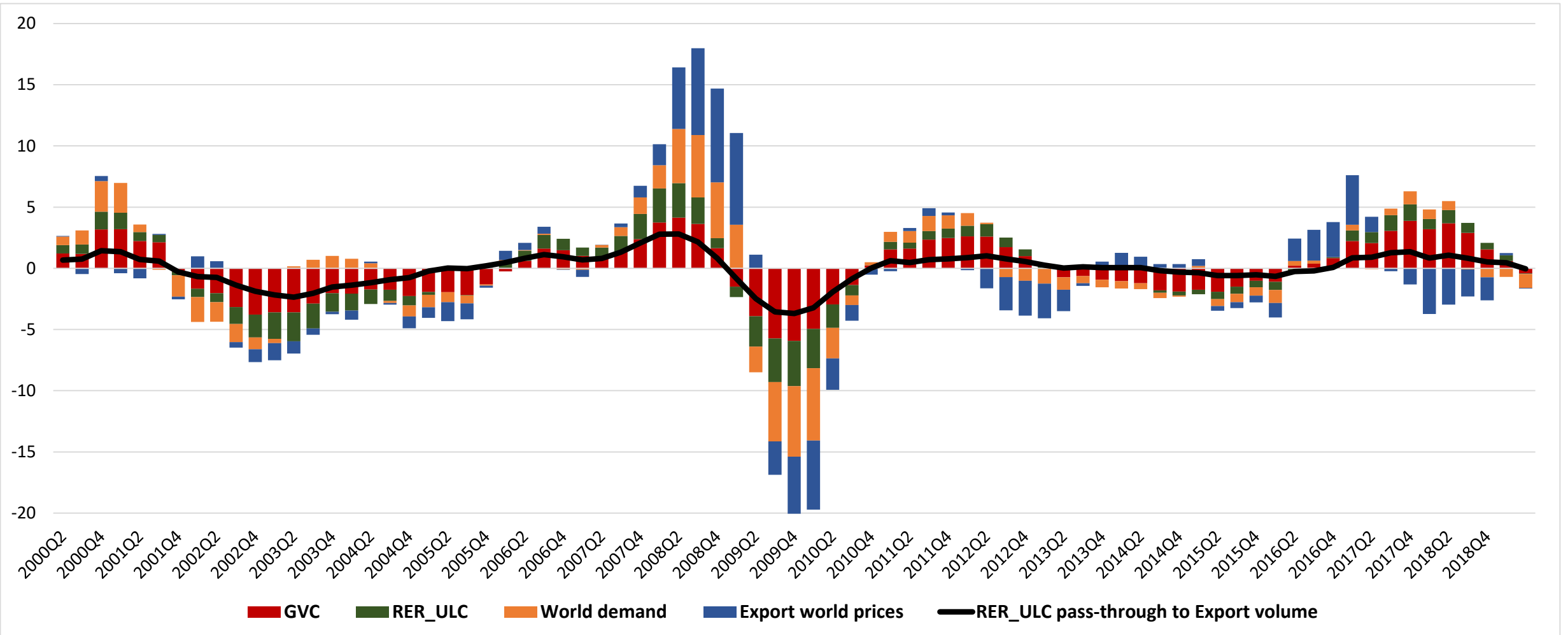
Nominal and real effective exchange rates of the zloty (index, 2000M01 = 100)



Source: BIS and OECD data

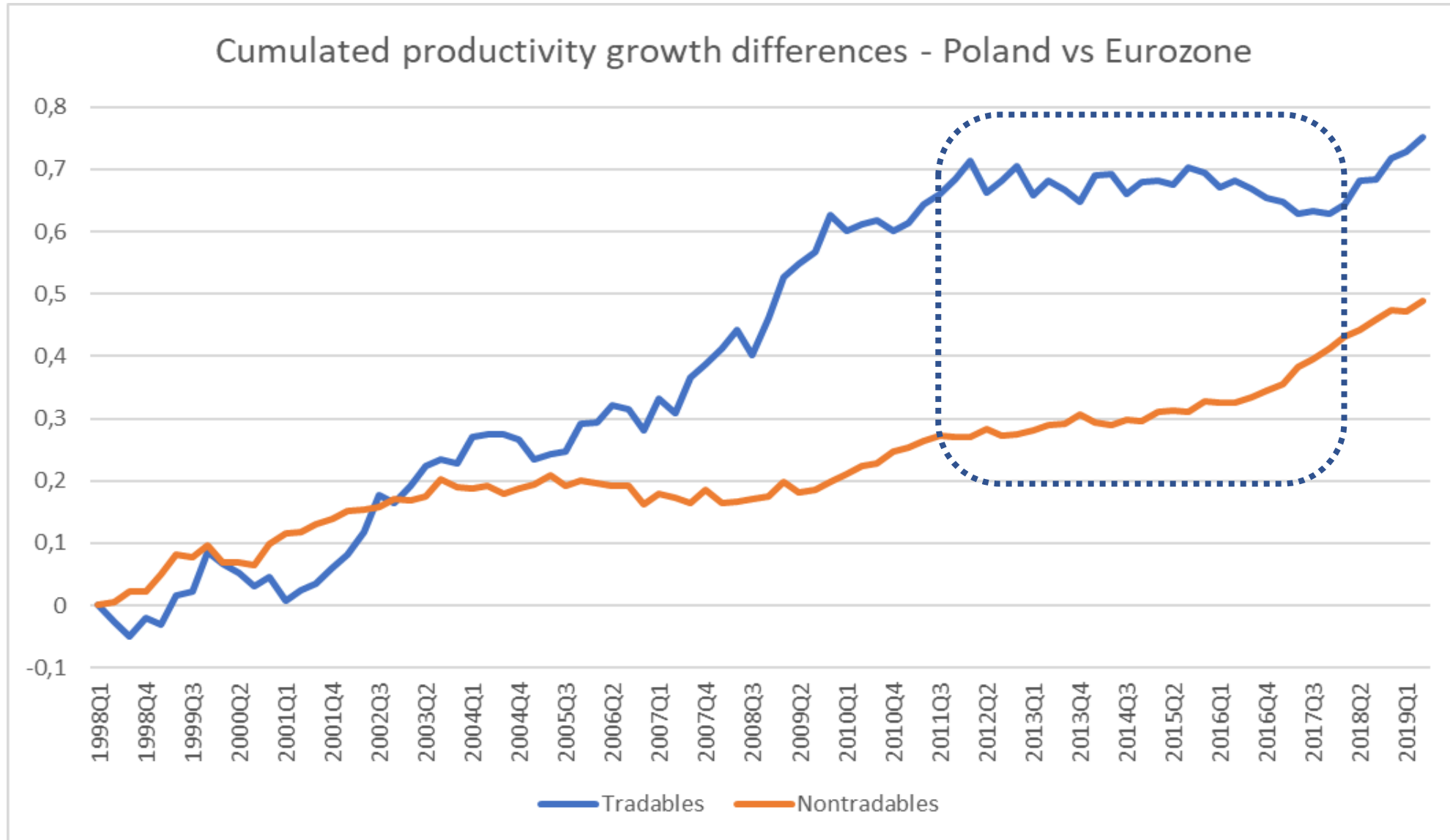
- The decreasing exchange rate pass-through
- and the diminishing BS effect
- reduce the value of the option to wait

The contribution of selected factors to export volume growth and RER_ULC pass-through to export volume



RER_ULC pass-through to export volume (ERPT) = IRF of export volume growth/impulse of nominal effective exchange rate deflated by relative unit labour costs
 ERPT has been close to zero during last ten years. However, it can considerably increase close to the extreme points of the business cycle

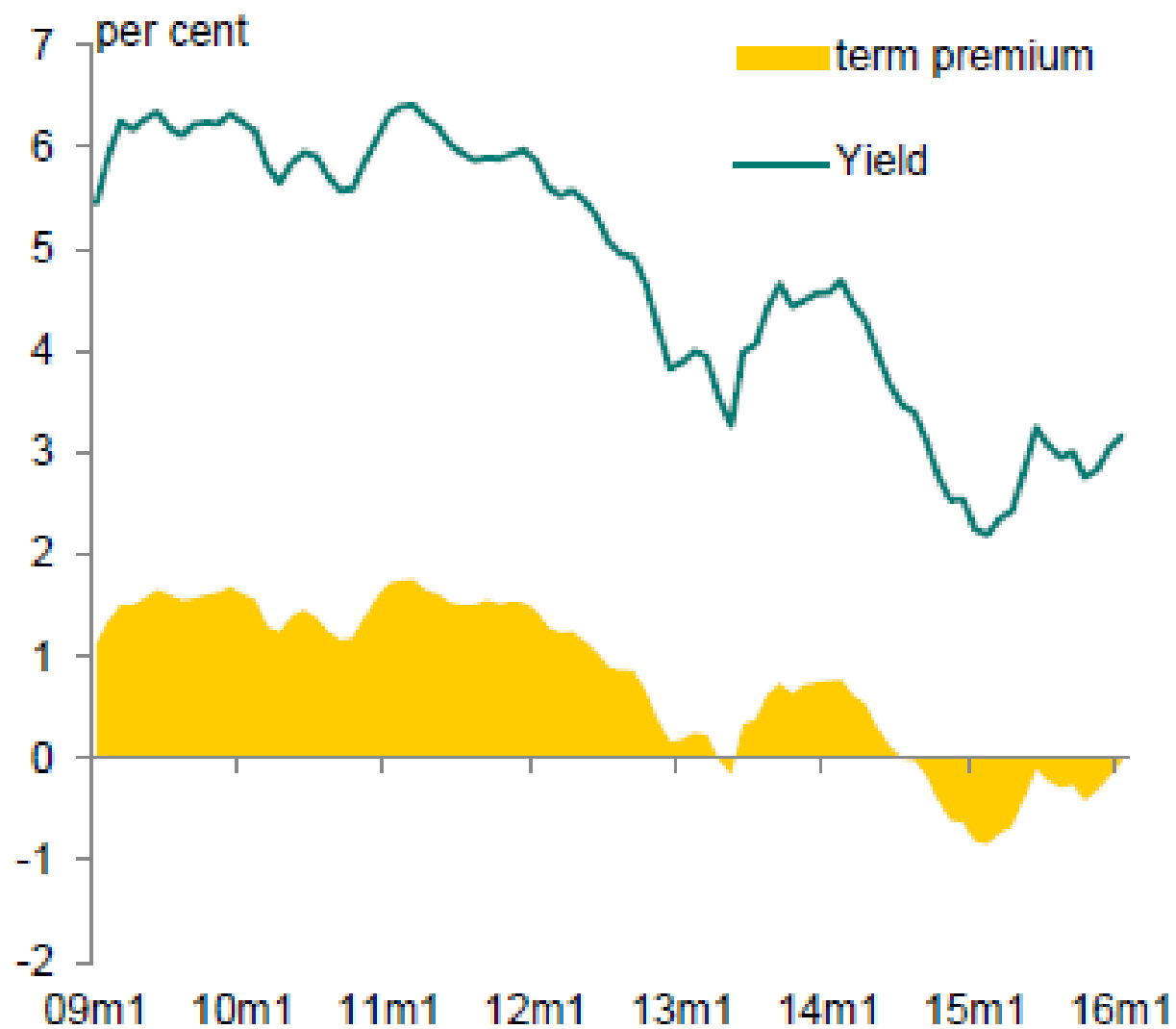
Shrinking BS effect



Source: Eurostat

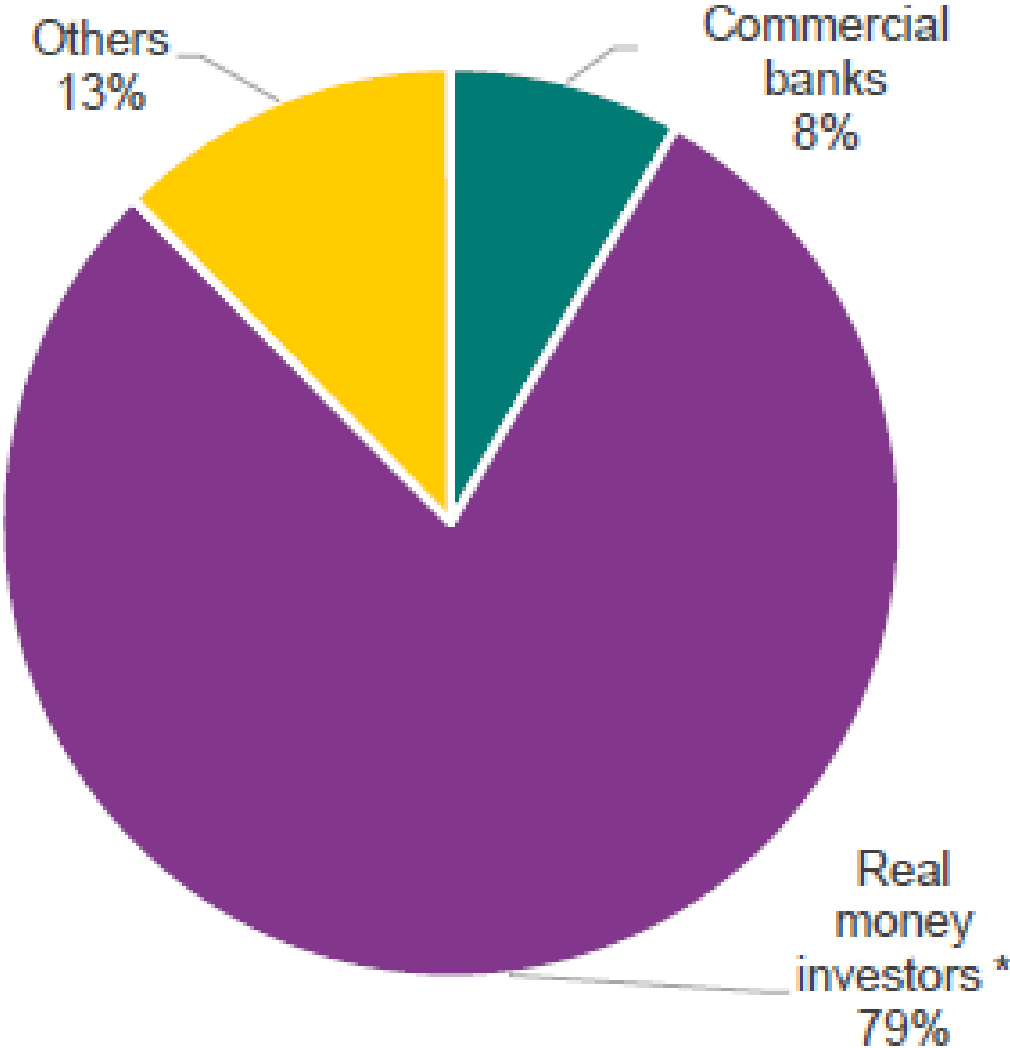
5. Symptoms of financial integration

10-year TBs yield decomposition



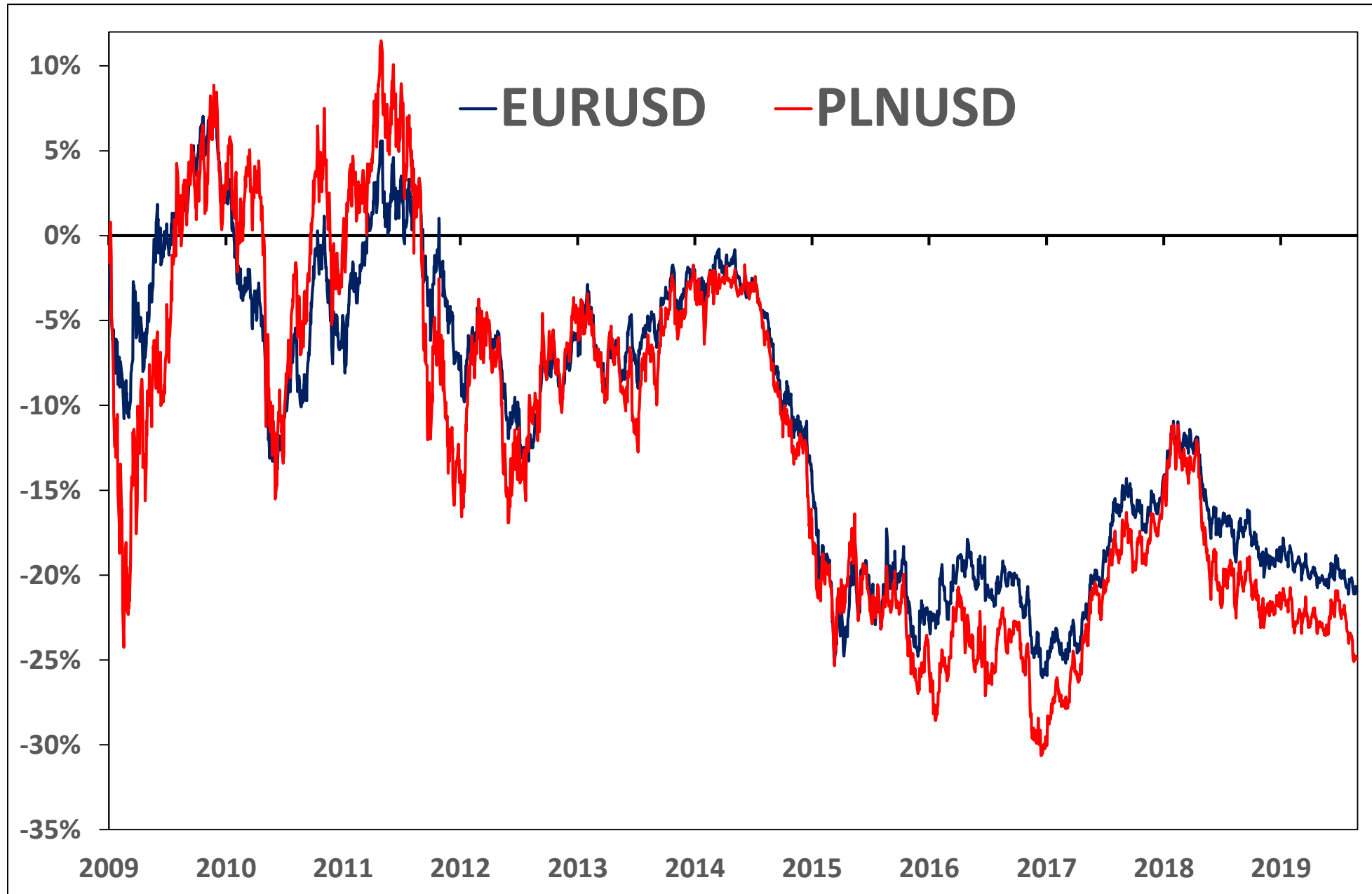
Source: Jabłecki, Raczko, Wesołowski (2016)

Public debt holders

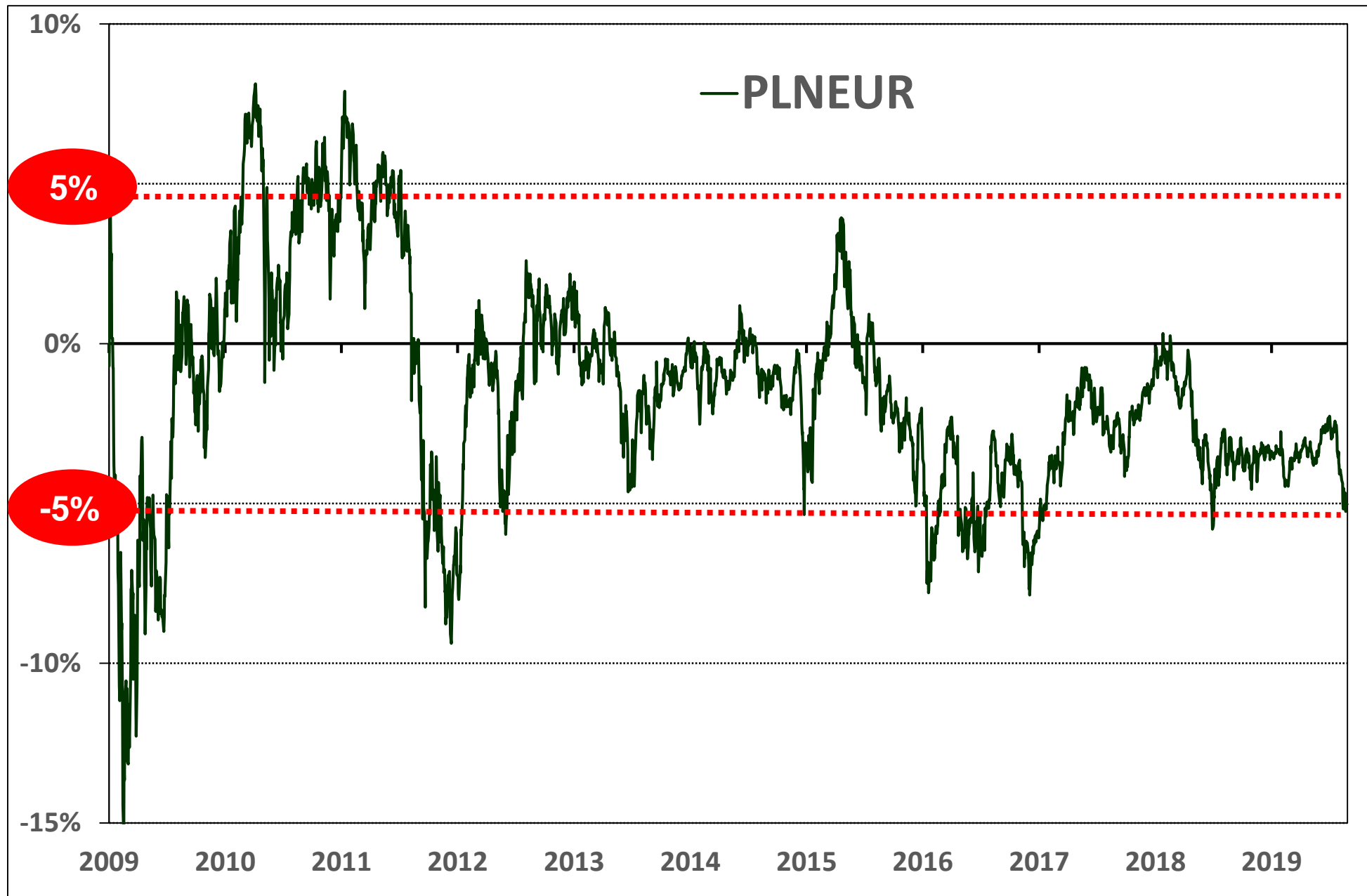


Source: Jabłeczki, Raczko, Wesołowski (2016)

5. What factors stabilize the EUR/PLN exchange rate?



Source: NBP



- Compressed interest rate differential (fewer opportunities for arbitrage)
- No substantial macroeconomic imbalances

6. General conclusions

- Economic reforms were introduced simultaneously with a return to democracy, which made them socially acceptable
- Joining the European GVCs accelerated economic convergence and facilitated rapid reduction of trade imbalances
- Economic and political transformation released the potential of CESEE's well-educated and egalitarian societies with long manufacturing traditions (e.g. Czech Republic)

7. New challenges: How to improve non-price competitiveness?

- How to make institutions more effective in promoting innovation?
- Inspirations can be drawn from a variety of sources: Israel, Taiwan, Ireland, and Nordic countries