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*Agata Szczukocka**

THE POLISH CAPITAL MARKET FACING INTEGRATION WITH THE EUROPEAN MARKET

1. Introduction

The process of adjusting the Polish economic system to the rules existing in the European Union started at the time of system transformation. Building of the capital market started from forming laws and establishing stock market and securities deposit. At that moment already the solutions used in the Union were taken into consideration.

The main purpose and at the same time great challenge for the Polish securities market is becoming a part of the European market structure on the basis of partnership so that the market may play important function in the Polish economy.

2. Capital market in Poland

Capital market has been separated as one of the segments of financial market. Capital market is the sum of all transactions of purchases and sales of financial instruments with redemption longer than a year (Jajuga 1998). The basic aims of capital market functioning are as follows: effective capital allocation among the companies emitting instruments of that market, the proper evaluation of the market instruments and gaining profit by investors. Dividing the capital market on the primary and secondary market, the following basic institutions of securities secondary market should be mentioned (Tarczyński 1997):

– Polish National Bank (Narodowy Bank Polski),

– Securities Commission (Komisja Papierów Wartościowych) and Warsaw Stock Exchange (Warszawska Giełda Papierów Wartościowych),

* PhD., Department of Statistical Methods, University of Łódź.

– National Deposit of Securities (Krajowy Depozyt Papierów Wartościowych),
– Stock Exchange,
– Unlisted securities market,
– Broking Houses (biura maklerskie),
– Investment banks,
– Pension funds/schemes,
– Insurance companies.

In the structure of the Polish securities market, similarly to the countries in which the market is well organized, the important role is played by Securities Commission.

The Polish capital market developed greatly within the first few years of its existence. Although it was being established from the very basis, it had no specified legal and institutional norms and it had little professional staff, over relatively short period of time it managed to develop into the market that meets the basic world standards. It is considered to be small but dynamically developing market based on the rules accepted in such model countries as the Unites States of America and the European Union countries.

While discussing the capital market in Poland, the problems it must deal with, cannot be ignored. One of the most important ones are legal and tax problems. Also the clearing system, high emission costs and high costs of participating in the capital market operations are also worth mentioning. Another problem is small development of the institutional and individual investors' sectors.

Strong competition of foreign secondary markets requires new structural and technical solutions on the Warsaw Stock Exchange. One of them is the possibility of establishing the common platform of stock exchange instead of the several ones already existing. What is more, the stock exchange privatization enables some foreign investors to enter it. Among the problems faced by the Polish capital market there is also small control of the owners and offence. This situation can be changed owing to the inner control organs (in banks and brokerage/broking houses), outer control organizations (KPWiG) and prosecuting and judicial institutions.

3. Polish and European regulations of capital market

Development of capital market in the world resulted in a situation in which the regulations concerning only securities and regulating them were not sufficient to protect investors. Trade in securities and other capital market instruments requires special regulations concerning market organisation, mediacy in trade transactions and simplification of taking investment decisions. In Poland such regulation is made through the act dated 21 August 1997 *The act on public trade in securities*, which became binding on 4 January 1998, replacing the act dated 21 March 1991.

In the European Union the regulation of capital market is guarded by the Committee of European Securities Regulatos – CESR. It was established in accordance with the decision of the European Commission (2001/1501/EC) dated 6 June 2001 as a result of accepting the so called Report of Wisemen Group by the Council led by Alexandre Lamfalussy. The Committee adopted all the output of the Forum of European Securities Commissions (FESCO) and it continues the works on all the projects started by the members of FESCO. Members of the Committee are institutions supervising capital markets of the countries of European Economic Area (non member countries of UE without vote capacity) and a representative of European Commission. The duties of CESR are as follows (Socha 2003):

– improvement of cooperation between the institutions supervising and regulating securities markets,

– acting as an advisory group of European Commission and preparing projects of securities regulations,

– activities aiming at constant and efficient putting new regulations into practice by the member countries.

In the years 1998–2000 Securities and Exchange Commission was a FESCO observer and at the moment it is a member of Consulant Group of the Institutions Supervising and Regulating Capital Markets of Candidate Countries for UE and it cooperates with CESR with reference to regulation works within UE.

In order to cooperate in setting common international standards in securities trade International Organization of Securities Commissions – IOSCO was founded in 1983. Currently it has 172 members composed of ordinary, affiliated and associated ones. In 1998 the Organization published the document entitled: The aims and principles of trade in securities.

The document includes 30 rules concerning the laws regulating trade in securities. The principles have three main purposes:

– investors protection,

– fair, efficient and transparent market functioning assurance,

– system risk reduction.

In order to achieve those aims, the 30 rules mentioned above must be put into practice according to the suitable laws. The rules can be grouped into eight categories:

A. Rules concerning regulation organ.

B. Rules concerning autoregulation.

C. Rules concerning execution of laws regulating securities trade.
D. Rules concerning cooperation in regulating.
E. Rules concerning emitents.
F. Rules concerning programmes of group investments.
G. Rules concerning market agents.
H. Rules concerning secondary market.

4. Strategy of capital market development

The government program focuses on the following strategy of capital market development:

I. European Union Integration

– To maintain the achieved harmonization of laws regulating the Polish capital market with the European Union instructions.

– To incorporate GPW and KDPW into European structures enabling them to become competitive in a region together with retaining investors and emitents matters.

– To form the ownership structure and the rules of GPW and KDPW acting that will promote development of national capital market and the demand of future competition on the common European Union market. It demands the Agenda Warsaw City 2010 project creating which aims at changing Warsaw into regional finance-capital centre such as London City, Frankfurt Finanzplatz or Paris Europlace. The project also aims at privatization of Warsaw Stock Exchange and the increase in the capitalization from the present 21% to almost 50% GDP within the next six years.

II. The use of open pension funds potential

– Privatization of the important companies of the Exchequer through the public capital market over the next few years. Privatization offers for pension funds.

– Development of the market of indebted securities, including the market of letters of deposit, treasury bonds, municipal and corporation bonds.

– Development of the electronic platform of treasury bonds turnover in accordance with the standards of the public capital market – System of Securities Dealers.

III. Development of public capital market as the source of capital retaining

– Development of mechanisms that promote financing infrastructural programs by pension funds, including the use of infrastructural funds of European Union.

– Preparing neutral and stable tax solutions. In case of taking eventual decision to impose taxes on the income earned on the public capital market, special tax rules should be prepared and announced at least 1,5 year in advance, so that investors have time to adjust.

– Increase in the efficiency of cooperation between Civil Service units and prosecuting units in tracking and punishing offence connected with public trade in securities.

– Increase in the clarity of financing units of self-governments.

Increase in the use of public capital in getting financial means for investment of the self-government units.

Taking some special system means i order to make the Polish capital market more competitive sustaining the proper level of safety in trade.

5. Advantages and dangers for the Polish capital market

The agreement on the unconstrained capital flow between Poland and EU (according to the art. 73 b of Maastricht Treaty) and putting into practice other liberties means that Poland will join united inner market of EU. All the benefits that can be expected have the following roots (Socha J. 2003):

– savings resulting from the end of trade barriers within European Union,

– savings resulting from the full liberalization of financial market,

– intensification of inner competition

– increase in the production range

– eliminating the restrictions connected with the access to public orders market

The possible effects in the Polish economy due to the introduction of unconstrained capital flow are as follows:

– increased inflow of capital (in various forms), contributing to the increase in its supply on the national market, will press for lowering interest rate, so it may happen that the value of capital will be lowered;

– the lowered value of capital will make it more accessible for investors, that means possibility to stimulate investment in the country and some other processes of growth;

– the lowered value of capital will result the increase in the accessibility for investors, which means the possibility of the investments stimulation and additional growth processes starting;

– the lowered value of capital results in fewer advantages for those who make some savings and more advantages for investors: net benefits of Poland as far as prosperity is concerned will be connected with the difference between the benefits of investors and losses of those who make savings;

– the rate of profit division among the main social groups in the country (profits of work factor versus income from capital) may become different; in Poland, the country receiving capital, an increase in benefits from work can be expected and at the same time a decrease in profit gained by capital owners; such a situation is highly welcomed by trade unions; that effect will only appear if markets will function properly;

– it is possible that the balance of payments may become worse for some time due to the liberalization of capital-financial market, depending on the structure of capital arriving to Poland; in case of large inflow of short-tem capital and appearance of some factors that have an adverse effect on the financial stability, the outflow of capital may appear that may have bad influence on monetary policy; at the same time the inflow of long-term investment in Polish economy (for instance direct foreign investment and reinvestment of the profits resulting from it) may subdue the above mentioned difficulties in balance of payments;

– integration of the market of production factors (including capital) can simplify restructurization and the process of liberalization of trade in customs union; liberalization of capital flow may activate dynamic effects of customs union;

– the integration of production factors market (including capital) can facilitate restructuring, which accompany the trade liberalization processes in the customs union; that is why the liberalization of capital flows can quicken the realization of the dynamic effect of the customs union;

– also the effect of forming and moving the capital stream may be observed that opposed forming and moving of capital stream in customs union between Poland and EU;

– also dynamic effects may take place through strengthening of competition between financial organizations in Poland, it will increase scale benefits and service quality; banking sector, protected in the past, will be negatively influenced but everybody involved in financial market will take advantage of it;

– also the effect of area concentration is possible to appear, that means in case of difference in the level of development of financial markets, that is present between Poland and EU member countries and in case of easy founding a company, transfer of the surplus of demand and supply to financial centres is possible, as well as the situation in which moneylender and borrower will move there all their activity; such an effect would be highly undesirable for Poland.

It is also worth emphasising that the wrong sequence of general liberalization processes between integrating sides can lead to great losses. Introduction of full capital mobility between Poland and EU, without removing tariff obstacles in trade, will result in loss for producers and reduction of profits for the government. Therefore, before forming customs union, common capital market should be first established. Since removing tariff obstacles in trade in industry articles is highly advanced, the above mentioned problem refers to tariff obstacles referring to agricultural articles.

EU members' experiences shows that the accession is a very important impulse for the economy development, including the capital market. Some numerical data prove that Poland also has such chances.

The value of companies quoted in the Warsaw Stock Exchange (29,3 billion Euro in the end of the year 2003) is almost the same as the sum of the capitalization of succeeding three Central European Stock Exchanges in respect of the volume: Hungarian Stock Exchange (13,2 billion Euro of capitalization), Czech Stock Exchange (12,3 billion Euro) and Slovenian Stock Exchange (5,6 billion Euro). This Stock Exchange is also a leader taking into account the turnover volume in the shares market, which amounted to 8,8 billion Euro. The increase in the main stock exchange index (WIG 20), which amounted to almost 34% proved that the polish market can be more attractive for investors than other European markets.

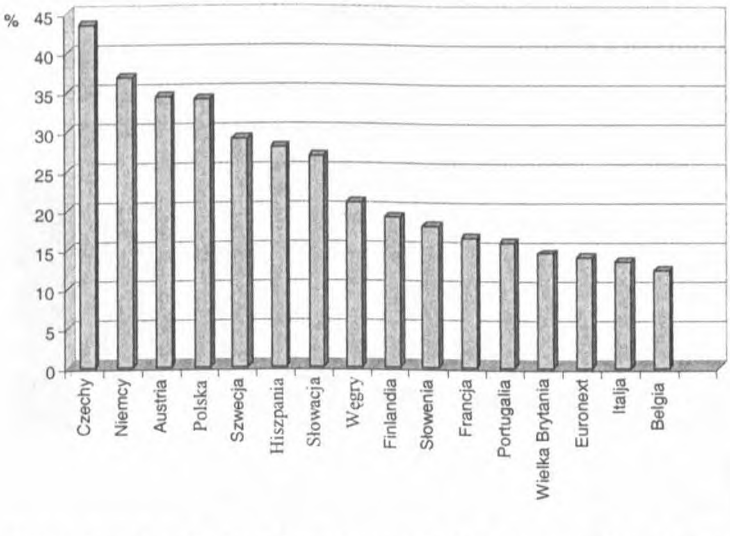

Fig. 1. The change of stock exchange indexes of some of the European stock exchanges in the year 2003

S o u r c e: *Annual Report of the Warsaw Stock Exchange.*

The levels of shares and forward contracts turnovers of the last year as well as the exchange capitalization of the national companies testifies to the international status of the Warsaw Stock Exchange.

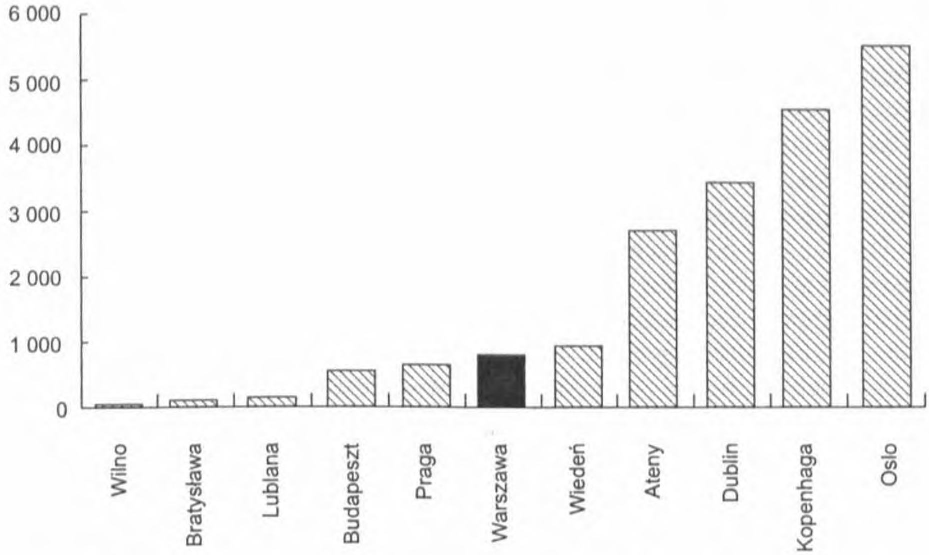

Fig. 2. Shares turnovers – monthly averages in the year 2003 (billion Euro) – individually calculated

S o u r c e: As same as Fig. 1.

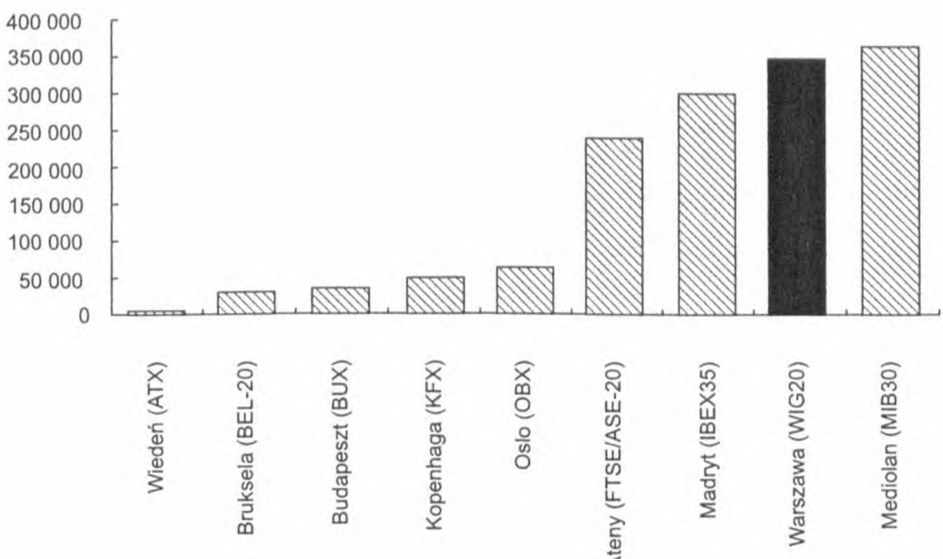

Fig. 3. Volume of the forward contracts turnover on the main indexes – monthly average in the year 2003

S o u r c e: As same as Fig. 1.

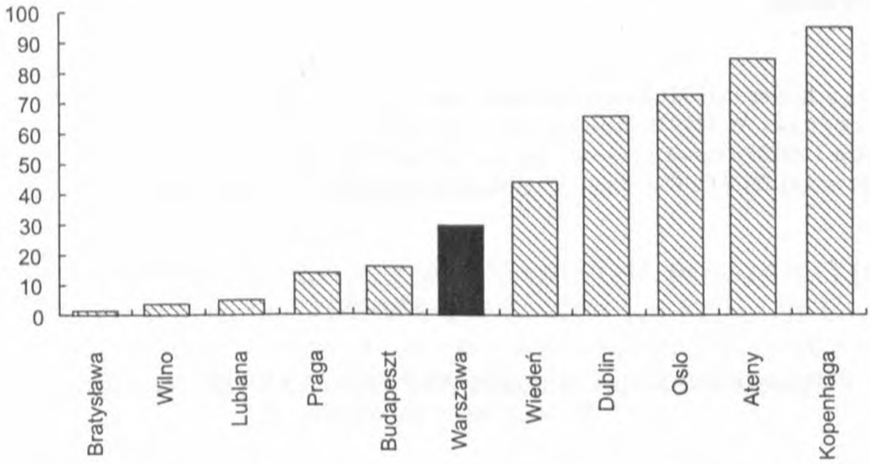

Fig. 4. Exchange capitalization of the national companies – December 2003 (billion Euro)
S o u r c e: As same as Fig. 1.

There are various advantages of the membership agreement. One should expect that our European region companies' interest in the Warsaw Stock Exchange securities quotation will increase. The above data also suggest that the risk of the transfer of the national companies quotation to the foreign floors will decrease. On the other hand, the securities transactions of European countries can become the new source of the stock exchange members' income.

6. Conclusion

Nowadays capital market is an important part of every free market economy. It enables companies to obtain, relocate and invest capitals in such a way that they bring profit.

As results from the above mentioned facts and conclusions, the Polish capital market although it is well-prepared for the integration with the European Union, has still many problems to solve if it wants to become similar to those existing in the countries of well-developed economies. It is worth mentioning that the Polish financial market is considered to be solid, transparent and reliable, it means that legal rules referring to that field of economy conform to the world standards. However, lack of efficiency, liquidity and innovations results in such a situation that many companies decide to invest its savings in banks, giving similar return on investment and smaller investment risk. It seem that the solution to that problem and many other can be integration process.

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Agata Szczukocka

POLSKI RYNEK KAPITAŁOWY W PERSPEKTYWIE INTEGRACJI Z RYNKIEM EUROPEJSKIM

W artykule starano się szczególną uwagę zwrócić na szanse i korzyści, jakie mogą zaistnieć dla polskiego rynku kapitałowego w wyniku integracji z rynkiem europejskim. Skoncentrowano się także na strukturze rynku kapitałowego w Polsce i regulacjach prawnych. Przybliżony został także program rządu dotyczący strategii rozwoju rynku kapitałowego w Polsce.