

Changes at the Polish Ministry of the State Treasury[©]

Starting this month, the Polish Ministry of the State Treasury (“MST”) has a new Minister. This is Mrs. Aldona Kamela-Sowińska. She was in the ministry before at a senior level, so she is not new to the Ministry and its activities. She should be, in our view, classified as a professional appointee, not a political appointee. She is an economist by training.

The timing for her could not be worse. She has at most six or seven months on the job, according to conventional wisdom, after which a new government (there are parliamentary elections in the Fall) will replace her with another political appointee. But that’s not all.

The Polish privatization program is facing some very serious problems. The new budget counts on 18 billion (thousand million) Polish złotys (about \$4.5 billion) in privatization proceeds this year. By the day hopes of achieving such revenues are dimming.

A major component of this program is continuing and aggressive privatization in the energy sector. The single largest component being counted on was a second tranche sale of Polish telecom TPSA to France Telecom. But, the price of TPSA’s shares have dropped so far in trading on the Warsaw Stock Exchange that the France Telecom option price is no longer attractive, or even viable. France Telecom has declined to exercise its option to buy another 10% of the shares of TPSA.

Privatizations in the energy sector seem to move at one of two speeds: slow or stopped. Disagreements within the government, reflecting divided public acceptance of the process and strong opposition from within the sector, have brought the process to a near standstill - again. The new Minister of MST has indicated that privatization of CHPs will get the priority. The on again, off again, privatization of the giant Bełchatów lignite, mine-mouth complex seems to be moving back to an “off again” mode.

A number of factors are at work here, both internal and external to Poland. First, the internal.

There has always been opposition to the privatization of the energy sector in Poland from both within the sector itself and amongst the public at large. When it comes to basic social services, the public (in any country) is highly risk averse. Since there is considerable overcapacity in the industry, and since the government still maintains electricity prices to consumers at below cost levels, the consumer sees no benefit from privatization. Electricity supplies are abundant and cheap.

Privatization of the power generation and distribution sectors is seen by the coal miners as a threat to their jobs, so there has been opposition from the coal sector. Partly this is due to the existence of a tangled web of unpaid electricity bills owed to state-owned companies by state-owned companies. As long as there is no privatization, there is little or no pressure to sort this out. The coal mines, steel mills, and railroad are big debtors to the power industry.

The management and unions of individual enterprises have a common fear of privatization; that they will lose their jobs. Hence, they oppose it in general. Some managers are more progressive than others, but in general opposition to privatization goes right to the top, protestations to the contrary notwithstanding.

Factors external to Poland are having a depressing effect on the privatization of the energy sector in Poland.

For some time now, the number of interested suitors for power generation and distribution assets has been thinning out. Some of this is due to consolidation in the industry. Some of this has been due to the perception by many foreign firms, especially US-based firms, that the opportunities were better elsewhere. Some of this was due to the hot stock markets (the “dot com” phenomenon), which meant that capital got better returns elsewhere.

More recently, the dominance of a few state-owned and “national champions” in the energy bidding has scared off many shareholder owned companies from places like the U.S. and the U.K. Companies that don’t have to compete for their own capital in the capital markets but get it from “non-discretionary providers” (tax-payers and captive monopoly customers) can afford to bid more for “strategic reasons” than can shareholder owned companies.

Also, in recent months, the hot stock markets in Europe and the U.S. have turned sour, changing the whole dynamic of risk taking even more to Poland’s disadvantage. Whereas in the past investors didn’t find Poland attractive because they could get higher rates of return by staying “at home,” now investors are becoming highly risk averse and avoiding foreign adventures. This is even starting to happen to the foreign state-owned companies as their governments are getting more and more worried about their own budgets.

On top of this, foreign investors who need returns on their investments have been concerned for some time as to the risk profile of the Polish power sector as it is being restructured while being privatized. The lack of clarity about returns on equity capital in a regulated Polish electricity market has been a strong deterrent for some sector investors.

The California crisis is having an effect on Poland. There has been considerable debate in Poland as to whether or not Poland could find itself in the same predicament as California. Poland was following a deregulation and restructuring path somewhat emulating California. The problems there have caused some in Poland to suggest slowing down. The recent pronouncement by the new Bush administration that the problems in California could tip the U.S. recovery from soft landing to hard landing was not encouraging for the Poles. They cannot withstand a hard landing.

What do we see ahead?

The privatizations already underway will be completed. The pressures on the government to get money in the door are too high for any other outcome, although they may slow a little.

The upcoming sensitive privatizations, like Bełchatów, may be delayed for some time considering the divided opinions in the government and the upcoming elections in the Fall.

Some more CHP auctions may occur this year beyond those already announced. But, we doubt the government will announce any more distribution company or system power plant sales before the elections.

We look for actions on the part of the government to become less and less decisive as the elections approach. Not good news for privatizations, nor for the new Minister. We believe that she deserves a better break. Her recent presentation to members of the American Chamber of Commerce in Poland left everyone positively impressed. Given more time, and a more rationale climate than a pre-election one, we believe she could accomplish a great deal for Poland and for the sector.