

Poland: The journey to Developed Market status

FTSE Russell announced the promotion of Poland to Developed market status as part of the September 2017 FTSE Country Classification annual review of markets. This significant achievement is the first promotion of a country from Advanced Emerging to Developed market status to occur within the Country Classification scheme for nearly a decade. The transition will take place in conjunction with the FTSE Global Equity Index Series (GEIS) semi-annual review in September 2018.

In this FTSE Russell paper we highlight the FTSE Country Classification scheme and outline the rigorous process followed by FTSE Russell, supported by the Country Classification Advisory Committee, and explain its importance for FTSE GEIS, the widely-followed benchmark index series used to measure the performance of global equity markets. We highlight the market infrastructure improvements and economic advances introduced by Poland to achieve Developed status and note some of the clear signs of a deepening and strengthening of the country's capital market.

Key points

- Following the recommendations of the FTSE Country Classification Advisory Committee and with the full support of the Regional Equity Advisory Committees and the Policy Advisory Board, Poland will be reclassified from Advanced Emerging to Developed market status with effect from the FTSE GEIS semi-annual review in September 2018.
- Reclassification as a Developed market is the fruit of continuous improvements in Poland's capital markets infrastructure, supported by the country's steady economic progress.
- Poland has the eighth largest economy in the European Union and the largest among the central European members.
- As of September 2018, Poland will leave the FTSE Emerging All Cap Index (where its weight, as of March 2018, was 1.33%) and join the FTSE Developed All Cap Index, where its index weight is projected to be 0.154%.

The FTSE Country Classification System

The FTSE Country Classification system¹ was introduced in 2004 as a structured, objective and transparent framework for determining equity markets' development status. The introduction of the new classification system followed a market-wide consultation with FTSE clients, conducted in 2003.

In early versions of the global equity indexes which were available at the time, distinctions between developed and emerging markets tended to be somewhat arbitrary. Such distinctions often depended on the relative wealth of countries, with subjective judgments about the market infrastructure sometimes playing a role.

This relative lack of rigor in the way markets were classified made it hard for investors to gauge the likelihood of countries moving between categories. By contrast, the more transparent and objective Country Classification process followed by FTSE since 2004 helps foster a spirit of engagement that encourages countries to adopt global best practices in pursuit of promotion.

The guiding principles for market classification by FTSE Russell are as follows:

- Quality of Market – the quality of regulation, the dealing landscape, custody and settlement procedures, and the presence of a derivatives market are all taken into account;
- Materiality – a country needs to be of material size to warrant inclusion in a global benchmark;
- Consistency and Predictability – a pathway to classification changes is set out by announcing a “Watch List” of countries that are being considered for promotion and demotion as well as the criteria by which countries are judged;
- Cost Limitation – the cost of implementing a change is taken into account when assessing a market for promotion or demotion;
- Stability – a phased approach is taken to the introduction of new countries, meaning that a new country would only join as an emerging market and promotion would only occur in response to permanent changes in market status and global acceptance; and
- Market Access – international investors should be able to invest and withdraw funds in a timely and secure manner at reasonable cost.

Each year, FTSE Russell releases two Country Classification announcements: an interim announcement at the end of March and an annual announcement at the end of September. Absent any extraordinary circumstances, a minimum notice period of one year is provided before reclassifications are implemented, allowing investors and market participants ample time to prepare.

Countries being considered for reclassification are placed on the Watch List, which provides the wider investment community with an opportunity to provide input both to FTSE Russell as well as to the market and regulatory authorities in the countries concerned.

The Country Classification process is underpinned by the FTSE Russell Country Classification Advisory Committee, a global group of independent market practitioners with technical expertise in trading, portfolio management and custody. The members of this committee are able to provide first-hand experience of the markets concerned and corroborate the reports provided by the local market authorities. Extensive engagement takes place with a variety of stakeholders in those markets being considered for reclassification by FTSE Russell, a process supported by the Country Classification Advisory Committee. Final recommendations on the Watch List markets are shared with the Regional Equity Advisory Committees and the Policy Advisory Board which is comprised of FTSE Russell's most senior clients.

¹ See <http://www.ftse.com/products/indices/country-classification>.

Requirements for development categories

An individual equity market's classification within FTSE GEIS as either Developed, Advanced Emerging, Secondary Emerging or Frontier is determined by the Quality of Markets (QoM) criteria, which cover 21 areas against which a market is assessed. The criteria cover four themes: Market and Regulatory Environment, Custody and Settlement, Dealing Landscape, and Derivatives.

- Countries must meet a set number of Quality of Markets criteria to achieve a particular development status;
- The economic status and relative economic wealth of a country, as measured by its gross national income (GNI) per capita rating, are taken into account;
- A minimum of three eligible securities meeting entry requirements is required to create an individual country index (index-eligible securities are those which meet predefined thresholds for minimum voting rights, investability and liquidity²).

The relevant economic status requirements and minimum Quality of Markets criteria for each development category are shown in the table. For example, for a country to reach Developed market status, it must meet the 21 Quality of Markets criteria and show high relative national income levels.

Economic status and Quality of Markets criteria by development status

Category	Definitions of economic status	Quality of Markets Criteria	Market size entry requirements
Developed	High Income GNI countries with developed market infrastructures (QoM)	Passes 21 of 21 QoM Criteria	Minimum 3 eligible companies required to create a country level index
Advanced Emerging	Upper Middle Income GNI countries with advanced market infrastructures and High Income GNI countries with lesser developed market infrastructures	Passes 15 of 21 QoM Criteria	Minimum 3 eligible companies required to create a country level index
Secondary Emerging	Lower Middle Income GNI countries with reasonable market infrastructures and Upper Middle Income GNI countries with lesser developed market infrastructures and significant size	Passes 9 of 21 QoM Criteria	Minimum 3 eligible companies required to create a country level index
Frontier	Restricted emerging markets	Passes 5 of 21 QoM Criteria	None

Source: FTSE Russell, data as of March 2018.

² See the FTSE GEIS Ground Rules, Section 6, as at March 2018, available at http://www.ftse.com/products/downloads/FTSE_Global_Equity_Index_Series.pdf

As of March 2018, the FTSE Country Classification framework covered 24 Developed, 11 Advanced Emerging, 12 Secondary Emerging and 29 Frontier markets.

FTSE Country Classifications as of March 2018

Developed	Advanced Emerging	Secondary Emerging	Frontier
Australia	Brazil	Chile	Argentina
Austria	Czech Republic	China	Bahrain
Belgium / Luxembourg	Greece	Colombia	Bangladesh
Canada	Hungary	Egypt	Botswana
Denmark	Malaysia	India	Bulgaria
Finland	Mexico	Indonesia	Cote d'Ivoire
France	* Poland (Developed from September 2018)	Qatar	Croatia
Germany	South Africa	Pakistan	Cyprus
Hong Kong	Taiwan	Peru	Estonia
Ireland	Thailand	Philippines	Ghana
Israel	Turkey	Russia	Jordan
Italy		UAE	Kazakhstan
Japan			Kenya
Netherlands		* Kuwait (Sec Emerging from Sept 2018)	Latvia
New Zealand			Lithuania
Norway			Macedonia
Portugal			Malta
South Korea			Mauritius
Spain			Morocco
Sweden			Nigeria
Switzerland			Oman
UK			Palestine
USA			Qatar
			Romania
			Serbia
			Slovakia
			Slovenia
			Sri Lanka
			Tunisia
			Vietnam

* Poland to be promoted to Developed market status, effective from September 2018.

** Kuwait to be promoted to Secondary Emerging market status, commencing from September 2018.

*** Saudi Arabia to be promoted to Secondary Emerging market status, commencing from March 2019.

Poland improvements shown through the Quality of Markets matrix

The evolution of Poland's equity market between 2004 to 2017 from the international investor's viewpoint is set out in the table below. In particular:

- Previous restrictions on the availability of omnibus and segregated custodial account facilities are considered as having been addressed
- Its foreign exchange market, which was considered insufficiently free and well-developed in 2004, has met the criteria for a pass assessment since 2011
- Since 2011, the country has been considered as having a developed derivatives market and its stock lending market was considered unrestricted from 2015
- Poland moved from an upper middle to a high GNI per capita rating from 2015 onwards, showing the results of the country's consistent economic growth rates

Poland – FTSE Quality of Markets 2004 - 2017

FTSE QUALITY OF MARKETS CRITERIA - POLAND									
CRITERIA	Developed	Advanced Emerging	Secondary Emerging	Frontier	2004	2011	2013	2015	2017
World Bank GNI Per Capita Rating					Upper Middle	Upper Middle	Upper Middle	High	High
Market and Regulatory Environment									
Formal stock market regulatory authorities actively monitor market (e.g., SEC, FSA, SFC)	X	X	X	X	Pass	Pass	Pass	Pass	Pass
Fair and non-prejudicial treatment of minority shareholders	X	X			Pass	Pass	Pass	Pass	Pass
No or selective incidence of foreign ownership restrictions	X	X			Pass	Pass	Pass	Pass	Pass
No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	X	X	X	X	Pass	Pass	Pass	Pass	Pass
Free and well-developed equity market	X	X			Pass	Pass	Pass	Pass	Pass
Free and well-developed foreign exchange market	X	X			Fail	Pass	Pass	Pass	Pass
No or simple registration process for foreign investors	X	X			Pass	Pass	Pass	Pass	Pass
Custody and Settlement									
Settlement - Rare incidence of failed trades	X	X	X	X	Pass	Pass	Pass	Pass	Pass
Custody-Sufficient competition to ensure high quality custodian services	X	X	X		Pass	Pass	Pass	Pass	Pass
Clearing & Settlement - T+2 / T+3	X	X	X	X	T+3	T+3	T+3	T+3	T+2
Settlement - Free delivery available	X				Pass	Pass	Pass	Pass	Pass

FTSE QUALITY OF MARKETS CRITERIA - POLAND									
CRITERIA	Developed	Advanced Emerging	Secondary Emerging	Frontier	2004	2011	2013	2015	2017
Custody - Omnibus and segregated account facilities available to international investors	X	X			Not Met	Not Met	Restricted	Restricted	Pass
Dealing Landscape									
Brokerage - Sufficient competition to ensure high quality broker services	X	X	X		Pass	Pass	Pass	Pass	Pass
Liquidity - Sufficient broad market liquidity to support sizeable global investment	X	X	X		Pass	Pass	Pass	Pass	Pass
Transaction costs - implicit and explicit costs to be reasonable and competitive	X	X	X		Pass	Pass	Pass	Pass	Pass
Stock Lending is permitted	X				Fail	Restricted	Restricted	Pass	Pass
Short sales permitted	X				Pass	Pass	Pass	Pass	Pass
Off-exchange transactions permitted	X				Pass	Pass	Pass	Pass	Pass
Efficient trading mechanism	X				Pass	Pass	Pass	Pass	Pass
Transparency - market depth information / visibility and timely trade reporting process	X	X	X	X	Pass	Pass	Pass	Pass	Pass
Derivatives									
Developed Derivatives Market	X				Fail	Pass	Pass	Pass	Pass

Source: FTSE Russell, data as of March 31, 2018.

The first point--restrictions on the availability of omnibus and segregated custodial account facilities--was considered to be the last impediment to Poland's promotion to Developed status (the country had been on the Watch List for promotion since 2011). This reflects a change in the European regulatory environment since the financial crisis.

Polish law recognizes the rights of the beneficial owner (the end investor). However, the rights of nominee holders (intermediaries) are not recognized. Therefore, although omnibus account structures are available in Poland, local market practice is to use segregated accounts.

In the meantime, increased European financial market regulation aimed at ensuring the safekeeping of investor assets has caused a trend towards the use of segregated accounts across the region. Hence, what were previously considered as inefficiencies in the omnibus account model in Poland are no longer considered to be a significant impediment to awarding the country developed market status.

FTSE Global Equity Index Series (GEIS)

FTSE GEIS fulfils investors' requirements for a benchmark to measure the performance of global equity markets on a logical, consistent and accurate basis. It provides comprehensive exposure to an opportunity set of around 7,400 large-, mid- and small-cap stocks across 47 countries, with an aggregate net market capitalization of US\$52 trillion, covering approximately 98 percent of the world's equity market.³

FTSE GEIS includes benchmarks that subdivide the global equity universe into modular design elements, promoting easier market analysis and product segmentation. These benchmarks draw from the starting set of equities in different ways (see the graphic below):

- By country and region
- By industry, supersector, sector and subsector
- By capitalization band (large-, mid- and small-cap)
- By market development status (developed, advanced emerging and secondary emerging)

The FTSE GEIS

FTSE Developed

\$44.6 trillion net market cap

~5,700 stocks

FTSE Emerging

\$4.7 trillion net market cap

~2,100 stocks

FTSE Global Small Cap

\$5.8 trillion net market cap

~4,600 stocks

FTSE All-World[®]

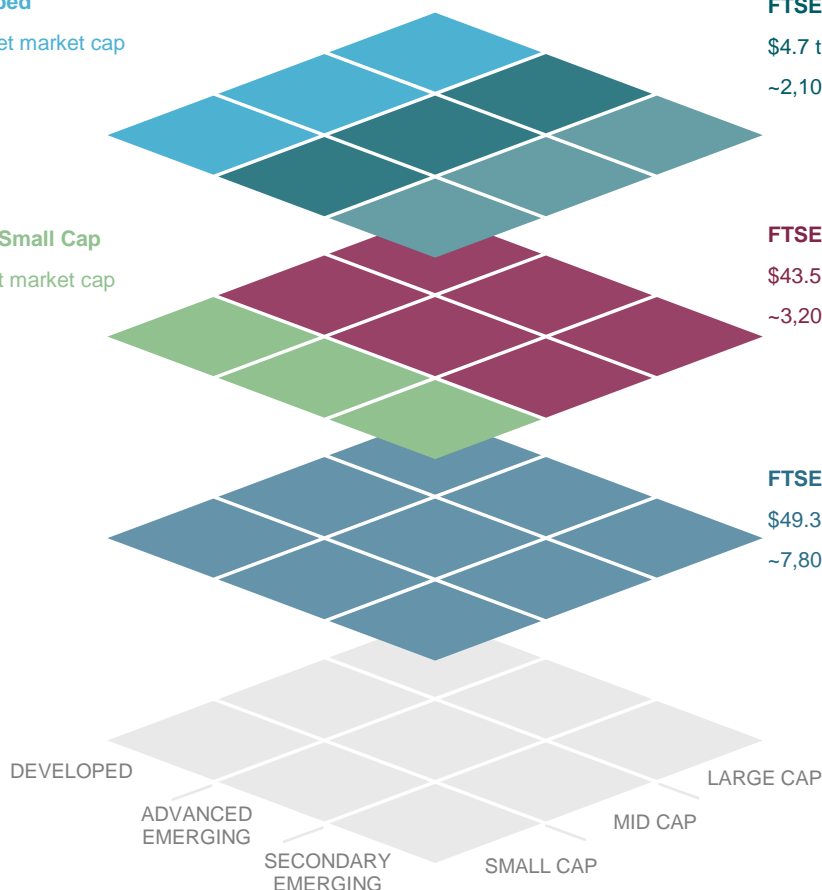
\$43.5 trillion net market cap

~3,200 large & mid cap stocks

FTSE Global All Cap

\$49.3 trillion net market cap

~7,800 large, mid, & small cap stocks



Source: FTSE Russell, data as of September 29, 2017. For more information please see the [FTSE Global Equity Index Series Ground Rules](#).

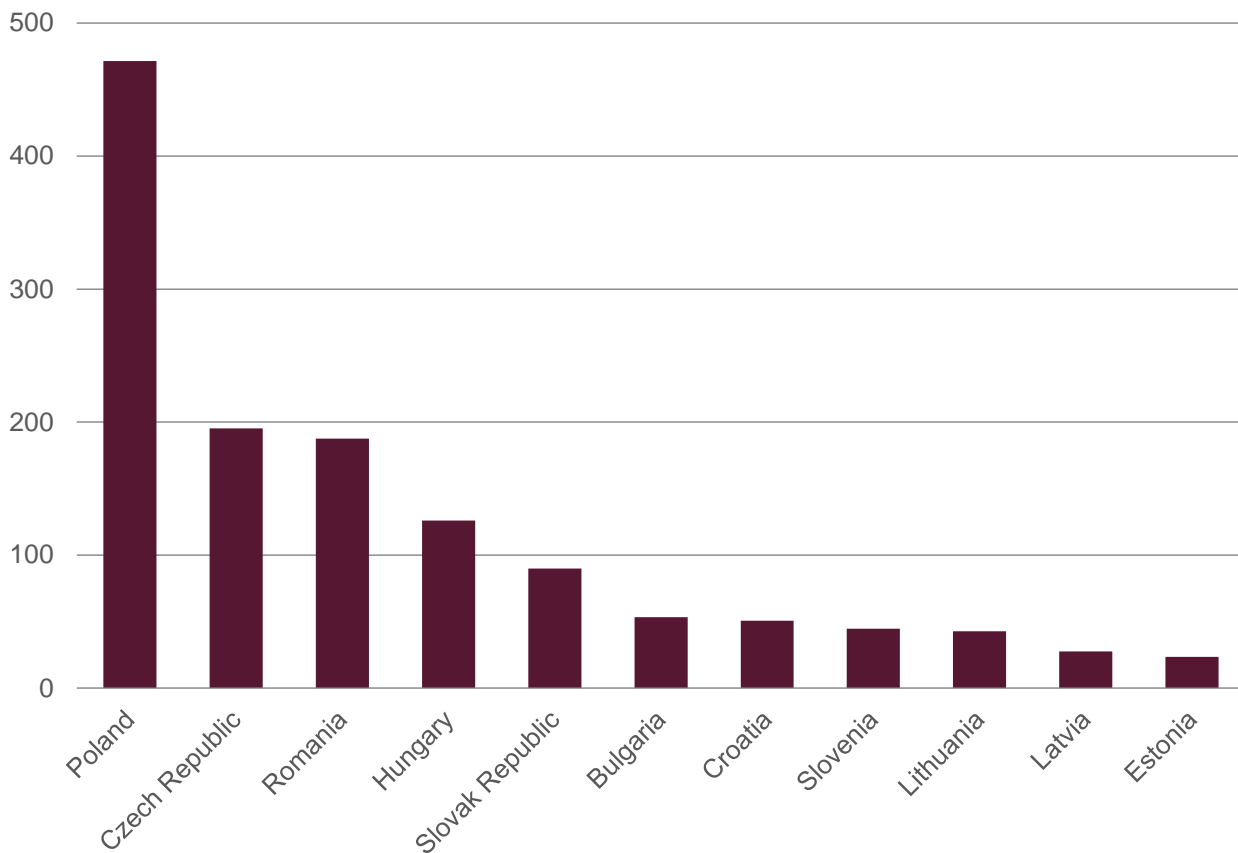
³ Data as of December 31, 2017.

Poland: Key facts

Located in central Europe to the east of Germany, to the north of the Czech Republic and Slovakia and to the west of Belarus and Ukraine, Poland has a population of 38.5 million, making it the ninth most populous country in Europe.

The country has the eighth largest economy in the European Union (EU) and the largest among the former Soviet bloc members of the EU (eleven countries that joined the EU in three stages: in 2004, 2007 and 2013).

GDP of EU accession countries from CEE (Current US\$bn, 2016)



Sources: CIA Factbook, voxeu.org, World Bank, the Economist, Economist Intelligence Unit

Economic statistics

- GDP growth +3.2% (2018, forecast)
- Industrial production +7.4% (February 2018, year on year)
- Consumer price inflation +1.3% (March 2018, year on year)
- Unemployment rate 6.8% (February 2018)

Poland has long had a reputation as a business-friendly country with largely sound macroeconomic policies.

The country has attracted significant levels of inward investment since its accession to the European Union in 2004, boosted by Poland's integration into the European Single Market. Together with other EU accession countries, total exports from and foreign direct investment into Poland have increased much faster since joining the EU than in the rest of the Organization for Economic Co-operation and Development (OECD) countries over the same period.

Poland’s economic output is split by sector as follows: agriculture, 2.6%; industry, 38.5%; services, 58.9%. Major industrial exports include machinery, electronic equipment, vehicles, furniture, and plastics.

FTSE Poland All Cap Index Price Performance



Source: FTSE Russell, data from December 31, 2002 to March 30, 2018 Index levels are in Polish zloty. Past performance is no guarantee of future results. Please see the end for important legal disclosures.

What is the index impact of Poland’s promotion?

Poland’s reclassification from Advanced Emerging to Developed market status in September 2018 means the country’s equities will exit certain FTSE Russell indexes and join others.

An example of the prospective index changes can be seen in the table, showing Poland in the context of neighboring markets from central and eastern Europe.

As of September 2017, Poland had a considerably larger investable market capitalization than the Czech Republic and Hungary, two other Advanced Emerging countries, but also a larger investable market capitalization than Austria, a Developed market.

However, Russia, which is classified as a Secondary Emerging market, has a larger equity market than all four of the other countries in the table combined.

As of September 2018, Poland will leave the FTSE Emerging All Cap Index (where its weight, as of March 2018, was 1.33%) and join the FTSE Developed All Cap Index, where its projected index weight will be 0.154% (recognizing the fact that the overall capitalization of the world’s Developed markets is nearly ten times larger than that of the world’s Emerging markets⁴).

⁴ As of February 28, 2018, the FTSE Developed All Cap Index had a net market capitalization of \$47.06 trillion, while the FTSE Emerging All Cap Index had a net market capitalization of \$5.34 trillion).

	Austria	*Poland	Czech Republic	Hungary	Russia
FTSE Country Classification	Developed	Developed	Advanced Emerging	Advanced Emerging	Secondary Emerging
Index Eligible Securities	28	38	6	5	47
Invt. Mkt Cap (USD m)	61,694	70,965	10,523	19,671	211,574
Weight within FTSE GEIS Universe	0.120%	0.138%	0.020%	0.038%	0.411%
FTSE Emerging All Cap Index Weight	n/a	n/a	0.196%	0.367%	3.948%
FTSE Developed All Cap Index Weight	0.134%	0.154%	n/a	n/a	n/a
*Projections of Poland as a Developed market					

Source: FTSE Russell. Data as of March 30, 2018.

As of March 30, 2018, an indicative list of Polish equities that would be eligible for the FTSE Global Developed Index included 38 names across the large-, mid- and small-cap categories.⁵ The final confirmed list of Polish securities eligible for the index in conjunction with the September 2018 semi-annual review will be published after the Developed Europe regional markets have closed on Friday 24 August 2018.

Capitalizing on developed market status

Developed market status within FTSE's Country Classification framework requires compliance with 21 out of 21 Quality of Markets criteria, covering the market and regulatory environment, custody and settlement, the dealing landscape and the existence of a developed derivatives market.

In other words, countries gaining Developed market status are implicitly committed to the maintenance of an open capital market, enabling outside investors free access to the local securities market, as well as the right to repatriate assets without significant impediments.

The benefits of an open capital market accrue both to the country concerned and to overseas investors: for the country, investment can be financed more cheaply by accessing overseas savings rather than relying solely on domestic capital; and outside investors gain access to greater growth opportunities, as well as an additional source of diversification.

Of course, opening capital markets also imposes a degree of fiscal and monetary discipline on the government, together with the possibility of capital flight if the economy is mismanaged.

In Poland's case, the government has a stated commitment to boost the capital market and continue to strengthen the investment arm of the Polish economy. The Polish Ministry of Finance, in cooperation with the European Bank of Reconstruction and Development and the Warsaw Stock Exchange (WSE) has requested support from the European Commission to establish a Structural Reform Support Program.

This program will include a new strategy for the capital market, the identification of barriers to further development and recommendations in regards to the strategy for the further deepening of the Polish capital market.

In 2017, the WSE witnessed a healthy increase in trading volumes and a large increase in the capitalization of local companies (see the table and chart below).

⁵ See http://www.ftse.com/products/downloads/FTSE_FAQ_Document_Poland.pdf.

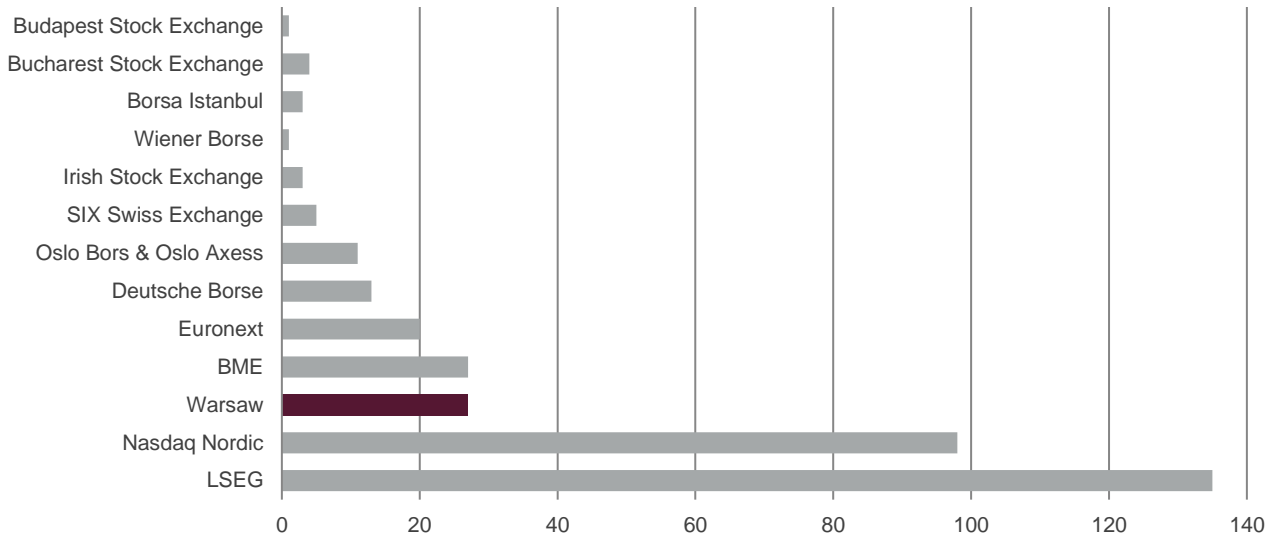
Turnover value [€m], Equities, Electronic Order Book

Exchange	Turnover 2016	Turnover 2017	Change y/y
Warsaw Stock Exchange	43 665	55 819	28%
Bucharest Stock Exchange	1 641	2 006	22%
CEESEG - Vienna	27 976	33 377	19%
Budapest Stock Exchange	7 348	8 688	18%
Malta Stock Exchange	78	88	13%
Deutsche Börse	1 184 365	1 300 957	10%
NASDAQ Nordics & Baltics	643 951	704 425	9%
Boerse Stuttgart	16 860	18 310	9%
SIX Swiss Exchange	782 501	835 179	7%
Euronext	1 601 434	1 707 503	7%
Oslo Børs	98 041	103 312	5%
Luxembourg Stock Exchange	74	78	5%
Irish Stock Exchange	23 543	24 143	3%
BME (Spanish Exchanges)	618 930	619 121	0%
Athens Exchange	12 879	11 387	-12%
CEESEG - Prague	6 213	5 270	-15%
Cyprus Stock Exchange	78	58	-26%

Source: FESE, as of December 31, 2017.

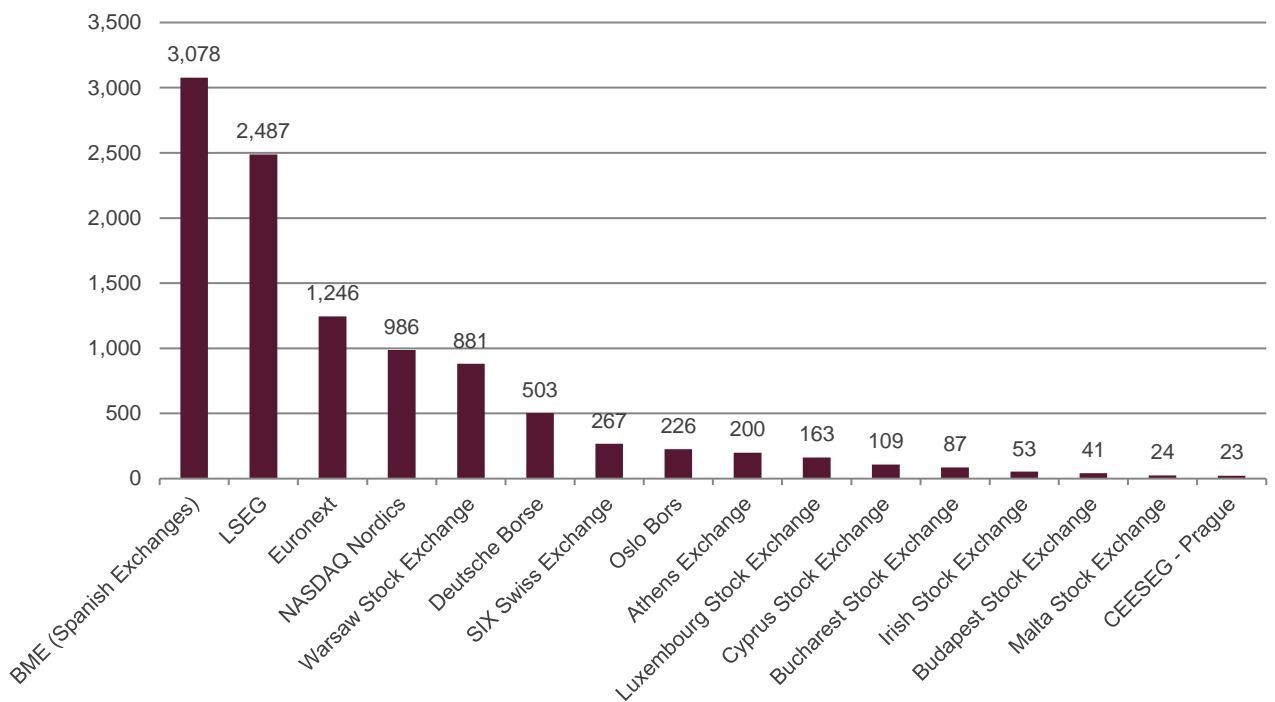
Increasingly, the WSE is acting as a regional hub for local enterprises wishing to access equity capital. The exchange witnessed the third-largest number of Initial Public Offerings (IPOs) of any European stock exchange during 2017, and fifth amongst all European exchanges in terms of the number of listings (see the charts).

The Warsaw Stock Exchange ranked third in Europe in 2017 by number of IPOs



Source: PWC IPO Watch 2017.

Number of listings on European exchanges – Q1 2018



Source: World Federation of Exchanges, FESE..

Meanwhile, the WSE Group also operates a multilateral trading facility dedicated to small and medium companies, a market for corporate and municipal bond issuers and a power exchange, offering trading in electricity, natural gas, property rights, guarantees of origin and CO2 emission allowances.

Together, these statistics and initiatives indicate a likely deepening and strengthening of Poland’s capital markets for the years to come.

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FTSE Russell index expertise and products are used extensively by institutional and retail investors globally. For over 30 years, leading asset owners, asset managers, ETF providers and investment banks have chosen FTSE Russell indexes to benchmark their investment performance and create investment funds, ETFs, structured products and index-based derivatives. FTSE Russell indexes also provide clients with tools for asset allocation, investment strategy analysis and risk management.

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