

# POLAND'S ECONOMIC CREDIBILITY INDEX



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# **POLAND'S ECONOMIC CREDIBILITY INDEX**

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## Introduction

The "Poland's Economic Credibility Index" was created thanks to the cooperation of the European Financial Congress and the Open Eyes Economy Summit. For the first time, its abridged version was presented at the European Financial Congress held in Sopot on 06 June 2022. The full version of the report was announced at the seventh edition of the Open Eyes Economy Summit congress in Krakow on 22 November 2022.

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## Preface

Credibility cannot be expressed as zero-one (it is or it is not), but it can be graded. It can concern virtually any social sphere, including the state, but also the economy. In order to describe the category of "economic credibility of the state" with the use of the theory of economics, it is necessary to make an argument: credibility - trust - predictability - calculation - cooperation. Since we relate economic credibility to the economy, the calculation takes the form of an economic calculation, and cooperation becomes economic cooperation.

To talk about economic credibility, one should bear in mind specific economic agents. Their decisions, actions, directly or indirectly, assess economic credibility of the state. It is the economic agents that calculate the associated risk (economic, political, regulatory, or administrative). At the same time, low or high credibility of the state also affects directly or indirectly - the conditions (including various parameters) of running a business. Therefore, **credibility constitutes an important economic value, but also a regulatory category: it influences conditions for economic activity which can be favourable or unfavourable.**

There are numerous subjective (that is, it concerns different actors) and objective (there are different kinds of it) references for credibility. Both these dimensions cannot be separated from each other, if only because some of the economic conditions are defined (determined) directly (e.g. tax rates). The majority of them, however, are the result of many influences, including social perceptions and expectations (e.g. the level of inflation as a consequence of inflation expectations). Additionally, it influences economic parameters through variables such as trust, information, or knowledge.

An obligation is part of credibility. It is an obligation which we respect, and not just promise. Therefore, it is relational in nature, as it is based on trust between the parties to the social relationship. In the case of power, an important reference to it is the citizens' recognition of the actions by the government as valid.

Legitimacy is born from the citizens' recognition of the state as theirs, from the readiness to defend it, and from respecting the rules established by the state. The opposite of legitimacy is civic disobedience, which also manifests itself as civic anarchy, disregard for one's country, a kind of autarky, withdrawal, distancing oneself from the country and its affairs. As a result, however, when a crisis situation occurs, it is clearly visible how the deficit of legitimacy manifests itself in the state's inability to solve problems, in making ineffective, costly, inaccurate, and delayed decisions. Equating civil disobedience exclusively with protests is therefore a mistake.

Reducing legitimacy to the rule of law is a manifestation of the self-closing of the legal system and its civil alienation. This is when the legally defined procedure displaces and replaces the axiological order. It itself becomes the normative foundation. Formalistic legalism causes that legitimacy disappears and the state loses its social legitimacy. The constitutional order becomes the order of legal, casuistic correctness.

As legitimacy weakens, the power of unlimited political decision-making seemingly increases. However, without rules embedded in legitimacy, political choice leads to only one thing - the maintenance of power. And this is what distinguishes the politics of rules from the politics of events, the politics of principles from the politics of facts.



When the public authority loses its economic credibility, it resorts to propaganda and buying off various groups important for the political interest. This leads to e.g. reduction of trust in the domestic currency and inflation. Direct consequences of the low economic credibility of the state include: higher level of risk and related costs, lower economic efficiency, lower productivity of capital and labour, higher debt servicing costs, and lower resilience to shocks.

The value of fiat money is based on trust in the issuer, and this trust in the issuer depends on its economic credibility. It is hard to imagine effective fight against inflation without trust in the issuer.

The key to understanding the importance of the state's economic credibility lies in noticing the relationship between the short-term (current) and long-term (future) consequences of economic activities and phenomena. We may therefore look at it through an interpretation of Keynes' theory (2011). If in economic activity we are guided primarily by the interest rate (which, as Keynes emphasizes, is a current phenomenon) and the marginal efficiency of capital, then the meaning of the future disappears in management and perpetuates the present. It is different when the present is linked to the future through productive capital (ibid., p. 128). It is the production (development) investments that open the way to the future and form the basis for meeting the challenges.

It is easy to see that resilience is lost by "settling" in the present and exploiting these resources that bring temporary success. Each success then turns into a problem as it leads to a schematic behaviour, and that - to routine. While focusing on winning now, we forget about creating the ability to adapt to new rules or situations. Growth results from the use of current factors, it is happening in the present. Development is possible when we build a bridge between the past (heritage) and the future. Growth gives strength, however, it does not confer resilience.

The bridge stands for, among others, productive investments, especially the innovative ones. And this is what Keynes pointed out. Complementarity of private and public investment is of fundamental importance. Public investment is not meant to displace or replace private investment. They are necessary in the formation of the economic infrastructure, but at the same time they constitute spatial limitations, without which short-term private interest would dominate over the long-term developing public interest.

The low economic credibility of the state weakens its long-term and productivity orientation. It is conducive to strengthening the short-term, speculative, and transactional orientation. Our analysis shows that Poland's economic credibility has decreased in recent years. This is what stands behind the recent low level of private investment in the Polish economy, despite the high rate of economic growth maintained in the years 2014-2019, as well as the economic recovery after the 2021 pandemic recession.

The way in which the state functions, that is as a great financial institution, is of fundamental importance to all its citizens. Everyone – whether they want it or not - is a participant in the state's financial system, both on the revenue side (the broadly understood tax system), and on the expenditure side. Thus, citizens are a specific kind of "shareholders" of the state, which they maintain using their taxes, and at the same time they are its "creditors". Inevitably, the state's debt, in one way or another (e.g. as a consequence of inflation), becomes a liability of its citizens. How the state finances its functioning, including public debt, and what is included in expenditures, exerts a huge impact on redistribution of

resources in the economy and the economic situation of citizens (Biga, Hausner, Możdżeń 2021, p. 88).

The state's financial system is a system of many interconnected vessels. Whether it works efficiently depends closely on economic credibility of all its participants, but above all, on the credibility of the state itself. A market economy is based on credibility of the state. Its weakening drives vulnerability of the economy and renders it less resilient to various types of economic shocks. Kamil Pruchnik (2021) emphasizes that low credibility causes the state's inability to prevent a banking crisis (*ibid.*, pp. 51–52). Its outbreak results in a dramatic increase in the price of financing economic activity. Credit risk and the cost of credit soar, leading to a recession and a wave of bankruptcies. The process loops and the economic downward spiral intensifies (*ibid.*, p. 129). But this process can be interrupted by effective state intervention. This, however, is not possible and effective if the state does not have sufficiently high credibility.

In order to maintain high economic credibility of the state, it is of great importance to establish and observe rules which can be determined as socially beneficial constraints.

Introducing and respecting these rules (e.g. related to environmental protection) is the foundation of economic credibility of the state.

The consequences of circumventing fiscal rules were clearly described by Hyman Minsky. He paid particular attention to significant redistributive effects and the emergence of uncontrollable wage-price spirals (Minsky 1990).

The authors of the OECD report "Beyond GDP" also point to the serious adverse distributional effects of unconventional monetary policy (Stiglitz, Fitoussi and Durand 2018, p. 70). Low (real negative) interest rates cause, among others, that the elderly (pensioners) are gradually losing their life savings and the value of the shares of their rich and influential owners is growing rapidly. Policy justified by the need of maintaining relatively high employment has redistributive consequences which undermine its impact on sustaining continuous growth. At the same time, it generates a decline in trust in the government and credibility of the state. The intergenerational consequences of unconventional monetary policy and expansionary fiscal policy are now gaining weight and cause strong social tension. The redistributive effects of unconventional monetary policy favour the rich at the expense of the poor.

Analysis of redistributive, including intergenerational, effects of financial policy (both fiscal and monetary) is necessary because it clearly shows the broader economic phenomenon of debt transfer (Stiglitz, Fitoussi and Durand 2018, pp. 49–50). This phenomenon causes the debt of one economic sector (households, private enterprises, or public sector) to spill over to the other sector. It applies not only to the flow from households and private enterprises to the public sector (which attracts the attention of many economists), but also vice versa. This is why the "national account" should even more encompass this circulation and the dependencies resulting from it. This is what the authors of the "Beyond GDP" report postulate. In particular, their recommendation concerns taking into account the interchangeability and interdependence of various types of assets in the national accounts' system. Growing indebtedness of the public sector (the state) must not be underestimated. Sooner or later it will - one way or another - lead to indebtedness of other sectors. The economic crisis and recession - the loss of some productive potential and accumulated wealth - are bound to ensue in consequence. It is therefore absurd to say that the present

public debt is not a burden for future generations. It does matter in two ways: directly financial and indirectly material – as it reduces the accumulated wealth. The aging of modern societies exacerbates this problem. Joseph Stiglitz, Jean-Paul Fitoussi, and Martine Durand (2018, p. 86) show in the report that a light-hearted financial policy has contributed to an increase in the frequency of episodes of large loss of income in many countries.

The occurrence of the "debt transfer" phenomenon means that the arguments justifying an increase in public debt as economically cheaper than private debt are misleading. The currently cheaper public debt is bound to become private debt in the near future, causing another wave of public debt growth. One should also bear in mind that destructive financial policy in one country has negative effects also on an international scale. It applies in particular to such country's economic partners.

The phenomenon of "debt transfer" results from the fact that debt ties the present with the future in a different way than it is in the case of work and wages. Debt transfer is of different social space and time-based nature, which is determined by the debtor-creditor relationship and the resulting expectations and obligations. An important variable of this bond is money, which expresses and measures the amount of debt. However, money itself is a form of debt. In the case of inflation, money loses its value, which affects the amount of debt. In this sense, the bilateral debtor-creditor relationship becomes a broader social relationship. Its space-time aspect is expanding. And inflation (as well as many other variables) may also have its role to play. Transfer and redistribution of debt are further influenced by: diversified and variable fiscalisation of various types of economic activity and volatility of the exchange rate. Cash flows do not only reflect current transactions, but also influence the shaping of long-term relationships between market participants. The stronger the impact, the more money in the economy is endogenized, this being a consequence of the weakening of fiscal rules and the actual loss of independence of the central bank.

Denying the importance and circumventing socially beneficial constraints leads to deformation of the economic structure. Some of its elements gradually gain a dominant position and take on the role of a hegemon. Cartelization of the industrial economy may serve as an example thereof. Nowadays, the hegemon's position is held by large virtual platforms (GAFA). Structural deformation may take the statist form, in which state entities are given superior position, thus subordinating market players to themselves and imposing such rules of the economic game which are favourable to themselves only. This may currently be observed in Hungary or Poland. But the cases of China or Russia are even more conspicuous. In these and many other countries we are dealing with the formation of a state-national market economy.

Ineffectiveness or low effectiveness of rules, including fiscal rules, does not usually result from the construction of such rules, but from who and how uses these rules or treats them. Rules are restrictions on discretionary powers. They do not eliminate these discretionary powers but limit them: one is able to do a lot, but one is not able to do everything. Those who make decisions tend to avoid restrictions. They often choose to cut corners. Therefore, there must be rules in place to prevent such conduct. The constitutional principle of the rule of law is one of them. But if this rule is challenged, the entire normative order is reduced. At the same time, sadly, it is common knowledge that eventually there are no formal and legal provisions which may not be weakened or even removed by determined decision-makers.

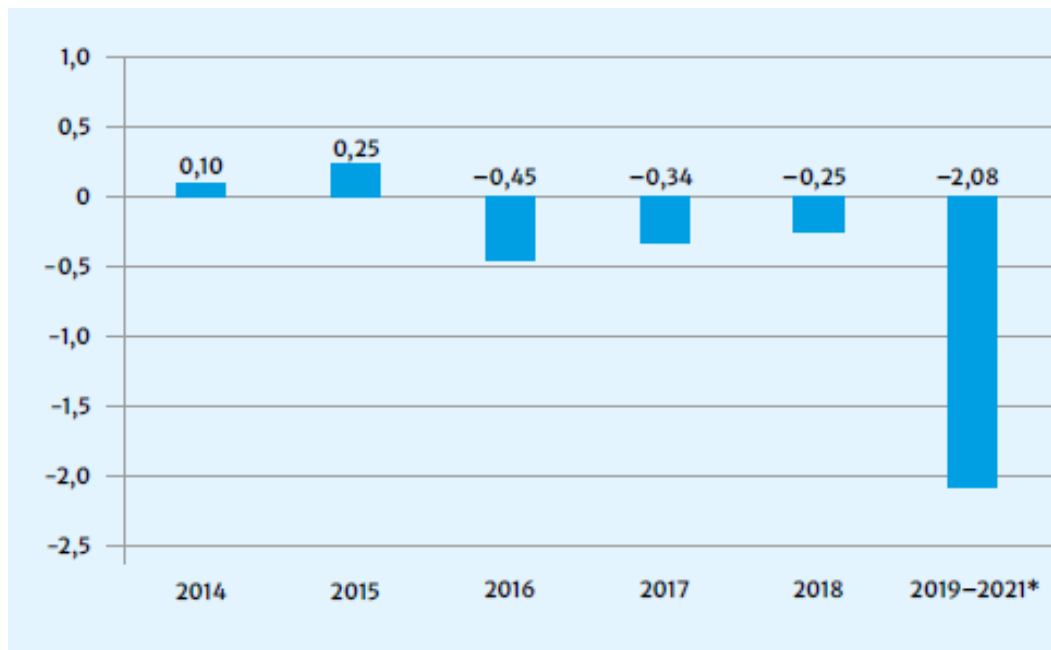
A disturbing proposal to finance government expenditure by central banks is the MMT (Modern Monetary Policy) concept, which assumes that an important source of the government's revenue should be the issuance of money by the government (in fact by the central bank, which in this concept becomes an integral part of the government). Then creating money "out of nothing" is limitless, and fiscal expenditures lead directly to an increase in the amount of money in circulation. It is difficult to understand the belief that the effects of such situation will be only beneficial, and that no side or undesirable effects are to take place. Especially if, as a last resort, the solution comes down to making entries in the books of the central bank, and its balance sheet total grows indefinitely. But should the abolition of fiscal rules be introduced by the MMT supporters, this absurd situation will eventually force them to admit that some limiting rules are needed. And then a question returns of what these rules should be, but also who is to establish them, how they are to be established, and who is to guarantee their observance.

Normative order in society exists not by means of sanctions themselves, but as a result of cultural (axio-normative) social choice and empowerment, which form the basis of its formal and legal foundation. Therefore, if someone demands abolition of rules, including fiscal rules, because they are ineffective, they should bear in mind that such argumentation is bound to lead to the weakening of the entire normative order and all the rules written into it. Then, the rules gradually cease to apply, and so the resulting limitations as well as the resulting social benefits disappear. There is no credibility of the state without following the rules that this state has established. Observance of the rules ensures predictability, and without it, stabilization of economic conditions necessary for the functioning of the economy cannot be achieved.

Crucial for economic credibility of the state is respecting international obligations, i.e. bilateral agreements concluded with other states, and even to a greater extent multilateral treaties often associated with membership in international organizations. These define the functioning of domestic economic agents in the economic dimension in the international arena and the involvement of individual and institutional foreign entities in the economic life of the country.

Economic credibility of the state is a specific type of public good that is and must be instrumentalised in order to benefit from it. The crux lies in the fact that the means of instrumentalizing this good should sustain and produce it, and not destroy it. Of fundamental importance is the quality of economic information produced by the state and its agencies. The reverse is tampering with statistics or government propaganda, rather than integral information. Such instrumental exploitation of credibility leads to lowering trust and undermining credibility.

**Chart 1.** Poland's economic credibility index

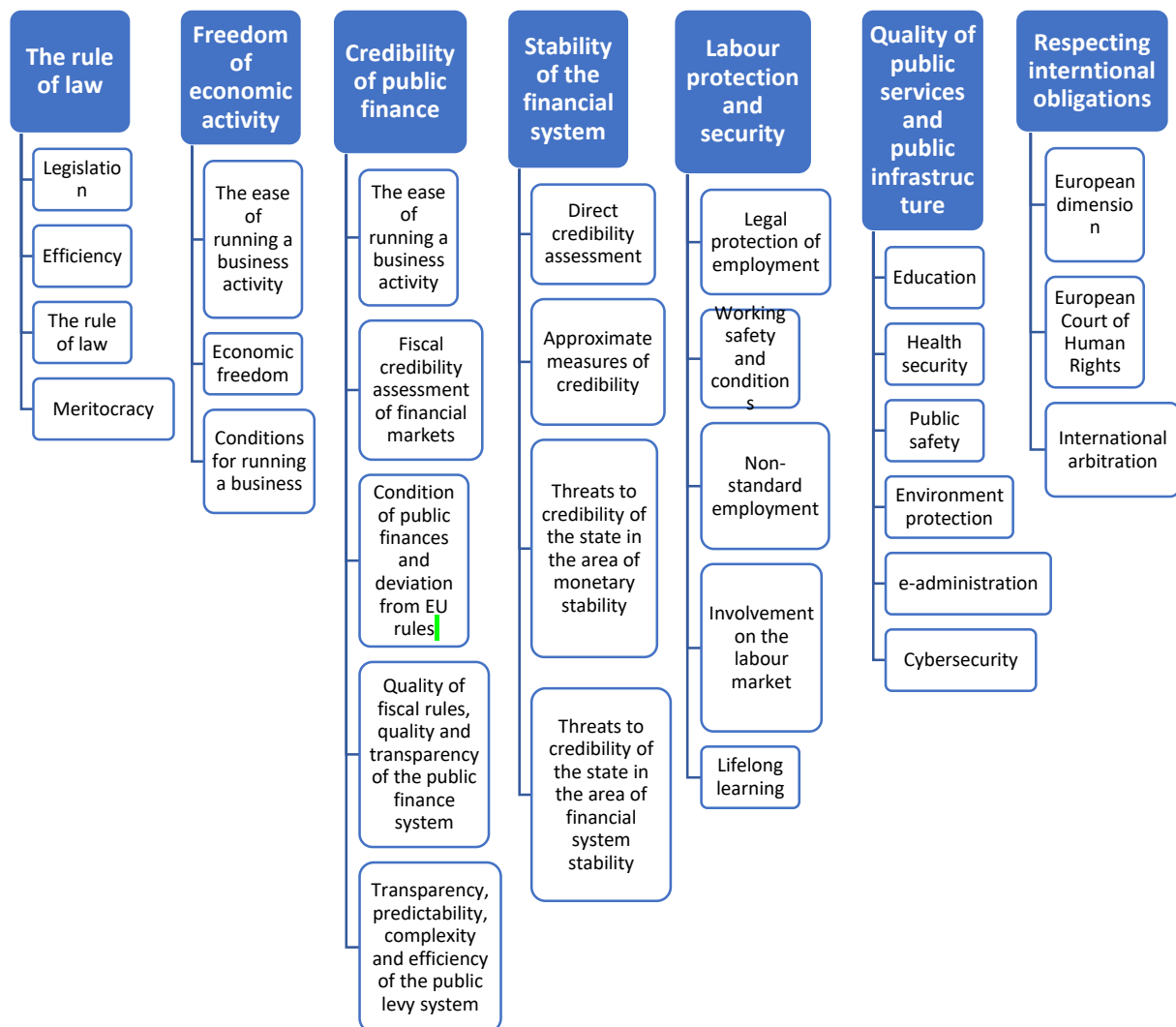


\* due to the fact that some of the used databases contained the most up-to-date information for the year 2021, while some of them for the year 2019 only, the index was calculated using the common period 2019-2021, of which the latest available data was classified for calculations

## I. How the index was created - methodology

Poland's economic credibility index was developed for **seven areas of social and economic life** and in **29 assessment dimensions**.

**Figure 1.** Layout of areas and dimensions for the assessment of the index of economic credibility of Poland



Source: own study

The index construction procedure included several stages. There were collected available and reliable measures, which could parameterize the issue of economic credibility. **More than 150 indicators** were selected from a variety of national and international databases. These were subject to a two-stage **verification procedure** involving in particular:

1. calculation of the **coefficient of variation** in the years 2008-2021 according to the formula:

$$V = \frac{s}{\bar{x}}$$

where:  $s$  – standard deviation

$\bar{x}$  – arithmetic average

The low coefficient of variation was the basis for rejecting the measure due to the fact that it did not differentiate the observed phenomenon over time and as such did not have the appropriate information value;

2. conducting an **analysis of correlation** between all indicators, which allowed for rejecting those indicators which were strongly related to each other and carried the same or similar information value.

A number of **105 indicators** was positively assessed, where each was classified as a **stimulant** (an increase in its value means a positive impact on the level of economic credibility) or a **destimulant** (increase in its value means a negative impact on the level of economic credibility).

The measures subjected to **normalization** according to the formula:

$$x' = \frac{x - \text{median}}{\text{quarter deviation}}$$

where:  $x'$  – normalized value,  $x$  – source value of the indicator

This enabled comparison of indicators expressed in different measurement units. There was obtained distribution of measure values, in **which "0" means no observed changes, negative values mean regression** in relation to the average value from the years 2008-2021, and **positive values - improvement** in relation to the average value in the analysed period.

Normalized values formed the basis for building sub-indices in individual dimensions and areas, and consequently for the final index of Poland's economic credibility. The sub-indices



were built with the use of weights assigned to individual indicators and dimensions. The total index was created by assigning appropriate weights to the analysed areas.

Availability of the data necessary for constructing the index was a bit of a challenge. Some databases had up-to-date information for the year 2021, but others only for 2019.

Therefore, when determining the index, a common period 2019-2021 was adopted, in which the latest available data was classified for the calculations.

The final value of the index consists in synthetic information about the changes, which took place in each of the analyzed years compared to the average level for the years 2008–2021. A positive value means improvement in credibility in comparison with the reference period, while a negative value means deterioration, and "0" means no change has been observed. A detailed interpretation of the results is presented in the table.

<b>Value of the index of economic credibility of Poland</b>	<b>Interpretation What happened to economic credibility</b>
< -2	very big drop
-2 < -1	big drop
-1 < -0.5	average drop
-0.5 < 0	slight drop
0	no change
0 < 0.5	slight improvement
0.5 < 1	average improvement
1 < 2	big improvement
> 2	very big improvement

## Weights used in calculating the index

(percentage)

### I. The rule of law

Dimension 1. Legislation	25
Dimension 2. Efficiency	25
Dimension 3. The rule of law	25
Dimension 4. Meritocracy	25

Legislation	Number of pages of legal acts which entered into force in specific years	30
	Lack of any documentation from consultations conducted by the Government Legislation Centre (RCL)	40
	No reference of the authors to the opinions submitted at the Government Legislation Centre	30
Efficiency	Relation of resolved court cases in relation to those submitted in a specific year	50
	Average duration (in months)	50
The rule of law	Restrictions on government powers	60
	Enforcement of legal provisions	40
Meritocracy	Civil service - employment	50
	Access to public information	25
	Supreme Audit Office - notifications to the spokesperson	25

### II. Freedom of economic activity

Dimension 1. The ease of running a business activity	50
Dimension 2. Economic freedom	25
Dimension 3. Conditions for running a business activity	25

The ease of running a business activity	Starting business	10
	Obtaining a building permit	10
	Obtaining access to electricity	10
	Registration of property	10

	Obtaining a loan	10
	Protection of minority investors	10
	Paying taxes	10
	International exchange	10
	Protection of respecting contracts	10
	Winding up a business activity	10
Economic freedom	Ownership rights	8
	Government integrity	8
	Efficiency of the judiciary	8
	Tax burden	8
	Government expenditures	8
	Fiscal situation	8
	Freedom of (running) a business activity	8
	Freedom of work	8
	Monetary freedom (the right to healthy money)	8
	Freedom of trade	8
	Freedom of investment	8
	Financial freedom	8
		-
Conditions	WGI – Worldwide Governance Indicators (ranking position)	25
	WEF – Institutions (ranking position)	0
	WEF – Infrastructure (ranking position)	25
	WEF – Health and Education (ranking position)	25
	WEF – Secondary education and training (ranking position)	25

### III. Credibility of public finance

Assessment of fiscal credibility by financial markets	25
Condition of public finance	25
Quality of fiscal rules, quality and transparency of the public finance system, disintegration of public finances	25
Quality and transparency of the tax system	25

Assessment of fiscal credibility by financial markets	Country's average credit rating from the top three rating agencies	33
	Five-year CDS contracts	33
	Long-term rate spread (to Germany)	33
	Public debt (percentage of GDP)	17
	Nominal deficit (percentage of GDP)	17

Condition of public finances	Structural deficit (percentage of GDP)	17
	Deviation of the SFP nominal deficit from 3 percent (square)	17
	EDP Government debt (0/1)	17
	Deviation of the structural SFP deficit from the MTO (1%)	17
Quality of fiscal rules, quality and transparency of the public finance system, disintegration of public finances	Standardised fiscal rules index	17
	Public Finance Transparency Index Open Budget Survey > OBI	17
	Debt beyond parliamentary control - indicator (percentage of debt)	17
	Difference between the national deficit and the deficit according to the EU methodology	17
	Bonds instead of subsidies (percentage of debt)	17
	Medium-term budgetary framework indicator	17
Quality and transparency of the tax system	International Tax Competitiveness Index	25
	Law Barometer - Grant Thornton - tax law	50
	The tax component of the Doing Business Paying Taxes index	25

#### IV. Stability of the financial system

Direct credibility assessment	25
Approximate measures of credibility	25
Threats to credibility of the state in the area of monetary stability	25
Threats to credibility of the state in the area of financial system stability	25

Direct credibility assessment	Percentage of people negatively assessing activity of the National Bank of Poland	100
Approximate measures of credibility	Inflation expectations of entrepreneurs	50
	Share of cash in the M3 money supply	50
Threats to the credibility of the state in the area of monetary stability	Volatility of 15% truncated mean	25
	Square of the inflation deviation above the target	25
	Square of the output gap	25
	Money supply (square of the deviation of the money supply dynamics from the dynamics of potential output plus the inflation target)	25
Threats to the credibility of the state in the area of	Loans (dynamics of receivables from the non-financial sector as compared with dynamics of the GDP potentially increased by the inflation target)	25

financial system stability	Links between the government and banking sector (share of receivables from central and local government institutions in banks' assets)	25
	Real interest rates on deposits	25
	Valuation of banks on the Warsaw Stock Exchange (price to book value at the end of the year)	25

#### V. Employment protection and safety

Legal protection of employment	20
Working safety and conditions	10
Non-standard employment	20
Labour market participation	30
Lifelong learning	20

Legal protection of employment	Temporary contracts	50
	People with 12 months or less job tenure (aged 25 or older)	50
Working safety and conditions	Accidents at work resulting in an absence of over four days	50
	Fatal accidents of work	50
Non-standard employment	Part-time employment as percentage of the total employment	50
	Precarious employment	50
Labour market participation	Employment rate (20-64 years)	20
	Female employment rate (20-64)	40
	Employment rate (55-64 years)	40
	Employment rate of people aged (55-64)	
Lifelong learning	Indicator of participation in education and training in the four weeks preceding the survey	100

#### VI. Quality of public services

Education	25
Health	25
Security	20
Environment	20
E-administration	5
Cybersecurity	5

Education	Points earned in the PISA ranking	33
	Gross enrollment rate	33

	Public expenditure on education by education level and programme orientation - as % of GDP (Pre-primary to tertiary education)	33
Health	Medical doctors licenced to practice medicine per 10,000 population	20
	Life expectancy for men aged 45	80
Security	Criminal offences (number)	15
	Offences against family and guardianship (number)	15
	Detection of perpetrators of crimes - of an economic nature (%)	15
	Detection of perpetrators of crimes - against life and health (%)	15
	Share of national defence spending in GDP	40
Environment	PM10 and PM2.5 dust emissions (average annual concentration)	30
	Municipal waste collected by one person (in kg)	70
E-ADMINISTRATION	Number of people with a trusted profile (in millions)	100
CYBERSECURITY	Number of unique security incidents reported to CERT Polska	100

## VII. Respecting international obligations

EU dimension	33
European Court of Human Rights	33
International arbitration	33

EU dimension	Judgments on finding infringements of obligations of the EU member state	-20
	Judgments on finding infringements of obligations of the EU member state (favourable to Poland)	-20
	New infringement cases	-20
	New references for a preliminary ruling from Poland	-20
	Number of infringements of Community law initiated by the European Commission against Poland	-20
European Court of Human Rights (ECHR)	Poland in the European Court of Human Rights: complaints taken by the ECHR	-25
	Poland at the ECHR: rulings	-25
	Poland at the ECHR: key rulings not implemented by the Polish government	-50
International arbitration	International arbitration (General Prosecutor's Office) - number of powers of attorney	-33
	Claims confirmed (in million euros)	-11
	Proven claims (in million dollars)	-11
	Confirmed amount of claims (in PLN million)	-11
	Number of arbitration proceedings	-33

## **II. The rule of law and security of business transactions**

### **The importance of the rule of law for the economic credibility of the state**

The rule of law, understood broadly, exerts a significant impact on the security of economic transactions. If we limited this concept to strictly economic topics (tax legislation, court economic cases, etc.), we would omit numerous issues important for the functioning of the business. It would then be impossible to understand the basic reasons of economic successes and failures of individual states, as discussed in detail by, among others, Daron Acemoglu and James Robinson (2012).

An important part of economic credibility of the state are matters related to law-making and application thereof. Predictability of regulations and the ability to efficiently pursue claims exert a significant impact on running a business. In the course of thought: reliability - trust - predictability - calculation - cooperation, legal elements are particularly important for predictability (stable legislation in accordance with the rules of art) and cooperation (encouraged by well-functioning courts). Should we base it on the theory of games, the operation of courts may be reduced to the fact that they change non-cooperative games into cooperative ones (Cooter, Ulen 1988).

The importance of an independent judiciary is not to be overstated. This is the guarantee of the state's credibility in a situation, where other authorities fail to follow the established rules. Such violation may consist in unauthorized interference with the freedom of economic activity or in favouring state-controlled economic entities. Courts are a guarantor of the stability of trade between private entities (Marciano, Melcarne and Ramello 2019; Chemin 2020).

### **Analytical dimensions of the rule of law**

The "rule of law" area has been divided into four dimensions. Three dimensions correspond to individual elements of the classical separation of powers. The first one is legislation - it concerns the whole of legislation. Taken into account are the number of the passed laws and compliance with the standards of good legislation, in particular consultations on projects. The second dimension focuses on efficiency of the judiciary. It analyzes the number of settled cases in relation to those cases that have been received within the same period, and the average duration of proceedings in the first instance courts. The third dimension - the rule of law - relates to activities of the executive (the degree to which it is bound by law) and the level of enforcement. This triad is complemented by the fourth dimension - meritocracy - which reflects the condition of the civil service, access to public information, and the question of violations of the public finance discipline.



**Table 1.** Weights of individual dimensions for the area of the rule of law

	<b>Weights</b>
Dimension I – legislation	25%
Dimension II – efficiency	25%
Dimension III – the rule of law	25%
Dimension IV – meritocracy	25%

<b>Value of the 2020 Credibility Index for the Rule of law area</b>	<b>-1,06</b>
Value of the 2020 Credibility Index for dimension I - legislation	<b>-0,57</b>
Value of the 2020 Credibility Index for dimension II - efficiency	<b>-3,35</b>
Value of the 2020 Credibility Index for dimension III – the rule of law	<b>-0,13</b>
Value of the 2020 Credibility Index for dimension IV - meritocracy	<b>-0,20</b>

Source: own study

### Dimension 1. Legislation

The focus of this dimension falls on both the number and the quality of the law being made. It consists of three indicators. The first one is the number of pages of legal acts published in the Official Journal of Laws in the following years (data from Grant Thornton from the [barometrprawa.pl](http://barometrprawa.pl) report). The indicator does not appear as flawless - it may be greatly influenced by, for instance, the need to adapt to the legal system of EU regulations. Nevertheless, the phenomenon of excessive regulation - which is manifested in, among others, volume of legal acts - stands in stark contradiction to the fundamental "ignorance of the law is harmful" principle.

The second and third indicators consist in compliance with the principles of good legislation, which include the need to conduct thorough consultations on the content of a draft legal act. For the purposes of measuring this phenomenon, two categories of data have been used: the percentage of drafts, for which there has been no documented public consultation (indicator 2) and the percentage of drafts, in which the authors do not refer to the submitted opinions (indicator 3). While the second measure points to the omission of consultations, the third one reflects the fears that such consultations may have been of a façade nature.

**Table 2.** Weights of indicators in the area of legislation (percentage)

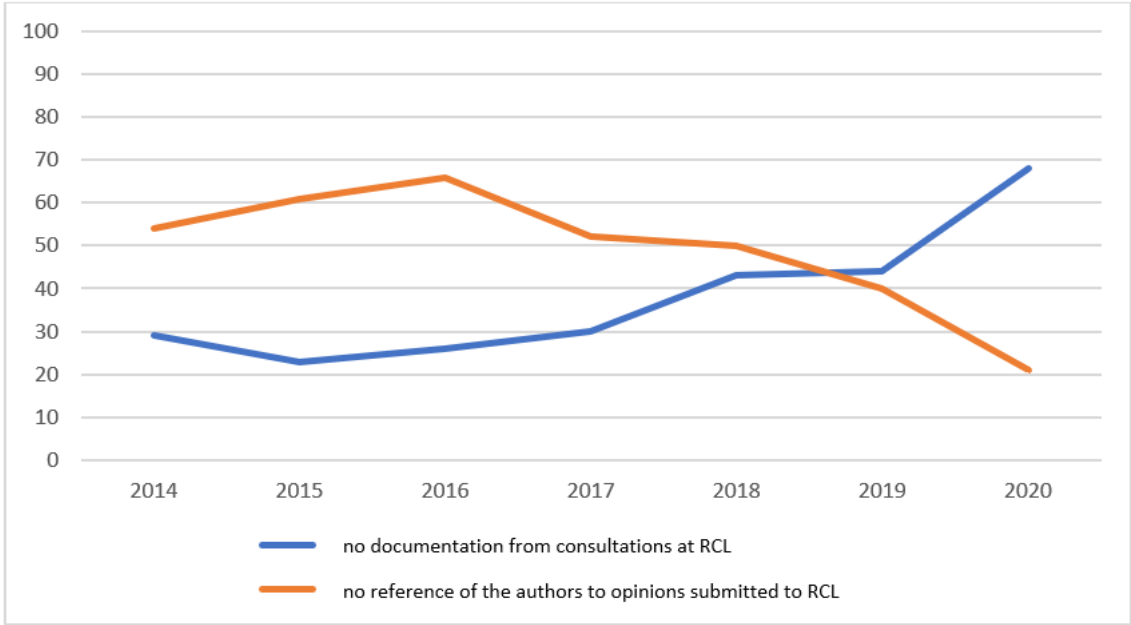
Legislation	Number of legal acts that entered into force in specific years	-30%
	Lack of any documentation from consultations at RCL	-40%
	No reaction on the part of authors towards opinions issued by RCL	-30%

Source: own study

The conclusions are not optimistic. It is true that the number of pages of legal acts which have come into force in recent years is evidently smaller than in the record year of 2016, when over 35,000 pages' worth of regulations were "produced". Nevertheless, the level oscillating around 20,000 pages remains high. This number prevents even brief reading of the applicable regulations - not only by ordinary citizens, but also by lawyers, who, even in their specialized areas, are finding it difficult to keep up with the changing regulations. Unequivocal interpretation of a rather clear decrease in this indicator in 2020 (below 15,000 pages) has not been simple. There are many indications suggesting this is not a harbinger of a new trend, but an effect of the inability to "normal" work of the authorities involved in the law-making process during the pandemic. Especially that in 2021 the "production of law" soared again, and the first half of 2022 saw some 14,487 of typescript pages.

For the rule of law, the content, i.e. the quality of the law, and not its quantity, is of the greatest importance. But this is difficult to study and assess in an objective manner. Analysis of compliance with the principles of good legislation may shed more light. In this process, extensive public consultations is essential. Unfortunately, since 2015 we have observed a continuous increase in the number of drafts for which no documented consultations were run - in 2015 it was 29%, in 2019 - 44%, and in 2020 - as much as 68%. The pandemic does not justify the omission of consultations, as these are largely carried out in writing. Additionally, where a need for meetings and conversations arose, there was a possibility of convening videoconferences.

**Figure 2.** Percentage of drafts for which there are no documented public consultations or reference to the submitted opinions.



Source: Grant Thornton, [barometrprawa.pl](http://barometrprawa.pl)

The increased percentage of drafts, for which no consultation was conducted, should be attributed to the abuse of the device of parliamentary legislative initiative. In this mode, public consultations are not required. We observe a growing phenomenon of submitting drafts as parliamentary ones, although in fact they are government-issued documents. This practice is aimed at circumventing the principles of good legislation. The number of such cases is increasing.

On the positive note, since 2016 there has been a decrease in the number of drafts, in which the authors do not refer to opinions submitted to the Government Legislation Centre. In the last five years, this percentage has dropped from 66% to 21%.

**Dimension 2. Efficiency of the judiciary**

The efficiency of the judiciary is described by two indicators. The first one is the ratio of the number of cases submitted to courts in a given year, to the number of cases settled in such period. This proportion allows to see growing backlogs in courts and the periods in which the capacity to settle cases is higher than the ongoing receipt of documents. The second indicator stands for the average duration of court proceedings, calculated as a weighted average on the basis of information provided by individual courts. It applies to civil, criminal, insurance and labour law, economic, family, and bankruptcy proceedings. Taken into account are first instance cases resolved by regional and district courts. Both indicators are based on official data sourced from the statistics database provided by the Ministry of Justice.

**Table 3.** Weights of indicators in the area of efficiency of the judiciary (percentage)

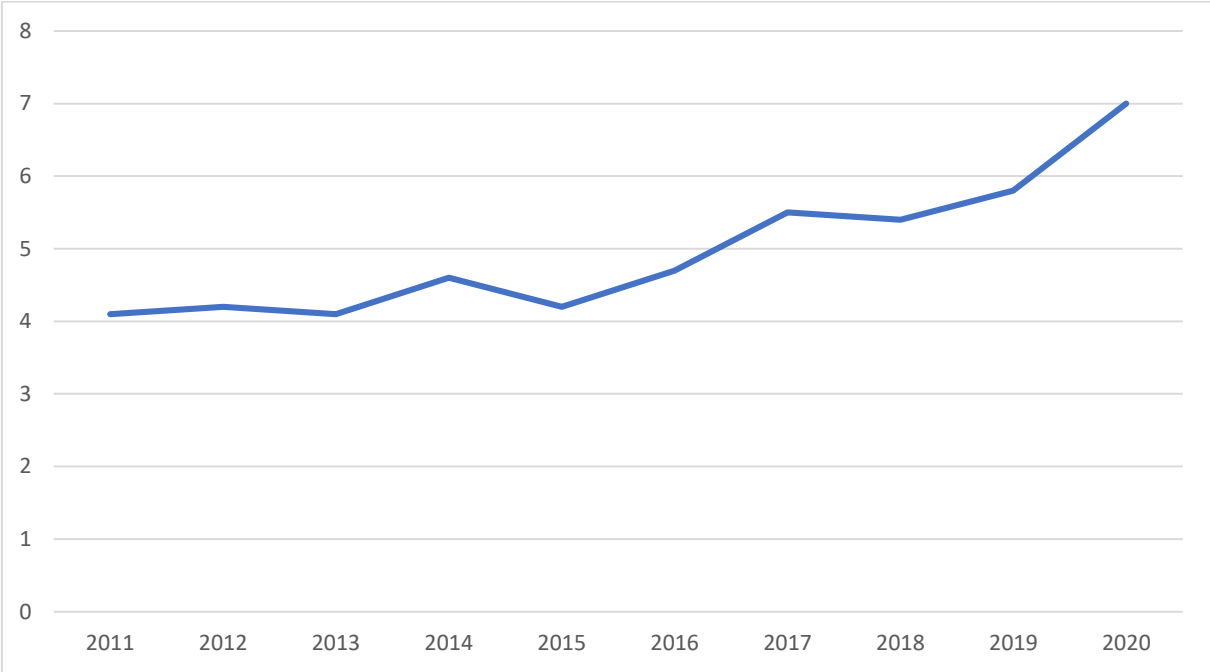
Efficiency	Containing the number of submitted cases	-50%
	Average duration (in months)	-50%

Source: own study

The data analysis shows that one of the greatest problems of the Polish judiciary, namely lengthiness of court proceedings, is getting worse. In 2020, the average duration was almost seven months. In the years 2011-2016, proceedings lasted less than five months. The slower handling of cases in 2020 can be partially explained by the pandemic - in the years 2017–2019 the average duration was around 5.5 months. In this perspective, the deterioration is clear, though not dramatic.

In recent years, the average duration of proceedings in the cases categorized as important from the index point of view, has not been favourable. In procedural civil cases, the duration is on average almost 10 months in regional courts, and in district courts - almost 15 months. Even civil cases, which in principle are simple and heard in non-contentious proceedings, last a long time – the average time in regional courts is about 7.5 months, and in district courts - 10.5 months. Moreover, even the "fast track" in the payment order and writ proceedings means a long waiting time for a decision - five months in regional courts, and even a month longer in district courts. The average duration of commercial proceedings is by no means better - in regional courts it is approximately 13 months, and in district courts it is eight months.

**Chart 2.** Average duration of court proceedings in the first instance court (in months).



*Source: the Ministry of Justice*

In this context, therefore, it comes as no surprise that in recent years the indicator showing the relationship between cases resolved in relation to those submitted in a given year has also deteriorated significantly. Until 2015, the percentage of unfinished cases in the year in which they were submitted to the courts was in the range of 13%-16%. In the following years, it was much above 20 percent. This shows that the undertaken reforms not only do not improve the justice system, but also result in more and more bottlenecks.

**Dimension 3. The rule of law**

Analysis of this dimension is based on the World Justice Project's annual Rule of Law Index, compiled with the use of eight indicators. For the purposes of the country's economic credibility index, two of them are taken into account. The first indicator concerns the extent to which power itself is bound by law, which includes both constitutional norms and institutional measures. The role of independent media and their control function over the authorities are also taken into account. The second indicator is the level of enforcement of legal provisions. Importantly, this category relates exclusively to implementation and enforcement of legal provisions, and does not consider whether the regulations themselves are appropriate. It is therefore a rather narrow understanding of the rule of law.

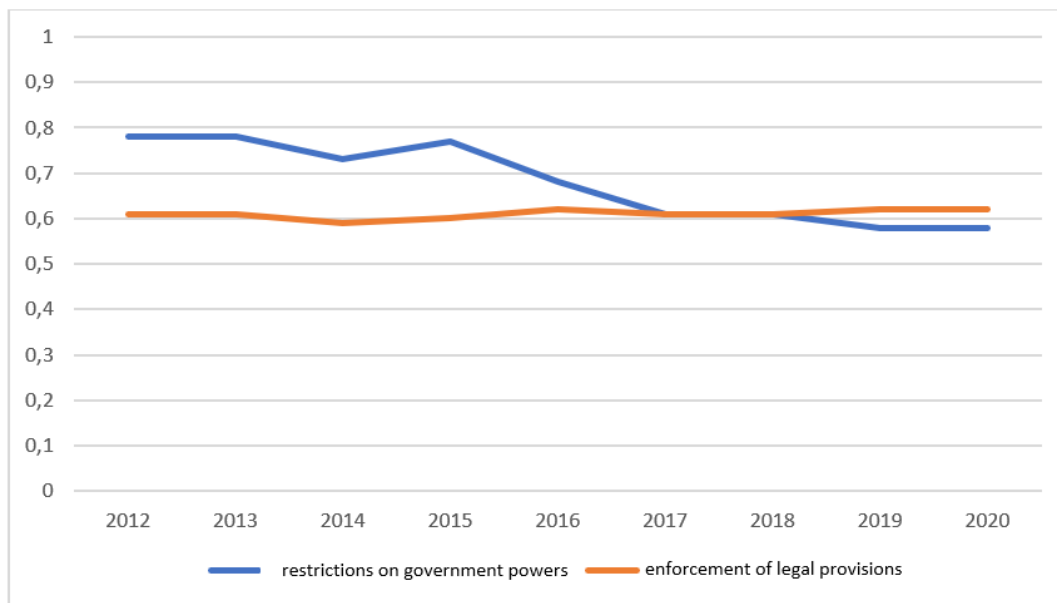
**Table 4.** Weights of indicators in the area of the rule of law (percentage)

The rule of law	restriction on government's powers	60%
	enforcement of legal provisions	40%

Source: own study

Deterioration in this area is also visible. In 2015, Poland's result was 0.71 (on a scale of 0-1), and in 2020 it was only 0.66. We are ranked 28th in the group of 128 surveyed countries. When it comes to limiting the powers of the government, Poland's result is 0.58 (a decrease from 0.77 in 2015) and is only slightly higher than the global average (0.55). However, it clearly differs from the countries of the region (understood as the EU, EFTA, and North America), for which it amounts to 0.75. As for the second aspect - enforcement of legal provisions - Poland's score is 0.62, with a global average of 0.54 and a regional average of 0.72. In this respect, the situation has remained stable over the years (in 2015 it was 0.60).

**Chart 3.** The rule of law



Source: World Justice Project, Annual Rule of Law Index

It is worth checking how Poland scored against other countries in the Visegrad Group. The situation in Hungary appears the worst. Every year, progressive degradation of the rule of law is observed. In the area of binding the power by means of law, Hungary achieved a score of 0.40 in 2020 (Poland 0.58). In 2020, the level of enforcement of legal provisions in Hungary is estimated at 0.47, and in Poland at 0.62. One may conclude that in our country the indicators are at a higher level.

The situation in the Czech Republic is different. This country fares clearly better when assessing whether the authority is bound by law (0.73 as compared to 0.62). The same is true for the law enforcement level (0.71, compared to 0.62 in Poland). The result in the

overall Rule of Law Index in 2020 for the Czech Republic was slightly better - 0.65, while for Poland it was 0.61. Both countries have scored similarly.

#### Dimension 4. Meritocracy

One may find it difficult to imagine an economically credible state, whose functioning would not be based on meritocratic mechanisms (understood as the opposite of nepotism or oligarchy). However, this area is challenging in terms of parameterization. For the purposes of the index, there have been used three indicators. The first one is the number of civil service members. The second indicator is the question of open access to public information, which is determined by the Global Right to Information Rating. The third indicator is the number of notifications of the Supreme Audit Office addressed to the public finance ombudsman about suspected violations of the public finance discipline.

**Table 5.** Weights of indicators in the area of meritocracy (percentage).

Meritocracy	civil service – employment	50%
	Freedom to Information: Right to Information	25%
	Supreme Audit Office – notifications to ombudsman	25%

*Source: own study*

One of the pillars of a credible state are its highly qualified officials who, as far as possible, are not susceptible to political pressure. This role is played by the civil service corps. In recent years, however, no proper development of this element of public administration has been observed. First of all, attention should be paid to the fact that the last two years saw no possibility of obtaining the status of a civil servant by means of passing an examination. There has been set a limit of appointments at the level of the number of graduates of the National School of Public Administration in a given year, who therefore fill all vacancies.

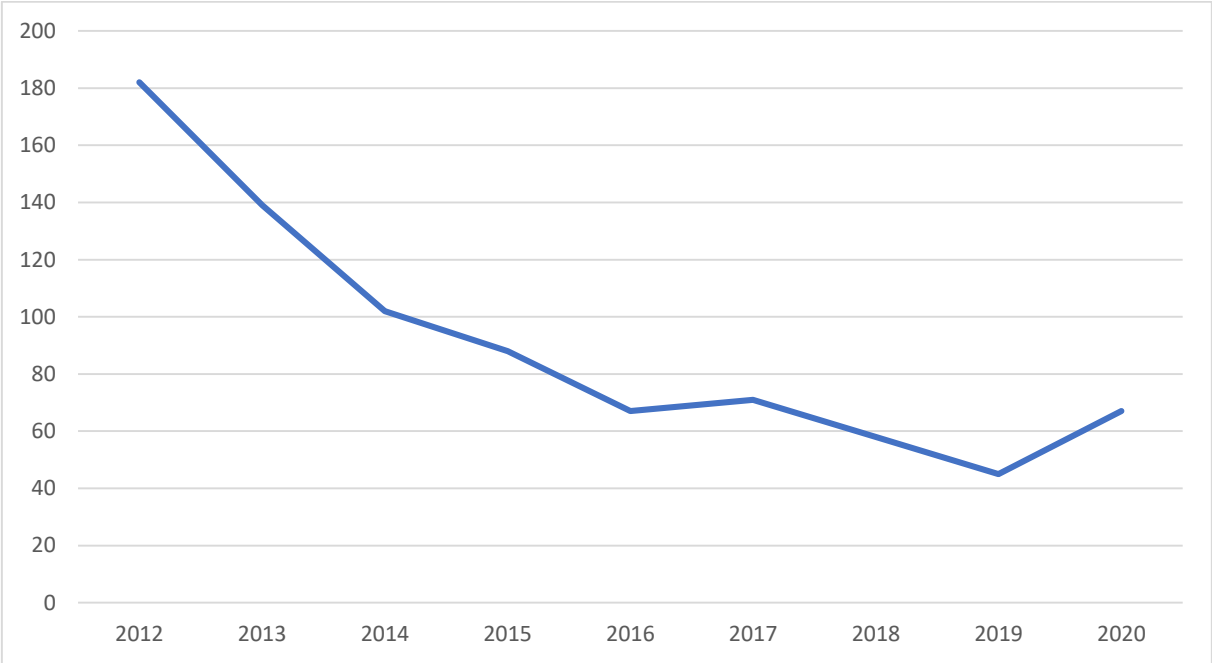
Therefore, a talk about building a strong civil service is challenging if there are only a few dozen of people joining the service each year. Data shows that the total number of civil servants in recent years has remained constant. Without development of this institution - also in terms of numbers - it is difficult to achieve features which are desirable from the point of view of economic credibility of the state, such as: stability, continuity of activities, professionalism, and independence.

The second indicator determining meritocracy concerns universality of access to public information. In the Global Right to Information ranking, our country has obtained a score of 79 points (out of 150 possible) in recent years. This score does mark an improvement in relation to the years 2011-2014, when it scored some 61-62 points. However, it is still difficult to consider such result as satisfactory, the more so as transparency of the actions of public authorities is a necessary condition for its effective control.

One should note, however, that this result is relatively high. The countries of the "old" European Union have even worse ratings: France - 64, Germany - 54, Belgium - 59. The situation looks slightly better in Sweden - 101, in Italy – 85, or the Netherlands - 82.

Comparisons within the Visegrad Group countries place Poland on a moderately good position: Czech Republic - 72, Slovakia - 68, and Hungary - 87.

**Figure 3.** The Supreme Audit Office - notifications to ombudsman about suspected violations of the public finance discipline.



Source: the Supreme Audit Office

The last indicator of the analyzed dimension relates to the activity of the Supreme Audit Office. Applied here is the information on the number of notifications made to the public finance discipline ombudsman about suspected violations of public finance discipline. Recently, this value has been evidently lower than in the years 2012–2014, when it exceeded 100 notifications made each year. The following results were recorded in consecutive years: 2016 – 67 notifications, 2017 - 71, 2018 - 58, 2019 - 45, and 2020 - 67. This suggests a smaller scale of violations of the public finance discipline. But it may also be the result of a lower effectiveness of inspections carried out by the Supreme Audit Office.

**Table 6.** Value of the state credibility index for the area of the rule of law in 2020 and indicators after standardization.

<b>Value of the Credibility Index in 2020 for the area: The Rule of Law</b>	<b>-1.06</b>
Value of the Credibility Index in 2020 for dimension I - legislation	<b>-0.57</b>
Value of the Credibility Index in 2020 for dimension II - efficiency	<b>-3.35</b>
Value of the Credibility Index in 2020 for dimension III – the rule of law	<b>-0.13</b>
Value of the Credibility Index in 2020 for dimension IV - meritocracy	<b>-0.20</b>



## Summary

<b>Standardization</b>	2016	2017	2018	2019	2020
Number of pages of legal acts which entered into force in specific years	6,32	2,27	1,34	1,58	-0,78
Lack of any documentation from consultations at RCL	-0,44	0,00	1,44	1,56	4,22
No reference by the authors to the opinions sent to RCL	1,33	0,00	-0,19	-1,14	-2,95
Management of received documents	0,83	0,41	0,94	2,22	3,35
Average duration (months)	0,07	1,21	1,07	1,64	3,36
Restriction of government's powers	0,00	-0,78	-0,78	-1,11	-1,11
Enforcement of legal provisions	1,33	0,00	0,00	1,33	1,33
Civil service – employment	-0,02		-1,49		-0,33
Freedom to Information: Right to Information	0,00	0,00	0,00	0,00	0,00
Supreme Audit Office – notifications to ombudsman	-0,14	0,00	-0,45	-0,90	-0,14

*Source: own study*

The decline in economic credibility of the state related to the area of the rule of law is largely affected by the deteriorating quality of legislation – chiefly resulting from avoidance of public consultations on draft laws. This cannot be compensated by the greater percentage of drafts, in which the authors responded to the submitted comments. Nevertheless, this is a positive circumstance which should not be overlooked. It may imply that if consultations are in fact taking place, their nature is not a façade one.

At the same time, we are witnessing a significant deterioration in the efficiency of the judiciary system. Unfortunately, proceedings are lengthy - even in the procedures which (in theory) should allow for quick redress. Hence, the implemented reforms of the judiciary have not brought about any improvement.

Poland is not making satisfactory progress in developing a meritocratic approach. Whilst in some cases regional comparisons are in our favour, the absolute numbers point to there still being much room for improvement. This is possible, for instance, in the case of the ease of access to public information. For the purposes of building economic credibility of the state, strengthening the civil service would also seem necessary. Here, unfortunately, the opposite efforts are being observed.

In order to improve credibility of the rule of law, a number of actions in each of the discussed dimensions must be taken. The most important amongst them seems to be preventing avoidance of consultations on draft laws. What could serve here, first of all, is extending an obligation to perform an ex ante impact assessment, also for parliamentary drafts. This is our first recommendation to change the behaviour with a view to increasing Poland's economic value.

Moreover, no improvement of efficiency of the judiciary may be achieved without changing the practice of writing justifications of judgments. These are extremely extensive, therefore, their drafting is burdensome for judges. What is more, such justifications do not fulfill their purpose well, as they are published with a long delay and are usually difficult to understand.

Thus, a significant proportion of the judiciary is engaged in an activity, the usefulness of which is questionable.

It is possible to implement the proposed change to the content and form of justifying judgments in the judiciary environment. What it boils down to is - often informal - criteria for assessing the quality of judgments during the proceedings and assessing the quality of judge's work in promotion proceedings.

The third recommendation is restoring the possibility of obtaining the status of a civil servant by passing relevant examination. This would require a significant increase in the appointment limit. Until 2021, the limit was set at the level of the number of graduates of the National School of Public Administration, which meant that the alternative route to appointment - based on high quality work in the office (experience-based) and on passing the exam - was closed.

### III. Freedom of economic activity

#### Freedom of economic activity as a condition of economic credibility of the state

Freedom of economic activity is one of the fundamental human freedoms. It guarantees the autonomy of human will. It also favours the effective use of production factors. For the economic credibility of the state, it is necessary to maintain a reasonable balance between the freedom of management and restrictions resulting from financing public goods, and the protection of weaker market participants.

Freedom of economic activity is closely related to the institutional component of the social and economic environment, and as such it is an essential condition for development.

For a long time it was believed that keeping order and protecting the markets, in the first place, could justify interference of the state in restricting the freedom of economic activity. However, as the capitalist economy was developing, there was emerging another belief, that interference is also needed to reduce the so-called market failure, i.e. to limit negative external effects or the use of market power by some entities. When describing economic freedom, we can use two perspectives: *sensu stricto* (freedom of: contracts, setting up and running a company) and *sensu largo*, which defines its conditions: external and internal security - national defense and police and market protection (judiciary), favourable macroeconomic environment, healthy money, efficient administration, economy-friendly legislation, including protection of competition. We can also talk about goods producing positive externalities, while financed largely from taxes: research, education, health care, and many other public services. But economic freedom should also take into account a broader context. After all, in the case of a potential investor in the high-tech industry, e.g. electronics or pharmacy, low taxes will not compensate for the shortage of engineers, polytechnic schools or other companies with whom to compete while learning from each other.

Nevertheless, excessive burdens on entrepreneurs and excessive interference with the freedom of economic activity may result in reduced efficiency of markets. These cease to function properly as the relationship between individual effort and benefits resulting therefrom disappears.

In recent decades, research into institutional determinants of economic development has gained increasing importance in the mainstream economics. Reasons of this situation may stem from several circumstances (Marody and Wilkin 2002, Ratajczak 2009, Geodecki 2016):

- development of the economy of transaction costs, symbolically crowned with the Bank of Sweden awards for North (1993) and Williamson (2009);
- analyses of natural institutional experiments resulting in different trajectories of economic and technological growth in capitalist and socialist economies;
- globalization and an increase in investors' demand for information on investment conditions in different countries, which resulted in the development of the system of international institutional indicators;
- limitations encountered by the growth theory while attempting to explain the propensity to pro-social behaviour and investment in new technologies.

From the point of view of the economy of transaction costs, the importance of institutions which protect transactions, and thus the markets in which exchange takes place, should be emphasized. The ease of setting up and running a business, as well as protection of the parties to the transaction (protection of minority investors, time and effectiveness of recovering debts from contractors in courts, etc.) allow for reducing transaction costs and increasing the number of potential partners. Langlois (2003) argues that, as the institutional conditions improve, the scope of market operation increases and the tendency to concentrate subsequent phases of value chains in individual enterprises decreases. In such way, specialization in the economy deepens (Beckmann 2000, Matysz 2003), which significantly boosts efficiency of management. Good institutions, understood not only as organizations, but also norms and customs, extend the scope of freedom of establishing and running a business. Such is, for instance, the principle of respect for private property, originated, among others, by the Judeo-Christian tradition expressed in the commandment "You shall not steal". In some socialist countries, there is no private ownership of real estate, which renders planning activities related to ownership more difficult

Moreover, in the spirit of the economy of transaction costs - along with technological development – there can be observed an increase in the specificity of resources involved in economic exchange. Technical progress, enabling production of more and more advanced products, drives investments in more and more complex production equipment. Transactions between the supplier and the recipient should be appropriately secured. There must also be institutions sanctioning the partner's unfair behaviour. Otherwise, in the face of rising investment costs and no protection, motivation of entities to cooperate would be lower and lower (Williamson 1998). This explains the importance of measurement of quality of market institutions facilitating running a business and market exchange for the assessment of economic credibility of the state in the sphere of freedom of economic activity.

The institutional environment - the analytical level first distinguished by Williamson (2000) determining the amount of transaction costs in the economy - is referred to as the property rights economy. Protection of property is embedded in the logic of a well-functioning market mechanism to such an extent that it is often equated with the economic freedom. It was not only representatives of liberal thought to have come to such a conclusion, although Hayek was the first to appreciate the importance of freedom for welfare in the "Constitution of Liberty" (Polish edition, 2006). Institutional uncertainty prevents individuals from operating, which in turn exerts a fundamental impact on the long-term economic growth and competitiveness of economies. Effective protection of property rights enables technological changes, as stated by Acemoglu et al. (2006):

*Without property rights, individuals will not have the incentive to invest in physical or human capital or adopt more efficient technologies. Economic institutions are also important because they help to allocate resources to their most efficient uses, they determine who gets profits, revenues and residual rights of control. When markets are missing or ignored (as they were in the Soviet Union, for example), gains from trade go unexploited and resources are misallocated.*

Fundamental to the increasing efficiency of economic activity is the issue of resources, the access to which is granted to domestic economic entities. In the evolutionary theory of the company (Nelson & Winter 1982, Alchian 1950), the functions of genes are performed by routine - the ways entrepreneurs operate - and innovations are the equivalent of biological

mutation. The ability of companies to survive is influenced by both the internal adaptability and friendliness of the environment. In Porter's (1990) theory of competitive advantage of nations, of particular importance is the engineering and scientific base. Porter's conclusions were based on, among others, an influential report of the World Economic Forum on competitiveness of national economies (Global Competitiveness Report - Schwab 2015), emphasizing that access to a technological base, as well as basic resources: education or infrastructure, affects the ability of entrepreneurs to increase operational efficiency. In the theories of technological catch-up, particular importance is attached to the administration monitoring the needs of entrepreneurs in this regard (Evans 1995, Amsden 2001, Fagerberg & Godinho 2005). For the system of assessing economic credibility of the state, this means that apart from the quality of institutional environment and freedom of management, access to human capital resources and modern infrastructure is just as important.

### **Analytical dimensions of the area of freedom of economic activity**

The proposed synthetic indicator of freedom of economic activity includes:

- freedom of economic activity in the strict sense based on several groups of international indicators related to the ease and freedom of conducting economic activity and freedom to conclude contracts (a synthetic indicator of the ease of doing business and contracting);
- freedom of economic activity in the broad sense covering, apart from freedom in the strict sense, two subgroups of indicators:
  - institutional conditions for the freedom to conduct business activity and conclude contracts,
  - related to infrastructural conditions and human capital.

The measures adopted for the analysis of the "freedom of economic activity" have been grouped in three dimensions:

1. the ease of doing business - based on the World Bank's Doing Business series indicators;
2. economic freedom - indicators of economic freedom published in the report "The Economic Freedom of the World" by the Heritage Foundation;
3. conditions for running a business activity
  - institutional - the basic ones are the World Bank's Worldwide Governance Indicators,
  - infrastructural and within the area of human capital – adopted as the baseline were the IMD World Competitiveness Yearbook indicators.

Both groups of conditions indicators reflect the concept of positive freedom, the premise of which is the right level of interference enabling functioning of markets. Even the most free-market methods of determining the scope of freedom of economic activity assume that many areas cannot operate without appropriate regulations (e.g. financial market). Similarly, many branches of the economy are not able to function efficiently without good transport

and telecommunications links or without the appropriate level of competences, which employees acquire in schools.

**Table 7. Weights of individual dimensions for the area of freedom of economic activity (percentage)**

	Weight in percentage
Credibility for dimension: ease of conducting business activity	50
Credibility for dimension: economic freedom	25
Credibility in 2020 for dimension: conditions for conducting business activity	25

Source: own study

### Dimension 1. The ease of running a business activity

The positive value of the index describing the ease of running a business activity consists of 10 sub-measures from the Doing Business series, relating to the items listed in Table 8, each having a weight of 10% of the value for the dimension. One may observe that in the years 2008-2020, most of them improved in terms of the ease of running a business activity, with the exception of property registration. As a result, this dimension had a strong positive effect (with a value of 0.39) on the synthetic index for the area (0.21) (see Table 10).

**Table 8. Values of partial indicators of the ease of doing business in 2020 against the 2008–2020 median**

	Weight in percentage	2020	Median for the years 2008–2020
Doing business	10	82.9	82.5
Dealing with construction permits	10	76.4	71.1
Getting electricity	10	82.3	77.9
Registering property	10	63.9	70.5
Getting credit	10	75.0	75.0
Protecting minority investors	10	66.0	66.0
Paying taxes	10	76.4	72.3
Trading across borders	10	100.0	81.1
Enforcing contracts	10	64.4	63.4
Resolving insolvency	10	76.5	68.6
The ease of running a business activity (place in the ranking against the EU-28)	-----	15	13

Dark gray marked fields indicate values below the median, and light gray marked fields indicate values lower than the median.

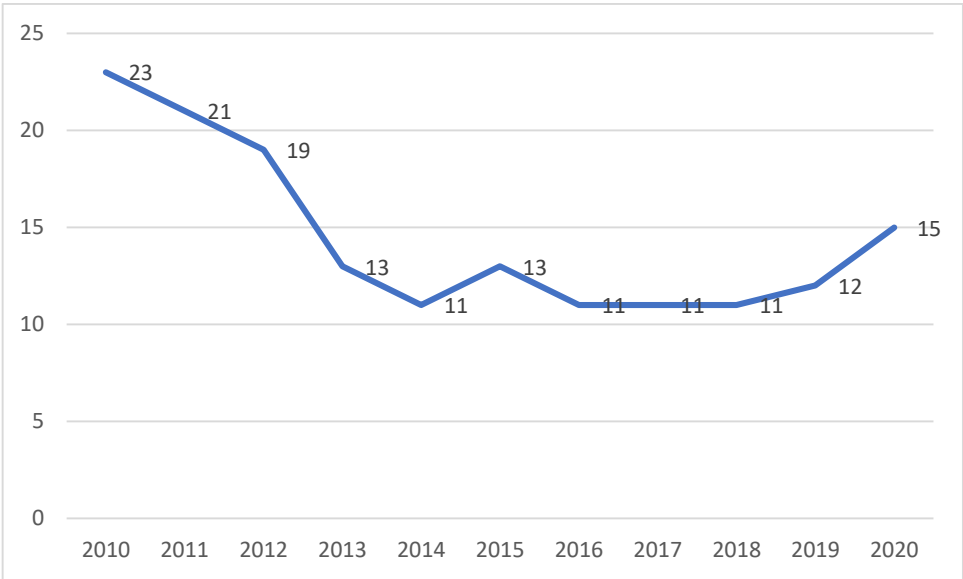
Source: own study

In terms of assessment of the ease of doing business, Poland's position was significantly higher among the EU countries in the Doing Business ranking prepared by the World Bank in the years 2010–2013. It moved from position 23 to 13. In the following years - until 2019 - the positions in the EU-28 ranking ranged from 11 to 13, and in 2020, the total rating of the World Bank gave Poland the 15th place.

Standing behind such dynamics in the assessment were significant improvement by 2015 in most aspects of starting a business, obtaining access to electricity and loanxs, as well as shortening civil proceedings and simplifying bankruptcy proceedings. On the other hand, deterioration of Poland's position in the ranking after 2017 was influenced by the extension of the time of property registration and the time necessary for settlements with the tax authorities, as well as improved positions of other countries in the ranking.

The position of Poland in the 2020 ranking means a regression in comparison with the years 2013–2019, and a marked improvement compared to the years 2010–2012.

**Chart 4.** Places in the EU-28 ranking in terms of ease of doing business, Doing Business, World Bank



Source: own study based on World Bank data

The World Bank's assessment of Poland in the Doing Business ranking seems stable, although marking a noticeable increase in difficulties in establishing and running a business in the last five years.

In September 2021, the World Bank decided to discontinue the Doing Business series due to a controversy over how the value of features is measured in some countries. The Bank

announced development of a new methodological approach under the working name of Business Enabling Environment (BEE) (announced in April 2022).

## Dimension 2. Economic freedom

The positive value for the dimension of economic freedom is shaped by 12 partial indicators from the series "The Economic Freedom of the World", The Heritage Foundation. The weight of each indicator is 8.33 percent (see Table 9). The value of most indicators in 2020 is higher than the median for the years 2008-2020, which translates into a positive value (0.39) of the synthetic indicator for the second dimension and a positive impact on the value of the synthetic indicator for the entire area of freedom of economic activity (0.21) (see Table 7).

**Table 9.** Values of partial indicators of the economic freedom dimension in 2020 against the median for the years 2008–2020

	Weights in percentage	2020	Median for the years 2008–2020
Property rights	8.3	63.1	60.00
Government integrity	8.3	64.6	53.90
Judicial effectiveness	8.3	48.9	49.48
Tax burden	8.3	74.7	74.90
Government spending	8.3	48.8	46.65
Fiscal health	8.3	92.2	86.40
Business Freedom	8.3	62.6	63.30
Labour freedom	8.3	62.0	61.40
Monetary freedom	8.3	82.0	81.05
Trade freedom	8.3	86.4	86.95
Investment freedom	8.3	80	70.00
Financial freedom	8.3	70	70.00
Total economic freedom (place in the ranking against the EU-28)	----	18	18.5

Dark gray marked fields indicate values lower than the median, and light gray marked fields are equal to the median.

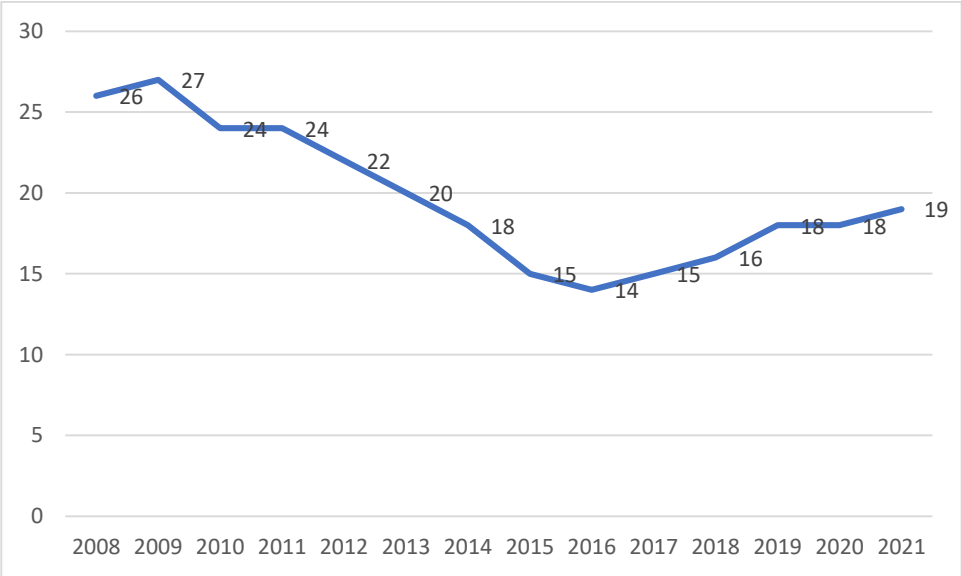
*Source: own study*

In the Heritage Foundation's assessment of economic freedom, a similar dynamics to that in the first dimension may be observed, although accents show slightly different distribution patterns. The ratios of government expenditure to GDP and the condition of state finances has improved, as well as the freedom to invest. In the years 2016–2019, indicators for



property rights, government integrity, and effectiveness of the judiciary deteriorated. The indicators of the freedom to run a business activity (based on the previously discussed assessment according to the Doing Business methodology) and the fiscal freedom expressed by an increase in tax burdens show a marked decline. As a result, the historically best 14th place in the Heritage Foundation's ranking of economic freedom among the EU-28 countries was achieved by Poland in 2016. Until 2019, there had been a slight deterioration, and the years 2020 and 2021 saw an improvement even above the 2016 level. However, the world was not stagnant and in other countries, the improvement was faster - as a result, in 2021, Poland was ranked 19th among 28 European Union countries (see Chart 6).

**Chart 5.** Places in the EU-28 ranking in terms of economic freedom



Source: own study based on "The Economic Freedom of the World" data, Heritage Foundation

**Dimension 3. Conditions for running a business activity**

The negative value of the indicator for the third dimension consists of the values of WGI (Worldwide Governance Indicators - World Bank) and indices calculated for the basic, scientific, and educational infrastructure according to the methodology of the International Institute for Management Development in Lausanne (IMD) used in the "World Competitiveness Yearbook" (WCY) report, each weighing 25 percent in dimension (see table 10). Their total negative value (-0.39) lowers the positive value of the synthetic index for area II - Freedom of economic activity (0.21)

**Table 10.** Values of partial indicators of the third dimension conditions in 2020 against the median in the years 2008-2020, positions in the ranking against the EU-28 and against other countries classified in the WCY

	Weights in percentage	Ranking position, 2020	Median for the years 2008–2020
WGI – Worldwide Governance Indicators*	25	0.78 (22nd out of 28 countries)	0.68
IMD WCY – basic infrastructure	25	0.60 (38th out of 63 countries)	0.60
IMD WCY – scientific infrastructure	25	0.48 (30th out of 63 countries)	0.57
IMD WCY – education	25	0.49 (31st out of 63 countries)	0.41

\* the 2019 issue

Source: own study

Partial indicators making up the WGI synthetic index were created on the basis of opinions of respondents gathered by economic intelligence institutions and are divided by the World Bank into six categories:

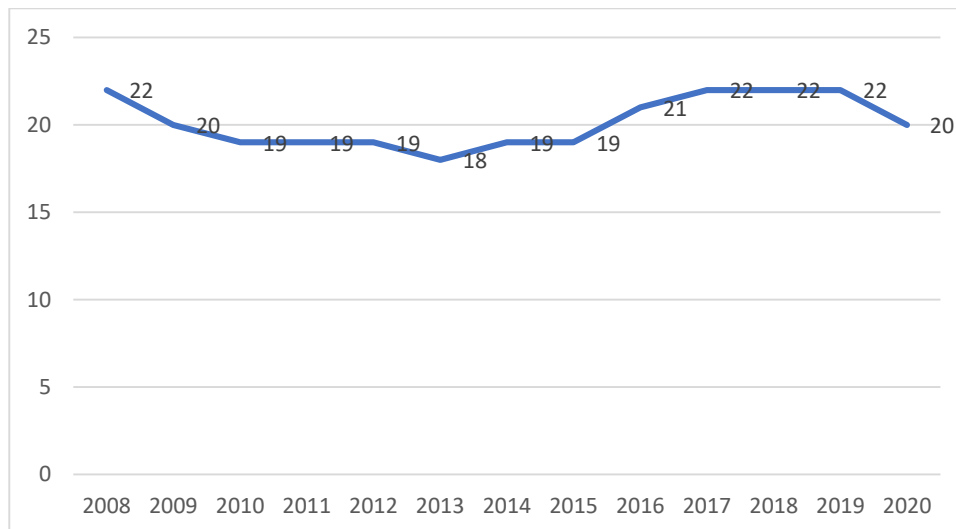
1. Voice and Accountability
2. Political Stability and Absence of Violence/Terrorism
3. Government Effectiveness
4. Regulatory Quality
5. Rule of Law
6. Control of Corruption

In all of them, certain setback has been observed in the last five years. Most of the categories remain at a relatively high level, although for the first three categories there has been slight deterioration in the value of indicators after 2015.

Opinions on the next two ones (the fourth and fifth categories) stabilized after a period of growth until around 2015. The “rule of law” was worst assessed by respondents - here the value of the assessment decreased after 2015 to a level slightly below the 2008 baseline level.

The WGI indicators were determined on the basis of opinions of managers, and these, after all, affect the propensity to invest in a given country. Hence, whatever the reasons for such low ratings, Poland's loss of credibility with regard to the rule of law is a fact. As a result, the collective indicator which we synthesized showed improvement in the institutional environment in Poland, from the 22nd to the 18th position among the 28 EU countries in the years 2008-2015, and then gradual deterioration to the starting position in the years 2016-2020, i.e. in the top 30 (see Chart 7).

**Chart 6.** Places in the EU-28 ranking in terms of Worldwide Governance Indicators, World Bank (compared to the EU-28)



*Source: study developed on the basis of Worldwide Governance Indicators of the World Bank*

Such development of the "rule of law" indicators in the recent years has been influenced by limitation of the judicial independence and weakening of the bargaining position of the business world towards the authorities in terms of regulations, including tax regulations. This has exerted an impact on assessment of the institutional environment in the third dimension, i.e. the conditions for conducting a business activity.

On the other hand, in the analysed period, there was observed an average stable position in terms of infrastructure and education. These define the scope of possibilities for economic entities to freely conduct economic exchange and freely use their competences and knowledge. Their assessment was based on the competitiveness index presented by the Swiss Institute for Management Development in the annual World Competitiveness Yearbook.

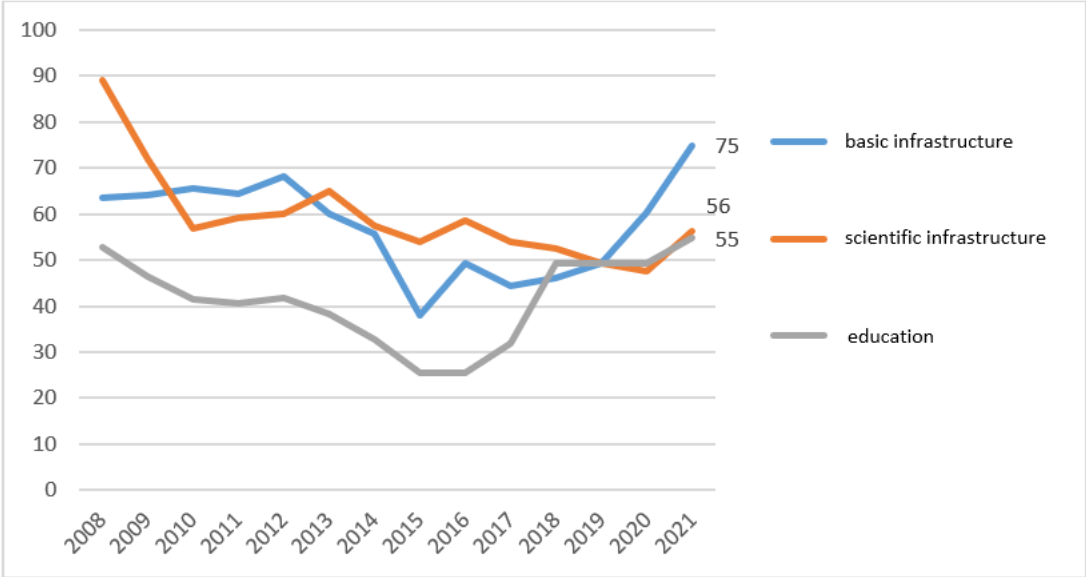
If a total of 100 countries participated in this ranking each time (which would facilitate comparisons over time), in the case of basic infrastructure, the IMD experts would record Poland's initial advance to the 38th position out of 100<sup>1</sup> countries in 2015 and subsequent deterioration in the ranking in which transport infrastructure is analysed : road, rail, and air transport. In the case of scientific infrastructure, Poland would advance from the 89th position in 2008 to the 56th position in 2020<sup>2</sup>. The high position in education has deteriorated - after advancing from 53rd to 25th position in the years 2008–2016, in 2021, Poland was ranked 55th. Chart no 9 shows the position of Poland in the ranking against the evaluated economies per 100 positions. In the 2021 ranking, Poland would be on the 75th, 56th, and 55th positions, respectively, out of the 100 countries assessed<sup>3</sup>.

<sup>1</sup> 24th position among 61 surveyed countries.

<sup>2</sup> This corresponds to a rise from the 49th position out of 55 economies in 2008 to the 31st out of 63 economies in 2020.

<sup>3</sup> In reality, slightly fewer countries and a different number from year to year were assessed. Therefore, in order to make the data clearer, the position of Poland in relation to 100 countries was recalculated.

**Chart 7.** Poland's position in the ranking in terms of selected aspects of competitiveness, World Competitiveness Yearbook, IMD (in relation to the countries included in the ranking and converted into 100)



Source: own study based on the World Competitiveness Yearbook data, IMD

The synthetic result for the entire area is 0.21 and is positive, which means that the 2020 result was slightly better than in the entire period 2008–2020.

**Table 11. Synthetic value of the economic credibility index of the state and its dimensions**

<b>Value of the economic credibility index of the state in 2020 for the area of freedom of economic activity</b>		<b>0.21</b>
Credibility for the ease of running a business activity dimension		<b>0.39</b>
Credibility for the dimension of economic freedom		<b>0.39</b>
Credibility in 2020 for the dimension of conditions for running a business activity		<b>-0.32</b>

### Summary and recommendations

In the last few years, economic credibility of the state in the area of freedom of economic activity has gradually deteriorated, although it still remains positive compared to the median of the years 2008–2020. The reasons for this tendency vary depending on the area in question, therefore, the recommendations below relate to all three dimensions.

- There is a need to monitor the situation related to deteriorating conditions of property registration, as well as the expected difficulties in paying taxes, resulting from implementation of new tax rules in 2022. Assessment of the ease of doing business in the context of the World Bank's works on developing a successor to the Doing Business methodology requires an update.
- In the case of the analysis of economic freedom, two components require corrective action - these are effectiveness of the judiciary and the tax burden on entrepreneurs.
- Measures aimed at rebuilding credibility of the rule of law, as well as strengthening investments in infrastructure, especially in transport, are recommended.

Changes in the environment taking place in the years 2020–2022, which are still poorly reflected in the presented summaries, have brought about further threats to freedom of economic activity. Few entrepreneurs consider the 2022 income tax reform to be beneficial. During the pandemic, the unresolved dispute over the rule of law was followed by further closures in some sectors of the economy, sometimes made overnight and based on non-transparent criteria. High inflation and uncertainty associated with the war in Ukraine have made planning difficult. But other economies are also experiencing these perturbations, therefore, Poland's position in international rankings does not have to decline. However, from the perspective of entrepreneurs, a talk about improved conditions for doing business is difficult.

## IV. Credibility of public finances

### Credibility of public finances and economic credibility of Poland

Public finances are phenomena, processes, and institutions related to the accumulation and distribution of public money at the disposal of public authorities and used for the performance of the state's functions. Public finances are present in almost all areas of the state's functioning, they concern all citizens as taxpayers and beneficiaries of transfers as well as public goods and services.

Credibility of the state and that of public finances are close-knit. Where trust in the state towards the authorities is low, trust in the system of public levies and in the fulfillment of tax obligations drops accordingly. What is more, if public finances are not transparent, trust in institutions handling public finance management is also low, whilst doubts as to effectiveness of spending public money are growing.

What is happening in a country in the public finance area is also observed beyond its borders. Financial markets and rating agencies take on a different perspective for assessing credibility from that of international institutions. The European Commission, of course, has a specific assessment perspective, which ensures compliance with the Stability and Development Pact (i.e. European fiscal rules) and coordination of the economic policy at the level of the entire European Union.

The term "fiscal credibility" does not have a single and precise definition. It is directly related to expectations towards public debt sustainability. An important condition for ensuring fiscal credibility is that the ratio of public debt to GDP does not threaten the intertemporal fiscal solvency of the government (Blanchard and Cottarelli 2010).

"The level of public debt is considered safe if the government may be expected to be able to reduce such public debt or at least stabilize it in most circumstances - including those permanent or persistently unfavourable - using the fiscal policy and without resorting to insolvency, increased inflation (inflation tax), or restructuring debt." (Dudek, Kotecki, Wojciechowski 2021). Public debt should be at such level that there remains fiscal space enabling one's actions in the event of unexpected circumstances, so as to protect important state interests. For instance, we must ensure such fiscal space to deal with the pandemic or threats to internal or external security. This means that the fiscal capacity of the state should not be absorbed to the maximum, but a safety margin in case of unforeseen circumstances will be ensured at all times.

Determining the safe level of public debt uses three basic elements:

- maintaining the government's solvency,
- a politically, socially, and economically viable fiscal policy path enabling return to lower levels of public debt,
- sound foundations for economic growth.

The lack of economic credibility of the state may lead to permanent imbalance in public finances, and eventually to loss of solvency and a financial crisis. This drives up the likelihood of socially "painful" cuts in spending and higher taxes, an economic crisis, recession, higher unemployment, and inflation, and ultimately a decline in social welfare.

For construction of the index, there has been applied a broader concept of credibility of public finances than the macroeconomic approach described above, i.e. "fiscal credibility" or the external perspective or the perception of financial markets and rating agencies. It is necessary to take into account the internal perspective, i.e. the point of view of citizens. Here, transparency of public finances, openness, social control and civic participation in the budget process are crucial aspects. Transparency and predictability as well as the complexity of the public levy system are great importance.

There are authoritarian, undemocratic countries, with sound finances based on monopoly, often on raw materials. Such countries may have a low probability of insolvency, high ratings, low debt, or low debt servicing costs. But their public finances are not transparent, nor are they subject to parliamentary and social scrutiny. This leads to the instrumental use of finance for political purposes, and results in low efficiency of spending public funds and wastage. As a result, it leads to the loss of social trust in the state and the public finance system, and fosters low tax morality.

### **Dimensions of the analysis in the area of public finances**

Economic credibility of the state with regard to public finances has been analysed in four dimensions:

1. assessment of fiscal credibility by financial markets;
2. condition of public finances;
3. quality of fiscal rules, quality and transparency of the public finance system;
4. transparency, predictability, complexity, and efficiency of the public levy system.

Each of these four dimensions in Poland's economic credibility is treated as a sub-index having the same weight - 25 percent.

### **Dimension 1. Assessment of fiscal credibility by financial markets**

This dimension is defined by three indicators:

- country's average credit rating,
- five-year CDS contracts,
- the difference of the domestic long-term interest rate to Germany.

Equal weights were adopted for these three measures describing the perception of fiscal credibility by the financial markets included in this area (1/3).

The country's average credit rating from the major rating agencies: Moody's, Standard & Poor's and Fitch. Each of the agencies codes their ratings using letters, but on a slightly different scale. According to these three agencies, the credit rating of Poland's long-term government debt in a foreign currency is A2, A- and A-, respectively. Therefore, the rating scales of these institutions are standardized on a linear scale from 1 to 21, with 1 being the lowest rating and 21 the highest. Next, a single average rating was calculated. Currently, the unified rating for Poland is 15.3 points out of 21, which is approximately 73% of the highest rating, e.g. that of Germany. The standardized average rating is sourced from the IMF database (Kose et al. 2017). For the purposes of this analysis, the percentage of the highest rating is used.

The purpose of ratings is to assess solvency of the country. The lowest rating score means the country is insolvent, that is bankrupt. The highest rating score stands for high credibility and certainty of investing in Treasury debt securities.

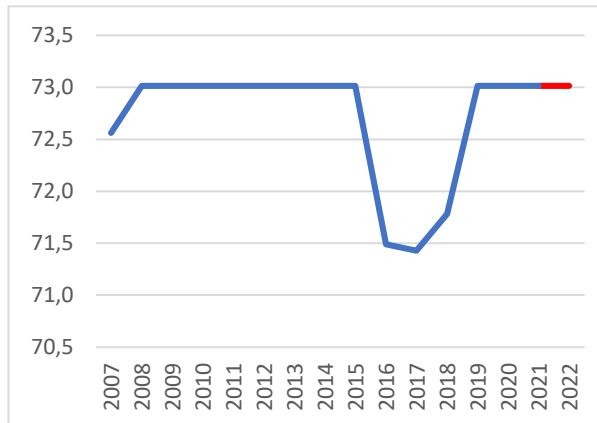
The attitude towards credit rating agencies is stable. It has remained at a similar level since 2016, although at that point it was lowered.

Credit rating agencies conduct regular assessments and therefore the analysis should be supplemented with current market indicators. The first such indicator is the current valuation of five-year CDS (Credit Default Swaps) contracts, which allows for comparing probability of losing financial liquidity in a given country. The second indicator is the difference between the domestic long-term interest rate and Germany, i.e. spread of 10-year Polish bond yields to German bond yields.

Both of these indicators have remained stable or improved in recent years; however, the available data for 2022 shows abrupt deterioration. The five-year CDS contracts more than tripled: from approximately 40 basis points (bps) to over 140 bps in the third quarter of 2022. Greater relative growth was recorded only in Russia, which is a de facto bankrupt. The price level of CDS contracts is in the top ten of the listed countries. However, such a strong increase is a dangerous signal. An average growth of the spread to German bonds was from the level of 230 bps in 2021 to approximately 500 bps at the end of July 2022 (in July, the spreads were seen to break even at the level of 620 bps).

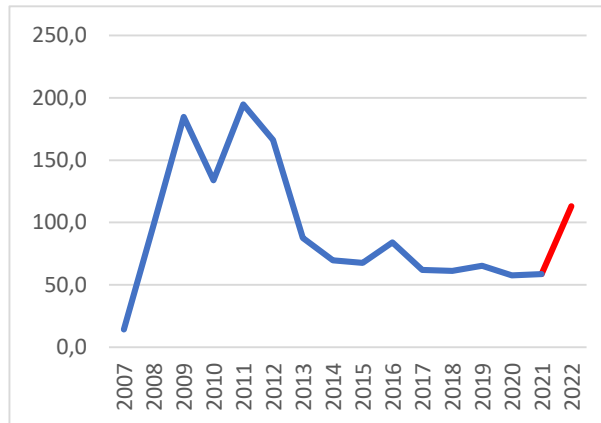


**Chart 8.** Country averaged credit rating (highest = 100)



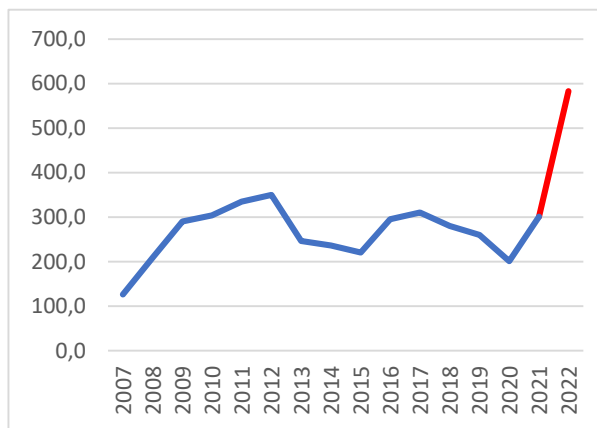
Source: IMF.

**Chart 9.** Five-year CDS (Credit Default Swaps) contracts in bps



Source: IMF and worldgovernmentbonds.com.

**Chart 10.** Spread of 10-year bonds against Germany (bps)



Source: EUROSTAT and worldgovernmentbonds.com

\* Figures 9 and 10 for the year 2022 assume the July 2022 values.

In 2021, financial markets read fiscal credibility in positive terms, agency ratings were stable, and so were CDS, although spreads had already increased. However, the beginning of 2022 heralded significant deterioration in the indicators of this dimension. Ratings remained stable, but rating agencies would list numerous risks. If the values of CDS and spreads remain at the current level or deteriorate, the economic credibility in terms of market perception will worsen in relation to 2021.

## Dimension 2. The state of public finances and deviation from the EU rules

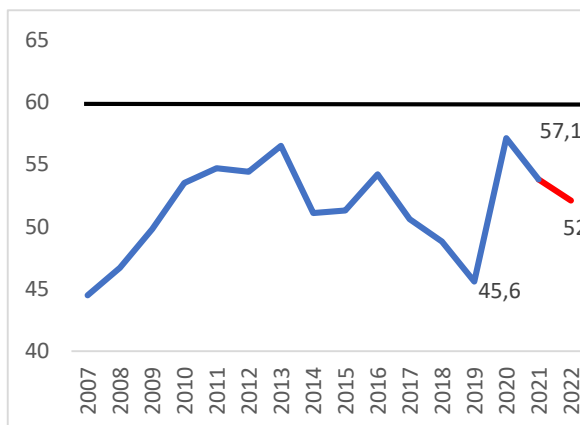
In this dimension, there were adopted six indicators:

- public debt - as a GDP percentage,
- nominal result - as a GDP percentage,
- structural result - as a GDP percentage,
- deviation of the nominal deficit from 3% of GDP,
- deviation of the structural deficit from 1% of GDP, and
- Excessive Deficit Procedure (EDP).

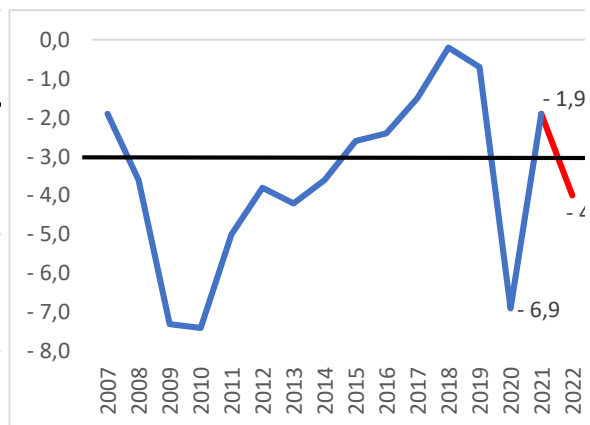
The individual components were given the same weights (1/6).

When analyzing the nominal and structural deficit, deviations from the reference value (in percentage points - pp.) were assigned a zero value if the variable did not exceed it, or when the value exceeded zero, the square deviation was calculated.

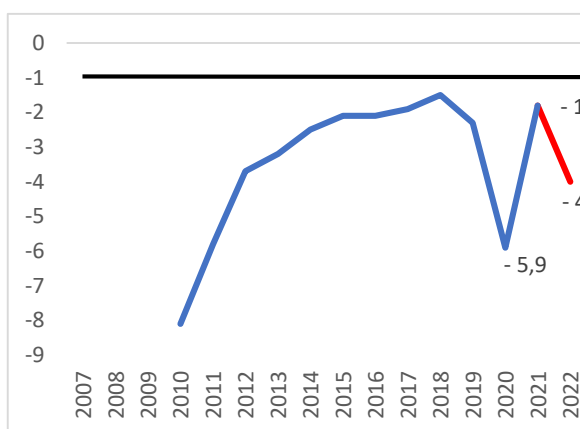
**Chart 11.** Public debt - ESA2010 (percentage of GDP)



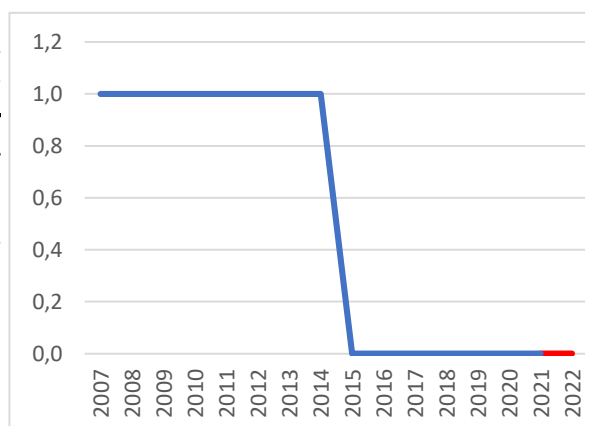
**Chart 12.** Nominal deficit (percentage of GDP)



**Chart 13.** Structural deficit (percentage of GDP)



**Chart 14.** EDP procedure (1/0)



In 2020, the deficit and public debt increased significantly as a result of the pandemic. The nominal deficit exceeded the reference value of 3%, while the structural deficit was also above the medium-term budgetary objective (MTO = 1%). However, the European Commission applied a general exit clause for all countries, i.e. the excess was possible and the Excessive Deficit Procedure was not implemented. The debt did not exceed 60%. In 2021, the deficit decreased and was less than 3%. However, the structural deficit exceeded 1%. According to forecasts of the European Commission, in 2022, the structural deficit in Poland will double.

In 2021, the value of the index related to the condition of public finances and deviation from the EU rules was positive. According to the forecasts and assumed increase in the deficit, in 2022, this value is likely to deteriorate.

### **Dimension 3. Quality of fiscal rules, quality and transparency of the public finance system**

In this dimension, there were adopted five indicators:

- standardized fiscal rules index,
- debt beyond parliamentary control - indicator (percentage of debt according to ESA),
- difference between the national deficit and deficit according to the EU methodology (percentage of the central sector deficit according to ESA),
- use of bonds instead of subsidies (percentage of the central sector deficit according to ESA),
- Open Budget Survey OBI - public finance transparency index.

Equal weights (1/5) were assumed for the five indicators included in the analysis of this dimension.

A synthetic index of fiscal rules calculated by the European Commission. This indicator analyses fiscal rules in all countries and describes their legal status. It assesses to what extent the rule is applied to the flows across the entire public finance sector, and to what extent – it is not. In other words, for example, what percentage of expenditure of the entire public finance sector is subject to the expenditure rule and what percentage of the entire public finance debt is subject to the debt rule, etc. The last available value of the index applies to 2019, therefore, this value was assumed as a constant for the years 2020 and 2021.

In order to determine the quality of fiscal rules and transparency of the public finance system, the scope of compliance with the public debt rule and issue of circumventing the expenditure rule and the state budget result were measured.

In Poland, public discussion concerning the budget focuses on financial parameters of the state budget, i.e. the category established each year by parliamentary law. An average recipient may be inclined to think that the state budget covers the entire state finances, but in fact it does not. Moreover, it reflects less and less the condition of public finances in general, being the result of various activities, the consequence of which is diminished transparency.

The state budget consists of central entities exclusively, mainly ministries, which perform important public functions, but this does not constitute the entire sector of state finances. The central budget itself does not include, among others, local government units, health fund, social insurance fund, and many other elements of the public finance sector. In recent years, however, the state budget has not even covered all of the "central" entities. What is more, there were established several units and funds, each having billions of zlotys' worth at their disposal, but not included in the state budget and therefore beyond control of the parliament.

Therefore, as an indicator describing transparency of public finances, there was used the difference between the state budget balance and the result of the central sector according to the European methodology (ESA). Importantly, this measure is calculated for all EU countries. In the years 2020 and 2021, the central sector deficit, not included in the state budget, accounted for approximately half of the real central sector deficit. And according to the government's plans, in 2022 it is to reach 72 percent. It is as if the government were to receive a discharge of 1/4 of central finances.

Transparency of national finances is also measured as the debt difference between the values measured according to the national methodology and the EU ESA 2010 methodology. It shows the scale of debt in entities and funds spending public money outside of the parliamentary scrutiny. This debt falls outside of the constitutional definition of debt. Recently, the scale of debt beyond the constitutional definition has significantly increased, and at the end of 2021 almost one-fifth of the debt fell beyond the debt definition.

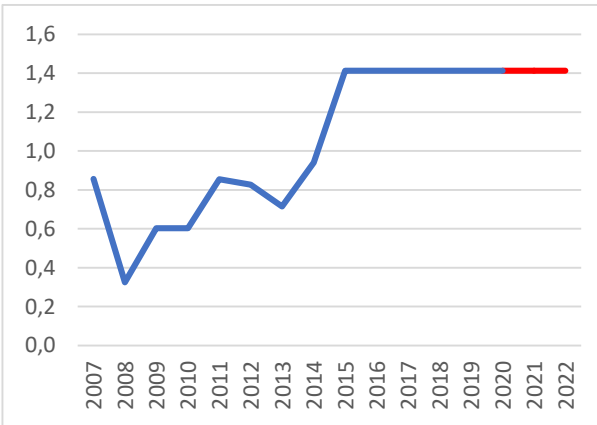
An indicator of circumventing the expenditure rule and the state budget is the practice of handing out treasury bonds. It consists in issuing treasury bonds, only to be transferred to other entities of the public finance sector, instead of subsidies (the Supreme Audit Office 2021, 2022). Such activity lowers the state budget results and enables the expenditure rule to be circumvented if the bonds were received by institutions whose expenses were not related to it. In 2021, bonds were given to the public media as part of allegedly compensating for low revenues from radio and television subscription. The situation is bizarre: individual public media entities, for example Radio Koszalin, receive a pool of treasury bonds from the State Treasury: these institutions must set up brokerage accounts for servicing the bonds, they must incur additional costs, the bonds should then be monetized (sold), and the money obtained from this sale is spent on the statutory purposes of these entities. In the past, these operations would be performed with the use of ordinary budget subsidies. The number of entities receiving hidden subsidies in this form is growing

rapidly. These include universities, the Polish Baltic Shipping Company, the National Media Institute, the Central Communication Port, and more recently, Polish mines. An administrator may receive the bonds only with a view to cashing them immediately and spending so obtain cash on public purposes. As a result, the state budget does not reduce its expenses by the value of these bonds. (Dudek, Kotecki, Kurtek 2022).

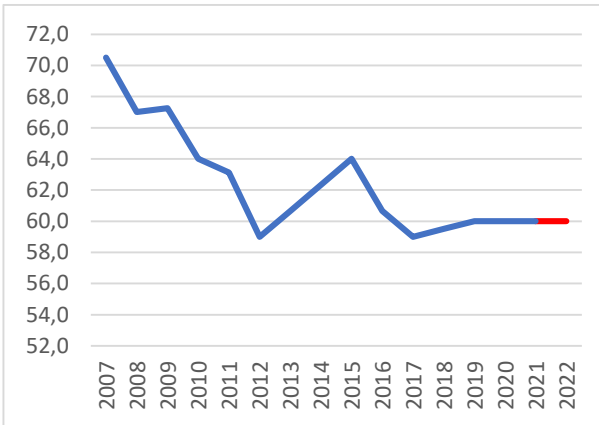
This practice distorts the image of public finances, even in the case of a more narrow approach to the national methodology. The ratio of the budget deficit and the State Treasury debt is subject to disintegration. In addition, such procedure creates additional costs for entities receiving bonds, generates extra costs of debt management on the part of the Ministry of Finance, because the Ministry has to divide these issues into various types of instruments so as not to disturb the functioning of the market. And the entities involved almost immediately dispose of these bonds. This is a curiosity unheard of anywhere in the world. The scale of this practice is already huge, and it is growing. In 2020, the value of these operations was PLN 18.3 billion, in 2021 it reached the level of PLN 22.3 billion, and in the first half of 2022 these emissions amounted to almost PLN 10 billion. In 2021, 'handed out bonds' accounted for almost half of the central sector deficit.

For the purpose of developing Poland's economic credibility, also used was the Open Budget Survey (Open Budget Index as part of the Open Budget Survey conducted by the International Budget Partnership). It is a study which assesses whether governments provide the public with access to budget information and the opportunity to participate in the budget process at the national level. The survey also looks into the capacity and independence of formal regulators. Obtaining data for the study is possible thanks to IBP's collaboration with civil society partners across 117 countries.

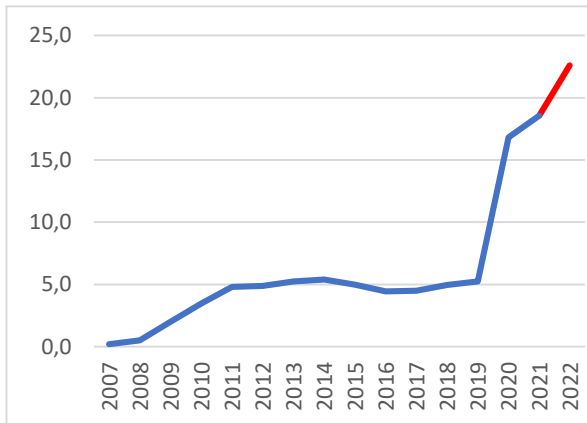
**Chart 15.** Index of fiscal rules (EC)



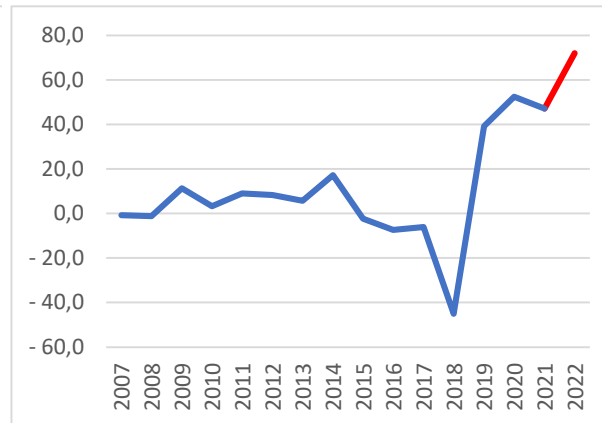
**Chart 16.** Open Budget Index



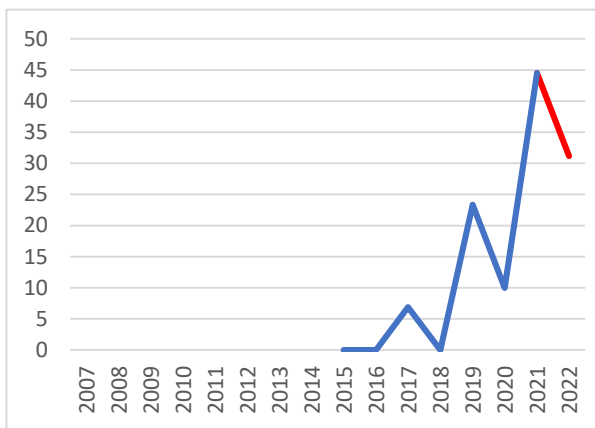
**Chart 17.** Debt beyond parliamentary control (percentage of debt)



**Chart 18.** Deficit outside of the state budget (percentage of deficit)



**Chart 19.** Bonds distributed instead of subsidies (percentage of deficit)



Sadly, the quality of fiscal rules and quality and transparency of the public finance system have decreased. Circumventing the existing fiscal rules and creating extra-budgetary funds have limited transparency of public finances, and thus credibility of their management.

#### **Dimension 4. Transparency, predictability, complexity and efficiency of the public levy system**

The state's credibility is low when the levy collection system is complex, non-transparent, and unpredictable. Taxpayers do not trust the state if they do not understand the tax system. A destructive spiral then forms. The lack of trust in the tax system is conducive to the low tax morality. Tax compliance is low, and tax gaps remain high. As a result, the oppressiveness and complexity of the tax apparatus grows, and this lowers already diminished confidence in the tax system. Frequent changes to the tax law, introduced by surprise, without proper consultation, also aggravate the negative phenomenon.

Three indicators were used to describe the predictability, complexity, and efficiency of the public levy system:

- index of international tax competitiveness,

- Grant Thornton Law Barometer within the area of tax laws,
- Paying Taxes index.

The lack of legal predictability is a significant problem, hence this component has been assigned a weight of 50%, whereas the other two components have a weight of 25%.

The International Tax Competitiveness Index is developed by the Tax Foundation (ITC - International Tax Competitiveness Index). In the last edition of 2021, Poland took the 36th place out of 37 OECD countries (Bunn, Asen, 2022). The system's complexity was rated the worst, although the index had been published before the changes introduced as part of the Polish Order.

Information on the volume and volatility of tax law is contained in the Grant Thornton Law Barometer study. In 2021, the number of adopted pages of tax laws was 269 pages, that is a fewfold more than in 2020, when 95 pages of tax regulations were passed. This is one of the three highest scores in the last three decades (Grant Thornton, 2022).

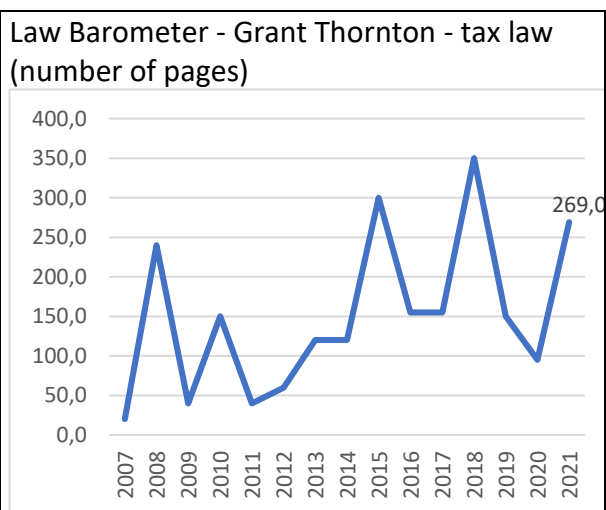
Used for creating the index was also the tax component of the Doing Business study, i.e. the Paying Taxes component. This index measures, among others, time consumption of fulfilling tax obligations. Computerization did reduce the time necessary for fulfilling tax obligations, nevertheless, we still do not perform well compared to other countries.

Overall, credibility related to the quality and transparency of the tax system was negative and 2021 saw it deteriorate even further.

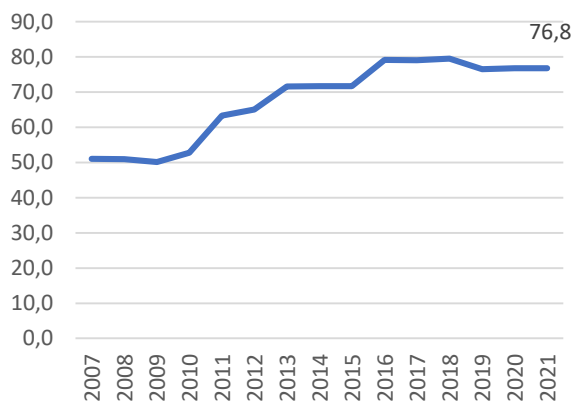
**Chart 20.**



**Chart 21.**



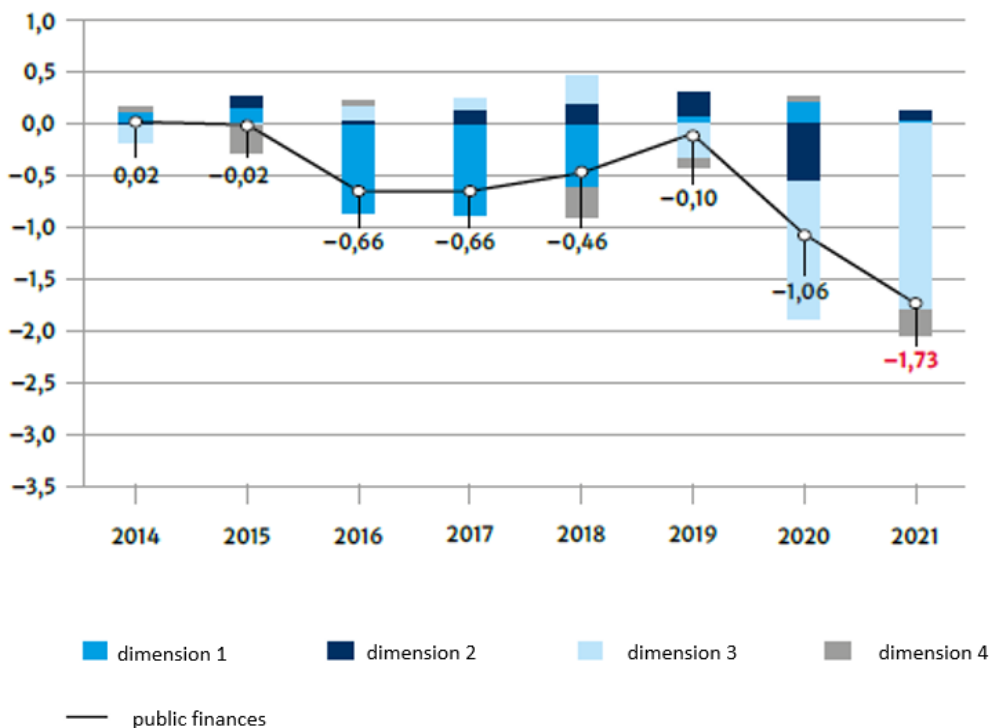
**Chart 22.** Paying Taxes index (pp, index)



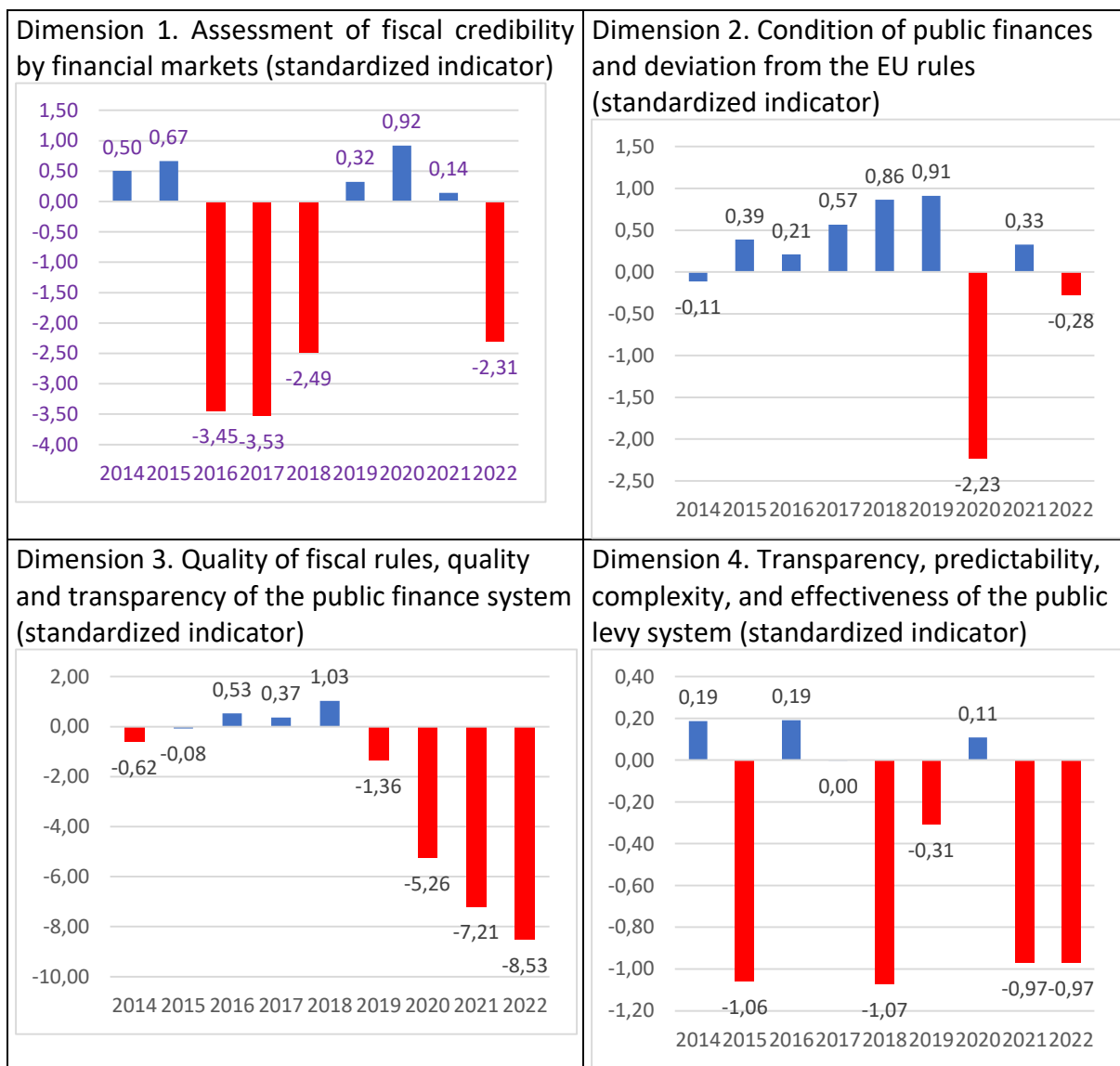
Source: World Bank

Last year marked deterioration of credibility of the state with regard to public finances. The credibility index was minus 1.73 against minus 1.06 in 2020. While the perception by the markets was positive until 2021, transparency of public finances worsened, taxes became more complex, and the international competitiveness of the tax system decreased. In 2022, the current trends and data in all areas taken into account, credibility will be negative, and the indicator for the area of public finances may drop down to approximately 3 points.

**Chart 23.** Value of the index of economic credibility of Poland related to the credibility of public finances







**Table 12.** Weights of individual indicators in areas and weights of aggregate indicators

Dimension	Weight of dimension (in percentage)	Indicator	Weight of indicators in the dimension (in percentage)
Assessment of fiscal credibility by financial markets	25	Country's average credit rating from the top three rating agencies	33
		Five-year CDS contracts	-33
		Long-Term Interest Rate Spread (to Germany)	-33
Condition of public finance	25	Public debt (percentage of GDP)	-17
		Nominal deficit (percentage of GDP)	17
		Structural deficit (percentage of GDP)	17

		Deviation of the SFP nominal deficit from 3% (square)	-17
		EDP (0/1)	-17
		Deviation of the structural SFP deficit from the MTO (1%)	-17
Quality of fiscal rules, quality and transparency of the public finance system, disintegration of public finance	25	Standardised fiscal rules index	20
		Public Finance Transparency Index Open Budget Survey> OBI	-20
		Debt beyond parliamentary control - indicator – debt percentage)	-20
		Difference between the national deficit and the deficit according to EU methodology	-20
		Bonds instead of subsidies – debt percentage	-20
Quality, transparency of the tax system	25	International Tax Competitiveness Index	25
		Law Barometer - Grant Thornton - tax law	-50
		Paying Taxes index	25

## Recommendations

In order to increase economic credibility of Poland, resulting from the condition of public finances, numerous actions must be taken. The first, immediate step aimed at restoring credibility of public finances (but not entailing any costs) is to restore their transparency:

- introducing an obligation to publish in the budget law financial plans of all units of the public finance sector in accordance with the EU methodology scope,
- introducing an obligation to publish detailed information on the application of the expenditure rule in the budget law,
- when presenting the budget, the deficit of all of the public finances should be disclosed, i.e. the deficit of the entire central budget (including funds, agencies, and other units) as well the deficit of the social security subsector,
- creating a public register of public finance sector entities along with financial information thereof, including information on employment and wages,
- creating a register of public levies.

Ultimately, a need arises for a comprehensive institutional and organizational reform of public finances, aimed at reducing funds, agencies, and redefining the "state budget" towards "the budget of the entire central sector" so that the government receives a full and faultless discharge.

The second action should be to seal and protect against tampering with fiscal rules:

- introducing to the constitution of a definition of public debt consistent with the EU methodology,
- sealing the stabilizing expenditure rule so that it covers all expenditure transactions recognized by the European methodology,

- covering the procedure of "handing out" Treasury bonds within the scope of the rule, i.e. treating them as subsidies (expenses),
- introducing the requirement to approve changes in fiscal rules by 2/3 of the parliament and having the exit clause from fiscal rules based on emergency states specified in the constitution, entering the state of epidemic into the constitution.

The third recommendation is appointment of a politically independent fiscal council, where prominent roles would be given to representatives of science and society with broad competences to assess and monitor all parameters and data within the area of public finances.

In addition, it is necessary to introduce a code and rules for introducing changes in the tax and contributions system, with a view to limiting frequency of changes in taxes and minimum vacatio legis, as well as enforcing an appropriate and reliable consultation process. Just as necessary is evaluation of the system for transparency and complexity. Simplification of the tax and contributions system is essential.

## V. Financial and monetary stability

### **Relationships between financial and monetary stability and economic credibility of the state**

Recognizing price stability as the primary goal of the central bank has been the canon of the monetary policy since the 1980s (Ciżkowicz, Rzońca 2011). Spells of high inflation usually coincide with periods of the deepest economic slumps. But inflation is not only costly when it is high. Its negative impact on economic performance has been confirmed by numerous empirical studies, including those carried out for countries where inflation has always been low (Ciżkowicz, Rzońca 2013). Inflation drives uncertainty and discourages investment, as well as it worsens investment effectiveness. There is no economic justification for allowing inflation, especially high inflation, and therefore the monetary stability should be treated as a measure of the state's predictability, without which the state cannot be considered credible (Fischer 1993).

It is impossible to ensure monetary stability without a stable financial sector – if for no other reason than because in a modern economy the banking sector is responsible for 80%-90% of the total money creation. A stable financial system in itself has a positive effect on the long-term economic growth. It lowers the cost of investing in profitable projects. It helps to improve supervision over cost-effective implementation of investments, and reduces its cost. It facilitates risk management by dispersing it and allowing investors to quickly withdraw from their investments. It is able to mobilize high capitals for the needs of investments, which can often be realized only in full or not at all. It makes it easier to launch a business as it reduces dependence of potential entrepreneurs on their wealth. Finally, it lowers the cost of concluding transactions thanks to the development of the payment system (Levine 2005).

If credibility of the state's conduct towards financial and monetary stability is questionable, it is difficult for the state to ensure such stability. In particular, it cannot stabilize expectations of economic agents. Meanwhile, these are important both for inflation and stability of the financial system. If, on the other hand, the state is credible, it is able to manage expectations (Blinder et al. 2008). Of course, there is always a risk that households and businesses will misinterpret communications of the state. If, however, such communications are clear, the risk is reduced.

The importance of the state's credibility with regard to financial and monetary stability has increased after the 2008 global financial crisis, the 2020 pandemic, and Russia's aggression against Ukraine (Blinder et al. 2017 or Coenen et al. 2017). First, these shocks have increased economic uncertainty, understood as a situation where a given economic choice may bring about different outcomes depending on the circumstances, to which households and companies are unable to assign objective probabilities (Bloom 2009). In such environment, the state's policy affecting efficiency of capital allocation in the economy should be as predictable as possible. Secondly, the scale of these turmoils was exceptionally large. The first two prompted many countries to take unconventional measures in relation to the financial system and in monetary policy. Implementing such measures requires reliable communication with the environment. States should strive to dispel fears of powerlessness. However, they should not give the false impression that they are able to solve all the problems revealed or caused by a crisis, pandemic, or threat of war. When the state acts unconventionally, it should explain the need for such measures or the manner of their implementation, present potential results and indicate the time of exit from unconventional policies. Without this, further

uncertainty looms (Meltzer 2014 or Taylor 2014), especially since households and companies cannot benefit from their experience. Thirdly, unconventional measures in the area of the financial system and monetary policy may incur additional costs (Rzońca 2014). They help to maintain zombie companies, i.e. enterprises unable to meet their liabilities, and thus hinder reallocation of capital and labour (Ciżkowicz et al. 2019). If they delay restructuring, they will prolong uncertainty as to the timing, scope, and effects of restructuring, while limiting possibilities of reducing such uncertainty by obtaining and processing information, because its quality is then low (see e.g. Ciżkowicz and Rzońca 2017).

### **Dimensions of the analysis with regard to financial and monetary stability**

Economic credibility of the state in the area of financial and monetary stability may be analysed in the following four dimensions:

1. direct dimension;
2. indirect dimension, with the use of proximate measures focusing on the effects of (or lack of) credibility of the state;
3. related to threats to credibility of the state in the area of monetary stability;
4. related to threats to credibility of the state in the area of financial stability.

The first two dimensions approximate the level of credibility of the state in the present and past, and the two latter - its likely changes in the future.

While creating an index from sub-indices which would allow us to assess the state's credibility in these four dimensions, we decided to assign equal weight to each of them. This approach makes it possible to reconcile the lack of changes in weights over time with minimization of discretion in assigning them. A similar approach was used when weighting the indicators making up each sub-index.

**Table 13.** Weights of individual areas adopted for calculating the value of Poland's economic credibility index for the area: the financial and monetary stability

<b>Value of the Credibility Index in 2021 for the area: financial and monetary stability</b>	<b>-2,49</b>
Value of the Credibility Index in 2021 for dimension I	<b>-2,13</b>
Value of the Credibility Index in 2021 for dimension II	<b>-2,58</b>
Value of the Credibility Index in 2021 for dimension III	<b>-4,47</b>
Value of the Credibility Index in 2021 for dimension IV	<b>-0,78</b>

	<b>Weights</b>
I. Direct assessment of credibility	25%
II. Proximate measures of credibility	25%
III. Threats to the state's credibility in the area of monetary stability	25%
IV. Threats to the state's credibility in the area of financial stability	25%

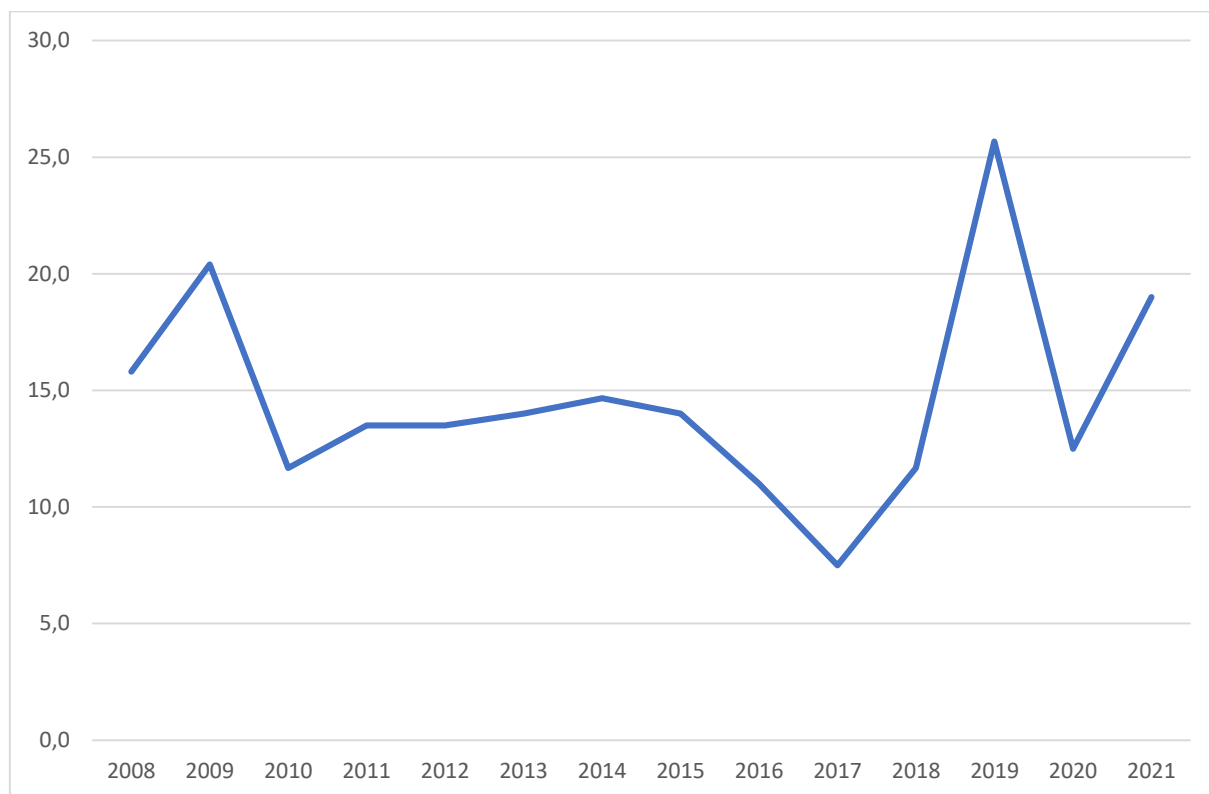
*Source: own study*

### **Dimension 1. Direct credibility assessment**

The National Bank of Poland (NBP) is the most important institution ensuring both financial and monetary stability. The Public Opinion Research Centre (CBOS) examines on a regular basis opinions about the NBP. Two times a year, respondents assess activities of the central bank and have a choice of three answers: good, bad, and hard to say. While building the index, we took into account the percentage of respondents who assessed negatively the activities of the NBP activity, as it is characterized by greater (relative) volatility and is less correlated with other components of the index.

Analysis of the state's credibility, measured in this indirect manner and concerning financial and monetary stability, leads to a disturbing conclusion. After a temporary improvement in 2020, the activity of the National Bank of Poland is assessed increasingly worse by the public. The percentage of negative evaluations increased to the level that was last seen in the years 2001–2005 (except 2019). At that time, the assessment fluctuated, but in comparison with other years it did stand out as significantly worse. Those years, however, were a period of defence of the independence of the central bank. Currently, there is no conflict between the NBP and the government. Worth mentioning is the fact that the percentage of positive evaluations of the NBP's activity is still almost two times as high as the percentage of negative evaluations.

**Chart 24.** Development of the indicator directly measuring credibility of the state in the area of financial and monetary stability in the years 2008-2021 - percentage of people negatively assessing the activity of the National Bank of Poland (percentage)



Source: CBOS

## Dimension 2. Intermediate measurement: proximate credibility measures

For the purposes of proximate (indirect) measurement of economic credibility of the state in the area of financial and monetary stability, we selected two types of effects of such credibility (or lack thereof).

The first effect is related to inflation expectations. A credible state should be able to stabilize them, even if the current inflation is distorted by various shocks. We adopted expectations of entrepreneurs as the measure of inflation expectations included in the index.

These are measured with the use of balance statistics determined by the Central Statistical Office, according to the formula:

$$B = (O1 + \frac{1}{2}O2) - (\frac{1}{2}O3 + O4)$$

Where individual numbers represent the percentage of respondents who say that prices:

O1 - will grow faster than current inflation,

O2 - will grow at the rate of current inflation,

O3 - will remain unchanged,

O4 - will fall.

The prerequisite for selecting this measure of inflation expectations is its high volatility and, at the same time, a lower level of correlation with other index components than in the case of other indicators. One should bear in mind that if the applied measure does not fully reflect the country's credibility in the area of monetary stability, it tends to overestimate rather than underestimate it in periods when inflation is boosted by shocks.

The second type of impact concerns the share of cash in the M3 money supply. Data on monetary aggregates is published by the National Bank of Poland. Providing that the state is credible, people should not be afraid of keeping money in banks. Then, the importance of cash in the money supply should decrease, because in such conditions it is a less secure form of money, less convenient in making payments, and usually burdened with a higher opportunity cost.

**Table 14.** Weights of indicators in the indirect dimension of Poland's economic credibility in the area of financial and monetary stability (destimulants have a negative value) in percentage

Proximate measures of credibility	Inflation expectations of entrepreneurs	-50%
	Share of cash in M3 money supply	-50%

*Source: own study*

Analysis of the indicators leads to the conclusion that the state's credibility with regard to the financial and monetary stability is deteriorating and has reached an all-time low in the entire analysed period.

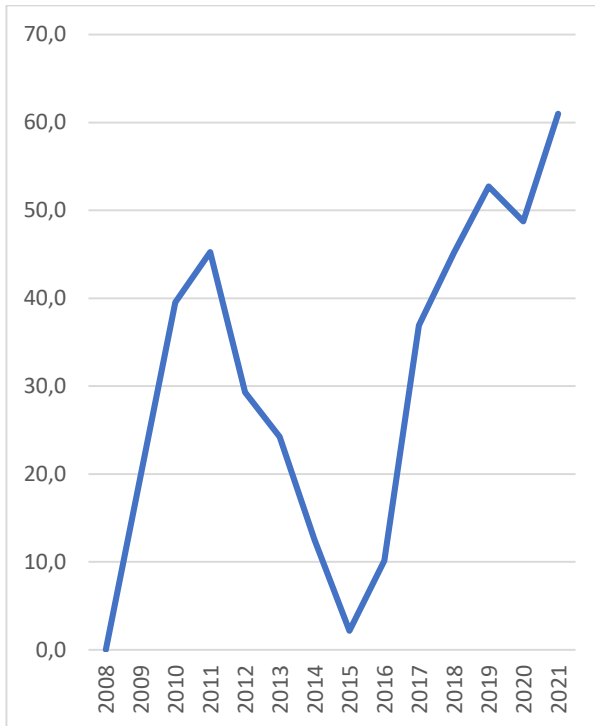
Inflation expectations of entrepreneurs have reached the highest level in the history of the measurement. If the state were credible in terms of monetary stability, then an increase in inflation in the part which has been caused by shocks - temporary in nature - should result in an increase in the percentage of entrepreneurs expecting prices to rise slower than the current inflation in the following periods, and as a result, it should bring about a decline in balance statistics. In a situation where the current inflation strongly deviates not only from the inflation target of the National Bank of Poland, but also from the upper limit of acceptable deviations, the all-time high predominance of entrepreneurs expecting further price increases at the rate of current inflation over those who expect prices to stabilize or fall, proves the low credibility of the inflation target. The target is the foundation of the monetary policy strategy adopted by the National Bank of Poland.

The share of cash in the money supply increased to the highest level since December 1996, i.e. since the central bank started publishing data on M3 and its components. The upward trend in this share was observed back in 2013, after a deep reduction of interest rates by the National Bank of Poland in response to the decline in demand dynamics during the debt crisis in the euro area.



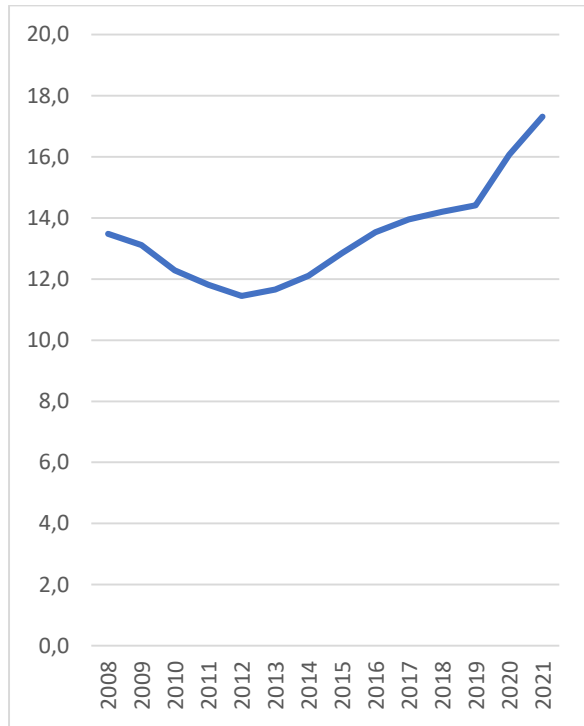
**Figure 4.** Development of indicators indirectly measuring credibility of the state in the area of financial and monetary stability in the years 2008–2021

Inflation expectations of entrepreneurs



Source: Central Statistical Office

Share of cash in the M3 money supply



Source: National Bank of Poland

### Dimension 3. Threats to credibility of the state in the area of monetary stability

Threats to the state’s credibility in the area of monetary stability are measured with the use of four indicators. These were selected taking into account two criteria: possibly high volatility and low correlation with other components of the total index. A similar approach was applied to other dimensions of this assessment.

The first indicator is volatility of 15% truncated mean. It is the only one of the core inflation indicators published by the National Bank of Poland, which is determined by statistical methods. It corresponds to the average weighted on a set of price groups arranged on an increasing scale of increases, the cumulative weights of which are greater than 15% and smaller than 85%. Truncation is symmetrical, i.e. it applies to both the strongest and the weakest price increases. This measure of core inflation is considered to best reflect the current price trends. Its high volatility, measured by the standard deviation of indicators from the last year, signals reduced predictability of price changes - even with regard to the general tendency.

The second indicator is the square of the deviation of inflation above the inflation target. This measure presents a threat to the credibility of the monetary policy foundation based on the inflation targeting strategy. The more inflation exceeds the inflation target - even due to shocks - the greater the risk of the so-called second round effects. This risk consists in

consolidating - due to an increase in inflation expectations embedded in, for example, wage demands - pushed inflation. However, there is no such risk when inflation falls below the target due to factors that will eventually subside. Workers will not accept pay cuts. Therefore, we only focus on deviations above the target.

The third indicator is the square of the output gap. The output gap, i.e. the difference between the GDP and potential output, compared to potential output, is estimated by the European Commission and its details are then published in the AMECO database. A potential output indicates production capacity of the economy. If the GDP is at the potential level, no threats to a stable price level on the demand side are observed. The indicator shows how the state handles stabilizing the total demand, which is of great importance for future inflation processes.

The fourth indicator is the square of deviations of the dynamics of money supply (published by the National Bank of Poland) from the dynamics of potential output (estimated by the European Commission), increased by the inflation target. The money supply may grow faster than the potential GDP growth plus the inflation target without any risk to monetary stability. This higher growth rate must correspond to the slowing velocity of money circulation accompanying the financial deepening (reflecting the increased importance of banks in the economy), which broadens availability of banking services. But the more the money supply dynamics is detached from the long-term nominal GDP growth rate (which is approximated by the sum of potential output growth and the inflation target), the greater the risk that imbalances emerging in the banking sector could threaten the long-term monetary stability.

**Table 15.** Weights of indicators in the dimension of threats to economic credibility of the state in the area of monetary stability (destimulants have a negative value) in percentage

Threats to the state's credibility in the area of monetary stability	Volatility of 15% truncated mean	-25%
	Square of the inflation deviation above the target	-25%
	Square of the output gap	-25%
	Money supply (square of the deviation of the money supply dynamics from the dynamics of potential output plus the inflation target)	-25%

Source: own study

Threats to the credibility of the state related to the monetary stability are on the rise. In fact, they have reached the most serious level since the adoption of the so-called continuous inflation target (i.e. the target usually set by the central bank after lowering inflation to a low level and which this bank strives to meet continuously, not just at the end of the year).

After 20 years, we are back to square one. The 15% trunkated mean has showed higher volatility than the last year only in the period ending the process of bringing inflation down to the low level, i.e. in 2001.

This is not just the result of the shocks, as indicated both by the period in which inflation is above the inflation target and the scale of this deviation. This period has lasted from June 2019 with three monthly breaks. From April 2021, inflation was above the upper limit for acceptable deviations from the target. In August 2021, this deviation reached a level that had

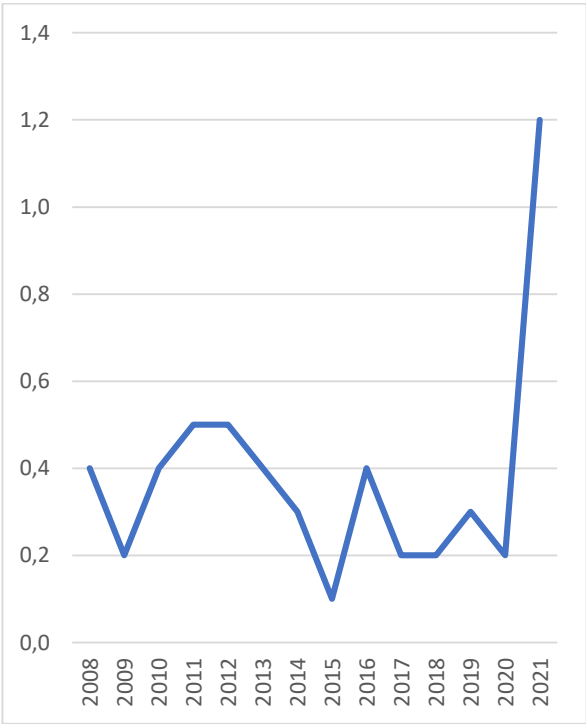
never been observed since the introduction of the continuous inflation target back in 2004. In the entire last year, the index of the square of inflation deviation above the target was over three times worse than the previous maximum value for the period in which the continuous inflation target was in force (and this year it has been getting only worse).

The square of the output gap in 2021 remained at a low level compared to the past. And just two years earlier, in 2019, it reached its all-time high since the introduction of the continuous inflation target. The threat posed by the demand for monetary stability was not mitigated by the state's policy, but by the pandemic, as a result of which total demand fell significantly below the potential of the economy.

In 2021, there was observed a significant decrease in the deviation of the money supply dynamics from the long-term growth rate of the nominal GDP. But it still remained quite high. Except the year 2020, it was higher only during the credit boom preceding the outbreak of the global financial crisis.

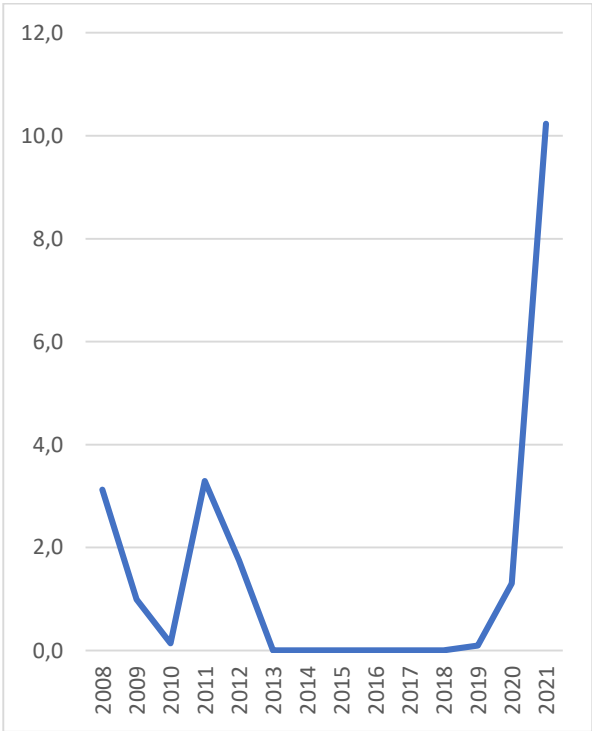
**Figure 5.** Development of indicators in terms of threats to credibility of the state in the area of monetary stability in the years 2008–2021

Volatility of 15% trimmed average



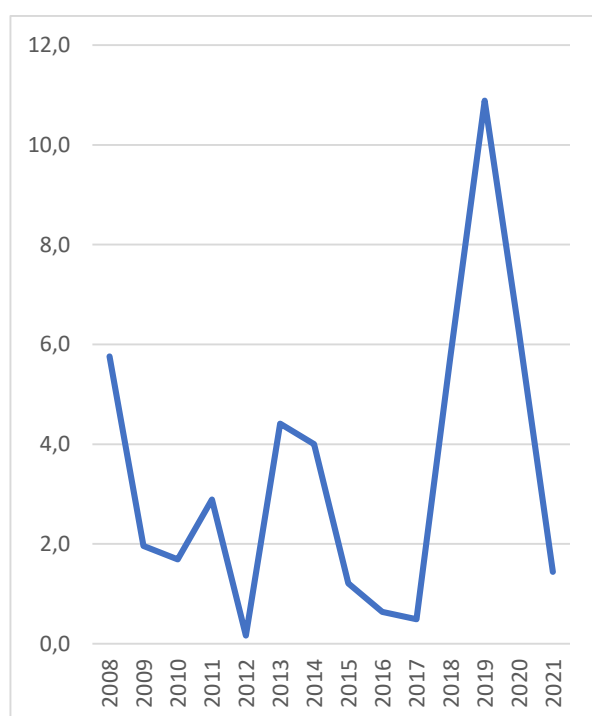
Source: National Bank of Poland

The square of the inflation deviation above the target



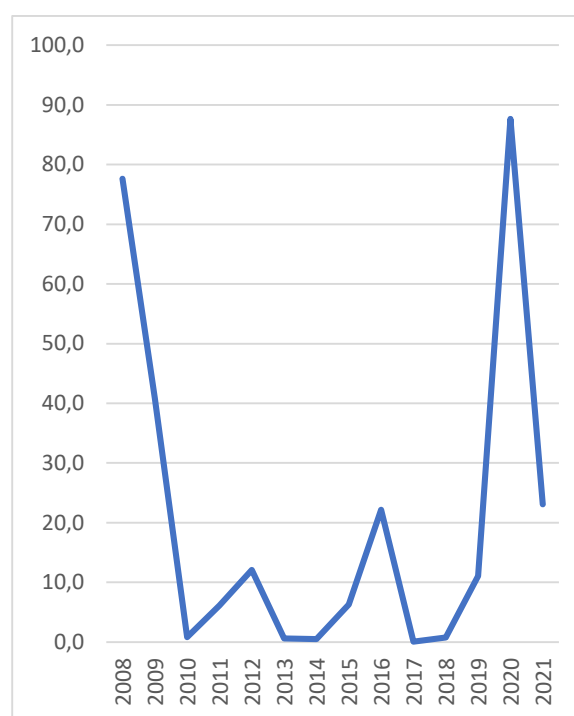
Source: Central Statistical Office

The square of output gap



Source: European Commission

The square of deviation of money supply growth from potential output growth plus inflation target



Source: National Bank of Poland and European Commission

#### Dimension 4. Threats to credibility of the state within the area of financial stability

We decided to measure these threats with the use of four indicators.

The first is the dynamics of loans to the non-financial sector as compared to the dynamics of potential output plus the inflation target. Data on the dynamics of loans to the non-financial sector were provided by the NBP. If a loan grows steadily faster than the economy as a whole, this signals a threat that the banking sector will expand to a size where it is no longer conducive to economic growth. The greater the deviation between these two types of dynamics, the higher the risk of turmoils in the banking sector.

The second indicator is the share of receivables from the general government in banks' assets. This ratio is calculated on the basis of data published by the National Bank of Poland. It reflects sensitivity of the banking sector to possible turmoil in public finance, as well as dependence of the general government on the banking sector.

The third indicator is the real interest rate on household deposits. Data on interest rates on deposits is published by the NBP. When calculating the real interest rate, we use the consumer price index published by the Central Statistical Office. Deeply negative real interest on deposits creates a risk of households withdrawing deposits from the banking sector and investing their savings in risky assets.

The fourth indicator is the price to book value for the WIG-banks index. Information about the indicator may be obtained, for example, from the Bloomberg website. This indicator approximates the health of the banking sector in the eyes of investors. It reflects investors' assessment of the ability of banks to generate profits and, as a result, their ability to increase capital, including by using equity issues, and not just retaining profits. Their ability to generate profits largely depends on regulations and, more broadly, on the economic policy and its credibility in the eyes of investors. In turn, the ability to increase capital is of fundamental importance for the stability of banks.

Data analysis shows the last year's slight decrease in the risks, but these risks are still relevant compared to the past. They were greater only in the years 2019–2020 and before and during the global financial crisis (i.e. in the years 2007–2009).

In terms of credit dynamics, there are no visible threats to financial stability. Since the debt crisis in the Euro zone, its growth rate has been, with the exception of two years (2015 and 2019), lower than potential output growth plus the inflation target.

The problem laid elsewhere, i.e. in the fact that banks did not find it profitable to expand their lending. They preferred to buy Treasury Securities instead of granting loans. From 2019, the share of Treasury Securities in banks' assets has been greater than the share of corporate loans. Banks have an almost 50% share in the Treasury Securities market.

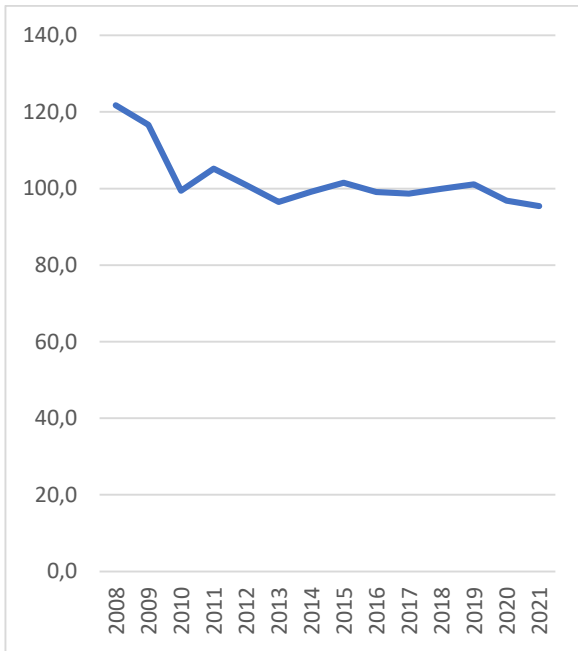
From 2017, the interest on deposits has been negative in real terms. For the past three years, it has been setting new historical lows (for the period, in which the National Bank of Poland publishes relevant data).

Last year, however, the valuation of banks improved significantly. In relation to book value, it was still below the median during the analysed period, yet it was above pre-pandemic levels and greater than one. However, data for this year indicate that the improvement was short-lived.

**Figure 6.** Development of indicators in the dimension related to threats to credibility of the state in the area of financial stability in the years 2008-2021

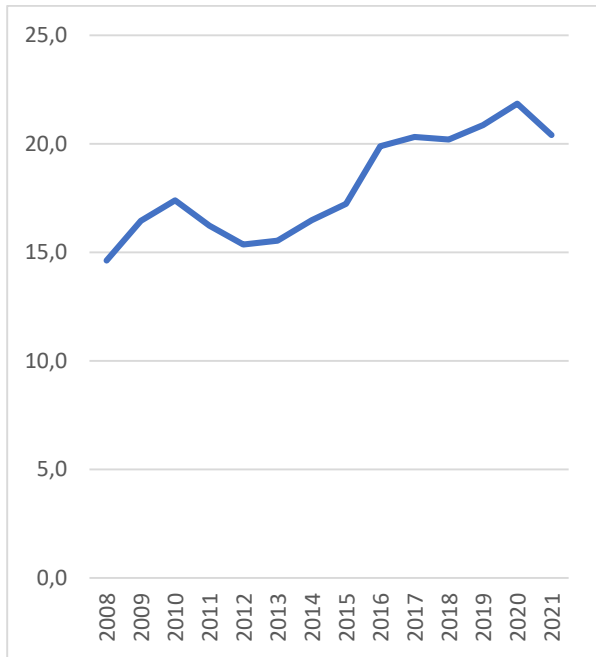
Dynamics of receivables from the non-financial sector compared to the dynamics of potential GDP increased by the inflation target

Share of receivables from general government in bank assets



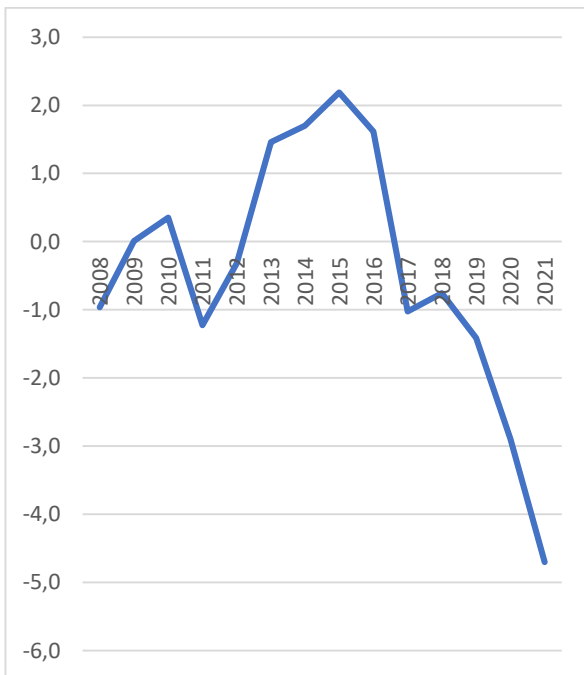
Source: National Bank of Poland

Real interest rate on deposits

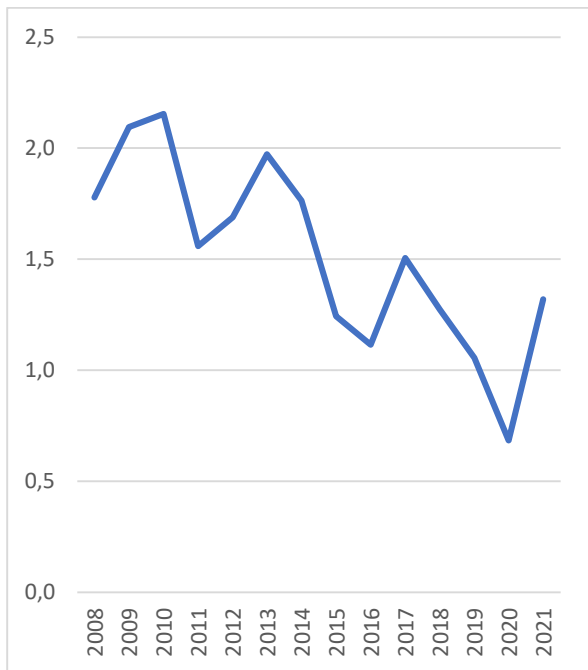


Source: National Bank of Poland

Valuation of banks on the Warsaw Stock Exchange (price to book value)



Source: National Bank of Poland



Source: Bloomberg

**Table 16.** Value of Poland's economic credibility index for the area of financial and monetary stability.

<b>Value of the Credibility Index in 2021 for the area of financial and monetary stability</b>	<b>-2,49</b>
Value of the Credibility Index in 2021 for dimension I	<b>-2,13</b>
Value of the Credibility Index in 2021 for dimension II	<b>-2,58</b>
Value of the Credibility Index in 2021 for dimension III	<b>-4,47</b>
Value of the Credibility Index in 2021 for dimension IV	<b>-0,78</b>
	<b>Weights</b>
I. Direct assessment of credibility	25%
II. Proximate measures of credibility	25%
III. Threats to the state's credibility in the area of monetary stability	25%
IV. Threats to the state's credibility in the area of financial stability	25%

Source: own study

## Summary

**Table 17.** Indicators after standardization for the last five years

Standardization	2016	2017	2018	2019	2020	2021
Percentage of people negatively assessing activity of the National Bank of Poland	-1,11	-2,53	-0,84	4,83	-0,51	2,13
Inflation expectations of entrepreneurs	-1,11	0,00	0,53	1,02	0,77	1,56
Share of cash in the M3 money supply	0,21	0,59	0,82	1,00	2,49	3,61
Volatility of 15% truncated mean	0,44	-1,33	-1,33	-0,44	-1,33	7,57
Square of the inflation deviation above the target	-0,11	-0,11	-0,11	-0,02	1,13	9,66
Square of the output gap	-0,76	-0,82	1,42	3,61	1,63	-0,42
Money supply (square of the deviation of the money supply dynamics from the dynamics of potential output plus the inflation target)	1,00	-0,64	-0,59	0,18	5,89	1,08
Loans (dynamics of receivables from the non-financial sector as compared with dynamics of the potential GDP increased by the inflation target)	-0,27	-0,48	0,13	0,69	-1,33	-2,02
Links between the government and banking sector (share of receivables from general government in banks' assets)	1,20	1,40	1,34	1,65	2,12	1,45

Real interest rates on deposits	1,55	-0,35	-0,16	-0,63	-1,70	-3,00
Valuation of banks on the Warsaw Stock Exchange (price to book value at the end of the year)	-1,36	-0,90	-0,85	-1,55	-2,76	-0,69

Source: own study

In summary, in 2021, economic credibility of Poland in the area of financial and monetary stability reached its lowest level in the analyzed period. Two sub-indices reached their all-time low. These were: the sub-index measuring effects of the state's credibility (or lack thereof) and the sub-index of threats to the state's credibility in the area of monetary stability. Three out of four sub-indices deteriorated. Only one sub-index, which approximates threats to the state's credibility in the area of financial stability, improved. However, its value was still among the lowest in the history of the measurement.

**Table 18.** State reliability index and sub-indices in the area of financial system and money stability in the years 2008–2021

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total index, including:		-0,96	0,50	-0,31	0,22	0,55	0,46	0,51	0,39	0,66	-0,07	-1,95	-1,07	-2,49
Direct assessment of credibility	-0,83	-2,70	0,84	0,10	0,10	-0,10	-0,37	-0,10	1,11	2,53	0,84	-4,83	0,51	-2,13
Consequences of (lack of) credibility		0,64	0,37	0,40	1,08	1,15	1,33	1,33	0,77	-0,29	-0,67	-1,01	-1,63	-2,58
Threats to the state's credibility within the area of the monetary stability	-2,47	-0,43	0,11	-1,09	-0,55	-0,14	0,12	0,76	-0,14	0,73	0,15	-0,83	-1,83	-4,47
Threats to the state's credibility within the area of financial stability	-2,18	-1,35	0,69	-0,63	0,24	1,30	0,74	0,05	-0,18	-0,34	-0,62	-1,13	-1,31	-0,78

Source: own study

The first measure boosting reconstruction of credibility in the area of financial and monetary stability (that would not involve any costs) could be a change in the communication policy of the central bank. Communication should become either more restrained or closer to international standards. By restraint in communication, we understand that representatives of the central bank appear less frequently in the media. If public appearances do not build its credibility, then they should be less frequent. By approximation to the communication standards of central banking we understand its focus on the mandate of the NBP. The focus



of the central bank's communication should fall on (restoring) a stable level of prices and factors influencing the prospects of returning inflation to the target, and not engaging in any political disputes.

Other activities promoting credibility may incur costs. These include in particular: resignation from banking tax (at least with regard to new loans) and exemption of interest on deposits from capital gains tax (i.e. the so-called Belka tax). The first solution is supported by a much greater tax burden on banks in Poland than elsewhere in Europe. It may also lead to weakening banks' incentives to replace loans with treasury bonds, which are exempt from capital gains tax, and additionally do not require banks to involve equity, as the regulator allows them to be assigned zero risk. This would help to reduce sensitivity of the banking sector to possible turmoil in public finance, as well as to weaken dependence of the general government on the banking sector. The second solution focuses on raising the effective (i.e. after tax) interest rate on deposits, which in real terms remains deeply negative, despite significant increases in the NBP interest rates. This would reduce the risk of households replacing bank deposits with more risky assets.

## VI. Employment protection and safety

### The importance of employment protection and safety for economic credibility of the state

Employment protection and safety constitute an important aspect of the economic policy and functioning of labour market institutions. The 2019 Eurobarometer survey shows that three-quarters of the European Union citizens believe that technology brings benefits in the workplace. Two-thirds also say it has a positive impact on societies and will improve their quality of life. In its 2019 World Development Report (The World Bank 2019, p. 2), the World Bank emphasizes that despite optimism, concerns about the future continue to exist. Citizens of developed economies are concerned about the wide impact of technology on employment. They believe that growing inequalities, exacerbated by the emergence of the so-called gig economy (that is, among others, freelance work in cooperation with various platforms, such as, for example, Uber), reduce stability of employment and the sense of security.

### Dimensions of the analysis related to labour protection and security

The area of labour protection and security has been divided into five dimensions:

1. employment protection;
2. safety and working conditions;
3. non-standard employment;
4. labour market participation, and
5. lifelong learning.

Table 18 shows the value of: Poland's economic credibility index for the area of labour protection and security, and its five dimensions in the years 2019-2021, and the weights assigned thereto. In the case of dimensions 1, 3, and 5, the weight was assumed at the level of 20%. The greater weight was assigned to dimension 4 (labour market participation) - 30%. The indicators used for analysing this dimension are also monitored in the framework of the employment strategy in Europe (see Employment Performance Monitor<sup>4</sup>). On the other hand, a lower weight is assigned to the dimension related to safety and working conditions (2), due to the relatively low level of occupational accidents in Poland.

**Table 19.** Weights of dimensions for the area of labour protection and security.

<b>Value of the index of economic credibility of Poland for the area of labour protection and security *</b>	<b>1.66</b>
Value of the credibility index in 2019 for the dimension 1. Employment protection	<b>3.49</b>
Value of the credibility index in 2019 for the dimension 2. Labour protection and security	<b>1.04</b>

<sup>4</sup> <https://data.consilium.europa.eu/doc/document/ST-11372-2020-INIT/en/pdf>

Value of the credibility index in 2020 for the dimension 3. Non-standard employment	3.16
Value of the credibility index in 2021 for the dimension 4. Labour market participation	1.80
Value of the credibility index in 2020 for the dimension 5. Lifelong learning	-1.56

	<i>Weights in percentage</i>
Dimension 1. Employment protection	20
Dimension 2. Safety and working conditions	10
Dimension 2. Non-standard employment	20
Dimension 4. Labour market participation	30
Dimension 5. Lifelong learning	20

Source: own study

### Dimension 1. Employment protection

This dimension takes into account the risk of lower legal protection of employment. The risk may be related to the duration of the signed contract, as well as short-term employment.

This risk is illustrated by two indicators. This is - first of all - the share of people with temporary contracts, which, in accordance with the Labour Code, are subject to slightly limited protection (e.g. such persons have a shorter notice period). Secondly - it is the share of people with 12 months or less of work experience. It is also a group facing a higher risk of losing their jobs. The weights of both indicators within this dimension are equal (Table 19).

Both of these indicators are destimulants, that is, the desired direction is a decrease in their value.

**Table 20.** Weights of indicators in dimension 1. Legal protection of employment (destimulants have a negative value) in percentage.

		<i>Weights</i>
1. Legal protection of employment	Share of temporary employment in total employment	-50
	Persons with job tenure of 12 months or less (aged 25 or more) against the number of employees in this age group	-50

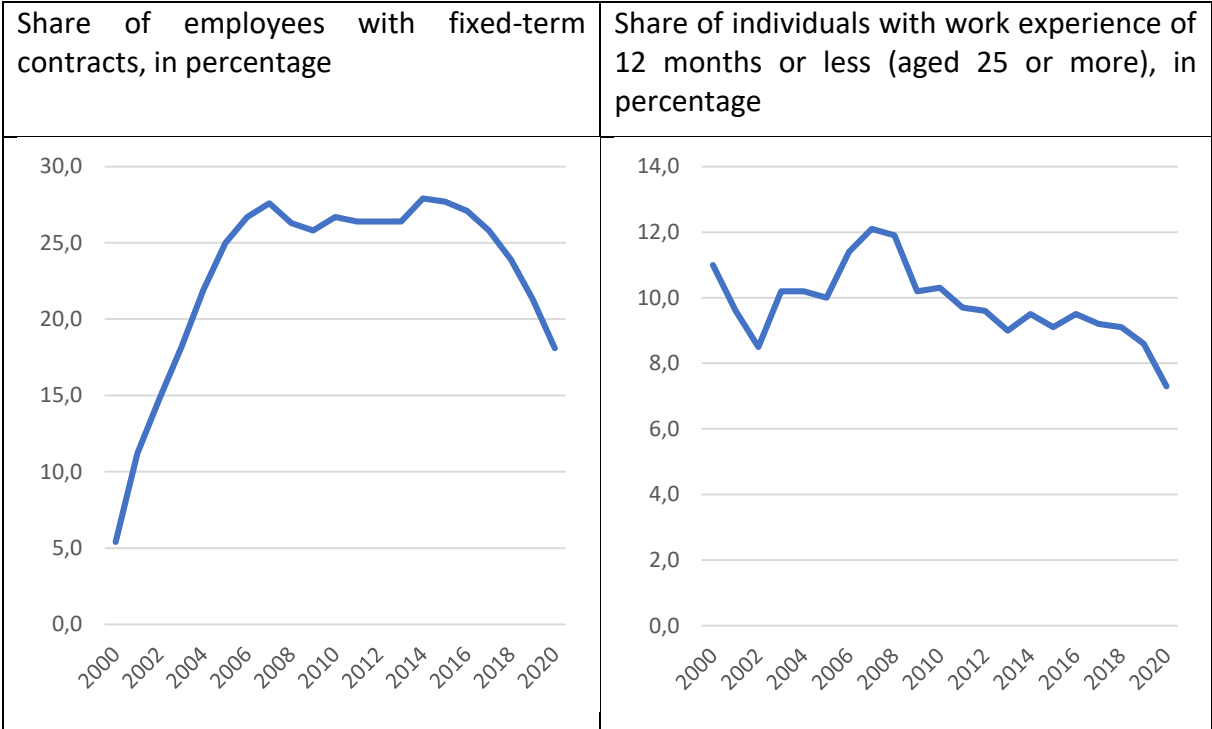
Source: own study

As already mentioned, temporary contracts enjoy a lower level of employment protection, which is why their large share in the labour market proves the lower level of security observed in this market. As can be seen in the chart 25, at the beginning of the century there was observed a dynamic increase in the share of fixed-term contracts. However, their decline has been visible since 2014. This is the effect of legal changes implemented following the public discussion on employment on the so-called junk contracts (Gatti et al. 2014).

The second indicator - the percentage of individuals working at their current employer for periods shorter than 12 months, can be treated as an indicator of effects of employers' reluctance to extend the employment periods. In addition, individuals working for shorter periods at their current employer also have limited protection in the labour market. As can be seen in the chart, in recent years, especially after 2016, we have observed a rapid decline in the share of people with short work experience among the employed.

This means that work security in terms of legal employment protection is improving.

**Chart 25.** Development of indicators in the dimension. Legal protection of employment in the period 2000-2020



Source: Eurostat

**Dimension 2. Safety and working conditions**

In this case, taken into account were two aspects related to the occurrence of accidents at work. The first is occupational safety, measured by the occurrence of accidents at work resulting in sick leave exceeding four days and occurrence of fatal accidents at work. Both included indicators are destimulants, and their weight in this dimension is equal.

**Table 21.** Weights of indicators in the dimension of safety and working conditions (destimulants have a negative value), in percentage

		<i>Weights</i>
2. Safety and working conditions	Fatal accidents	-50
	Accidents resulting in an absence of 4 days or longer	-50

Source: own study

In Poland, occupational safety measured by standardized indicators of occupational accidents improved significantly after 2009. These rates are below the EU average, especially in the case of accidents resulting in sick leave.

The contribution of this dimension to the overall value of the index is positive.

**Chart 26.** Development of indicators in the dimension. Safety and working conditions in the period 2000–2020



Source: Eurostat

### Dimension 3. Non-standard employment

Another dimension of the analysis – important for Poland – is non-standard employment. Here, two indicators were taken into account:

- share of individuals working part-time,
- share of individuals in precarious employment (i.e. less than three months).

Both are destimulants.

**Table 22.** Weights of indicators in a dimension. Non-standard employment (destimulants have a negative value), in percentage

		<i>Weights</i>	
3.	Non-standard employment	Part-time employment (as a percentage of total employment)	-50
		Precarious employment (as a percentage of total employment)	-50

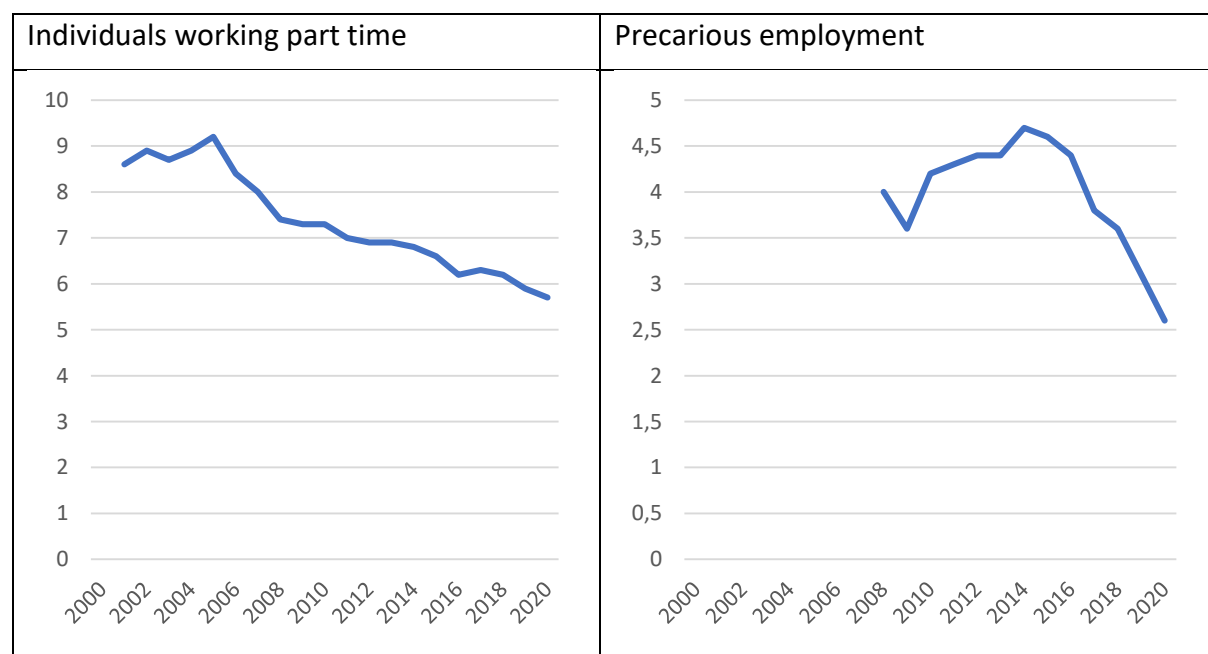
Source: own study

Changes in the values of both these indicators are positive. The share of part-time employees has been on a gradual decline (since 2006). In Poland, this share is considerably lower than the EU average.

After 2014, the share of people employed for periods shorter than three months also dropped significantly. Nevertheless, the values recorded in Poland are higher than the EU average.

Due to the improvement, contribution of non-standard employment to the index of economic credibility of Poland is positive and the highest of all dimensions related to labour protection and security.

**Chart 27.** Development of indicators in the dimension: Non-standard employment in the period 2000–2020



Source: Eurostat

#### Dimension 4. Labour market participation

In this dimension, the employment rates related to selected age and gender groups were taken into account. This is the percentage of individuals working in one of the three

populations: people aged 20–64, women aged 20–64, and people aged 55–64. Especially the last two groups pose a significant challenge from the perspective of this dimension of Poland's economic credibility.

The indicators are stimulants.

As indicated in Table 22, the weight of women and individuals aged 55-64 has been assumed to be higher (40%), due to the fact that these groups are more exposed to the risk of unemployment.

**Table 23.** Weights of indicators in the labour market participation, in percentage

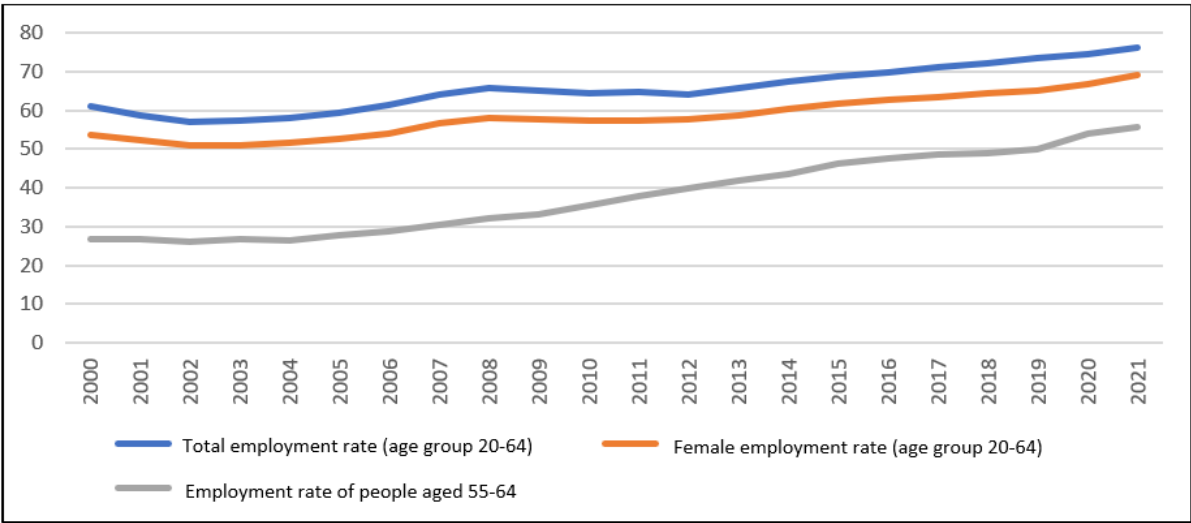
		<i>Weights</i>
4. Labour market participation	Employment rate (age group 20-64)	20
	Female employment rate (age group 20-64)	40
	Employment rate of people aged 55-64	40

Source: own study

The values of employment rates in Poland show an upward trend for each of the analysed populations. The value of the employment rate among the oldest people shows the fastest growth. On the other hand, a slight weakening of the dynamics of the increase in the value of the employment rate of femals has been observed.

Overall, the contribution of this dimension to the credibility index is positive.

**Chart 28.** Development of indicators in the dimension of involvement in the labour market in the period 2000–2020, in percentage



Source: Eurostat

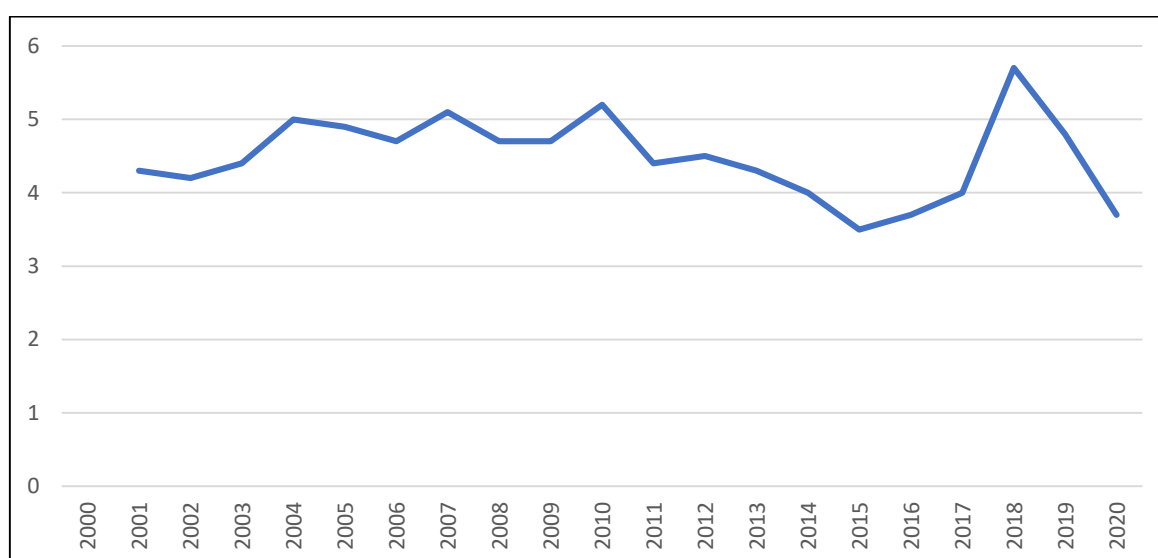
## Dimension 5. Longlife learning

Lifelong learning is the last dimension of employment protection and safety assessment included in the index. It is measured by a single indicator - participation in education and training in the four weeks' period preceding the survey.

As shown in the Chart xxx, this participation varies between 4% and 5%, and in 2020 it fell below 4%, which is one of the lower values recorded in the analysed period (the single lower value lower was recorded in 2015). Moreover, participation in education and training in Poland is significantly below the EU average.

The decline in participation in education and training also means that this dimension contributes negatively to the overall credibility index.

**Chart 29.** Development of the indicator in the lifelong learning dimension in the period 2000–2020. Participation in education and training of individuals aged 25–64, in percentage.



Source: Eurostat

**Table 24.** Value of the index of economic credibility of Poland for the area of oemployment protection and safety

<b>Value of Poland's economic credibility index for the area of labour protection and security</b>	<b>1.66</b>
Value of the credibility index in 2019 for the dimension 1. Employment protection and safety	<b>3.49</b>
Value of the credibility index in 2019 for the dimension 2. Safety and working conditions	<b>1.04</b>
Value of the credibility index in 2020 for the dimension	<b>3.16</b>



3. Non-standard employment	
Value of the credibility index in 2022 for the dimension 4. Labour market protection	1.80
Value of the credibility index in 2020 for the dimension 5. Lifelong learning	-1.56

### Summary

Four out of five labour market indicators point to improving employment protection and safety.

That working conditions in Poland have improved may be a consequence of implementation of provisions compliant with the regulations in force in the European Union. At the same time, the demographic situation is changing - shrinkage of working age population results in a decline in the labour supply. As a result, both an increase in involvement in the labour market and improvement in working conditions are observed. Employers are increasingly trying to ensure stable working conditions. The only dimension which requires significant improvement is lifelong learning. We are seeing a decline in the percentage of adults participating in education and training.

### Policy recommendations

Although the situation in terms of employment protection and safety is relatively favourable, there remains a need for more measures supporting development of human capital and increasingly better use of available labour resources. Greater importance is assigned to taking up activities aimed at significant increase in participation of individuals in various forms of education and training, with a view to developing skills and competences as well as individuals' adaptation to the current needs of the labour market.

## VII. Quality of public services and public infrastructure

### **The importance of the quality of public services for economic credibility of the state**

Governments around the world pay great attention to the quality of public services. Public service failure is the subject of particularly careful analysis. It can take various forms and concern less important aspects of life (e.g. failure to provide an ID card on time, obtaining a permit or license with incorrect data, failure to pay due benefits on time, or a late bus), but also basic matters from the perspective of the functioning and development of the society (e.g. poor quality of education or health care). Public service failures may be down to numerous causes. Van de Walle (2016) systematized them into six categories:

1. failure by ignorance - this means that public service users see failure while those in charge do not see it and therefore do not undertake activities aimed at improving the service;
2. failure by rigidity - this is the result of ossified bureaucratic structures or rules preventing effective operation of a public institution, and more importantly, preventing correcting its errors; these include, among others, rigid decision-making processes which prevent an institution from making independent decisions;
3. failure by failed intervention - this type of failure refers to a situation where inappropriate solutions are used, the public service responds to a specific situation, but the intervention is considered a failure;
4. failure by neglect - this is a result of the lack of interest in a given public service on the part of decision-makers, which results in its collapse;
5. failure by design – public authorities may deliberately design their services in such a way that their level is insufficient and poorly perceived, or that the use of the service is socially stigmatized; in the public sector, such shortcomings tend to occur in areas where demand is high but resources are limited (e.g. cumbersome procedures to apply for public subsidies, excessive bureaucracy to discourage applicants from applying for benefits or healthcare, or long application forms for research grants);
6. failure by association - failure by association occurs when a public service has a bad reputation, and this reputation obscures the real value of the service, then minor and occasional failures are interpreted by service recipients as serious and widespread.

Failure in the provision of public services is the effect of actions of public administration. It should be the main objective of public institutions to minimize such failure. This, in turn, will increase or decrease their reliability. Well-designed and delivered public services are undoubtedly an important element of perception and thus building the long-term credibility of the state.

## Dimensions of the analysis in the area of quality of public services and public infrastructure

Economic credibility related to the quality of public services and public infrastructure is measured in six dimensions:

1. **education;**
2. **health security;**
3. **public safety;**
4. **environment protection;**
5. **e-administration; and**
6. **cybersecurity.**

**Table 25.** Weights of dimensions used for calculating the index for the area of quality of public services and public infrastructure

	<i>Percentage weights</i>
1. Education	25
2. Health	25
3. Safety	20
4. Environment	20
5. E-administration	5
6. Cybersecurity	5

Despite the development, there is a development gap between Poland and highly advanced societies. Reducing it requires a radical increase in the level of intellectual capital to the extent that would allow for changing the position of our economy on a global scale. It is therefore so important that education, as one of the universal public services, keeps up with the needs of economic, technological, as well as and cultural development. Technological changes increase demand for activities requiring complex communication and involve interactions between individuals and groups in order to obtain information and be able to analyse it. [Organization for Economic Cooperation and Development (OECD) 2010]. These tendencies are more favourable to better educated individuals and societies, therefore education is still one of the basic factors in building the economic credibility of the state. This is the first dimension analysed in this part of the index.

Quick and effective access to health services, i.e. a combination of promotion, prevention, treatment, and rehabilitation, is essential for social development. This cannot be achieved without a well-functioning health financing system (Etienne et al. 2010). Healthcare is one of the most closely scrutinized public services. The health of the society is one of the basic determinants of the evaluation of the state's social policy. And while some of the ways to

promote and sustain health are outside of the sphere of influence of the health sector, such as the circumstances in which people grow up, live, work, and age, nevertheless, organization and operation of the public health system is essential. The state builds its credibility on the extent to which it provides citizens with health security. Therefore, it is the second dimension of the analysis.

The third dimension is the public safety system. It is assessed from the perspective of both internal and national, i.e. external, security. A good security system should display the following features (Korzeniowski 2012):

- a common goal and sense of unity in the structure of individual elements and the whole,
- a boundary setting out the extent to which the system can be distinguished from the environment,
- organizational efficiency, which is based on values, norms, and principles,
- efficient organization of the system, i.e. sound structure and good communication between individual links of the system,
- cooperation of organizational elements to ensure achievement of the goal,
- competent management.

The environment is included in another dimension creating an area evaluating the quality of public services. Environment protection consists in:

- preventing natural damage, natural resources,
- repairing the caused damage,
- reducing the risk of damage,
- encouraging the efficient use of natural resources, including energy saving measures and the use of renewable energy sources.

As part of the work on the credibility index, environment protection will be analysed from the perspective of three priorities:

- air protection,
- water protection, and
- soil protection.

E-administration - the fourth dimension - is a general term for online services offered by public authorities. Technologies used in e-administration serve various purposes, such as better provision of public services to citizens, better interaction with business, empowering citizens through access to information, or more effective public governance. Promotion of e-administration may help to: reduce corruption, increase transparency of public activities, improve the comfort of citizens in cooperation with the administration, and reduce the costs of functioning of public institutions. Good e-administration systems are built based on the concept of creating public value (Twizeyimana and Andersson 2019), where ICT systems have the potential to modify and transform processes carried out by public administration.

Cybersecurity - the sixth dimension of analysis of the quality of public services - is a recently frequently used term that has gained particular importance during the COVID-19 pandemic.

The table (Craigén et al. 2014) presents cybersecurity dimensions which inspired the index categorization.

Asset	Defined as "useful or valuable thing or person"
Capability	An acronym for organization and connection of resources, processes, and structures
Misalign	Alignment is defined as "placing (things) in proper or appropriate relative positions"
Occurrence	Incident or event
Organization	The institution's rules and procedures are organized to exploit the full competitive potential of its resources and capabilities
Process	It continues or is conducted as an action or series of activities
Property right	Authority to take specific actions in specific areas. It includes, among others, right of access, withdrawal, management, exclusion, and alienation
Protect	Protection against damage
Resource	Tangible and intangible assets of the institution used for development and implementation of the strategy

*Source: Craigén and others (2014)*

Fourteen indicators determine economic credibility of the state with regard to the quality of public services and public infrastructure. The final list was selected from 38 measures, which constitute an additional set of data, allowing to show a slightly wider context for interpretation of the results. The following factors influenced the final selection of indicators:

- for each dimension, there were selected at least one indicator from the data of national institutions and at least one indicator from the databases of international institutions; data in national databases is more up to date (usually from 2020), while international databases have longer data series according to a fixed methodology, but often ending in 2018 (e.g. Eurostat),
- first, the outcome indicators were sought, in the absence of appropriate data, input indicators were used,
- each indicator was tested for volatility and correlation to other indicators.

A sub-index was created for each dimension. A detailed list of the adopted indicators with proposed weights is shown below.

## Dimension 1. Education

**Table 26.** Adopted indicators, dimension - education \*

Indicator	Weight in percentage
Points scored in the PISA ranking	33.33
Gross enrollment rate	33.33
Expenditure on education (from pre-school care to higher education) as a percentage of GDP	33.33

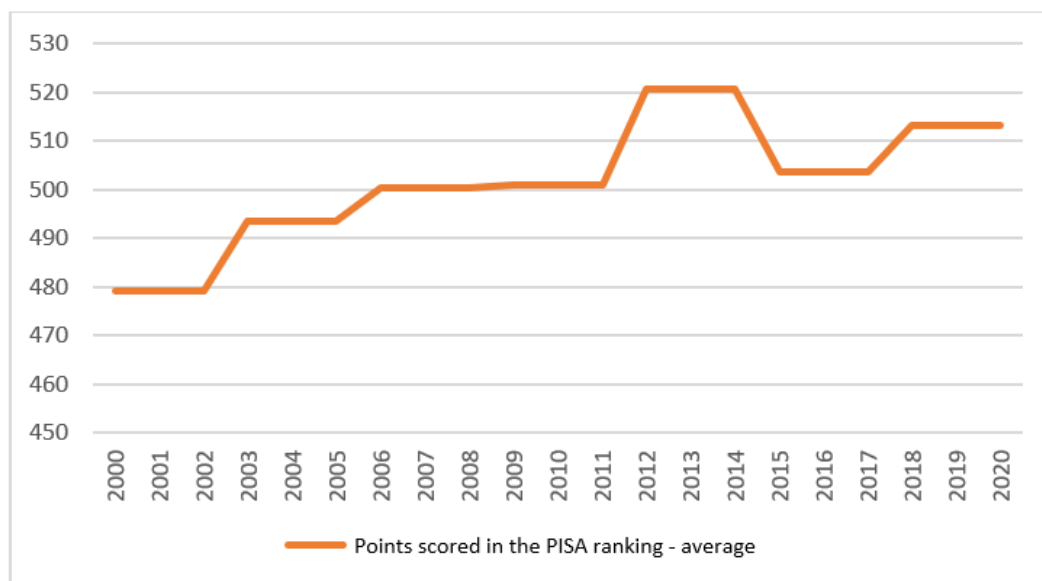
\* weight is 33.333333(3) percent

Data sources: OECD, Central Statistical Office, Eurostat

Value of the economic credibility index for the education dimension was **-0.18**, which means a regression in comparison with previous years.

Value of the credibility index for dimension 1. Education	- <b>0.18</b>
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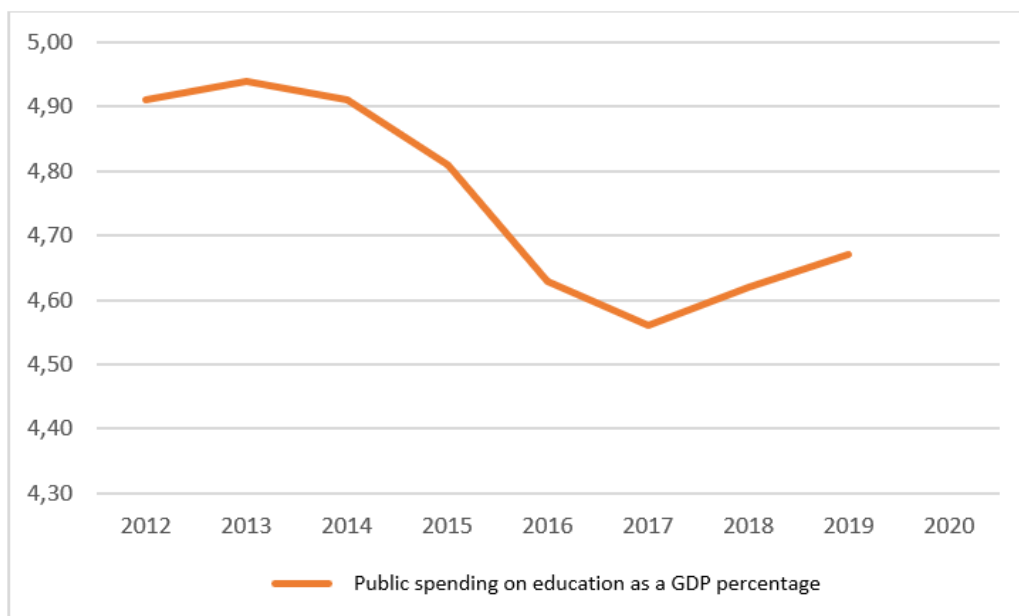
**Chart 30.** Points scored in the PISA ranking (average)



**Chart 31. Gross enrollment rate**



**Chart 32. Public spending on education**



Partial indicators in the education dimension indicate the following trends:

- Polish students perform well in PISA rankings and their position has been improving in recent years,
- gross enrollment rate remained at a very high level until 2013, while in 2015 there was observed a rather sharp decrease, since 2016 this rate has remained at the level of approximately 96%, which is lower than the one observed rate in the first decade of the 21st century,

- in recent years, a decrease in public spending on education has been visible and reached its minimum in 2017 (4.56 percent of GDP); a return to the value of approximately 5% should be the objective.

## Dimension 2. Health safety

**Table 27.** Adopted indicators, dimension - health safety

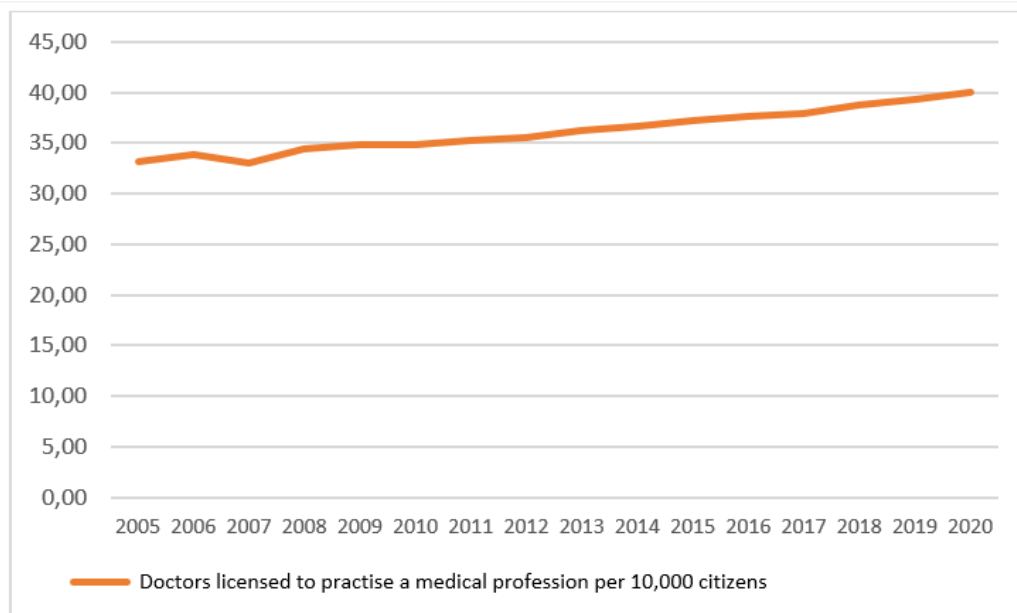
Indicator	Weight in percentage
Doctors licensed to practise a medical profession for 10 000 citizens	20
Life expectancy for men aged 45	80

*Data sources: OECD, Central Statistical Office*

In the health safety dimension, two indicators were used. The weights applied included an indication of the life expectancy measure for men aged 45, as this is a typical result/effect indicator. The value of the index for the health safety dimension was -0.57, which stands for regression in relation to the previous years.

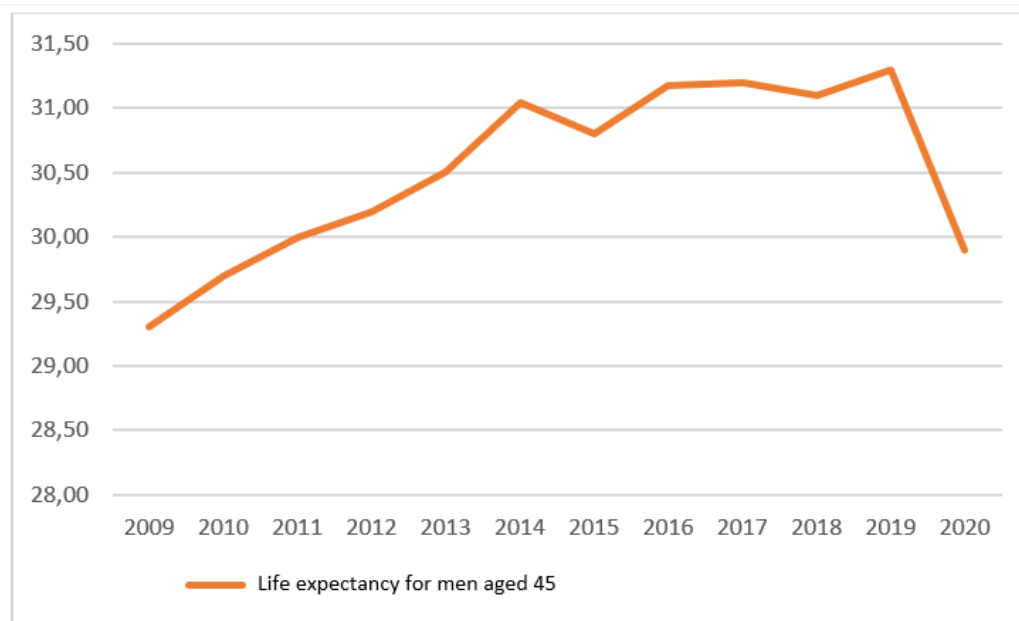
Value of the reliability index for the dimension 2. Health safety	- <b>0.57</b>
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**Chart 33.** Doctors licensed to practise a medical profession per 10,000 citizens





**Chart 34.** Life expectancy for men aged 45



In terms of health safety, on the one hand, one may observe a fairly stable increase in the number of doctors licensed to practise medicine per 10 thousand citizens. On the other hand, in 2020, an unprecedented decrease (by almost 1.5 years) was recorded in the value of the life expectancy rate for men aged 45.

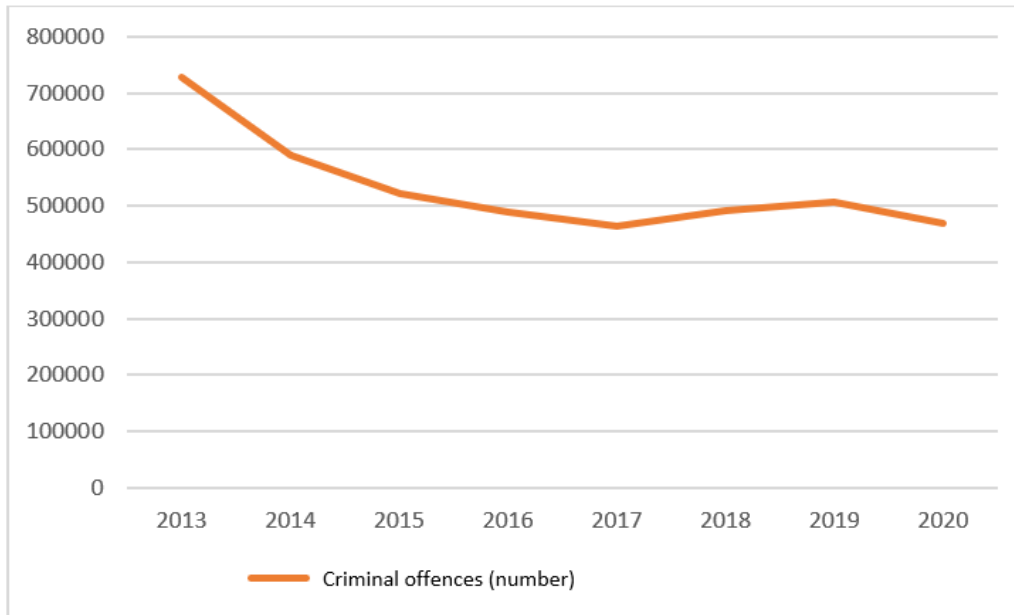
### Dimension 3. Public safety

**Table 28.** Adopted indicators, dimension - public safety

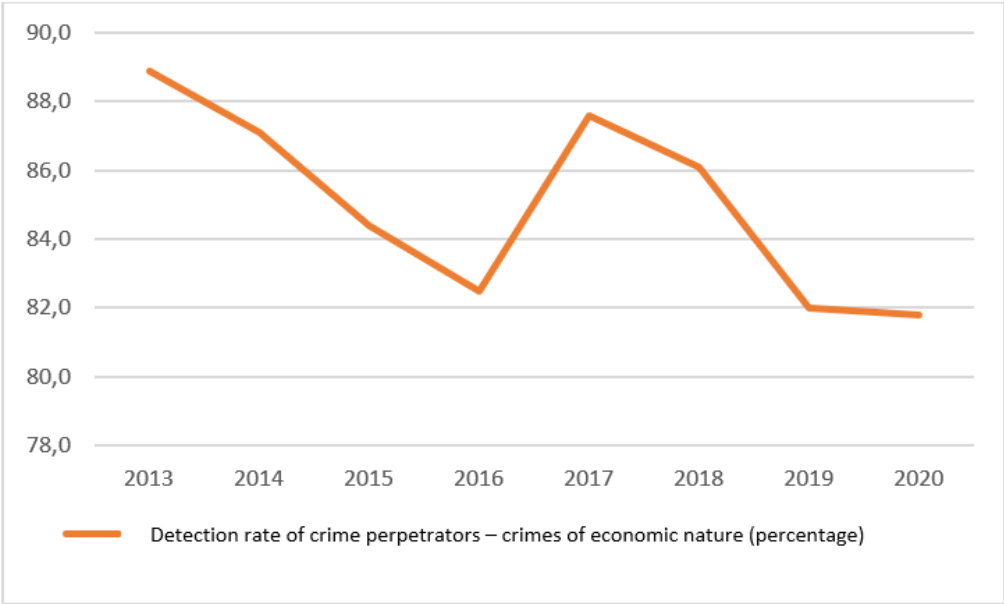
Indicator	Weight in percentage
Criminal offences (number)	15
Offences against family and guardianship (number)	15
Detection rate of perpetrators of economic crimes (percentage)	15
Detection rate of perpetrators of crimes against life and health (percentage)	15
National defense expenditure as a share of GDP (percentage)	40

Data sources: <https://statystyka.policja.pl/>, NATO

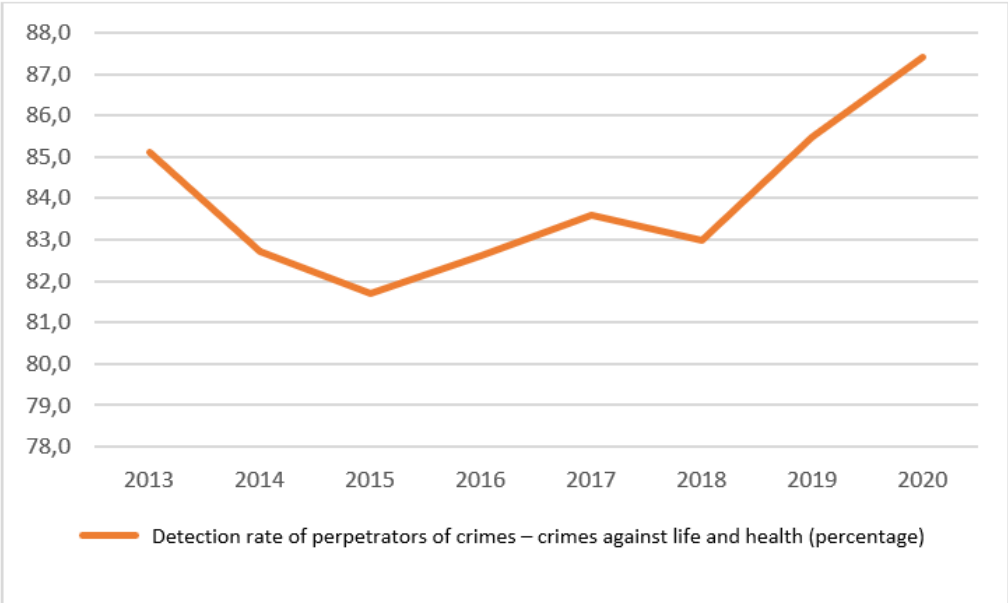
The public security dimension spanned internal security and security within the area of national defense against aggression of a foreign state. The overall rating was 1.29, which marks an improvement over the previous years.

**Chart 35.** Criminal offences (number of cases)**Chart 36.** Crimes against family and guardianship (number of cases)

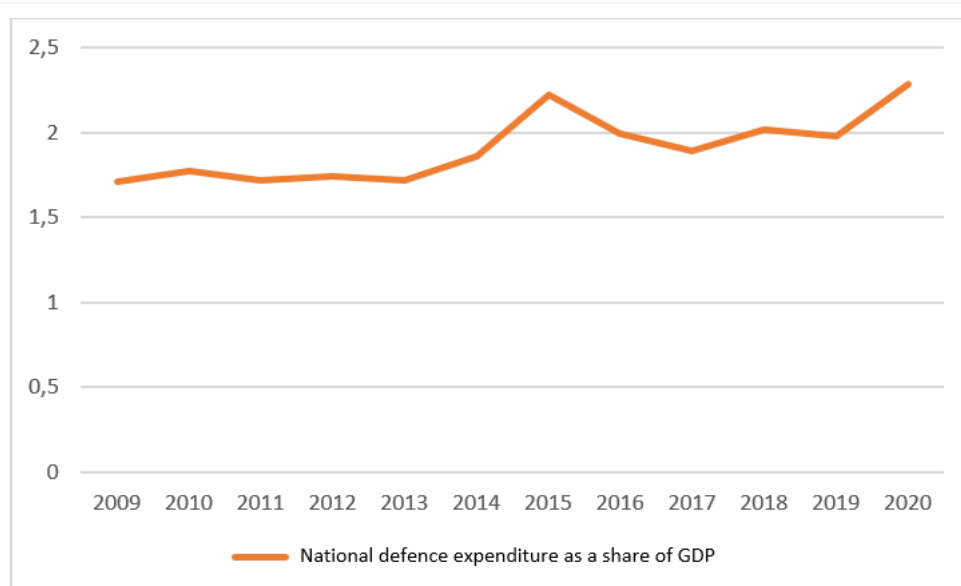
**Chart 37.** Detection rate of crime perpetrators – crimes of economic nature (percentage)



**Chart 38.** Detection rate of perpetrators of crimes – crimes against life and health (percentage)



**Chart 39.** Defence expenditure as a share of GDP



Public safety indicators point to the following trends:

- the number of criminal offences has recently been decreasing, although a slight upward trend was observed in the years 2017–2019,
- the avalanche increase in domestic violence related crimes is very worrying; in 2018, this indicator reached a level of almost 90 thousand notifications, which was a threefold increase compared to 2016,
- when it comes to detecting perpetrators of crimes, the effectiveness of law enforcement agencies in terms of crimes against life and health is increasing, while the effectiveness of detecting economic crimes is decreasing,
- the rate of spending on national defence has been growing since 2017, and in 2020 it significantly exceeded the value of the 2% GDP, this being a good result in comparison with other European countries.

#### **Dimension 4. Environment protection**

**Table 29.** Adopted indicators, dimension – environment protection

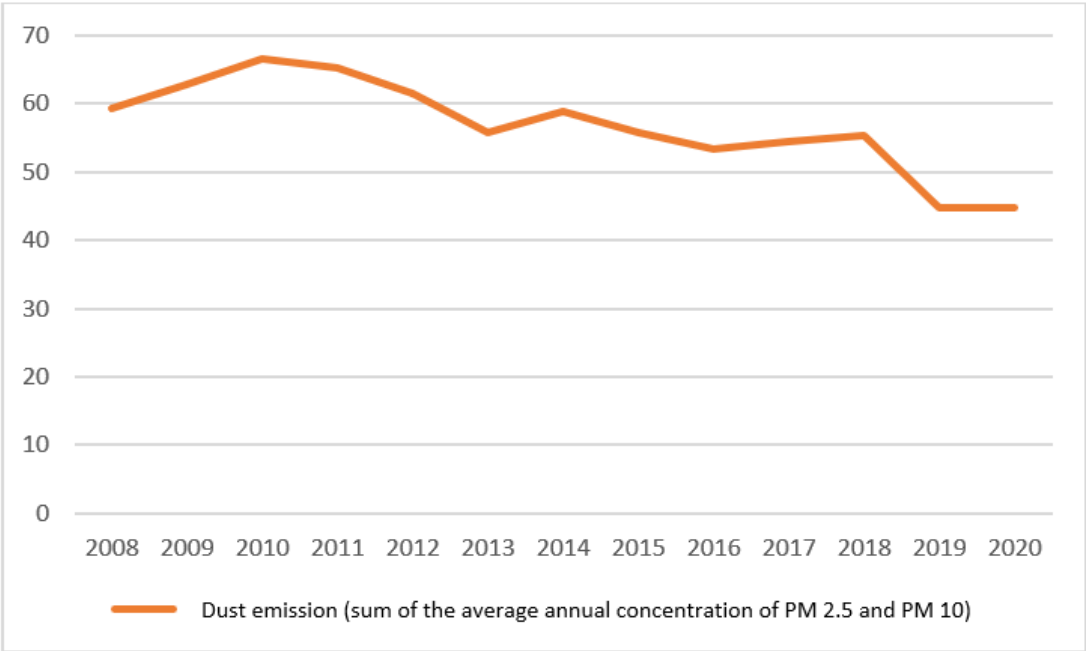
<b>Indicator</b>	<b>Weight in percentage</b>
Emission of PM10 and PM2.5 dust (annual average value of concentration)	30
Municipal waste collected by one person (in kg)	70

*Data sources: Eurostat, Central Inspectorate of Environment Protection, Central Statistical Office*

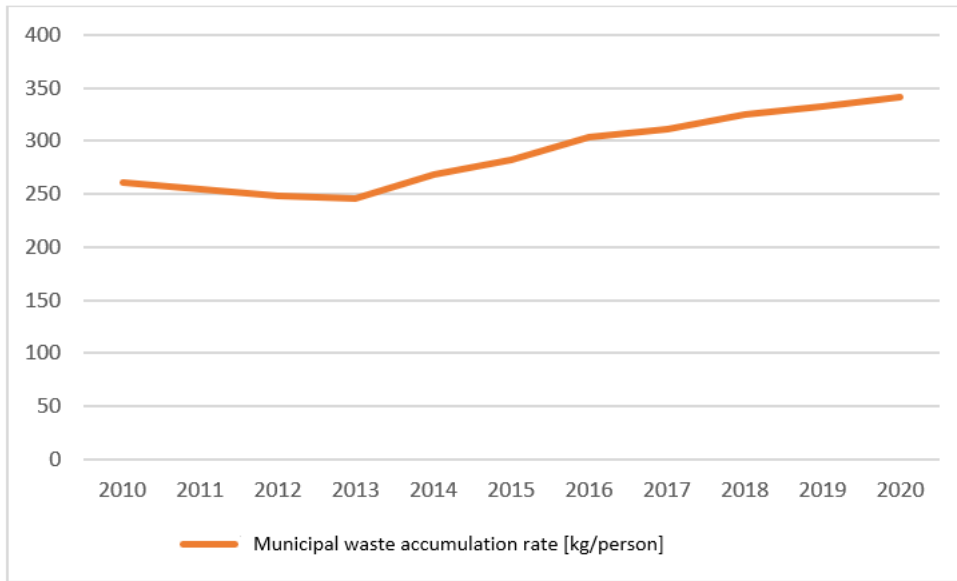
For the environmental protection dimension, two indicators were taken into account – these indicators analyse the government's activity in improving air quality and rational waste management. The value of the sub-index was -0.39, which translates into worsening of the situation in this respect as compared to the previous years.

Value of the credibility index for the dimension 4. Environment	- <b>0.39</b>
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**Chart 40.** Dust emission (sum of the average annual concentration of PM 2.5 and PM 10)



**Chart 41.** Municipal waste collected by one person (in kg)



The indicators selected for the environment protection dimension show that, despite some improvement, air quality in Poland continues to be very poor. The emission of PM2.5 and PM10 dust significantly exceeds the standards of the World Health Organization. The municipal waste accumulation index is also on the increase, which points to problems with its segregation and management.

### Dimension 5. E-administration

**Table 30.** Adopted indicators, dimension - e-administration

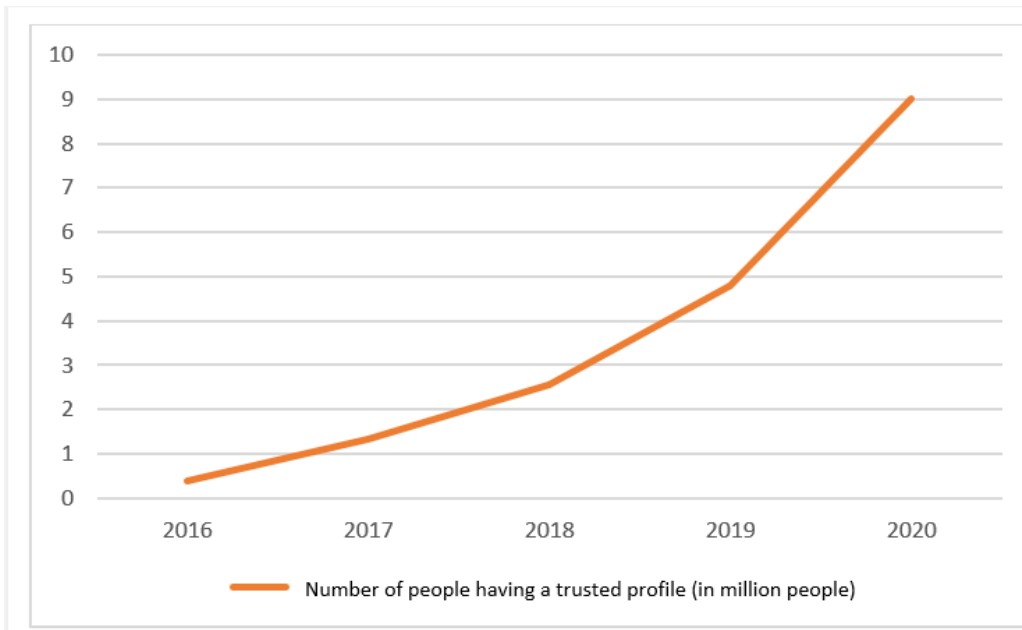
Indicator	Weight in percentage
Number of people having a trusted profile (in million people)	100

*Data sources: Integrated Analytical Platform*

Used for calculating the sub-index in the e-government dimension is a single indicator, the nature of which is synthetic and which shows the activity of citizens using the ePUAP platform. The final value of the sub-index reached the value of 2.14.

Value of credibility index for dimension 5. e-administration	<b>2.14</b>
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**Chart 42.** Number of people having a trusted profile (in million people)



The rate of people having a trusted profile is growing very quickly. An additional impetus for these changes has been the COVID-19 pandemic.

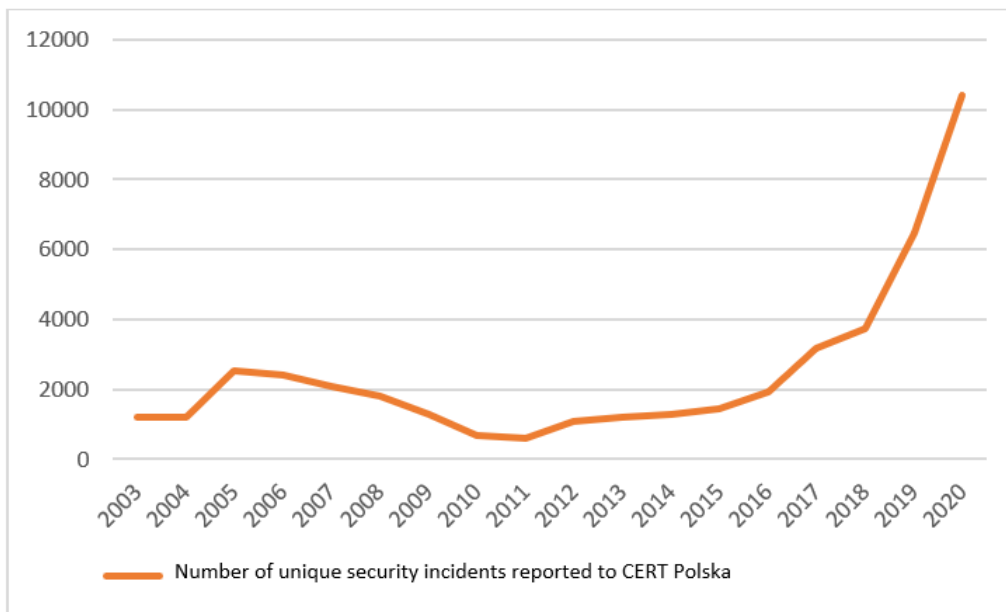
### Dimension 6. Cybersecurity

Within the area of of cybersecurity, there was used a single indicator (security incidents reported to CERT Polska). On this basis, the sub-index value was -11.97.

Indicator	Weight in percentage
Number of unique security incidents reported to CERT Polska	100

Value of the credibility for dimension 6. Cybersecurity	- <b>7.76</b>
---------------------------------------------------------	------------------

**Chart 43.** Number of unique security incidents reported to CERT Polska



Source of data: CERT Polska

The number of unique security incidents reported to CERT Poland is one of the few indicators related to cybersecurity and is available for a longer time series. It shows that as at 2017, the level of digital security in Poland has been in decline.

The value of the credibility index for the area of quality of public services

-  
0.29

### Summary

The assessment of Poland's economic credibility performed on the basis of six types of public services is varied. There are areas, the assessment of which is positive (public security, e-government), but there are also areas that are assessed as definitely negative (health security, environment, or cybersecurity), or rather negative (education). The value of the economic credibility index for the area of quality of public services finally amounts to -0.29, which means certain regression as compared to the previous years.

In recent years, Poland has recorded a relatively good ratio of expenditure on education in relation to the GDP. Its value is approximately 4.6% in 2018, which is a good level compared to other countries, e.g. Czech Republic - 4.2%, EU27 - 4.7%. Polish students also perform quite well in PISA tests and their position has been improving in recent years, although it looks different in individual branches of knowledge, e.g. reasoning in the natural sciences shows quite significant fluctuation. Worryingly, however, there has been a decrease in the enrollment rate and an increase in the number of pupils and students per teacher and



academic staff in comparison with the neighbouring countries (Poland - 14.5 people, Czech Republic - 13 people, Slovakia - 11.6 people, Hungary – 12.7 people).

Noteworthy is the fact that the year 2020 was particular for the healthcare sector due to the COVID-19 pandemic. This exerted an impact on the value of the government spending on health indicator, which in recent years had fluctuated around 4.5%, but in 2020, due to the COVID-19 pandemic, jumped to 5.24%. The number of doctors per 10 thousand of citizens in Poland has also been slowly increasing in recent years. These two indicators show some improvement, but in comparison with other countries Poland fares poorly. In the case of the first index, the Czech Republic spends around 6.5 percent of GDP. The number of doctors is also much lower than in other European Union countries. To sum up, in this dimension, the situation in terms of health security is unsatisfactory.

Looking at the data on public safety, one may easily notice that the crime rate statistics (number of crimes/detection) have improved in recent years. On the other hand, crimes against the family and guardianship are a problem, the number of which has increased dramatically since 2018, and so has declined detection of economic crimes. Data on national defence spending in Poland is positive. Since 2018, the indicator has fluctuated around 2%, which is a sound value compared to other European countries (e.g. Germany 1.5%). This dimension should be assessed positively.

Sadly, Poland still performs poorly in terms of the quality of the natural environment against the backdrop of other EU countries. Air quality remains to be very poor and very little improvement has been observed. The amount of waste produced is increasing, and while the share of RES in the energy structure has exceeded the assumed target of 15%, but this was achieved by changing the method of calculating the indicator by the Central Statistical Office. In this dimension, the authors of the report have taken into account the use of water quality indicators in Polish rivers, but there is a lack of reliable and systematic data. The overall assessment of this dimension is negative. In addition, the value of the indicators used in constructing the sub-index is significantly worse than in other European countries, which further strengthens this negative assessment.

In the case of e-administration, the COVID-19 pandemic was a strong stimulating factor in the use of remote forms of handling official matters by citizens, despite the low quality of the ePUAP system. Generally, however, a growing number of Poles uses various forms of e-government, which is also shown by other indicators (not included in the index). Therefore, this area merits positive assessment.

The situation in the cybersecurity area looks somewhat different. The scale of the threat of cyberattacks has been on the increase in recent years. This applies to both citizens and public institutions. The number of reported attacks has recently rocketed. The overall assessment of this dimension is therefore strongly negative.

Recommendations concerning those areas of social life, whose sound condition affects quality and security of public services:

- to ensure greater availability of teaching staff through the use of various incentives to take up teaching jobs,
- to increase dynamics of development of renewable energy sources, which, on the one hand, will allow to become more independent of traditional sources, and, on the

other hand, will contribute to improvement of the quality of the natural environment,

- to improve cybersecurity of public institutions, which have recently been highly exposed to more and more advanced and sophisticated cyberattacks

## VIII. Respecting international obligations

### The importance of respecting international obligations for economic credibility of state

Respecting international obligations by Poland is essential for its economic credibility. Of great importance are bilateral agreements concluded with other countries, but to an even greater extent, also multilateral treaties signed by the Polish government, often related to membership in international organizations. They define the economic functioning of Poland on the international arena and the engagement of foreign individuals, companies, and institutional entities in the economic life of Poland and vice versa: of the Polish companies and citizens abroad. According to the Polish constitution, international treaties take precedence over national legislation. The key significance of Poland's respect for international obligations originates from the fact that the Polish economy is characterized by a high level of internationalization and Poland's membership in the European Union and the Single Market (free movement of services, goods, capital, and people)<sup>5</sup>.

Membership in the EU means that compliance by Poland with international obligations should be examined primarily in the EU dimension. *Acquis Communautaire* constitutes a basic foundation of Poland's membership in the Single Market and in the EU. *Acquis* has an enormous impact on the Polish legal system and the functioning of the Polish economy in the EU and - on a global scale - on its trade, banking, stock exchange and investment relations with the outside world. It includes:

- founding and accession treaties as well as international agreements concluded by the Member States, which together constitute the so-called primary law,
- provisions issued on the basis of primary law by the EU authorities, which together form secondary law,
- international agreements concluded by the EU with external partners,
- judgments of the Court of Justice of the EU,
- declarations and resolutions of the European Parliament and of the Council,
- general principles of the Community law, i.e. specific norms of the Community law, which - as "unwritten" law - reflect rudimentary ideas about law and about structural and organizational principles. According to the Court of Justice of the EU, general principles are "inherent in the Treaties" and are only extracted externally as a result of interpretation in its rulings.

The rule of law is vital for the functioning of the EU and the Single Market in the EU dimension. Therefore, Poland's respect for international obligations is particularly important for:

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<sup>5</sup> The volume of Poland's trade in goods with foreign countries exceeds its entire GDP, while in the case of trade in services, it is about 20 percent. The value of cumulative direct foreign investments located in Poland amounts to over 40% of the GDP. As part of these indicators, the position of the EU is dominant. About 65% of Poland's foreign trade in goods and services is traded within the EU. Around 90% of the FDI stocks that Poland attracted, originates also from the EU countries. The EU funds (Multi-Year Financial Framework and National Recovery Plan), which Poland is to receive from the EU budget in the years 2021-2027, account for nearly 30 percent of its nominal GDP. Before the pandemic, the total share of tourism in Polish GDP was 5% and it was made up mainly of foreign tourists, most of whom came from the EU. In the case of the Single Market, Poland is also connected with countries being part of this market (Iceland, Liechtenstein, Norway, Switzerland), but not belonging to the EU.

- proceedings before the Court of Justice of the European Union, to which Poland is a party, rulings and preliminary rulings,
- violations of Community law by Poland reported by the European Commission
- complaints against Poland lodged with the European Court of Human Rights,
- rulings of these Courts concerning Poland and implementation thereof by the Polish authorities.

Analysis of the economic credibility of Poland, within the context of Poland's compliance with international obligations, may also be carried out whilst looking at arbitration proceedings pending against Poland in foreign courts, and deal by the General Prosecutor's Office. Poland is the only EU Member State which has not recognized the Washington Convention. This means that arbitration awards do not take legal effect in an automated manner, but must first receive an enforcement clause from a Polish court, i.e. the Polish government has additional possibilities of defence in a national court.

Poland's credibility in respect of compliance with international obligations is also largely shaped by the policy of the Polish authorities (implementation of judgments, international treaties and EU legislation as well as "changes" in the judiciary and their compliance with the international and EU law) and the Polish judiciary (its jurisprudence in response to judgments of the European judiciary).

It is difficult to assess Poland's compliance with international obligations since of greater importance than the number of judgments is the importance of individual key judgments on basic issues, i.e. fundamental rights, and consequently closely related to Poland's membership in the EU and the Single Market. In the years 2018–2022, the CJEU and the ECHR issued over 20 rulings on changes to the Polish judicial system related to fundamental rights. In the history of the European Union, never has been a case where so many rulings would find the Member State guilty of violating fundamental rights. Moreover, Poland made the unprecedented decision not to implement the CJEU judgment on the fundamental issue of organization of the Supreme Court, which was issued on 15 July 2021.

Poland's credibility has also been undermined by the jurisprudence of the Constitutional Tribunal, which has in fact been subordinate to the ruling party since 2016. Key judgments (15.07.2021, 7.10.2021, 24.11.2021, and 10.03.2022) selectively found the alleged inconsistency with the Polish Constitution of the interpretation of EU law and the interpretation of the European Convention on Human Rights by the Court of Justice of the EU and the European Court of Human Rights, especially in cases concerning independence of the judiciary and the right to a fair trial, as well as in matters related to the constitutionality of Poland's obligations to implement the provisions of the CJEU and the ECHR.

Under the rule of Law and Justice /Prawo i Sprawiedliwość/, since 2015, the prosecutor's office has been politically subordinated on an unprecedented scale (except for Hungary). Changes in the judiciary have led to serious transformations in the personnel structure of the Polish judiciary. The new National Council of the Judiciary, recognized by European courts as not elected in accordance with fundamental rights, nominated approximately 20% of the panel of judges in Poland (2000 judges). All these appointments are legally flawed. All judgments issued by these judges may be challenged through a complaint lodged with the European Court of Human Rights. This process has already started, and it does not only concern human rights, but also jurisprudence on economic activity. An excellent example of the latter phenomenon

is the case of Advance Pharma sp.z o.o. against Poland, in which the judgment of the ECHR unfavourable for the Polish side was issued on 03 February 2022<sup>6</sup>.

In consequence, Poland is along with Hungary, the only EU member state whose National Recovery Plan has not been approved by the European Commission. The latter justified the decision with Poland's problems with the rule of law and gave it three basic conditions, the so-called milestones (liquidation of the Disciplinary Chamber of the Supreme Court, restoration of independence to the disciplinary judiciary, and restoration of unlawfully dismissed judges to adjudication). The Polish government undertook to implement them, but has not yet fulfilled this obligation (as of 01 December 2022).

### **Dimensions of the analysis in the area of respecting international obligations**

Twelve indicators were used to calculate the sub-index. The indicators are grouped under three dimensions:

1. the EU dimension;
2. European Court of Human Rights;
3. international arbitration.

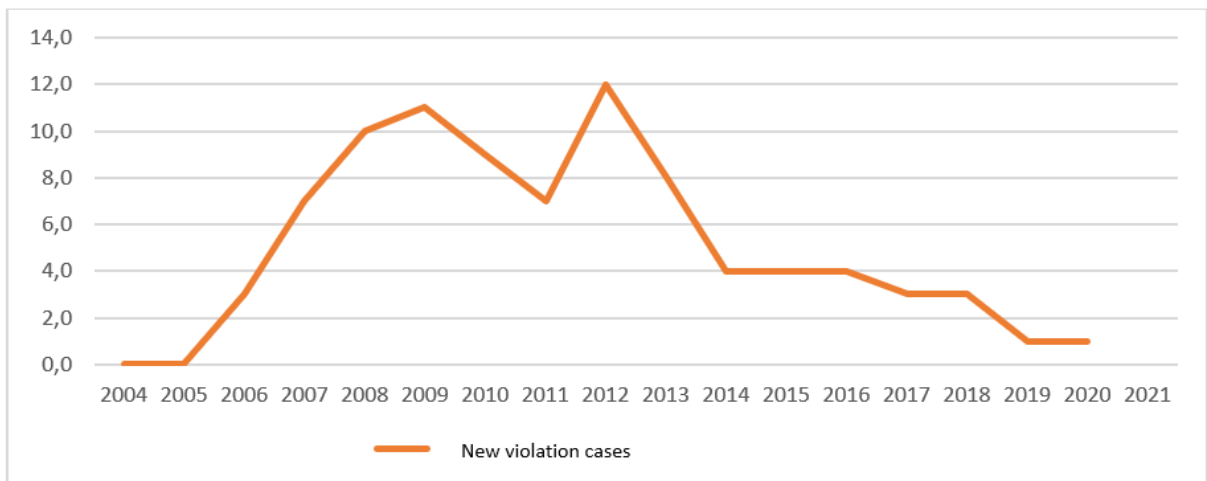
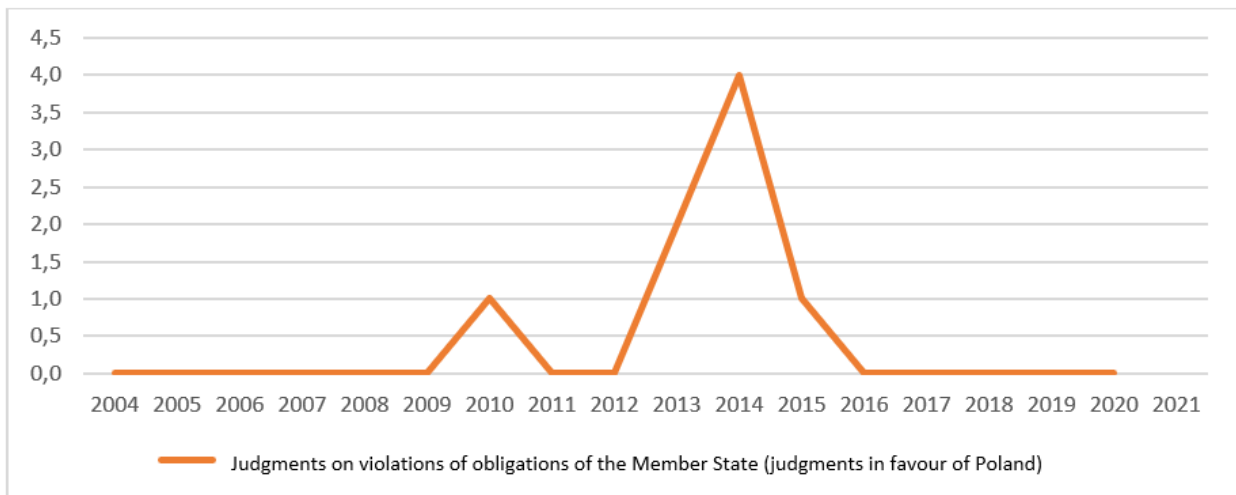
#### **The EU Dimension**

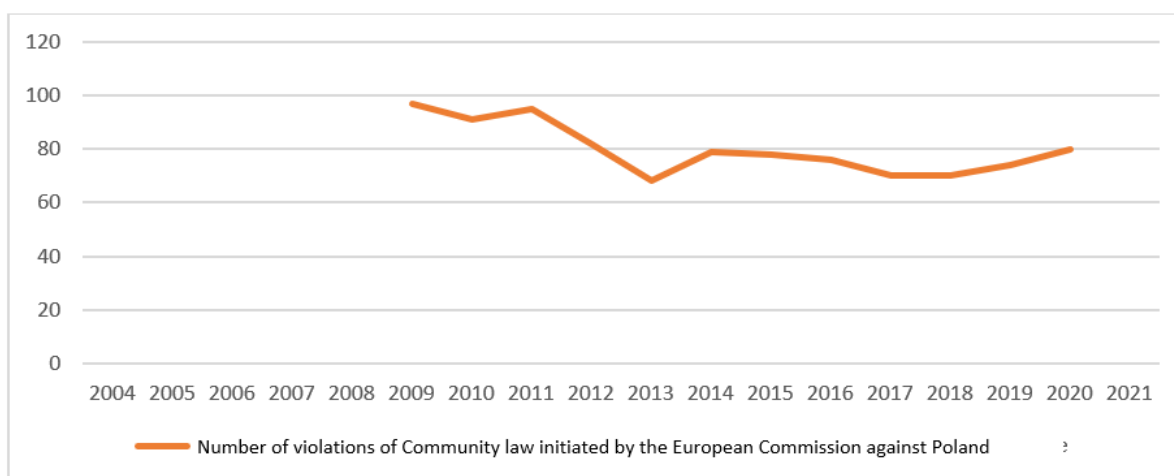
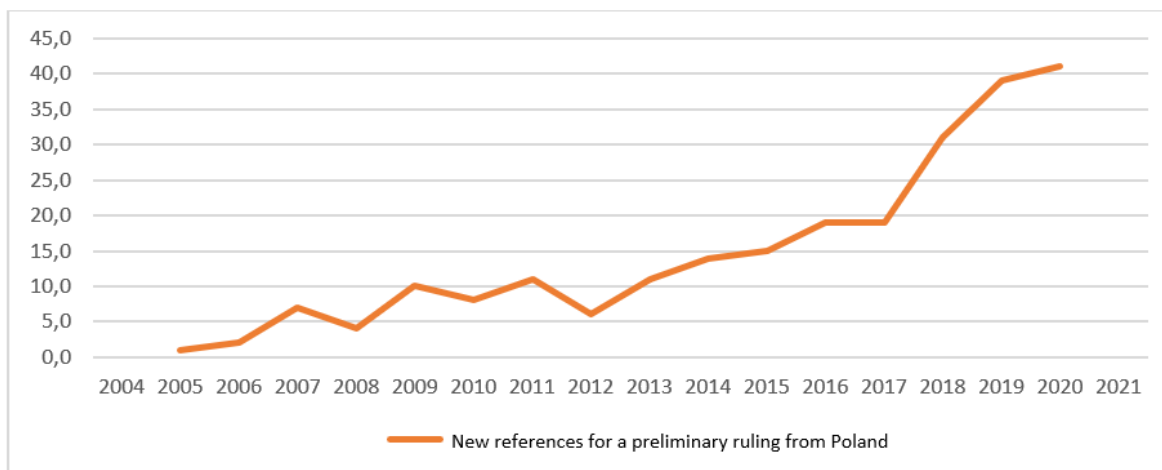
**Table 31.** Indicators and their weights in the EU dimension

<b>Indicator</b>	<b>Weight in percentage</b>
Judgments on violations of obligations of the Member State	20
Judgments on violations of obligations of the Member State (in favour of Poland)	20
New cases concerning violations	20
New references for a preliminary ruling from Poland	20-
Number of violation cases initiated by the European Commission against Poland	20

<sup>6</sup> The judgment concerns a company which filed a claim for damages against the State Treasury, and in the last instance in Poland its case was examined by a panel of three judges of the Civil Chamber of the Supreme Court. The claimant alleged violation of Art. 6(1) of the Convention for the Protection of Human Rights and Fundamental Freedoms (right to a fair trial). The company pointed out that the candidacies of all judges examining its case were presented to the president by the National Council of the Judiciary established following the amendment to the Act in 2017. The ECHR found that there had been a violation of the applicant's right to have the case heard by an independent and impartial court and ordered that it be paid EUR 15,000 as compensation and € 3,000 for incurred costs and expenses. The verdict is final.

**Chart 44.** Judgments issued by the Court of Justice of the EU concerning Poland





Credibility index value for the EU dimension	<b>0.61</b>
----------------------------------------------	-------------

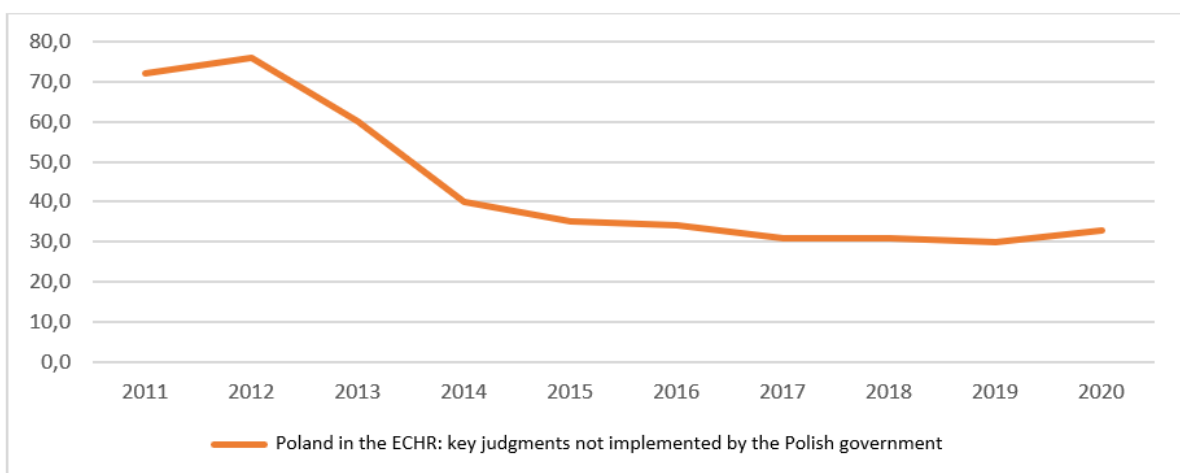
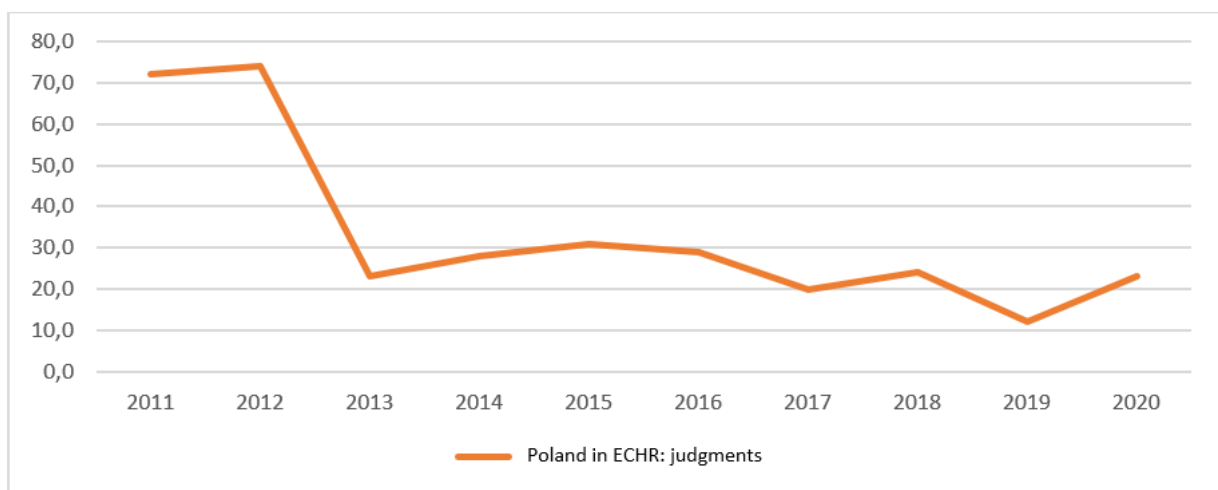
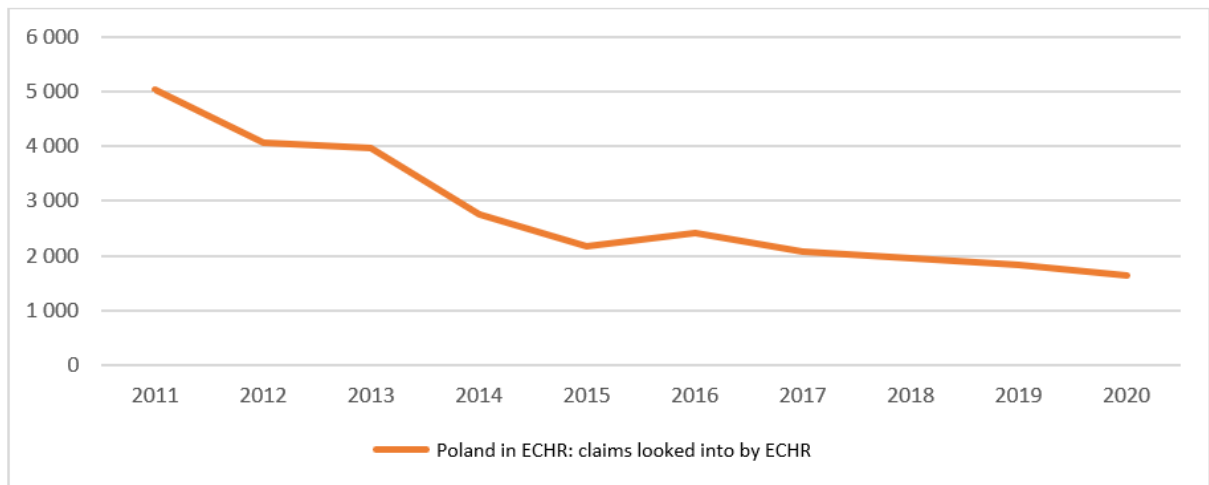
## European Court of Human Rights

**Table 32.** Adopted indicators

Indicator	Weight in percentage
Poland at the ECHR: claims examined by the ECHR	25
Poland at the ECHR: rulings	25
Poland at the ECHR: key rulings not implemented by the Polish government	50

In the case of the ECHR, since 2016, the previous downward trend of no implementation by the Polish government of key judgments has stopped. This means stagnation, or perhaps a possibility of a renewed increase in the number of non-implemented key rulings.

**Chart 45. Poland in the European Court of Human Rights**





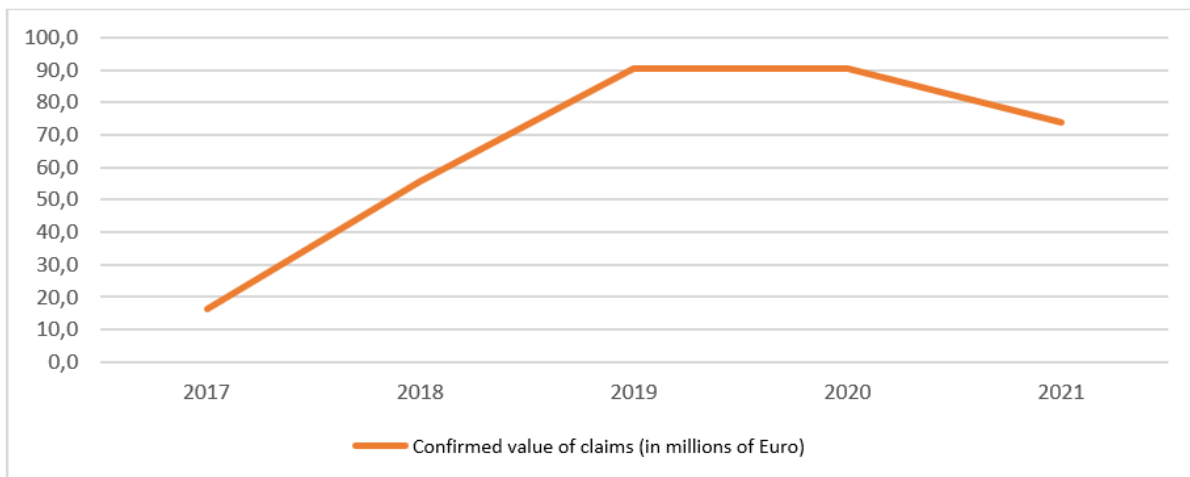
## International arbitration

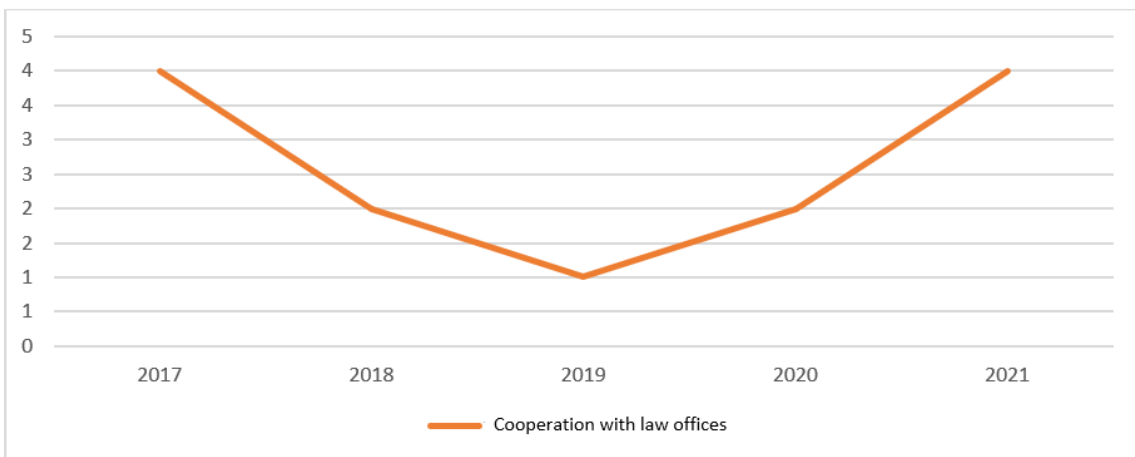
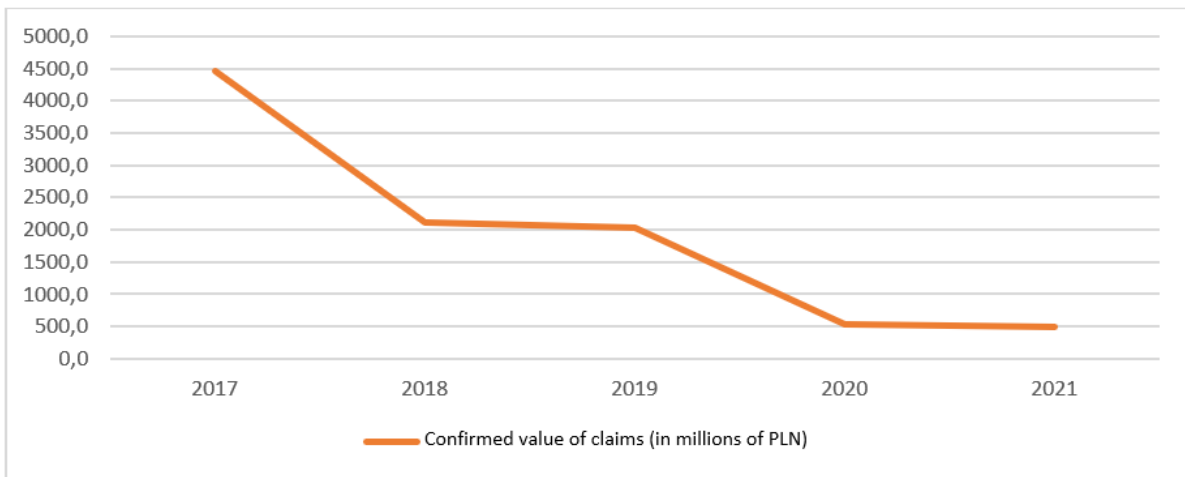
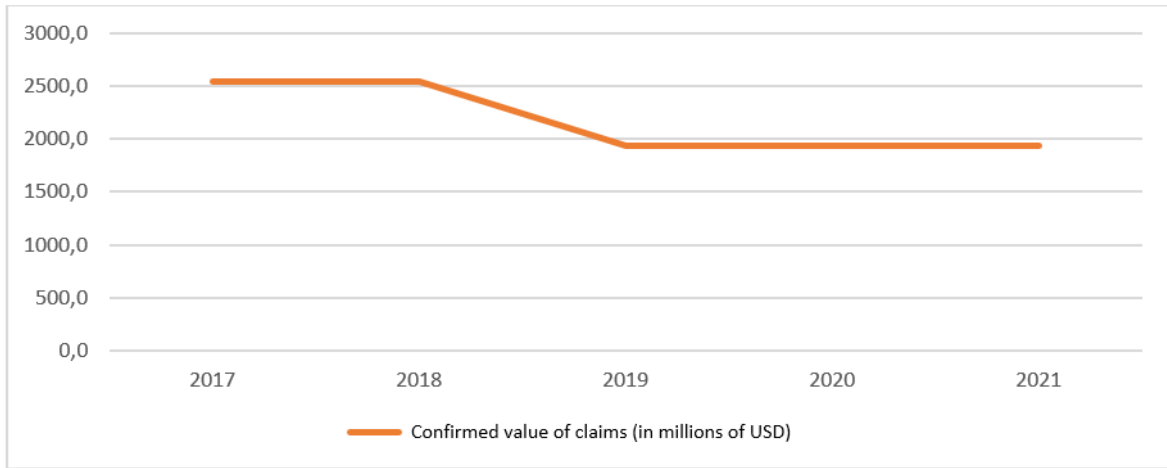
**Table 33.** Adopted indicators

Indicator	Weight in percentage
Confirmed amount of claims (in million euros)	25
Confirmed amount of claims (in million USD)	25
Confirmed amount of claims (in million PLN)	25
Cooperation with law firms in arbitration cases	25

In the period 2012–2017, the number and value of claims in contentious disputes between the Polish state and companies requiring knowledge of foreign law increased. Unfortunately, since 2017 the General Prosecutor's Office has not been providing data related to this problem in its annual reports. However, in June 2021, it informed the media that Poland was in the course of nine arbitration proceedings in which it was the defendant. The total value of these claims is PLN 12 billion, which means a further increase in the value of claims since 2017.

**Chart 46.** Value of claims against Poland in various currencies





Credibility index value for the international arbitration dimension	<b>0.13</b>
---------------------------------------------------------------------	-------------

<b>Value of the credibility index for the area: respecting international obligations</b>	<b>- 0.07</b>
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## Summary

The judgments of the CJEU and the ECHR confirm that the personnel and institutional changes in the Polish judiciary undermine Poland's international obligations resulting from the EU membership. These changes have brought about chaos in the legal system and, consequently, uncertainty of trading and protection of participants in court proceedings, especially in the case of EU investors. The latter operate within the framework of the European legislation and cannot invoke arbitration clauses contained in the bilateral investment treaties with the Member States terminated by Poland due to the accession to the EU. These investors must therefore defend their rights in common courts in Poland (as the EU courts), but their independence may be questioned. Moreover, this may result in further complaints to the ECHR. But the situation may deteriorate even further. None of the projects of the ruling party meets the three conditions (milestones) of the European Commission with regard to the National Recovery Plan. As a result, most likely, Poland will not receive money from the Recovery and Resilience Facility (RRF). Further individual and institutional complaints lodged with European courts and concerning violations of EU law by Polish authorities are also highly probable. As a consequence, a scenario is possible that EU states and institutions will decide to introduce a conditionality mechanism linking the Multiannual Financial Framework with compliance with the rule of law. In such case, Poland is bound to encounter a serious problem with the use of EU funds, which constitute a significant part of public investments in the Polish economy. The fundamental challenge for the functioning of the Polish legal system within the EU and for Poland's compliance with international obligations is the draft reform of common courts presented by the Ministry of Justice at the end of April 2022. If passed, numerous new violations of the EU treaties and the Charter of Fundamental Rights are to take place. All judges in Poland will be verified by the National Council of the Judiciary, which meets neither the obligations of the Polish Constitution nor the requirements of European legislation. This will mean a priori defectiveness of all judgments issued by Polish courts and, as a result, a possible large scale of complaints from citizens and companies, including foreign ones, to the European Court of Human Rights, invoking Poland's failure to fulfil its treaty obligations.

Recommendations for public authorities:

1. Full implementation of all CJEU and ECHR judgments.
2. Enforcement of Poland's obligations under the National Recovery Plan.

## IX. Qualitative research results

### Qualitative research methodology

The qualitative research complements the quantitative analysis of Poland's economic credibility. Its main goal is to identify factors which may pose a threat in the next three years.

The study was conducted using a modified Delphi group expertise method. The group of experts was composed of representatives of the academic community, public administration bodies, non-governmental and financial institutions, consulting companies and organizations associating entrepreneurs. The experts shared their knowledge and experience *pro publico bono*, expressing only their own views, and not the views of the institutions in which they are engaged.

The study consisted of two stages:

- Stage I: 12 April 2022 - 06 May 2022,
- Stage II: 09 May 2022 - 03 June 2022.

In the first stage, questionnaires were sent to the experts, asking them to identify the three most important threats to Poland's economic credibility in individual areas of the index. Obtained were responses of 116 experts, who indicated a total of 374 threats.

The indicated factors were grouped into homogeneous classes. Aggregation of threats made it possible to compile a list of several key threats in individual areas.

**Table 34.** The number of threats to Poland's economic credibility after the grouping procedure

No	Are of Poland's economic credibility index	Number of threats
1	The rule of law and security of economic transactions, meritocracy	11
2	Freedom of economic activity	15
3	Public finances – tax system	13
4	Stability of financial system and money	13
5	Labour protection and security	12
6	Quality of public services and public infrastructure	14
7	Respecting international obligations	8

Source: OEEs study.

In the second stage, the experts assessed significance and importance of the grouped and aggregated threats to Poland's economic credibility and probability of occurrence thereof. For each area of the index, lists of experts and threats were created.

Each expert had 100 points at their disposal to divide between the threats in terms of their importance. The greater the number of awarded points, the greater the significance of a given threat to Poland's economic credibility in the next three years. Additionally, the participants of the study gave their subjective assessment of the probability of occurrence of each threat (from 0 to 100%).

The results obtained from 115 experts were then averaged. In this manner, a map of threats to Poland's economic credibility was created for each of the seven analysed areas. Graphic presentation of aggregated opinions consisted in placing circles on the chart, where the average probability is indicated on the abscissa axis, and the averaged hazard weight on the ordinate axis. The diameter of the circles is the average of the products of the values: probability and weight. Thus, the greater the diameter of the circle, the greater the combined significance of discussed threat.

As a supplement to the threat map, there is given a percentage of experts pointing to a specific factor.

## The rule of law and security of economic transactions, meritocracy

In the area of the rule of law and security of economic transactions and meritocracy, there have been identified 11 threats.

**Table 35.** Threats to Poland's economic credibility in the area of the rule of law and security of economic transactions, meritocracy.

No	Threat
1.	Lack of transparency of rules and violation of rules in the law-making process (omission of consultations with stakeholders, abuse of special procedures, violation of the mode of submitting and the level of drafts)
2.	Instability of legal regulations weakening legal security of citizens and institutional entities and undermining trust in the state and its law
3.	Nepotism and politicization of positions in state-owned companies and public institutions
4.	Institutional destruction of the judiciary resulting in uncertainty about durability of judgments (threat to the protection of rights of citizens and businesses)
5.	Restricted access to the EU money due to rule of law conflict
6.	Actions of the government and public institutions weakening Poland's credibility in the international arena (selective presentation to the public opinion of information and arguments not supported by facts)
7.	Abuse in the area of obtaining, collecting, and using information about citizens and institutional entities by public institutions
8.	Combining function of the prosecutor general with position of the minister of justice
9.	Low effectiveness and predictability of the judiciary
10.	Problems in defining division of competences between state authorities
11.	Hindering (preventing) free media from performing a controlling function

Source: OEEs study.

The experts primarily identified threats related to the legislative process, including non- transparency of the rules and their violation in the law-making process (1) and instability of legal regulations weakening the legal security of citizens and institutional entities and violating trust in the state and its law (2). In the experts' view, improper conduct is found at all stages of the legislative process: from draft legal changes, which are often motivated by political interest, through the mode of submitting drafts, including the abuse of special procedures, omitting the stage of giving opinions and consulting with stakeholders and social partners, to threats resulting from the way of managing the work of the Sejm. Violations of the rules of law-making result in a low substantive level of the adopted regulations, and consequently lead to their frequent amendments which weaken stability of the regulations in force.

The second group of threats is related to institutional conditions of the judiciary. The experts pointed to institutional destruction of the judiciary resulting in a lack of certainty as to durability of

judgments (a threat to the protection of rights of citizens and businesses) (4) and the related limitation of access to EU funds due to the conflict over the rule of law (5). These are primarily changes in the Constitutional Tribunal and the unconstitutional establishment of the National Council of the Judiciary, resulting in undermining the principle of the separation of powers and independence of judges. An additional threat to Poland's economic credibility in the area of the rule of law is combining the function of the prosecutor general with the position of the minister of justice (8).

The experts have also brought about the threat resulting from abuses arising out of acquisition, collection, and use by public institutions of information about citizens and institutional entities (7).

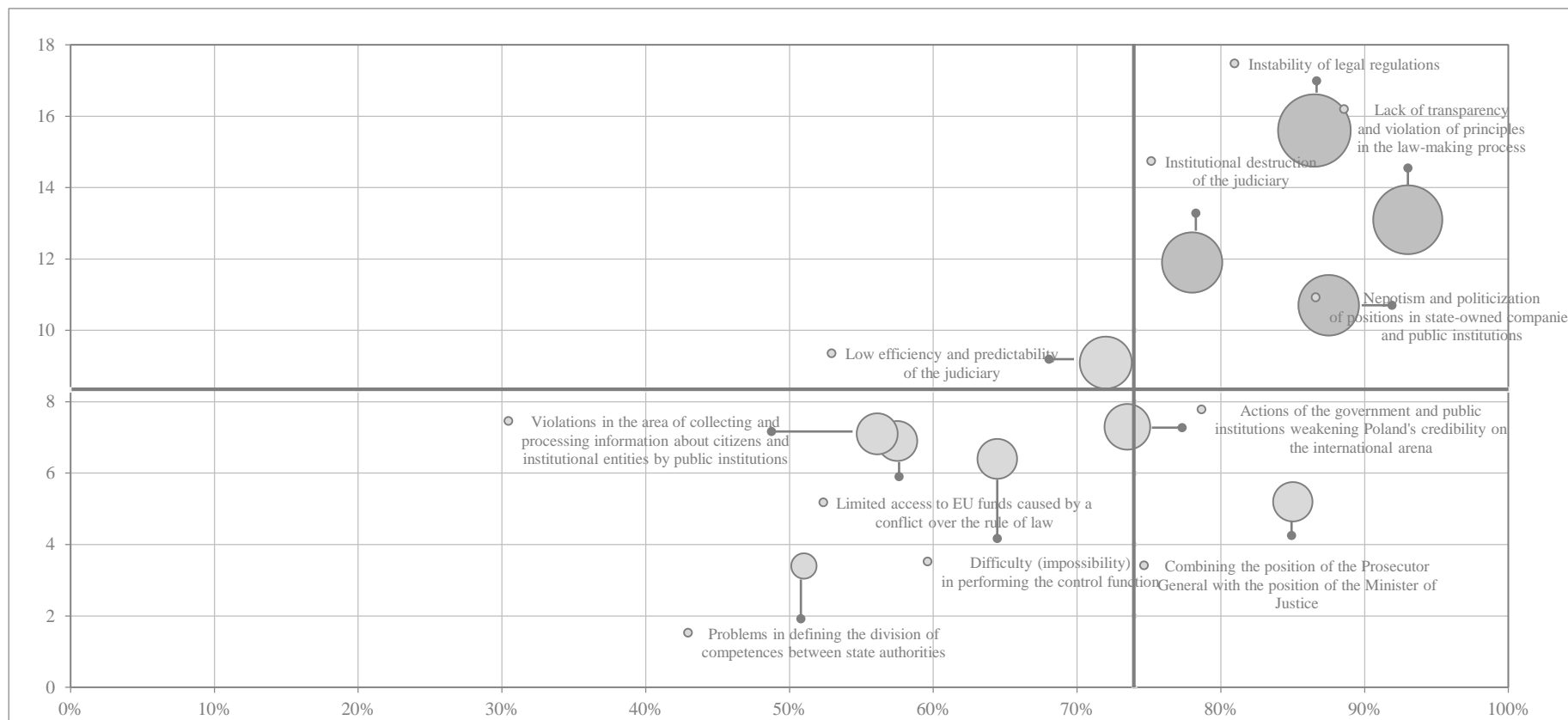
Just as dangerous are actions of the government and public institutions which weaken Poland's credibility in the international arena (selective presentation to the public opinion of information and arguments not supported by facts) (6).

In the experts' opinion, the analysis of economic credibility of Poland in the area of the rule of law requires taking into account such additional factors as:

- nepotism and politicization of positions in state-owned companies and public institutions (3), reflecting the state's personnel policy, in which the political affiliation of the management staff plays a crucial role, while the importance of actual competences is limited,
- low efficiency and predictability of the judiciary (9), manifested on the one hand by lengthiness of court proceedings, and on the other hand, by randomness of issued decisions,
- difficulty in defining the division of competences between state authorities (10), including between the police, prosecutor's office, and court,
- hindering (preventing) the free media from performing a controlling function (11), including primarily by impeding their functioning.

The map of threats to the discussed area shows four phenomena of great importance.

**Figure 1.** A map of threats to Poland's economic credibility in the area of the rule of law and security of economic transactions and meritocracy in the next three years



\* lines on the map were drawn on the basis of the average weight of threats and average probability of occurrence of a given factor.

\*\* size of the circle represents the average of the product of the weight and the probability of the occurrence of a given threat

Source: OEEES study



Instability of legal regulations is forecast to be the most important threat in the next three years as it will weaken the legal security of citizens and institutional entities and violate trust in the state and its law. The importance of this factor has been assessed by the experts at the level of 15.6 points, and the probability of its occurrence at the level of 87%.

The second most serious risk is the lack of transparency of the rules and their violation in the law-making process. The average importance of this factor was assessed at the level of 13.1 points. At the same time, this risk was assigned the highest predicted probability (93%).

In addition, institutional destruction of the judiciary (weight 11.9 points and probability of 78%) as well as nepotism and politicization of positions across State Treasury companies and public institutions (weight 10.7 points and probability of 88%) will be of significant importance for economic credibility of Poland.

Six out of eleven threats identified in the first stage of the study were considered significant by all experts (100% of indications in the second stage of the study) (see Table 36).

**Table 36.** Frequency of occurrence of individual threats to Poland's economic credibility in the area of the rule of law and security of economic transactions and meritocracy

No	Threat	Percentage of indications*	Weight ranking **	Probability ranking**
1.	Lack of transparency and violation of principles in the law-making process	100	(2)	(1)
2.	Instability of legal regulations	100	(1)	(3)
3.	Nepotism and politicization of positions in state-owned companies and public institutions	100	(4)	(2)
4.	Institutional destruction of the judiciary	100	(3)	(5)
5.	Restriction of access to EU funds due to conflict over the rule of law	80	(8)	(9)
6.	Actions by the government and public institutions weakening Poland's credibility in the international arena	100	(6)	(6)
7.	Violations in the area of collecting and processing information about citizens and institutional entities by public institutions	100	(7)	(10)
8.	Combining function of the prosecutor general with position of the minister of justice	80	(10)	(4)
9.	Low efficiency and predictability of the judiciary	90	(5)	(7)

10.	Problems in defining division of powers between state authorities	60	(11)	(11)
11.	Making it difficult (impossible) for free media to perform a control function	90	(9)	(8)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the threat with the highest weight/probability of occurrence

*Source: OEEs study*

## Freedom of business activity

In the area of freedom of business activity, there were identified 15 threats.

**Table 37.** Threats to Poland's economic credibility in the area of freedom of economic activity

No	Threat
1.	Ineffective law-making system resulting in high volatility of running a business activity
2.	Instability and lack of transparency of the tax system
3.	Limited labour supply and high level of employee protection resulting in high labour costs
4.	Politicization of regulatory changes in the area of economic law
5.	Inefficiency of public administration, including bureaucratisation, lengthiness of administrative procedures in business, personnel shortage and diversification of the level of service quality within public administration
6.	Politicization of state-owned companies and public administration
7.	Undertaking actions which distort competition or profitability of doing business, discriminate against arbitrarily selected industries, restricting the possibility of conducting business activity
8.	Ineffective fiscal control system, undermining trust in public institutions (violation of the principle of presumption of honesty, principle of presumption of facts in favour of the entrepreneur, or rules of resolving doubts as to the content of a legal norm in favour of the entrepreneur)
9.	Significant limitation of legal certainty related to institutional reconstruction of the judiciary and resulting in a decrease in certainty of economic transactions
10.	Inefficiency of the judiciary in economic cases (lengthiness and high costs of court proceedings)
11.	Technological risk (cybersecurity, blockchain, cryptocurrency market, payment systems) combined with structural barriers to the development of innovation
12.	Political risk resulting from war threats (restrictions on international trade, crowding-out effects by defense investments, investment risk - especially in some border regions)
13.	Risk related to competition law, in particular in the context of intellectual and industrial property rights
14.	Low legal status of economic self-government, limiting efficiency of entrepreneurs' representation before public authorities
15.	Financial barriers to business activity (limited access to capital, payment backlogs)

Source: OEES study

The experts indicated factors related to the issue of law-making. The first one concerns the weakness of law-making, resulting in high volatility of regulations within the area of running a business activity (1), instability and lack of transparency of the tax system (2), as well as limitation of legal certainty related to institutional reconstruction of the justice system (9).

The second group consists of threats resulting from inefficiency of public administration, courts, and tax authorities. The experts pointed to bureaucratization and personnel shortage, which result in lengthy administrative procedures (5) and inefficiency of the judiciary in economic matters (10) (lengthiness and high costs of court proceedings). The negative impact of competition-restricting measures was also emphasised, as they lead to reduction in profitability of running a business activity

and discrimination of selected industries (7). Included in this group was low efficiency of the fiscal control system, undermining trust in public institutions. It manifests itself primarily in violation of the principle of presumption of fairness and resolving doubts as to the content of a legal norm in favour of the entrepreneur (8).

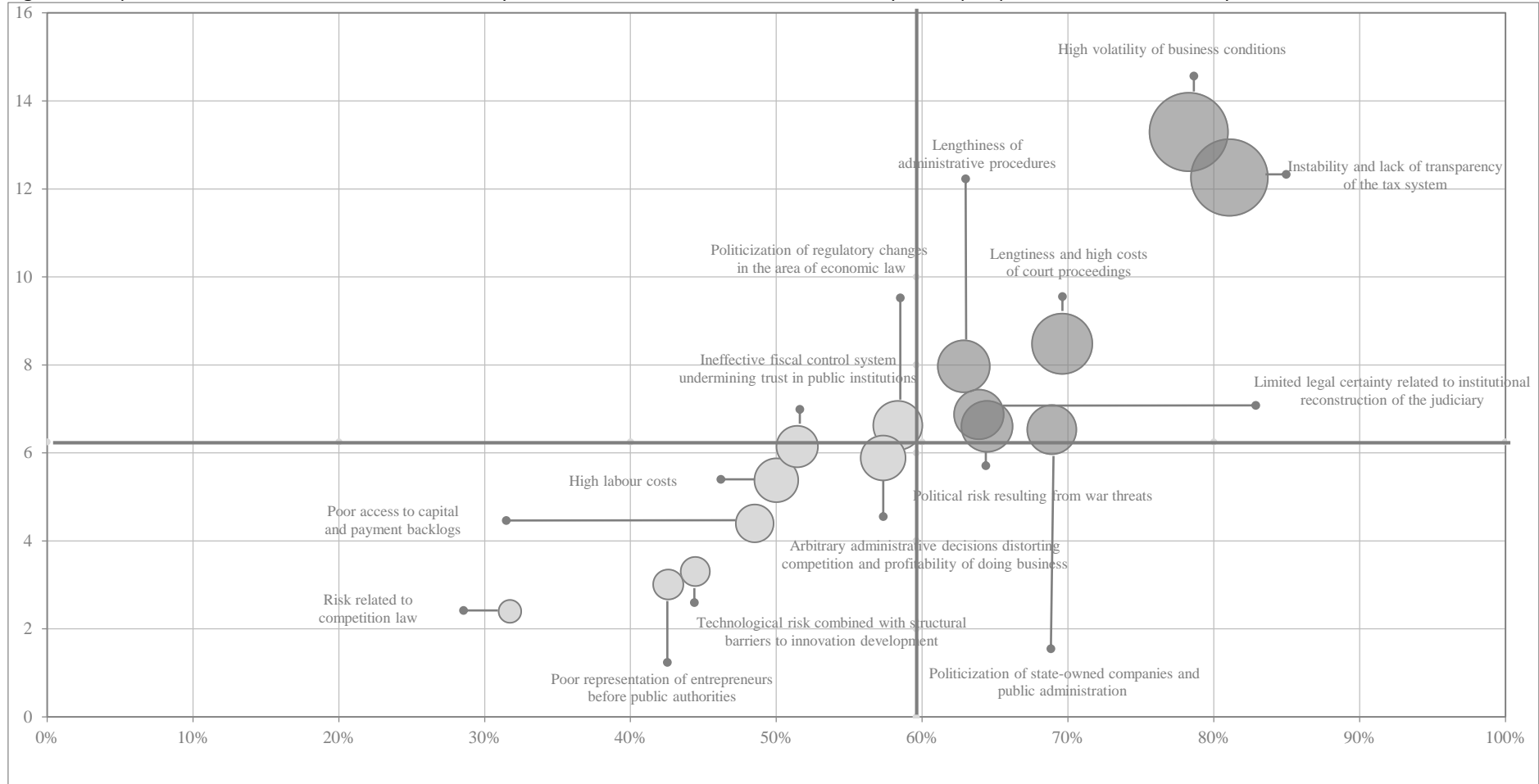
Another identified group of threats consisted of factors related to politicization of both public administration, including State Treasury companies (6), and the introduced regulatory changes in the area of economic law (4). In this context, the experts pointed to: weakening of protection of property rights, limiting economic freedom and introducing changes with the use of lower order legal acts, reducing the role of social consultations, and lack of adequate *vacatio legis*. As a result, enterprises do not have enough time to prepare and adapt to the new requirements.

While analysing threats to Poland's economic credibility related to the freedom of economic activity, the experts also formulated the following risks and barriers:

- political risk resulting from war threats - causing restrictions in international trade, intensifying the crowding-out effects of defense investments (12),
- high labour costs in conditions of limited supply on the labour market (3),
- financial barriers to business activity (limited access to capital, payment backlogs) (15)
- technological risk (including, above all, cybersecurity, blockchain, cryptocurrency market, payment systems) combined with structural barriers to innovation (11),
- poor representation of entrepreneurs before public authorities (14),
- risks related to competition law, in particular in the context of intellectual and industrial property rights (13).

The map shows seven threats of extraordinary importance.

**Figure 2.** Map of threats to Poland's economic credibility in the area of freedom of economic activity in the perspective of the next three years



\* size of the circle represents the average of the product of the weight and the probability of the occurrence of a given threat

Source: OEEs study

These include:

- high volatility of conditions for running a business activity (threat weight 13.3 points, probability of occurrence 78%),
- instability and lack of transparency of the tax system (12.3 points and 81% respectively),
- lengthiness and high costs of court proceedings (8.5 points with a probability of 70%),
- lengthiness of administrative procedures (ineffectiveness of public administration, including bureaucratization, staff shortages) with an average weight of 8 points and a probability of 63%,
- limited legal certainty related to institutional reconstruction of the judiciary, which may result in the lack of certainty in the scope of issued judgments, translating into a decrease in the certainty of economic transactions (6.9 points with the probability of occurrence at the level of 64%),
- political risk resulting from war threats exerting a negative impact and causing numerous restrictions on international trade, to which the experts gave an average of 6.6 points, and the probability was estimated at 64%,
- politicization of state-owned companies and public administration (average risk weight of 6.5 points and probability of 69%).

**Table 38.** Frequency of individual threats to Poland's economic credibility in the area of freedom of economic activity

No	Threat	Percentage of indications*	Weight ranking**	Probability ranking**
1.	High volatility of conditions for running a business activity	100	(1)	(2)
2.	Instability and lack of transparency of the tax system	97	(2)	(1)
3.	High labour costs	86	(11)	(11)
4.	Politicization of regulatory changes in the area of economic law	86	(6)	(8)
5.	Lengthiness of administrative procedures	100	(4)	(7)
6.	Politicization of state-owned companies and public administration	90	(8)	(4)
7.	Arbitrary administrative decisions distorting competition and profitability of running a business activity	93	(10)	(9)
8.	Ineffective fiscal control system undermining trust in public institutions	97	(9)	(10)
9.	Limited legal certainty related to institutional reconstruction of the judiciary	93	(5)	(6)
10.	Lengthiness and high costs of court proceedings	93	(3)	(3)
11.	Technological risk combined with structural barriers to innovation development	90	(13)	(13)
12.	Political risk resulting from war threats	93	(7)	(5)
13.	Risk related to competition law	76	(15)	(15)
14.	Weak representation of entrepreneurs before public authorities	83	(14)	(14)
15.	Poor access to capital and payment backlogs	79	(12)	(12)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the threat with the highest weight/probability of occurrence

Source: OEES study

### Public finances - the tax system

In the area of "public finance – the tax system", there have been identified 13 key threats.

**Table 39.** Threats to Poland's economic credibility in the area of public finances and the tax system

No	Threat
1.	Instability, lack of predictability of the tax system, lack of extensive consultations when introducing changes, short time for introducing changes
2.	Complexity, lack of transparent and rational rules of the tax system
3.	Non-transparency of public finances caused by the increase in the scale of off-budget financing
4.	Ineffective fiscal policy, including pro-cyclical change of fiscal rules, circumvention of the expenditure rule and lack of credible medium-term planning, lack of coordination of fiscal and monetary policies
5.	Increase in the cost of public debt financing
6.	Deterioration in availability of public debt financing
7.	Extensive social policy
8.	Disturbance of predictability of public revenue redistribution streams between the central and local government administration
9.	Deterioration of public finances (increase in public debt, lower government and local government balance)
10.	Conflict with the European Union, resulting in reduction of EU funds
11.	Growth in tax evasion and organized economic and financial crime
12.	Reducing the rank of the Minister of Finance in the Council of Ministers
13.	No management of the structure and quality of public expenditure, no rules for prioritizing expenditure

Source: OEES study.

The experts primarily pointed to instability and unpredictability of the tax system, combined with the lack of extensive consultations when introducing changes and a short time to implement them (1), as well as complexity and the lack of transparent and rational rules of the tax system (2). As for the first threat, attention was drawn to the so-called tax law inflation, as manifested by frequent and radical changes to regulations, including changes made during the tax year or changes with a retroactive date. Complexity and the lack of transparent and reasonable rules of the tax system intensify the introduction of numerous para-taxes and indirect levies, with the simultaneous application of tax reliefs and preferences. Additionally, the experts pointed to the solutions adopted under the Polish Order, which are unfavourable from the point of view of transparency of the tax system. These activities lead to interpretation difficulties and increase the risk of errors and abuse.

Non-transparency of public finances intensifies the scale of extra-budgetary financing (3), particularly special purpose funds and government programmes, which are not subject to ongoing budget reporting. Such conduct lowers the effectiveness of the stabilizing expenditure rule and significantly hinders control over public expenditure.

An emphasis was put on the threats resulting from ineffective fiscal policy (4), including a pro-cyclical change of fiscal rules, circumventing the expenditure rule, and the lack of reliable medium-term planning. There are concerns about the lack of coordination of fiscal and monetary policies.



Moreover, the experts identified factors related to public debt financing. Here, they pointed to the risk of increase in the cost of financing public debt (5), resulting in particular from the forecast increase in interest rates. Moreover, instability of the system further deteriorates availability of public debt financing (6). The decline in availability of debt financing may result from the global economic downturn combined with high inflation, as well as from demand constraints on the part of Polish banks and reduced activity of foreign investors.

Other threats concern public spending. Attention was drawn to the extensive social policy (7), deterioration of public finances: an increase in the level of public debt and a decrease in the government and local government balance (9), as well as the lack of management of the structure and quality of public expenditure, coupled with there being no expenditure prioritization rules (13).

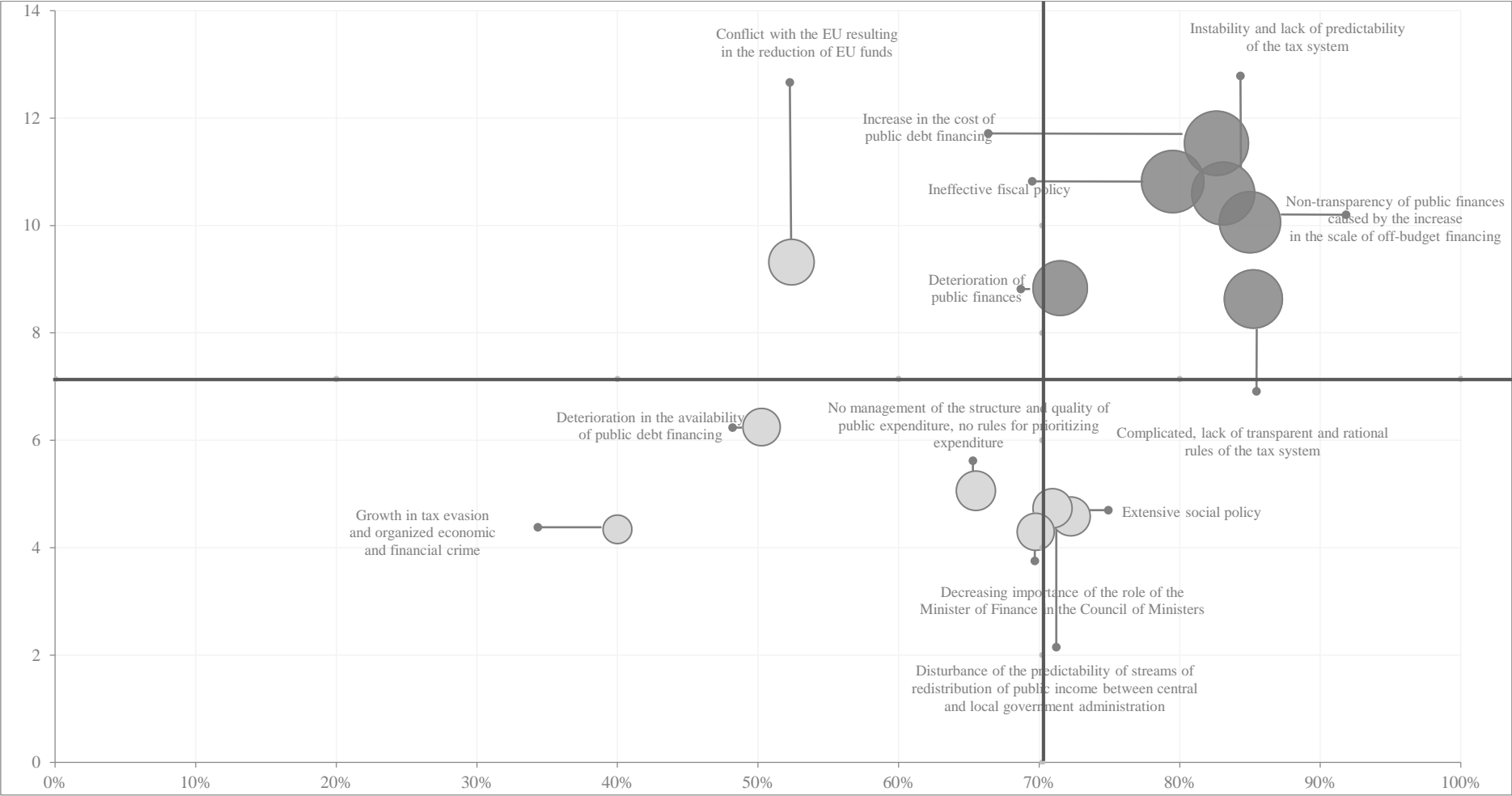
Moreover, a disturbance in the predictability of redistribution of public revenues between the central and local government administration was signaled (8). As part of this factor, the experts pointed to both progressive centralization of public finances and tax changes which are unfavourable for local government units.

Another threat identified by experts is the conflict with the European Union, resulting in reduction of EU funds (10). This threat includes, first of all, the breach of the rule of law, which may result in the loss or suspension of disbursement of some European funds, and in the longer term contribute to deepening of the imbalance in public finances and a decrease in Poland's fiscal credibility for foreign investors.

The factors which may appear as threatening in this area are also the increase in the scale of tax avoidance and organized economic and financial crime (11), as well as the factor related to the decrease in the rank of the minister of finance in the Council of Ministers (12).

The map shows six threats that are of extraordinary importance.

**Figure 3.** Map of threats to Poland's economic credibility in the area of public finances and the tax system in the perspective of the next three years



\* size of the circle represents the average of the product of the weight and the probability of the occurrence of a given threat

Source: OEEs study.

Particular attention should be paid to the threats located in the upper right-hand area. Here are the six most important threats. The greatest predicted increase in the next three years is the increase in the cost of financing public debt (average assessment of the importance of this threat was 11.5 points). At the same time, it is a factor with a very high forecast probability of occurrence (83%).

The second most significant threat is ineffective fiscal policy – the experts have estimated the importance of this threat at an average level of 10.8 points with the predicted probability of 80%.

The third threat is instability and unpredictability of the tax system (average assessment of the threat's importance was 10.6 points with the predicted 83% probability of occurrence). Another threat related to the national tax system is complexity, lack of transparent and rational rules of the tax system (average weight rating of 8.6 points). Moreover, this factor is characterized by the highest probability of occurrence - over 85%.

Significant threats forecast for the next three years also include: non-transparency of public finances caused by the increase in the scale of extra-budgetary financing (the importance of this factor was assessed at 10.1 points with the probability of its occurrence at the level of 85%) and deterioration of public finances (average risk weight 8.8 points and probability at the level of 72%).

**Table 40.** Frequency of individual threats to Poland's economic credibility in the area of the public finance and tax system

No	Threat	Percentage of indications*	Weight ranking**	Probability ranking**
1.	Instability and lack of predictability of the tax system	95	(3)	(3)
2.	Complexity, lack of transparent and reasonable rules of the tax system	91	(7)	(1)
3.	Non-transparency of public finances caused by the increase in the scale of off-budget financing	95	(4)	(2)
4.	Ineffective fiscal policy	91	(2)	(5)
5.	Increase in the cost of public debt financing	100	(1)	(4)
6.	Deterioration in availability of public debt financing	76	(8)	(12)
7.	Extensive social policy	81	(11)	(6)
8.	Disturbance of predictability of streams of redistribution of public revenues between central and local government administration	71	(10)	(8)
9.	Deterioration of the condition of public finances	91	(6)	(7)
10.	Conflict with the EU resulting in the reduction of EU funds	100	(5)	(11)

11.	Growth in tax evasion and organized economic and financial crime	86	(12)	(13)
12.	Reducing the importance of the Minister of Finance in the Council of Ministers	86	(13)	(9)
13.	No management of the structure and quality of public expenditure, no rules for prioritizing expenditure	81	(9)	(10)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the hazard with the highest weight/probability of occurrence

*Source: OEES study*

## Stability of the financial system and money

In the area of financial system and money stability, in the first stage of the study, 13 threats were identified.

**Table 41.** Threats to Poland's economic credibility in the area of the financial system and money stability

No	Threat
1.	Erroneous monetary and fiscal policy, including a lack of coordination in both areas
2.	Legal risk related to loan agreements (foreign currency loans, loans based on WIBOR). Instability of the regulatory environment, including "manual" control of the banking sector operations, disrupting market mechanisms (e.g. with regard to interest rates)
3.	Non-transparency of public finances, in particular caused by the increase in the scale of extra-budgetary financing
4.	Dramatic decline in the credibility of the National Bank of Poland/lack of reliable communication of the monetary authorities with market participants
5.	Deterioration of balance of financial institutions due to their recent appetite to purchase Treasury bonds (stimulated, among others, by the method of calculating the tax on bank assets), deterioration in the quality of the loan portfolio and insufficient high-quality corporate governance at state-controlled banks
6.	No effective counter-cyclical macro-prudential policy
7.	Politicization of financial safety net institutions
8.	Depreciation of the Polish zloty
9.	High level of inflation resulting in reduced demand and investment
10.	Institutional destruction of the judiciary
11.	Persistence of the inflation and wage spiral
12.	Low share of investments in GDP, posing a threat to the long-term development capacity of the Polish economy
13.	Insufficient forecasting competences in domestic financial institutions

Source: OEES study.

Expert indications allowed to identify, first and foremost, the threat related to erroneous monetary and fiscal policy (1). Low effectiveness of monetary and fiscal policies was emphasized, as well as the lack of coordination between them, defined as an effective policy mix. Attention was drawn to the inadequate and delayed reactions of the central bank to the rising inflation, harmful combination of the (tightened) monetary policy with (loosened) fiscal policy, manifested by the expansion of public expenditure policy and tax cuts amid the rapidly rising inflation.

Moreover, brought to light was instability of the regulatory environment (2). First of all, there was indicated the legal risk related to mortgage loans in CHF (risk of contract cancellation) and PLN loans (risk of litigation with regard to WIBOR rates; risk of administrative control of the price of loans or the

WIBOR rate). Another problem is the lack of reaction and no intention of the state to resolve the dispute between borrowers and banks, which, given the scale of this phenomenon, threatens the stability of banks and financial system in the long term. Attention was also paid to the risk caused by the lack of stability of the regulatory environment, including the "manual" control of the banking sector, disrupting market mechanisms.

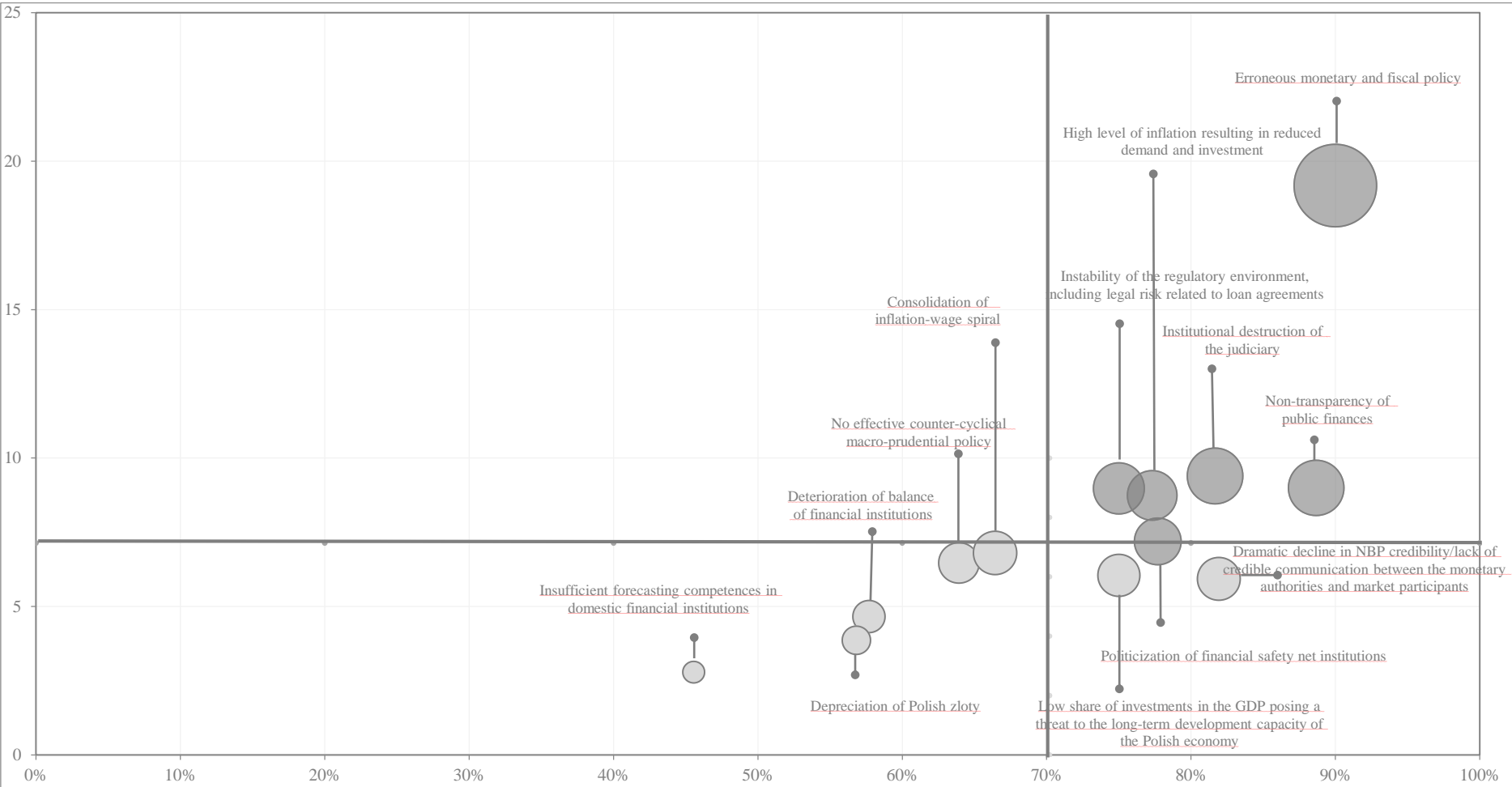
The most frequently indicated threats include non-transparency of public finances (3), caused in particular by the increase in the scale of extra-budgetary financing, which may lead to errors in the macroeconomic and macro-financial policy. The experts have also categorized the lack of an effective anti-cyclical macroprudential policy (6) and politicization of the financial safety net institutions (7) as a threat.

Another identified risk concerns deterioration of balance sheets of financial institutions (5). On the one hand, the experts emphasized high exposure of banks to treasury bonds (stimulated, among others, by the method of calculating the bank tax), which, in the face of rising interest rates, will adversely affect results of financial institutions and raise capital requirements. On the other hand, the experts observed threats related to deterioration of the quality of the loan portfolio and low level of corporate governance in the banks controlled by the State Treasury, which, in turn, may affect financial results of these banks.

Moreover, expert indications concerned threats related to the institutional destruction of the judiciary (10). According to the experts, politicization of the judiciary and the poor quality of law-making are not conducive to building a stable financial and money system.

The map of threats for the analysed area shows a group of six key concerns over the next three years.

**Figure 4.** Map of threats to Poland's economic credibility in the area of the stability of the financial system and money in the perspective of the next three years



\* the circle size represents the average of the product of the weight and probability of occurrence of a given threat

Source: OEEs study.

Erroneous and uncoordinated monetary and fiscal policy constitutes the greatest threat to the stability of the financial system and money (the average assessment of the importance of this threat was 19.2 points). Importantly, it is also a factor with the highest predicted probability of occurrence (90%).

The second most significant threat is institutional destruction of the judiciary, whose impact on the market was assessed by experts at 9.4 points, with the probability of occurrence at the level of 82%.

Non-transparency of public finances is the third most important factor causing concern of the experts. Its weight is assessed at an average level of 9 points with the predicted probability of 89%. The experts also express their concern as to instability of the regulatory environment (9 points), including the legal risk resulting from mortgage loan agreements and possibility of statutory interference in the process of determining interest rates on deposits in the banking sector, with the probability estimated at 75%.

Estimated at 77% was the probability of a high level of inflation resulting in a reduction in demand and investment in the economy, due to high interest rates (average assessment of the threat's importance was 8.7 points). The possibility of politicizing the institutions of the financial safety net - KNF, NBP, BFG is forecast at a similar level - 78%, although it has received a slightly lower weight - 7.2 points.

Two factors: radical decline in the credibility of the National Bank of Poland and lack of reliable communication between monetary authorities and market participants, as well as the low share of investment in GDP posing a threat to the long-term development capacity of the Polish economy, are considered highly probable (82% and 75%) by the experts. The importance of their impact on economic credibility of Poland is markedly lower than that of the previously mentioned factors - 5.9 and 6 points respectively.

**Table 42.** Frequency of individual threats to Poland's economic credibility in the area of stability of the financial system and money

No	Threat	Percentage of indications*	Weight ranking**	Probability ranking**
1.	Erroneous fiscal and monetary policy	100	(1)	(1)
2.	Instability of the regulatory environment, including legal risk related to loan agreements	93	(4)	(7)
3.	Non-transparency of public finances	87	(3)	(2)
4.	Dramatic decline in credibility of the National Bank of Poland/lack of credible communication between monetary authorities and market participants	73	(10)	(3)



5.	Deterioration of balance of financial institutions	80	(11)	(11)
6.	No effective counter-cyclical macro-prudential policy	87	(8)	(10)
7.	Politicization of financial safety net institutions	87	(6)	(5)
8.	Depreciation of the Polish złoty	53	(12)	(12)
9.	High level of inflation resulting in reduced demand and investment	73	(5)	(6)
10.	Institutional destruction of the judiciary	80	(2)	(4)
11.	Consolidation of the phenomenon of the inflation-wage spiral	80	(7)	(9)
12.	Low share of investments in GDP posing a threat to the long-term development capacity of the Polish economy	73	(9)	(8)
13.	Insufficient forecasting competences in domestic financial institutions	53	(13)	(13)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the threat with the highest weight/probability of occurrence

*Source: OEEs study*

## Labour protection and security

In the area of labour protection and security, 12 threats were distinguished.

**Table 43.** Threats to Poland's economic credibility with regard to labour protection and security

No	Threat
1.	Lack of universality of age management solutions and those supporting the activity of people at the retirement age
2.	Growing importance of non-standard employment, which limits job stability and employee development opportunities, lack of legal regulations with regard to remote work and other atypical working conditions
3.	Employment in the shadow economy
4.	Lack of flexibility on the labour market, including adapting competences to needs through lifelong learning, especially in the area of digital competences
5.	Difficulties in reconciling family and professional life, which exerts an impact on women's low professional activity
6.	Growing segmentation of the labour market resulting from the impact of various economic and institutional factors
7.	Institutional weakness in the area of labour protection and security, external and internal control of labour conditions and protection
8.	Asymmetry of information on the labour market (e.g. in terms of financial employment conditions)
9.	No migration policy
10.	High labour costs
11.	Weakness of organizational culture (autocratic management style, lack of sensitivity to occupational health and safety culture)
12.	Incompetent change management on the labour market related to the development of technology

Source: OEES study

The experts noticed, first and foremost, the risk associated with the lack of universality of solutions aimed at age management and supporting the activity of people in the retirement age (1). There is a shortage of relevant regulations and actions of employers, enabling, among others, suitable technical adaptation of workplaces, running training to update knowledge, or provision of health care for working senior citizens. The weakness of solutions for people at the retirement age implies high economic burdens for the entire group of working individuals.

Another threat stems from there being no migration policy (9) and the resulting policy of economic and social integration of foreigners (chiefly, Ukrainian citizens), which limits their access to work and will constitute a growth barrier.

The experts also pointed to the growing importance of non-standard employment (2) and the widespread weakness of the organizational culture (11), manifested by an autocratic style of management and low sensitivity to the culture of occupational health and safety.

They pointed out that the increase in non-standard forms of employment may limit the stability of work and possibilities of professional development because employers are not interested in incurring

expenditure on professional development of individuals working in non-standard employment, which deepens the duality of the labour market. The experts' key argument was that the primary goal of legal employment protection is to increase the stability of employment of individuals and the security of their income. Among other things, practices deregulating internal (company) working conditions are reprehensible. Excessive deregulation of the labour market may result in the widespread perception of the domestic labour market as not very employee-friendly. Poland's credibility should be measured by the degree of protection of employees against economic and social disadvantage due to non-standard employment. The experts also commented on the lack of legal regulations with regard to remote work and in other unusual working conditions, including the lack of protection and security of working conditions as part of remote work.

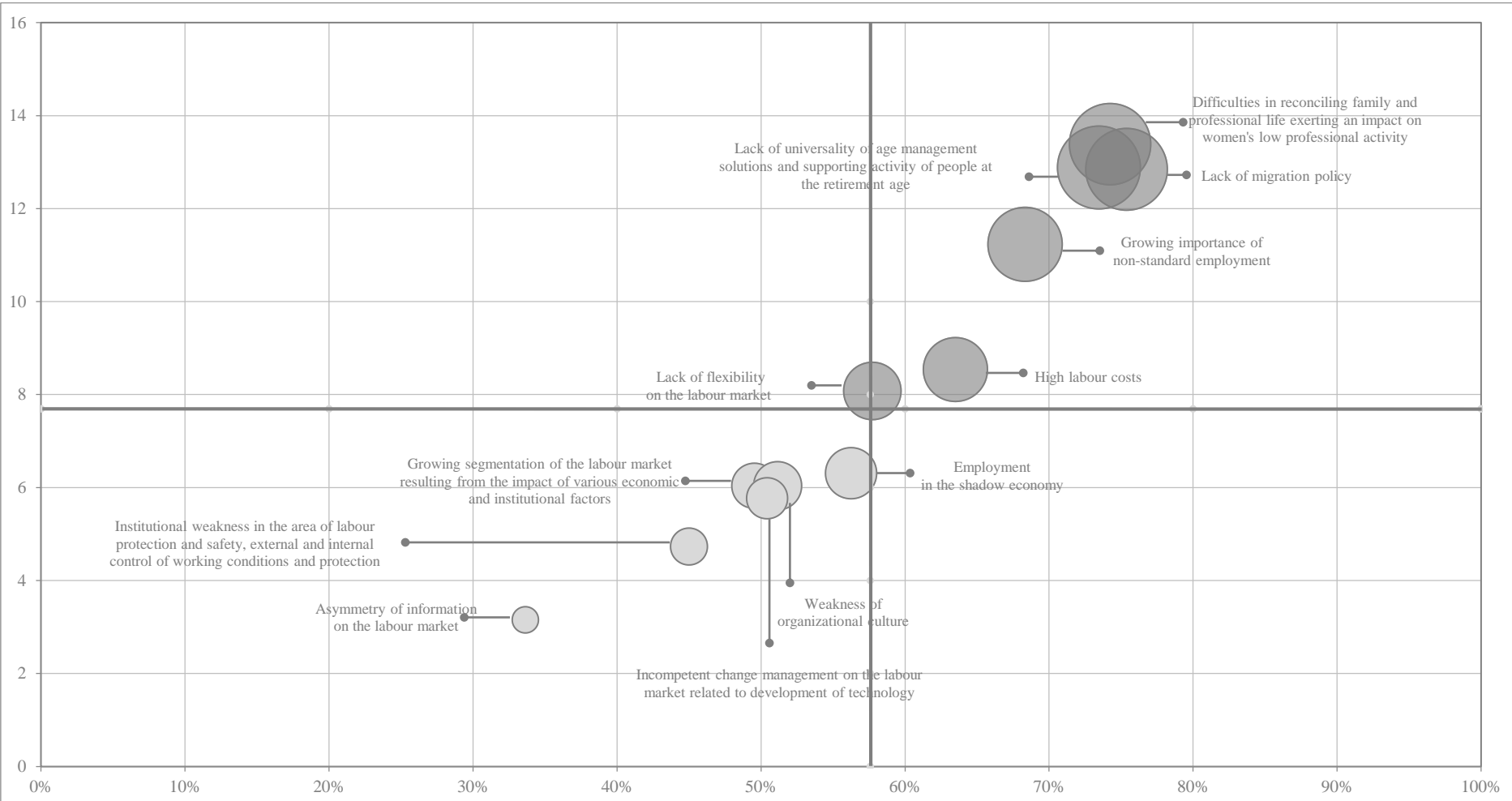
Economic credibility of Poland may also be limited due to:

- employment growth in the shadow economy (3) - the functioning of the shadow economy which, due to lower costs may offer a good/service at a lower price, destroys competitiveness. This means that employees remain outside of (or to a limited extent) social security systems (health, retirement, sickness, or accident related) or outside of the protection of labour law (health and safety, minimum wage, working time, holidays, or dismissals),
- lack of flexibility in the labour market (4) - lack of systemic solutions which would reduce susceptibility to any demand and supply shocks on a global scale, caused by e.g. political and climate factors,
- growing segmentation of the labour market (6) - coexistence of employees with stable and unstable employment contracts, with a limited possibility of moving to more stable segments, means discrimination against significant groups of employees: mainly those young, less qualified, after periods of inactivity (such as women returning to the labour market after maternity leave). The effects of discrimination are: easier job loss, lower wages and pensions in the future, poorer access to training and lower chances of obtaining a loan. A compromise proposal may be a uniform employment contract (SOE), concluded for an indefinite period, in which, however, employee rights increase over time of service;
- inadequate change management in the labour market related to the development of technology (12) - due to the growing percentage of sole proprietorships and/or employees, among others, in the platform work model. No regulation of platform work leads to a heightened risk of insufficient labour protection and security. Another challenge lies in adjusting the social security model to the reality of platform work.

The results of the analysis of threats in the discussed area show that within the period of next three years, the most significant threats (as shown in Fig. 5) will be:

- difficulties in reconciling family and professional life, resulting in low professional activity of women: an average weight rating of 13.4 points (the highest rated risk) with an estimated probability of 74%. The experts have emphasized limited access to childcare facilities, which makes it difficult for parents, especially women, to combine professional work and family responsibilities. This also stands for reduced competitiveness of women on the labour market. The experts have indicated that nearly 1.6 million economically inactive people in the working age indicate family and household responsibilities as the reasons for not looking for a job,
- lack of universality of age management solutions and supporting the activity of people in the retirement age: an average weight rating of 12.9 points with an estimated probability of 74%,
- no migration policy: an average weighting rating of 12.8 points with an estimated probability of 75%.

**Figure 5.** A map of threats to economic credibility of Poland in the area of labour protection and security in the next three years



\* the circle size represents the average of the product of the weight and probability of occurrence of a given threat

Source: OEEs study.

Listed among the most important factors negatively affecting labour protection and security was also the impact of non-standard forms of employment (an average weight rating - 11.2 points with a probability of 68%) and high labour costs (an average weight rating - 8.5 points with a probability of 64%). The experts stressed that excessive labour costs may be a factor encouraging entering the shadow economy.

Lack of flexibility on the labour market, including adapting competences to needs through lifelong learning, especially in the area of digital competences, is the last significant threat to Poland's economic credibility with regard to employment security, assessed at 8.1 points with a probability of 58%. The experience of the COVID-19 pandemic shows that making these solutions more universal would increase resilience of the labour market to supply and demand shocks.

The above-mentioned key threats to economic credibility of Poland in the area of labour protection and security [factors (5), (1), (9), and (2)] were also characterized by the highest percentage of expert opinions (see Table 44).

**Table 44.** Frequency of occurrence of particular threats to economic credibility of Poland in the area of labour protection and security

No	Threat	Percentage of indications*	Weight ranking**	Probability ranking**
1.	Lack of universality of age management solutions and supporting the activity of people at the retirement age	100	(2)	(3)
2.	Growing importance of non-standard employment	92	(4)	(4)
3.	Employment in the shadow economy	85	(7)	(7)
4.	Lack of flexibility on the labour market	85	(6)	(6)
5.	Difficulties in reconciling family and professional life, which exert impact on women's low professional activity	100	(1)	(2)
6.	Increasing labour market segmentation resulting from the impact of various economic and institutional factors	85	(8)	(10)
7.	Institutional weakness in the area of labor protection and security, external and internal control of labour conditions and protection	77	(11)	(11)
8.	Assymetry of information on the labour market	69	(12)	(12)
9.	Lack of migration policy	100	(3)	(1)
10.	High labour costs	69	(5)	(5)
11.	Weakness of organizational culture	92	(9)	(8)
12.	Incompetent change management on the labour market related to development of technology	85	(10)	(9)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the hazard with the highest weight/probability of occurrence

*Source: OEE study*

## Quality of public services and public infrastructure

In the area of the quality of public services and public infrastructure, there have been identified 14 threats.

**Table 45.** Threats to economic credibility of Poland in the area of the quality of public services and public infrastructure

No	Threat
1.	Progressive degradation of the environment and climate combined with the lack of effective regulations in key areas (e.g. heat energy, water policy, or renewable energy sources)
2.	Lack of coherent and credible health protection policy resulting in limited access to health services
3.	Low quality, organizational inefficiency, and politicization of public services
4.	Failure of the education system in terms of developing key competences on the labour market
5.	Insufficient level of computerization and digitization of public services
6.	Lack of trust of the society in public services resulting, among others, from ineffective communication or information warfare, and lack of discussion about civic co-responsibility for the welfare state
7.	Competency limitations of public service sector employees combined with low financial motivation of employees
8.	Lack of reliable analyses justifying implementation of infrastructure projects resulting in limited effectiveness of investment decisions
9.	Lack of solutions to the debt of independent public healthcare institutions
10.	Deficit of multi-level management - division of labour and responsibility between government administration and local government. Lack of coordination of activities implemented in individual ministries
11.	Financial consequences resulting from violations of EU treaties (suspension of payment of EU funds)
12.	Investment uncertainty related to rising prices of raw materials and energy; problems with their availability
13.	Public service overload (especially in education and health) caused by the unprecedented war-related refugee crisis in Ukraine
14.	Threats resulting from the level and structure of financing public expenditure

*Source: OEES study*

The experts are particularly concerned with the manner in which public money is spent. First of all, they pointed to the risk of limiting the level of expenditure on public services and a negative change in their structure (14). In their opinion, the current crisis will lead to an increase in the public finance deficit, one of the main consequences of which may be the need to reduce spending on public services and public infrastructure. Especially that in the medium term, the role of national defence spending in the structure of public spending is bound to increase.

At the same time, the decline in GDP dynamics will exert a negative impact on the income side of public finances. The uncertainty as to the prices of raw materials and energy as well as problems with their availability will also have a detrimental effect on the level of public investment (12). The experts also pointed to the lack of reliable analyses justifying implementation of infrastructure projects, resulting in limited effectiveness of the made investment decisions (8).



Another problem is the low quality, overburden, and under-financing of public services and related politicization thereof (3). These factors contribute to the public's distrust in organizations providing public services (6). In turn, their under-financing translates into insufficient computerization and digitization (5) and the competency limitations of public service sector employees combined with low financial incentives (7). In addition, the current international situation, i.e. the unprecedented refugee crisis triggered by Russia's attack on Ukraine, is overloading the public service sector, in particular with regard to education and health (13).

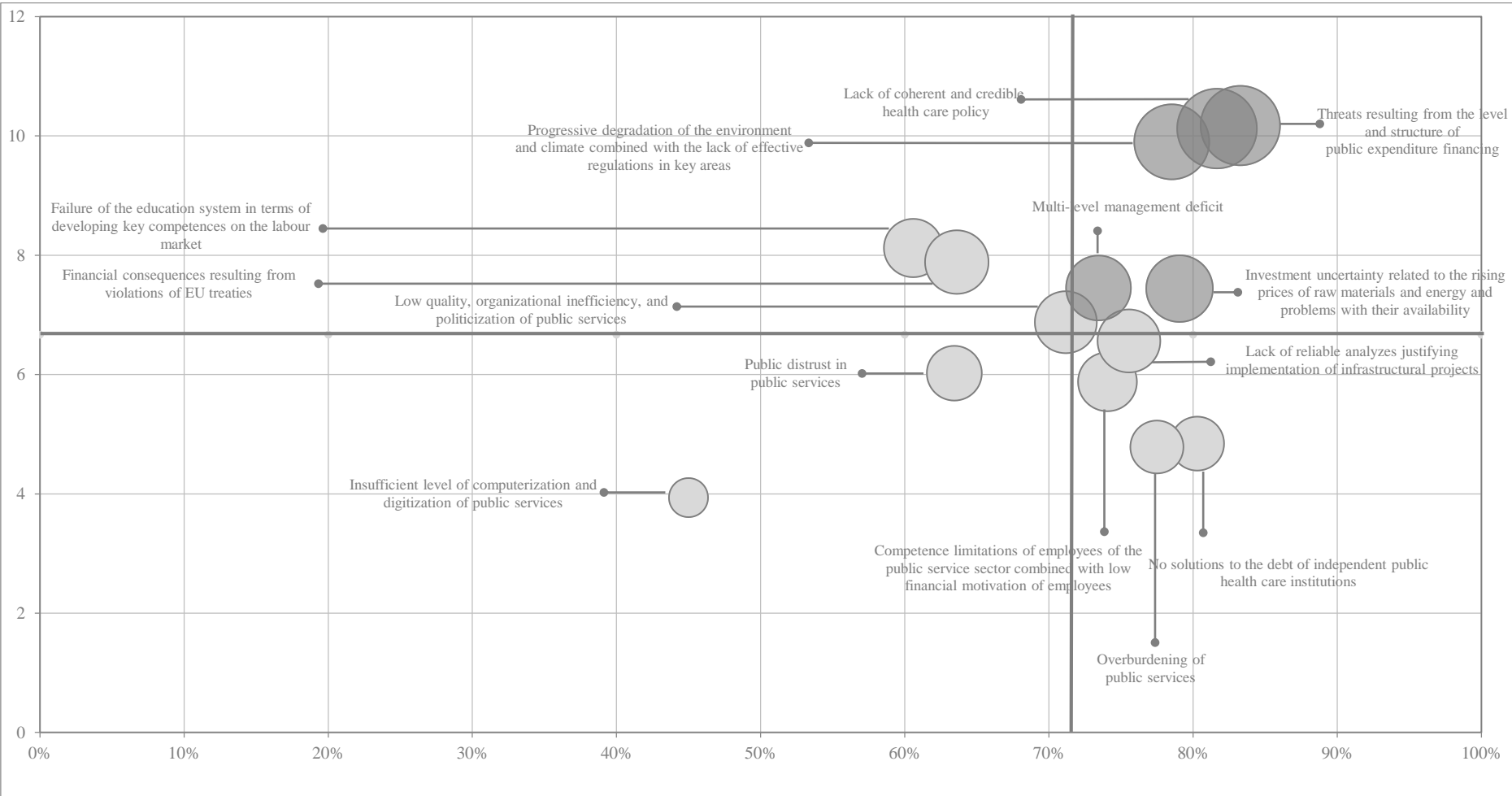
The experts emphasized issues related to the health care system: limited availability of health services (long deadlines for provision of health services, "conspicuous" character of some services, such as dental care) (2) and the lack of solutions responding to the debt of independent public health care institutions (9).

Other indicated threats concern, among others, environmental and climate degradation combined with the lack of effective regulation in key areas (1). Insufficient legal solutions are found chiefly within the area of heat energy, water policy, and renewable energy sources.

Addressed was also the failure of the education system in terms of shaping competences for the labour market (4), which is the effect of limited cooperation between universities and business.

The experts have pointed to financial consequences resulting from breaches of the EU treaties (concerns related to suspension of disbursement of EU funds) (11), as well as the deficit of multi-level management (10), the effect of which is the lack of proper coordination of activities, division of work and responsibilities between the government administration and local self-government.

**Figure 6.** Map of threats to economic credibility of Poland in the area of quality of public services and public infrastructure in the next three years



\* the circle size represents the average of the product of the weight and probability of occurrence of a given threat

Source: OEES study.

The experts recognized the unsatisfactory level and inadequate structure of financing public expenditure as the most significant threat. Average assessment of the weight of this threat was 10.2 points. The probability level is also the highest among all the analysed factors (83%).

A similar level of significance was found for:

- lack of coherent and credible health protection policy (average risk weight of 10.1 points with a probability of 82%),
- progressive degradation of the environment and climate combined with the lack of effective regulations in key areas – e.g. thermal energy, water policy, or renewable energy sources (average weight 9.9 points, probability 79%).

Extraordinary impact strength and probability of occurrence were also assigned to:

- deficit of multi-level management, i.e. appropriate cooperation between the government administration and local government: average weight 7.5 points and probability of 73%,
- investment uncertainty related to rising prices of raw materials and energy; problems with their availability: average weight 7.4 points and probability of 79%.

The lack of a coherent and credible health care policy and financial consequences resulting from violations of the EU treaties were listed as significant by all experts participating in the study (see Table 46).

**Table 46.** Frequency of occurrence of particular threats to economic credibility of Poland in the area of quality of public services and public infrastructure

No	Threat	Percentage of indications*	Weight ranking**	Probability ranking**
1.	Progressive degradation of the environment and climate combined with lack of effective regulations in key areas	94	(3)	(5)
2.	Lack of coherent and credible health care policy	100	(2)	(2)
3.	Low quality, organizational inefficiency, and politicization of public services	94	(8)	(10)
4.	Failure of the education system in terms of developing key competences on the labour market	94	(4)	(13)
5.	Insufficient level of computerization and digitization of public services	78	(14)	(14)
6.	Public distrust in public services	89	(10)	(12)
7.	Competence limitations of employees of the public service sector combined with low financial motivation of employees	89	(11)	(8)
8.	Lack of reliable analyses justifying implementation of infrastructural projects	89	(9)	(7)

9.	No solutions to the issue of debt of independent public health care institutions	83	(12)	(3)
10.	Multi-level management deficit	89	(6)	(9)
11.	Financial consequences resulting from violations of EU treaties	100	(5)	(11)
12.	Investment uncertainty related to rising prices of raw materials and energy and problems with their availability	89	(7)	(4)
13.	Overburdening of public services	83	(13)	(6)
14.	Threats resulting from the level and structure of public expenditure financing	94	(1)	(1)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the hazard with the highest weight/probability of occurrence

Source: OEEs study

## Respecting international obligations

In the area of respecting international obligations, there were identified eight threats.

**Table 47.** Threats to Poland's economic credibility in the area of respecting international obligations

No	Threat
1.	Institutional destruction of the judiciary
2.	Loss of trust in Polish courts in the European legal system, resulting in challenging the judgments of Polish courts abroad
3.	Politicization of the position of the prosecutor general
4.	Violation of the Treaty on European Union and the Treaty on the Functioning of the European Union with regard to the rule of law, combined with financial consequences of the above-mentioned violations (suspension of disbursement of EU funds)
5.	Loss of Poland's credibility as a member of international organizations (the European Union, Council of Europe) and the international community as a result of undermining the principle of respecting agreements
6.	Disturbance of good-neighbourly relations with other countries (e.g. Czech Republic - dispute over the Turów mine)
7.	Violation of the European Convention on Human Rights combined with the failure to execute the judgments of the ECHR
8.	Actions motivated by political interests aimed at restricting civil and political rights

*Source: OEES study*

There have been distinguished two groups of threats. Factors from the first group focus on threats in the national dimension. This is institutional destruction of the judiciary (1). Emphasized have also been the threats related to violation of the separation of powers or independence of the judiciary. Other threats included in the first group are actions limiting civil and political rights (8) and politicization of the position of the prosecutor general (there is no independent public prosecutor) (3).

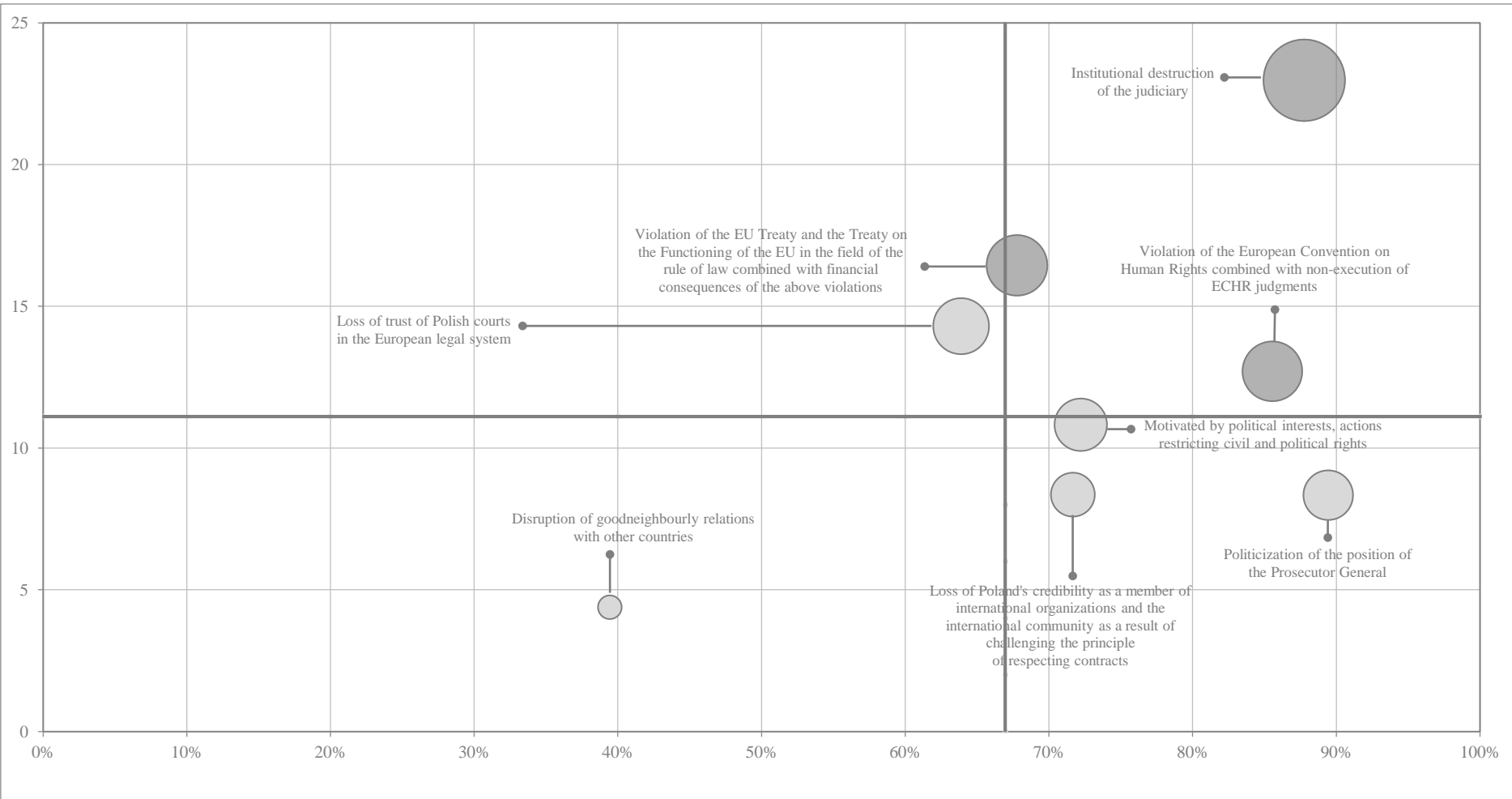
The second group includes threats of an international nature. Identified has been, among others, the risk related to violation of the EU Treaty and the Treaty on the Functioning of the EU within the area of the rule of law, combined with financial consequences of the above-mentioned violations, the consequence of which may be suspended disbursement of EU funds (4). The experts' responses also allowed to isolate the risk related to loss of trust in Polish courts in the European legal system, resulting in challenging the judgments of Polish courts abroad (2).

The risk factors in the second group are also:

- violation of the European Convention on Human Rights combined with non-execution of the ECHR judgments (7),
- loss of Poland's credibility as a member of international organizations and the international community as a result of undermining the principle of respecting agreements (5),

- disturbance of good-neighbourly relations with other countries (e.g. the dispute with the Czechs over the Turów mine) (6).

**Figure 7.** Map of threats to Poland's economic credibility in the area of respecting international obligations in the perspective of the next three years



\* size of the circle represents the average of the product of the weight and probability of occurrence of a given threat

Source: OEEs study.

The factor which, according to the experts, constitutes the greatest threat is institutional destruction of the judiciary. The average weight of the threat was 23 points, at the same time it was assigned the second highest probability of all analysed threats - 88%.

The second serious threat concerns violation of the Treaty on European Union and the Treaty on the Functioning of the European Union with regard to the rule of law, where the average force of impact was 16.5 points. However, according to the experts, probability of this threat materializing is 20% lower when compared to the first threat and amounts to 68%.

The last key threat (top right-hand part of the map) is violation of the European Convention on Human Rights, combined with failure to execute the ECHR judgments. Average significance of this threat is 12.7 points. However, in the experts' opinion, this factor is characterized by very high probability of occurrence in the next three years - 86%.

**Table 48.** Frequency of individual threats to Poland's economic credibility in the area of respecting international obligations

No	Threat	Percentage of indications *	Weight ranking**	Probability ranking**
1.	Institutional destruction of the judiciary	100	(1)	(2)
2.	Loss of trust in Polish courts in the European legal system	100	(3)	(7)
3.	Politicization of the position of the prosecutor general	89	(7)	(1)
4.	Violation of the EU Treaty and the Treaty on the Functioning of the EU with regard to the rule of law, combined with financial consequences of these violations	100	(2)	(6)
5.	Loss of Poland's credibility as a member of international organizations and the international community as a result of undermining the principle of respecting agreements	89	(6)	(5)
6.	Disturbance of good-neighbourly relations with other countries	89	(8)	(8)
7.	Violation of the European Convention on Human Rights combined with failure to execute the ECHR judgments	100	(4)	(3)
8.	Actions motivated by a political interest, restricting civil and political rights	89	(5)	(4)

\* refers to the percentage of experts who assigned to a given threat more than 0 points

\*\* indicates the hazard with the highest weight/probability of occurrence

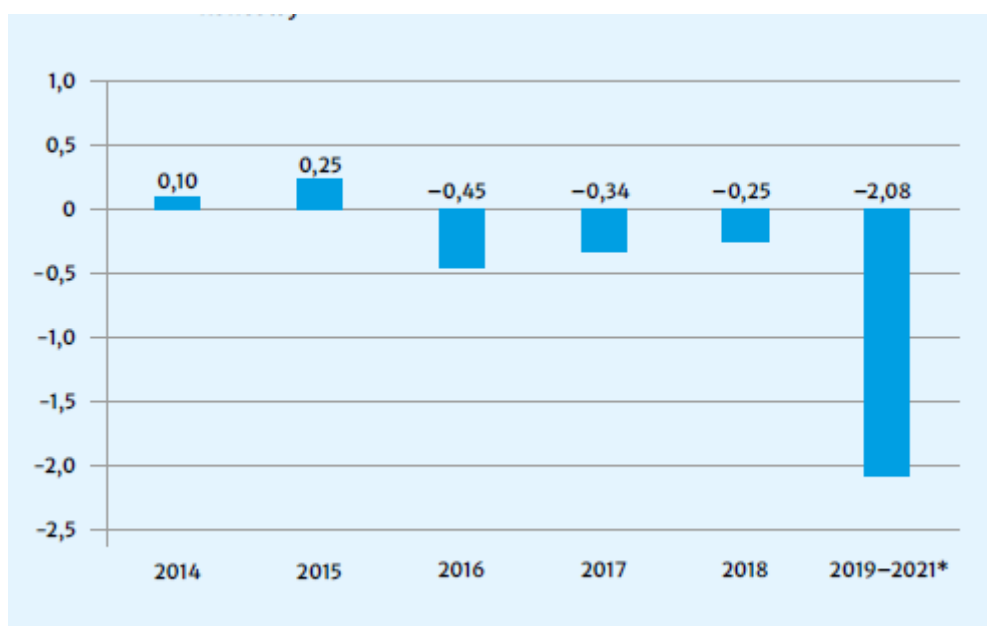
Source: OEEES study



## X. Summary

Sadly, as shown in our analysis for the years 2015-2021, economic credibility of Poland has significantly decreased, distinctively in the 2019-2021 period.

**Table 49.** Index of economic credibility of Poland - final result



\* due to the fact that some of the used databases contained the most up-to-date information for the year 2021, while some of them for the year 2019 only, the index was calculated using the common period 2019-2021, of which the latest available data was classified for calculations

**Table 50.** Partial index values

AREA	2014	2015	2016	2017	2018	2019-2021*
The rule of law	-0.15	0.12	-0.41	-0.40	-0.73	-0.99
Freedom of economic activity	-0.24	0.17	0.20	0.41	0.30	0.21
Credibility of public finances	0.02	-0.02	-0.66	-0.66	-0.46	-1.73
Financial and monetary stability	0.46	0.51	0.39	0.66	-0.07	-2.49
Employment protection and safety	-0.42	-0.37	-0.07	0.45	1.51	1.66
Quality of public services	0.09	-0.07	0.03	-0.15	0.05	-0.29
Respect for international obligations	-1.23	-0.34	-0.07	0.01	-0.10	-0.07

\* due to the fact that some of the used databases contained the most up-to-date information for the year 2021, while some of them for the year 2019 only, the index was calculated using the common period 2019-2021, of which the latest available data was classified for calculations

In each of the chapters, we have presented those indicators, which were used to study the value of the general index and the six analysed areas. We have also included information on what social and economic events or phenomena exerted impact on the value of the index.

On the basis of qualitative research (the number of experts participating in it was 116), we have indicated the most serious threats resulting from Poland's reduced economic credibility.

**Table 51.** The most serious threats to Poland's economic credibility in particular areas

Area	Threat with the highest weight/impact	Threat with the highest probability of occurrence
The rule of law	Instability of legal regulations	Lack of transparency and violation of principles in the law-making process
Freedom of economic activity	Highly unstable conditions of running businesses	Instability and lack of transparency of the tax system
Credibility of public finances	Increase in the cost of servicing public debt	Complexity and lack of transparent and rational rules in the tax system
Financial and monetary stability	Misguided monetary and fiscal policy	
Employment protection and safety	Difficulties in reconciling family and professional life, which have an impact on women's low labour force participation	Lack of migration policy
Quality of public services	Threats resulting from the level and structure of public expenditure	
Respect for international obligations	Institutional destruction of the judiciary	Politicization of the position of the prosecutor general

A direct consequence of the reduced economic credibility of our state is the persistence of inflation and low effectiveness of anti-inflation measures, in particular of the monetary policy. Among other things, the weakness of the Polish zloty and increased yields of domestic government bonds are of great importance. The recent literature strongly discusses the impact of the domestic economic system on intensification of inflationary phenomena. Among economic systems, there are both conducive to low and high inflation. Poland should be included in the latter category. When credibility of the state is lowered, inflationary tendencies become especially persistent, with external shocks and inflationary impulses they cause easily transferred to the system .

Low credibility of the state affects the credibility of all economic agents, and thus their adaptability.

A serious problem and difficulty in fighting inflation is the low credibility of the National Bank of Poland and monetary authorities. Since 2016, the central bank has been pursuing an unconventional monetary policy, with particular intensity since 2020. The experience of other recognized central banks is unequivocal: unconventional monetary policy must go hand in hand with conventional communication with market participants. In our country, however, an inadequate strategy is accompanied by extremely unconventional communication, especially by the Bank's governor.

Low credibility of the state weakens, among others, anchoring of inflation expectations and increase pressure from many different types of economic agents to launch protective and pro-inflationary interventions, as well as to introduce into the economic system various indexation mechanisms, the operation of which increases persistence of inflation. This is how the inflation spiral winds up. One should recall the years 1990–2005, when the difficult process of disinflation in Poland was successfully carried out. Back then, the inflation spiral was successfully suppressed. Poland's growing

economic credibility was definitely helpful. Unfortunately, the state's credibility in terms of financial and monetary stability hit the all-time-low in 2021, in the period covered by our research.

Low trust in the state exerts negative effect on trust in the public levies system and the fulfillment of tax obligations (the so-called tax morality). At the moment, this problem is on the increase.

Just as unfavourable changes are occurring, the structural weaknesses of our economic system, which contribute significantly to its highly inflationary vulnerability, are also growing. In our case, this includes:

- low level of savings and low propensity to save,
- building up the bubble on the real estate market,
- high level of monopolization and etatization of the economy,
- high share of raw materials and energy-intensive sectors,
- growing labour shortage and unfavourable demographic phenomena,
- high level of devastation of the natural environment, including pollution of surface waters.

A credible and stable financial system in itself has a positive effect on the long-term economic growth. Without it, one should not expect to overcome the fundamental structural weakness of the Polish economy, which is the low level of corporate investment in relation to GDP.

In this context, there must be placed a sensitive issue: unemployment. The indicators from the labour market area calculated by us point to the improving conditions of labour protection and security in four out of five dimensions included. The labour market makes up the part of the analysis in which we observe an increase in credibility of the state. Currently, we are on the brink of a recession and a serious economic crisis, which should encourage careful monitoring of the situation and the search for new solutions aimed at promoting productive employment.

Noteworthy is the structural and long-term dimension of the importance of the state's economic credibility. Therefore, when developing our index, we have not limited ourselves to the issue of fiscal credibility related to assessment by financial markets and rating agencies of the government ability to service public debt. Instead, we have supplemented the analysis with much broader perspective than that covered by the perception of financial markets and rating agencies .

The assessment of Poland's economic credibility in relation to the six dimensions of public services covered by the research presents a somewhat varied situation. There are public services whose condition can be assessed positively (public security, e-government), but there are also those whose assessment is negative (education) or definitely negative (health safety, environment, or cybersecurity).

The fundamental weaknesses of our state are distinctly visible. These include in particular:

- political arbitrariness and discretion,
- a low level of clerical competences which are regularly reduced as a result of the political and nomenclature (though informal) mechanism of filling vacancies,
- oversensitivity of public interventions - excessive frequency and use of inappropriate methods,
- replacing public communication with political (party) propaganda.

Our intention is to emphasize the importance of economic consequences of Poland's reduced credibility as well as its close links to the problems with the rule of law. Their occurrence has triggered noticeable increase in the risk of running a business in our country, which, among others, drives up its costs. Similarly painful is significant deterioration in the efficiency of the judiciary. Litigations are extremely lengthy - even in the case of those procedures, which (theoretically) should allow for quick enforcement of claims.

We did not deal with international comparisons in the first edition of the index. It is our intention to do it in the next edition of the index. Nevertheless, in a few cases we compared the data for Poland with the data from the countries of our primary peer group (the Visegrad Four). Also, taking into account the data not quoted herein, we may conclude that Poland's economic credibility is lower than in the case of the Czech Republic and Slovakia, and at a similar level to that of Hungary, a country whose credibility has significantly decreased in recent years.

Public and political power can contribute to both lowering and increasing Poland's economic credibility. The economic and political policy pursued for several years weakens credibility of the state. The report includes recommendations for actions in each of the discussed areas. And while they are assigned to the areas analysed in the report, their importance is not limited to a single area.

The rule of law and security of economic transactions:

- creating appropriate mechanisms so that the authorities would carry out real public consultations on drafts of regulations
- extending the obligation to conduct regulatory impact analysis (*ex ante*), also for parliamentary drafts
- it is necessary to change the rules of writing justifications for court judgments: these should be clear and short
- restoring the possibility of obtaining the status of a civil servant by way of taking an examination and raising the limit of appointees,
- introducing professional, not political, standards when filling positions in state-owned enterprises
- preventing institutional destruction of the judiciary

Freedom of economic activity

- monitoring the impact of government policies and regulations on conditions of running a business, currently especially resulting from frequent changes in tax regulations and fiscal burdens
- monitoring of deteriorating conditions of property registration
- improvement of efficiency of the judiciary
- remedial actions within the rule of law are particularly important for doing business

Credibility of public finances

- restoring transparency of public finances: introducing the obligation to publish in the budget law financial plans of all units of the general government according to the scope of the EU methodology
- introducing the obligation to publish detailed information on application of the expenditure rule in the budget law
- establishing a public register of general government entities, which would contain financial information, including information on employment and wages
- a comprehensive institutional and organizational reform of public finances consisting in reduction of funds and agencies, and redefinition of the "state budget" to the "budget of the entire central sector" so that the government would receive a full and faultless discharge
- protection against tampering with fiscal rules: introduction to the constitution of a definition of public debt, consistent with the EU methodology
- sealing the stabilizing expenditure rule so that it would cover, as a rule, all expenditure transactions as defined in the European methodology

- introducing the requirement of approval of changes in fiscal rules by 2/3 of the parliament and recording in the constitution exit clauses, i. e. situations in which no application of such rules is allowed
- change of the structure of public finance expenditure by means of reducing social transfers while increasing spending on key development objectives, e.g. on health policy, national defence, energy transformation, or migration policy

#### Financial and monetary stability of

- less frequent media coverage of central bank representatives and focusing its communication on the NBP mandate, that is, the issue of (restoring) a stable price level
- liquidation of the bank levy (at least in reference on new loans)
- exemption of interest on deposits from the capital income tax (i.e. the so-called Belka tax)

#### Employment protection and safety

- activities supporting development of human capital through lifelong learning, with particular emphasis on people with the lowest competences and skills
- effective use of available labour resources by increasing participation of adults, including those at risk of exclusion from the labour market, in various forms of education and training
- development of migration policy principles to include social and professional integration of migrants
- promotion of age management solutions and supporting the labour force participation of people approaching retirement age

#### Quality of public services and public infrastructure

- a greater influx of teaching staff should be ensured through the use of a variety of incentives for individuals to take up the teaching profession
- there is a need of a coherent policy within the healthcare system,
- especially in the context of the omissions in healthcare resulting from the COVID-19 pandemic
- radical improvement of attractiveness of work in the public sector is necessary,
- as this area loses the fight with the private sector for qualified employees
- it is necessary to increase dynamics of development of renewable energy sources, which, on the one hand, is going to contribute to improvement of the natural environment, and on the other hand, it is likely to improve independence from external suppliers of energy sources
- significantly improve cybersecurity and use the private sector experience in automation processes

#### Respect for international obligations

- all judgments of the Court of Justice of the European Union and the European Court of Human Rights should be implemented
- laws executing Poland's obligations under the National Recovery Plan should be passed

Some of the actions proposed in the recommendations may be implemented almost immediately. Others involve commencing a process. But no matter how long it takes to develop and implement these actions, now is the time to treat them seriously. Otherwise, Poland's economic credibility will continue to decline and will reflect increasingly serious internal and external problems.

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