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"European integration's contribution to the success of the Polish transformation"

25 years of transformation to a market economy in Poland. Panel session on transformation to a market economy in Poland and other post-communist states. How to explain differences in economic (e.g. growth, inflation) and non-economic indicators?

19 November 2014, Warsaw School of Economics (SGH), Warsaw

1. The transition to democracy and market economy together with the accession to the European Union, constituted mutually reinforcing processes of grand change.

While the date of accession was symbolic, the whole 1989-2004 period had in fact been adding strong incentives to the reform process.

The political environment in which the accession was conceived and implemented was paved with challenges and stumbling blocks.

The oldest of you remember Poland was even the only candidate country where political opposition to the EU accession existed. On the other hand however, all subsequent governments showed strong commitment, indicating they would spare no efforts to make accession a reality.

2. Here, in post-Communist countries, the pro-EU consensus was not as easy to achieve as one might think today, looking back on the last quarter of a century. Overall, though, the elite consensus emerged and provided a gravitational pull and a moral umbrella for sometimes tough decisions. In this sense, the years leading to accession were years of incredible preparatory work. 2004 did not happen out of the blue – it was a crowning moment of a sustained effort of 15 years aimed at making the Polish economy fit for Europe. Hand in hand with the package, different internal reforms received the external support of institutions like the IMF, World Bank, lenders, creditors, the European Bank for Reconstruction and Development etc., and, of course, the EU.

The fact that they all came in concerted efforts to the rescue of the Polish economy, also as a result of their recognition that Poland would not only become a EU member in the foreseeable future, but that it held the promise of becoming one of its most important members. It took a great vision to see that at that time, a time when Polish industry had to be slashed due to its obsolescence, when the consumer market was still underdeveloped and institutions like banks and financial supervisors necessary for the proper functioning of the free market were being constructed from scratch. It took a lot of political faith in the capacity of the Polish economy to revive itself in a short period as to be worthy of large-scale financial and material investment. Beyond any doubt, the perspective of Poland's joining the EU proved to be at that time a

crucial, however intangible, asset. This is one of the cases where the “intangible” won over the “visible”. It was a kind of bet from all parties involved, one which was won in the end.

3. From the very beginning of the transition, on the EU side they saw an enlargement to the East both as a moral and political obligation and a long term chance for Europe. It was not an easy decision – we have to understand that at that time such a bold move was full of unknowns. Brussels might have legitimately asked itself whether the CEEC countries would be able to meet the stringent accession criteria, whether they would not be a burden in general, how much their membership would cost. Now we do not appreciate it much, but the EU’s commitment was incredibly bold, forward thinking and exercised in a world full of uncertainty.

4. All potential candidates for membership accepted the challenge at hand, namely to aspire to the European Union as the finalité of the process of transformation and to adhere to the EU institutional and regulatory infrastructure. In Poland especially, this challenge was exemplary.

5. The Copenhagen criteria were the guidelines for pre-accession reforms and strategy but those countries had to meet also an additional set of criteria, namely those of article 3 of the EU Treaty, which relate to the social market economy. This added to the emerging political and economic orders, also the responsibility and the rights towards society.

The meaning of democracy in the Copenhagen criteria went well beyond the political system and embraced also a toolkit to achieve political and social peace. In the time of transition, this peace was not always easily achievable.

6. An important element of Poland's accession to the European Union was the whole process of preparing for accession and the way accession negotiations were linked to the domestic adjustment process.

I am also convinced that the quality of our membership, our capacity to exploit the potential benefits from integration were greatly facilitated and enhanced by the quality and soundness of Polish transformation, both in institutional and real economy terms.

7. It was largely recognized that the starting point for the transition to democracy and market economy and, as a consequence, also the transition itself had been more complex and challenging in Poland than in most other Central European Economies. This was reflected in the size and depth of macroeconomic destabilization, volume of foreign indebtedness, scale of inflation etc. A similar observation can be made with regard to the accession negotiations. Expectations and requirements on both sides, scope and scale of required change, relevance for the functioning of the internal market exceeded those of other candidates. Furthermore, the quality of the transformation allowed the Polish economy to regain its growth capacity relatively fast and to restore its development capacity in a sustainable way. These two factors played a supporting role in the process of exploiting benefits from EU membership.

8. During the first decade of transformation of the pre-accession period, it could be argued that the EU played a role more as a point of reference, as a type of template over the complex process of a wholesale change and a guarantor of future development, as opposed to the role of an active actor on the ground.

9. Prospects of accession contributed to the reorientation of trade and capital flows. Membership has increased the diversification of the export pattern, which in turn has reduced vulnerability to trade shocks. Poland has become a part of a European value chain. Additionally, with regard to the inflows of FDI, also today Poland has the highest position among all the NMSs as the prospective host destination for European FDI.

10. Benefits of accession are fruit of all those coming from the integration mechanism itself, in particular the single market freedoms, which have led to an increase in the standard of living through their contribution to growth. Real convergence has been advancing.

11. The accession has also generated a strong impulse to emigration. Migration flows are difficult to measure. Today probably the biggest emigration wave is over, however most likely a substantial number of those who left will not come back. Decreasing remittances seem to confirm this observation. Emigration decreased the supply of labour but it is worth underlying that most of it happened during the peak of unemployment. So it functioned also as a stabilizer.

12. Poland was the first to implement one of the most important reforms of the transformation - the decentralization of state through the local governance reform of 1991. The empowerment of local and regional authorities not only accelerated the emergence of civil society structures but played also a pivotal role in the efficient use of the European structural funding, whose management was from 2006 on based on decentralized system. This differed markedly from common practices in other CEEs.

Local government reform leading to establishing different levels of self-government proved to be a great success. It unleashed an enormous amount of energy and entrepreneurship at local and regional level.

Access to an unprecedented volume of structural funds increased both public and private investment, a result of the high leverage role of the funds. The structure of cofinanced investment accelerated real convergence, working towards an increase of competitiveness. The European Commission has introduced a major reform of the European regional policy to make it fit the needs of the NMSs, countries with a huge need of investment in their modernization.

The effective use of the structural funds distinguished Poland from some of the NMSs. The decentralization of the management system continues to be the only case among the NMSs. The strategic approach allowed to incorporate new know how into the development strategy. The quality of public administration responsible for the programs was improving at an accelerated pace.

Investment in infrastructure, entrepreneurship, innovation, research, human capital, quality of life - all that was conducive to growth and competitiveness. This investment has been creating a sound foundation for future long term development.

13. Compared to other CEEs, the Polish economy has been rather stable over the last decade. Many studies show that the volatility of both inflation and the output gap have been the lowest among the NMSs. The same is true for the current account deficit, one of the lowest in this group.

Poland avoided a recession, it avoided accumulating a massive private and public debt. It also avoided the instability of the financial system.

14. But the CEE are still catching-up economies. Unfortunately, on many issues they tend to be simply followers and do not really use their potential. Instead, they prefer to follow the path already taken by other member states, which have been in the Union longer. As they do this, they end up defending their rights to traditional growth models and are not sensitive to new opportunities. This is a pity.

Poland continues to be a catching up economy with a relatively low level of innovation. This will most likely remain a challenge for the years to come.

Membership in the EU could be a factor both accelerating the development of Poland's own innovation capacity and facilitating the absorption of foreign innovation.

For the timebeing, this potential benefit of membership is clearly used to a very limited extent. That is what I believe.

A thorough change is needed to avoid the risk of the middle income trap which is still there.

Poland must radically increase its own innovation capacity. There is however also an unused potential when it comes to its absorption capacity of the offer of the European single market and of its research program.

What Poland really needs to do is we should better capitalize on its privileged dual status, as a catching-up economy which is at the same time an EU member state. The catching-up element gives CEE economies dynamism and a competitive advantage in terms of growth, while the EU membership comes with added opportunities. We need to fully leverage this potential in a smart way.

15. To quote Fernand Braudel: "*History may be divided into three movements: what moves rapidly, what moves slowly and what appears not to move at all.*"

Whether something moves slow or fast depends on your point of view. I happen to think that EU membership was one of the propelling forces at work here. The thing which we need to monitor now is whether this trend will be sustained in the subsequent phases of membership, whether it will survive past the impetus of the first ten years.

We also have to keep in the back of our minds the fact that while membership itself is a continuous opportunity, it is not an unfinished lease on development. EU is not a perpetuum mobile for success, especially if we think about the fact that it is just emerging from a multi-faceted crisis. Whether our long-term transformation success will be validated within the EU's structures in the near future will also depend on what path we decide to take with reference to the most important decisions that are still before us. And here I think about what Braudel, looking at Poland would put into a category of "*something that does not appear to move at all*": namely, the momentous decision of when to join the euro. I know that there are many people in Poland that think that this is not the most propitious time to talk about it. But if we don't talk about it, the problem will not go away. We cannot put our head in the sand and pretend that it somehow will solve itself.

16. As of 2015, only three EU member states of the ten which joined the EU in 2004 will not be the members of the common currency area: Hungary, Czech Republic and Poland.

Integration by its very nature provides conditions and factors that contribute to growth. The most difficult challenge ahead of Poland stems from the fact that in the decades to come the integration within the common currency area will be the core of the integration progress. The integration process within the EU as such might slow down. Further progress on the internal market front might first of all benefit euro zone economies.

The big CEE economies remain outside the eurozone. They can be taken on board current reforms just as "opt-ins." Such a participation however makes them second class countries in the reform effort.

Being in the eurozone is not a pain that we should avoid, but a chance that we should exploit. For that, we need courageous leaders, of the same type that we had in the initial transformation period.

Then we took the risk and chose the EU. It turned out to be the right choice. Now the other historic choice is before us. We cannot turn away from the history that is calling us.

17. Transitions to democracy are defined in political science as volatile processes which are completed once an agreement on democratic rules has been successfully reached.

At what point can we say that we are dealing with a consolidated democracy? Some argue that this occurs at the point at which political actors comply with the minimal procedural requirements of democracy.

But consolidation does not stop in the political arena. As democracies mature, we need to put in place also the subjection of non-governmental forces to the resolution

of conflict within specific laws, procedures and institutions, as sanctioned by the new democratic process.

Citizens must begin to identify with the state. At this point, "nation-building" commences. A sense of national identity, of national consciousness thus emerges. The political unit slowly acquires a social dimension. Our additional challenge was the European identity that came as an additional provocation for both society and individuals.

18. The CEE has come a long way and its nations have certainly made a significant leap towards one day becoming mature democracies. Of course, we are not there yet. While some of the old divisions between East and West have faded along with economic progress, the CEE still retains a weak economic and political role in the EU in terms of level of influence. Economically, the GDP of all new member states (from the 2004 and 2007 enlargements) is only 8.1% of EU GDP. Politically, the CEE area is still side-lined in major debates. It takes time to reach critical mass, at which point one can really have a say.

The CEE area also still suffers from perception issues, which inevitably impact its ability to position itself as desired in the EU. One important consideration here is the corruption stereotype associated with some of the CEE economies, while the phenomena itself is also affecting the West. There are facts of life and then there are perceptions at the EU level.

The CEE was also not immune to the crisis. The crisis episode revealed how the area is actually very heterogeneous. Different economies suffered different effects, Poland survived the crisis without a recession, Latvia lost one fifth of its GDP at the peak of the crisis and required financial assistance from the EU.

19. Europe finds itself deeply differentiated or even fragmented today. We see dividing lines crossing a number of areas: competitiveness, appetite for reform and integration, capacity to grow. The story of Central and Eastern Europe (CEE) is strikingly similar. Differentiation however will unfortunately undermine convergence capacity and weaken the growth potential of the single market.

The starting point for accession into the EU was very different for Central and Eastern European economies in terms of political maturity, societal problems, capacity and willingness to reform etc. All the same, all these members did however share a common sense of identity. We hoped that entry into the EU would help us fulfil our common destiny. What is interesting to note is that our countries are in a sense still very different today, ten years later, and that the sense of a common destiny has faded with the passing of time.

Today we see here and there a resurgence of nationalist tendencies, a resurfacing of historical resentment, which we used to see happening mainly in the older member states. We also see divisions on other topics, from climate policies, fiscal policies (such as diverging views on the fiscal compact), financial sector reform (the banking union for instance stands out as a more appealing project to some than to others) to foreign policy (the Ukraine-Russia crisis is a case in point) and migration. It remains

striking how little the new member states actually cooperate and how they have not succeeded in fully leveraging some of their common interests. We see it certainly if we look at the 2004 and 2007 accession, but even narrowing it down, to the V4, still we notice a lack of cohesiveness.

Why are these phenomena present? This is certainly at least in part an outcome of EU level divisions, of differentiations between those in and those out of the euro, those in and those out of Schengen. So we face institutional differentiations, but also political ones. On the one hand, some of us do not fulfil the criteria for entering the eurozone yet, these are clear objective hurdles. But often we are also confronted with missing political will, as is the case for the accession of some members states into the Schengen area. These attitudes slowly lead to the creation of a political periphery among the new member states. In turn, this limits our ability to set the agenda, to reach critical mass in order to be influential. Adding fuel to the fire is also the perception that we might not be mature, fully-fledged democracies. Episodes such as those witnessed in Hungary exacerbate this perception.

The question moving forward is whether the CEE, like Europe, will continue to operate along various dividing lines and how Europe can help the CEE become more united. If we continue to be divided, then we may legitimately worry about the risks that this approach could bring along with it. Speaking with a united voice, identifying common interests and sticking together on them would be much more advantageous. If we, as the CEE succeed in building a strong core, we might be able even to give Europe the impetus it needs to slowly blur divisions until, with time, they eventually fade away.