REPORT

Euro Re/new: Scenarios for Poland

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Mission of the Reform Institute is to support continuous improvement of the process of formulation, implementation, monitoring and evaluation of public policies in Poland, Europe and all over the world. The ultimate goal of our efforts is to improve the quality of public policies.

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1. Why do we need to restart the discussion about euro adoption in Poland?[1]

The euro area was created 25 years ago as the crowning achievement of the European Union's internal market: the single currency was to eliminate exchange rate fluctuations and reduce the transaction costs of trade between Member States, increasing European economic potential and contributing to the well-being of its citizens. The political dimension was of equal importance: the European Economic and Monetary Union (EMU) embodies a commitment to deepening of European integration. Nevertheless, the dissonance between the ambitions and institutional design almost led to EMU's collapse in the turbulent first quarter-century of the single currency. Today, however, the prospect of a euro area breakup is unlikely, and the centre of gravity in debates is increasingly shifting towards strengthening the institutional design and the pursuit of a more environmentally and socially sustainable economic model.

For Poland, which signed up to joining the euro area in the Athens Treaty (ratified in a 2003 referendum), joining the third stage of the EMU[2], or at the very least clearly articulating the path to that end, is today politically and economically highly desirable. If done in the right way and with appropriate preparation, it could create the conditions to help the country face some of the biggest challenges its facing yet: institutional renewal following almost a decade of rule of law backsliding, boosting the sustainability transition, and giving a new dimension to Poland's security toolbox.

In this report we develop this argument by, first, explaining how the transformation of the EU, Poland-euro area relations and of Poland itself changes the cost-benefit analysis of joining the common currency (Section 2). Second, in Section 3 we tackle the question of whether Poland would benefit from joining the euro area, looking at economic, political, social and rule-of-law related aspects as well as the new security context. Our goal being outlining the best possible route into the common currency for Poland, in Section 4 we consider lessons to be drawn from four idealised integration scenarios of countries thriving and stagnating within the euro area, as well remaining on the out. Finally in Section 5 we outline tentative recommendations for a multi-year reform programme oriented at adopting euro in Poland intended as a first step towards a broad stakeholder discussion. Section 6 concludes.

So far, the discussion on Poland's accession to the third stage of the EMU, has been characterised by varying levels of intensity and complexity. Its intensification is typically driven by crisis events (e.g. the Greek government debt crisis, the escalation of Russian aggression against Ukraine in 2022), subsequent euro area enlargements (e.g. Croatia in 2023) or the macroeconomic situation (e.g. persistent high inflation).

Despite the changing economic and political environment, the discussion's parameters remain surprisingly fixed. Firstly, EMU's own transformation is largely overlooked with insufficient consideration paid to:

- new currents in economic thought, such as those pointing to the limited ability to

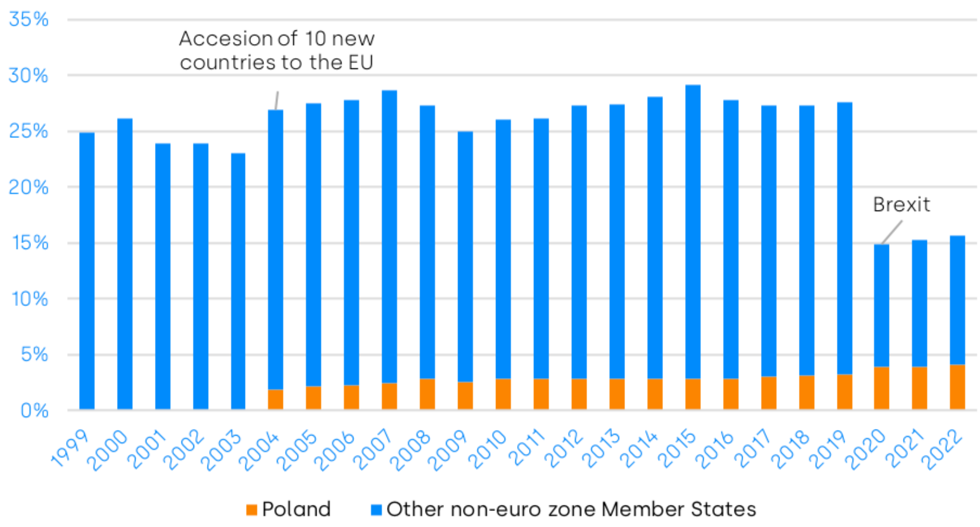
1 The authors would like to thank the participants of the Reform Institute seminar *Is it Time for the Euro? The Determinants and Scenarios for Poland's Adoption of the Single Currency*, held on 10 July 2023, for valuable comments and suggestions to an earlier version of this report.

2 Eurozone membership is divided into three phases. Stage one is the establishment of the free movement of capital between Member States. Stage two is the convergence of Member States' economic policies and the strengthening of cooperation between Member States' national central banks. Stage three is the implementation of the common monetary policy. According to the treaty provisions, Poland is a so-called "member state with a derogation" from the third phase of EMU (Article 139(1) of TFEU).

shape monetary policy independently in the context of integrated financial markets, or so-called monetary sovereignty (Rey 2015, Murrau and van 't Klooster 2022) or the relationship between corporate governance and inflation (Weber 2023);

- EMU's institutional transformation, including the transformed role of the ECB and the integration of new social and environmental goals in euro area policy (Ananicz, Buras, Smoleńska 2023, cf. Nowak 2019);
- technological transformation, e.g. regarding digital currencies (European Commission 2022);
- the new tasks that monetary policy fulfils in terms of global challenges (e.g. sustainability transformation (Smoleńska 2023);
- the shifting balance of power between euro area and non-euro area Member States in the EU, especially in the aftermath of Brexit (see Fig. 1).

Figure 1. Share of non-euro area Member States in EU's GDP



Source: Own elaboration based on Eurostat data

At the same time, the opponents to joining the euro area continue to emphasise to the cushioning effects of autonomous monetary policy making and the preservation of a floating exchange rate in the face of economic shocks, disregarding the evident constraints over local monetary policy autonomy in the context of global integrated markets. Autonomous monetary policy is only beneficial if it is implemented more effectively by national institutions than by the European Central Bank (ECB). Meanwhile, the higher levels of inflation in Poland than the EU's average and their persistence after the pandemic and the escalation of the war in Ukraine, point to the ineffectiveness of the National Bank of Poland's (NBP) actions. In addition, following the escalation of Russia's invasion of Ukraine in February 2022, having a floating exchange rate in a crisis proved more an element of deepening uncertainty than stabilising the economy. The scope for monetary policy autonomy is further limited in the context of synchronisation of business cycles with large trading partners and high level of integration within global value chains.

Secondly, although arguments related to economic (e.g. implications for economic growth) and political issues (e.g. security, influence within EU structures) are intertwined in the discussion in Poland, they are treated largely in a disjointed manner, without a deeper reflection on the feedback between them. This omission obscures the potential of Poland as a full member of the EMU, in terms of the agency of its national public institutions in implementing policies related to the adoption of the single currency and influence over the shape of economic integration.

Detailed analytical work on joining the euro area in Poland was carried out last in 2015 within the Ministry of Finance of the Republic of Poland (2009–2015) and the National Bank of Poland (NBP) (2007–2016). In 2015 the position of the plenipotentiary for euro area within the Ministry of Finance was abolished. In 2016, Adam Glapiński, strongly associated with the Law and Justice (PiS) party and a strong opponent of joining the euro area on "sovereignty" grounds, took over the helm of the NBP. Before that, in 2014, a team of NBP experts identified the pillars of Poland's integration into the eurozone, distinguishing three dimensions:

- **external** (situation in the euro area);
- **relational** (convergence criteria);
- **internal** (situation in Poland).

This approach continues to provide a solid framework for assessing Poland's road to the EMU, however the changing geopolitical and economic conditions have transformed the factors which should be considered in this context of each of the three dimensions (see Fig. 2 for summary).

Figure 2. Dimensions of Poland's integration into the euro area

Dimensions of Poland's integration into the euro area		
situation in the euro area/global context	convergence with the euro area	situation in Poland
▪ ongoing EMU reform (institutional strengthening, risk sharing, enlargement) ▪ global context (escalation of conflicts, weaponisation of interdependence) ▪ euro in the global monetary hierarchy ▪ creeping differentiated integration of the eurozone within the EU (as opposed to the formal one) ▪ sustainability transition (European Green Deal)	▪ new membership criteria (institutional issues, corporate governance) ▪ economic integration, level of synchronisation of business cycles ▪ Poland's divergence with respect to economic and legal criteria	▪ integration with the euro area as a new growth project ▪ monetary stability in the context of the necessary import of technologies (including the military ones) ▪ euro debate as a factor enhancing the quality of public debate on economic policies ▪ prospect of rebuilding and strengthening socio-economic institutions

1.1. The situation in the eurozone and the broader macroeconomic context

The Polish discourse on the situation in the euro area does not acknowledge the significant EMU transformation that has taken place since 2010. Arguments referring to the situation of individual countries dominate: the Greek public debt crisis or Italy's economic problems. Meanwhile, following the expansion of the ECB's role in eurozone stabilisation, also in the face of new challenges (pandemic, climate change; see: Smoleńska and Tokarski 2022), the creation of new solidarity mechanisms (European Stability Mechanism) and the introduction of counter-cyclical tools (macroprudential policy), the EMU is today much better prepared to face external shocks.

Moreover, the EMU transformation continues. Discussions are underway to strengthen risk-sharing mechanisms, which remain fragmented (e.g. deposit guarantees in the banking union, capital markets), and fiscal rules. The euro's place in the global monetary system is also under transformation. The unprecedented EU debt in the context of the

NextGenerationEU facility, and the increasing use of the single currency as part of the sustainable finance trend brings forward the prospect of creating a euro "safe asset" and strengthening its international role (ECB 2023, Smoleńska 2023, Lupinu and Machura-Urbaniak 2023, cf. van 't Klooster 2023). While it is certainly too early to talk about the end of the dollar's dominance in the international monetary system, the trend towards economic multipolarity, fragmentation and the increased role of global e-commerce platforms may have a destabilising effect on economies using currencies that are "lower" in the global hierarchy, as in the case of the zloty (PLN). It is also worth noting the growing role that central banks are playing in a world of the "weaponised interdependence" (Farell and Newman 2019, Lagarde 2023), e.g. through their ability to freeze other central banks' reserves in a given currency (as in the case of Russia's central bank reserves, Quaglia and Verdun 2023). Being a part of a larger monetary system means being able to influence the use of an additional tool of economic pressure on countries undermining the global order. In addition to Russian aggression on Ukraine, the drive towards multipolarity is evident in the economic confrontation between the U.S. and China[3], the shrinking number of democracies in the world, or the growing competition for production technologies (e.g. semiconductors) and resources (raw materials, including rare earth metals). These trends favour accelerating Poland's integration into euro area structures as an additional guarantee of stability and agency.

3 www.piie.com/microsites/rebuilding-global-economy

From the perspective of non-euro area member of the EU, a key concern is the dynamics of the EMU's separation from the EU-wide structures. Formally, this trend has been halted in recent years. Neither a separate euro-budget nor a special committee of the European Parliament has been created to date. Instead, we can observe the examples of "creeping" differentiation that occurs at the level of policy implementation. For instance, the EU's pandemic Recovery and Resilience Facility is of special relevance to the euro area. The procedures for the coordination and peer review of the National Recovery Plans (NRPs), even if they take place in an EU-wide formats, deepen the EMU economic governance. This effect was reinforced by the fact that Poland – as one of the largest beneficiaries of the programme – *de facto* remained on the margins of this process due to problems with the rule of law until spring 2024 (likewise another EU integration outlier we discuss below: Hungary). Furthermore, as the single currency matures and the EU's centre of gravity shifts towards the euro area countries (especially after Brexit in 2020 and Croatia's adoption of the euro in 2023), even where internal market regulation issues are resolved among the EU-27, the euro area institutions (especially the ECB and the Eurosystem) play a key role in their implementation: the example of sustainable finance being a case in point (Smoleńska, 2023). These trends may well increase the risk of marginalisation of "euro-outs" more than the formal differentiated integration, as the latter typically includes safeguards for non-euro countries (e.g. "inclusive" Euro Summits under the 2012 Fiscal Compact, special double majority voting procedures within the EU's bank regulation agency, the European Banking Authority).

The change in dynamics between the eurozone countries and the "euro-outs" is of particular importance in the context of the sustainability transition. The 2019 European Green Deal and the 2021 Climate Law green various areas of the EU economic regulations, such as the EU budget, fiscal rules, public procurement, and state aid law (Ananicz, Buras, Smoleńska, 2021). The EU financial market regulations are particularly affected by this trend (Smoleńska, 2023). New laws leverage the structural position of finance, inter alia, through regulatory incentives for the uptake of instruments such as green bonds and loans. This trend requires adequate coordination of economic, financial and monetary policies at the national and EU levels, which so far has progressed faster within the euro area, for instance with regard to the integration of sustainability concerns into monetary policy-making (Smoleńska, Weber and Opoka 2023).

1.2. Poland's convergence with the eurozone and related criteria

To become a full member of the EMU, a country must fulfil a number of legal and economic convergence criteria set by the Maastricht Treaty (Czerniak and Smoleńska 2019). These include:

- a high degree of price stability (an inflation rate below the average of the three best-performing Member States in terms of price stability);
- stable public finances, as measured by the level of debt (below 60 percent of GDP) and deficit (below 3 percent of GDP);
- maintaining fluctuations in the exchange rate against the euro within the range provided by the European Exchange Rate Mechanism of the European Monetary System (ERM II) for at least two years (the standard fluctuation range is +/−15 percent, but can be changed at the request of a member state);
- the sustainable nature of convergence as measured at the levels of long-term interest rates (10-year profitability of bonds should be below the average profitability in three countries with the most stable prices).

Two factors make the analysis of Poland's convergence with the euro area more complex today, than it was a decade ago.

Figure 3. Economic convergence indicators

		Price stability	Government budgetary developments and projections			Exchange rate		Long-term interest rate
		HICP inflation	Country in excessive deficit	General government surplus (+) /deficit (-)	General government debt	Currency participating in ERM II	Exchange rate vis-à-vis the euro	
Bulgaria	2020	1,2	No	-4,0	24,7	Yes	0,0	0,3
	2021	2,8	No	-4,1	25,1	Yes	0,0	0,2
	IV 2022	5,9	No	-3,7	25,3	Yes	0,0	0,5
Czech Republic	2020	3,3	No	-5,8	37,7	No	-3,1	1,1
	2021	3,3	No	-5,9	41,9	No	3,1	1,9
	IV 2022	6,2	No	-4,3	42,8	No	3,9	2,5
Hungary	2020	3,4	No	-7,8	79,6	No	-8,0	2,2
	2021	5,2	No	-6,8	76,8	No	-2,1	3,1
	IV 2022	6,8	No	-6,0	76,4	No	-3,1	4,1
Poland	2020	3,7	No	-6,9	57,1	No	-3,4	1,5
	2021	5,2	No	-1,9	53,8	No	-2,7	1,9
	IV 2022	7,0	No	-4,0	50,8	No	-1,5	3,0
Romania	2020	2,3	Yes	-9,3	47,2	No	-2,0	3,9
	2021	4,1	Yes	-7,1	48,8	No	-1,7	3,6
	IV 2022	6,4	Yes	-7,5	50,9	No	-0,5	4,7
Sweden	2020	0,7	No	-2,7	39,6	No	1,0	0,0
	2021	2,7	No	-0,2	36,7	No	3,2	0,3
		3,7	No	-0,5	33,8	No	-3,0	0,4
Reference value		4,9		-3,0	60,0			2,6

Source: ECB (2022)

First, full EMU membership criteria have evolved significantly, both formally and informally, since the debt crisis. While the Maastricht Treaty (1992) criteria for debt and deficit levels have not changed, new euro members are now additionally required to join the European Banking Union (two years before adopting the single currency) and the European Stability Mechanism (ESM), as well as to accept the broader role of European Central Bank (ECB) with respect to financial stability. As the experience of Bulgaria and Croatia between 2020-2022 shows, negotiations to join the third phase of the EMU now may include legal convergence in the area of corporate governance (especially with regard to state-owned companies), money laundering laws and the quality of statistics. Euro integration is therefore no longer reduced to a matter of monetary or economic policy only: the institutional environment is a critical dimension of EMU membership today. From Poland's perspective, this transformation requires a rethink of the whole framework of negotiation of entry into the third phase of EMU[6].

Second, Polish economy has also changed. The assumption that the exchange rate mechanism provides a fall-proof cushion against economic shocks overlooks key dimensions of Poland's already advancing EMU-integration, namely: the deepening of economic ties (60% of Poland's exports go to the EMU), the synchronisation of the business cycle (especially with Germany), and the convergence of market institutions (Borowski, Czerniak, Farkas 2022). Reaffirming euro convergence objective by the new government would constitute a clear signal that Poland is fulfilling its Treaty obligations and remains committed to a multidimensional cooperation with EU institutions. As Poland's new EU strategy takes shape, policy makers need to take stock of convergence/divergence dynamics and assess their implications for any euro-agenda.

1.3. Poland's economic policy and institutional framework

Polish economy developed spectacularly in recent years, however the growth model based on cheap and skilled labour is slowly running its course. Therefore, the discussion on maintaining the potential of the Polish economy should also consider how currency integration can become an additional factor supporting the next stage of the development of Poland's socioeconomic model. In terms of the wealth of its citizens, Poland is much closer to the EU average, despite the accumulating troubles resulting from, among other things, the persisting inflation. Euro integration, provided that an appropriate programme and strategy are prepared, can serve as a development incentive, especially in the context of a broader sustainability transformation (inter alia, by increasing access to capital or lowering the cost of financing). The analyses of the costs and benefits of Poland's euro area integration have consistently highlighted the need for complementary appropriate macroprudential policies and those that will support business competitiveness and innovation (NBP 2014, Czerniak and Smoleńska 2019).

The competitiveness of the Polish economy, still based on low wages, with low R&D expenditures, in the context of the energy transition and the war in Ukraine, means that the import of technology, including military technology, will remain high in the near future. In this context, currency stability would be desirable.

At the same time, Poland's internal capacities need to be strengthened before embarking on the path of eurozone integration at full speed. Years of instrumentalisation of the discussion on euro area membership (especially instrumentalising the "sovereignty" argument)[4] have eroded the level of public debate and translated into low level of awareness of the euro area issues among Poles (Eurobarometer 2022, Kurs na Euro 2023). The project of institutional renewal in Poland following the rule of law downsliding cannot be limited only to the judiciary challenges and needs to comprise as well civil service and quality of public debate. Furthermore, Poland needs to strengthen the relevant government agencies (e.g. financial supervision) and re-establish NBP's credibility.

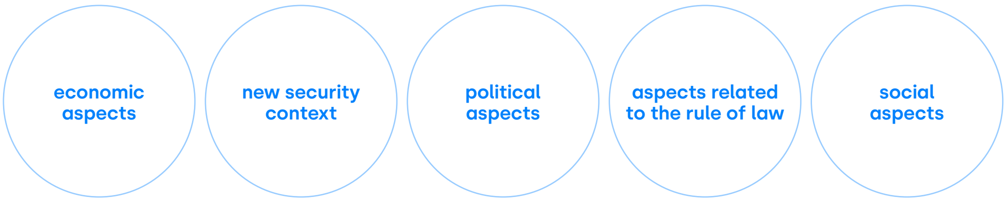
4 See, for example, the Analyses of the Ministry of State Assets concerning the effects of Croatia's adoption of the euro: WWW.GOV.PL/WEB/AKTYWA-PANSTWOWE/CHORWACJA-W-EURO--PIERWSZE-DOSWIADCZENIA Cf. Falagiarda, Gartner, Mužic, Pufnik (2023).

5 "Kurs na Euro" is a nationwide campaign of the Economic Freedom Foundation. Its aim is to start an intense debate on Poland's accession to the euro zone, inform about the benefits of adopting the common currency, prepare recommendations for necessary reforms and initiate the process of joining the euro zone by consistently putting pressure on those in power. Ref. HTTPS://KURSNAEURO.PL/#O-PROJEKCIE

2. Would Poland benefit from adopting the euro?

The discussion of the economic, institutional and political costs and benefits has been going on in Poland for years, supported by extensive literature on the subject[6], which focuses mainly on economic aspects. Full participation in the third stage of the EMU is a multifaceted process that also encompasses political and social dimensions. In addition, the war in Ukraine has shown that security concerns are also of great importance in the analysis. In this section we further examine the factors relevant for assessing the benefits of Poland's euro area entry, this time focusing on economic, political, social, rule-of-law and security aspects.

Figure 4. Factors relevant for assessing the benefits of Poland euro area entry



2.1. Economic aspects

In numerous economic publications on the adoption of the single currency, the main focus is the analysis of potential gains and losses. The most significant benefits generally include lower interest rates, which mean lower borrowing costs for businesses and citizens, as well as cheaper debt service for the public finance sector. Benefits also include lower transaction costs, elimination of exchange rate risk and greater price transparency. By joining the euro area, countries gain access to the monetary policy framework, as well as the European Central Bank's (ECB) financial stabilisation instruments. The adoption of the euro also would have a positive impact on the stability of the overall macroeconomic situation, which facilitates increased trade, foreign investment inflows and economic growth. In view of the progressing level of financial integration within the eurozone, quality of financial supervision and regulatory framework or greater access to capital markets for financing the sustainability transition, which would help reduce its high cost in Poland, should also be considered. In terms of mortgages and housing policy, the adoption of the common currency would not only entail cheaper access to capital, but also open new opportunities to protect borrowers, for example through easier access to fixed interest rates (e.g. due to banks' greater access to the mortgage bond market).

Full EMU membership also comes at certain costs, such as financial contributions to the European Stability Mechanism and the risk of monetary policy mismatch with the needs of a particular economy. An important issue following the adoption of the common currency is the lack of ability to mitigate shocks through adjusting the exchange rate, which in the case of Poland played a major role during the global financial crisis and the crisis in the euro area (Brzoza-Brzezina et al. 2012)[7]. For this reason, some well-known economists, including Paul Krugman, have in the past been critical of Poland's adoption of the single currency (Krugman 2012). It is also necessary to consider the fact that the project is far from completion, and that the states that are members of the currency union are assuming part of the risk associated with its stabilisation. In addition, the euro adoption path necessitates certain adjustment costs, for example those associated with meeting the convergence criteria. On the other hand, delaying entry into the third stage of EMU

6 The most comprehensive publications in this respect were the 2004, 2009 and 2014 reports of the National Bank of Poland. Other publications worth mentioning include: Żukrowska and Sobczak 2003; Orłowski 2004; Dąbrowski and Rostowski 2006; Wójcik 2008; Rosati 2009; Visvizi and Tokarski 2014; Czerniak and Smoleńska 2019; Götz, Nowak, Orłowski 2019. An important place for the debate on the issue of adopting the euro in Poland is the daily newspaper Rzeczpospolita, where the topic is regularly addressed at the beginning of each year.

7 However, it is important to note the short-term effect of the currency's weakening in the context of the crisis related to the escalation of Russian aggression against Ukraine.

also imposes certain costs on the economy, such as higher interest rates (Czerniak and Smoleńska 2019). Some studies based on theories of optimal currency areas point out that small open economies benefit most from participation in a currency area (Alesina and Barro 2002). Although Poland is the largest economy in the region, it is classified into this group, while its close economic and financial ties with the euro area mean that the margin benefit from having its own monetary policy is insignificant (Goczek and Mycielska 2017).

In economic terms, it is very difficult to determine a definite balance of costs and benefits of euro area membership. A key issue is how and when to join the common currency area, as a too rapid and ill-prepared integration into the eurozone could generate costs that could outweigh the benefits of the process (Czerniak and Smoleńska 2019). The existing literature on Poland's integration into the euro area has emphasised that the scenario of accelerated growth after the adoption of the single currency should be viewed as an opportunity that can be taken advantage of, but this depends not only on the healthy macroeconomic foundations of the candidate country, but also on reforms of the eurozone architecture aimed at strengthening its stability (NBP 2014). Adopting the path of integration with the eurozone should be part of a broader reflection on the future of the Polish economic model and its reforms (Tokarski 2013). Since the milestones for joining the third phase of the EMU are spread over time (including the obligation of two-year membership in the ERM II mechanism and the Banking Union), it is necessary to treat euro adoption as a multi-year, multi-stage and complex programme.

2.2. New security context

The security implications of integration into the euro area have not been addressed in the debate on the subject so far, although this factor has been an important aspect of the discussion in the Baltic states, which joined the third phase of the EMU between 2011 and 2015. It was only after Russia's invasion of Ukraine in 2014 that publicists and experts began to pay attention to this aspect (Wojtyna 2014, Cichocki 2015). In the current situation, after the Russian escalation of the conflict in 2022, Poland has become an important aid hub for Ukraine, and security issues have come to dominate the way we think about the economy or international politics. This raises the question of whether euro area membership would have a positive impact on security in the face of current and future threats. From a macroeconomic point of view, it seems that currency stability is a major advantage not only in view of long-term armament procurement plans that involve significant borrowings in foreign currencies, but also in the case of hybrid actions that could target the stability of the Polish currency.

Security aspects are also directly linked to Poland's image as an active player in the international and EU arena, which is interested in further optimal development of economic integration in Europe. As a member of the euro area, Poland could more effectively strive to shape its economic governance system in a way that would be more responsive to security issues. An example is the possibility of leniency for some military spending under the reformed fiscal rules.

2.3. Political aspects

The political dimension of euro area membership is often underestimated. The integration can increase a country’s credibility and influence in the international arena both within the EU and beyond, as it is a token of economic strength and stability. Higher credibility is associated with the entry into the European Union's closest circle of integration and the opportunity to exert greater influence on many EU policies, such as those concerning the internal market or the budget. This is particularly important in the case of Poland, which is one of the larger Member States.

Poland's entry into the third stage of the EMU would open opportunities to apply for key positions in the euro area structures, including that of a member of the ECB's Governing Council and president of the Eurogroup. However, an obvious prerequisite for candidates vying for the top posts would be sufficient experience in managing international institutions and a vision for the further development of economic integration in Europe. Poland as a country not entangled in the "old" EMU conflicts, would have a chance to have its own candidacies supported by a wider group of states. Articulating a path toward the common currency would further help Poland regain credibility in EU politics, tarnished mainly by problems with the rule of law. In this context, reaffirming the commitment to join the euro area – in line with Treaty obligations – would further substantiate Warsaw's renewed commitment to taking joint responsibility for the integration project. It would also reflect positively on Poland's credibility as a country that is to assume the presidency of the Council of the European Union in 2025. A stronger Poland in the European Union would also be a more valuable partner for the US and Ukraine. In the long term, adopting the euro would also cement Poland's ties to Western economic structures and – in the long run – prevent attempts at Polexit.

2.4. Aspects related to protecting the rule of law

There has been a marked deterioration in the rule of law in Poland in recent years. Articulating a path toward the euro area should be part of a programme to restore standards of the rule of law, particularly in the area of economic policy. Integration into the EMU would force Poland to strengthen its fiscal framework. Poland's budgetary policy would then be more transparent and closely monitored by the European Commission and other members of the euro area, making it more difficult to use the state's financial resources to build clientelist networks at the expense of the implementation of basic public policies. Another problem in the case of Poland is that decisions on the state's financial liabilities are made without any real control over spending (NIK 2022). Upon entering the EMU, Poland would have to create a Fiscal Stability Council, which would provide independent assessments of the government's fiscal policy. Integration into the eurozone would also facilitate the restoration the credibility and operational independence of the National Bank of Poland, which would play a key role in the process of planning and introducing the single currency into circulation (Skolimowski 2023). In this way, the National Bank of Poland could once again become a participant of key ongoing discussions on central banking, including as part of the Basel Committee or the Network for Greening the Financial System (NGFS; Smoleńska, Weber, Opoka 2023). Defending the rule of law is also part of building the resilience of the state and its institutions to external threats. Poland, after Russian aggression in Ukraine, has become a logistics centre for Kiev, making it a potential target for Russia's aggressive actions. A war-exhausted Russia can opt for destabilisation of its neighbours through hybrid means, so strengthening the institutions of the state, the rule of law, democratic pluralism and preventing polarisation of public life have an enormous importance to Poland's resilience to the threats from Russia and Belarus.

2.5. Social aspects

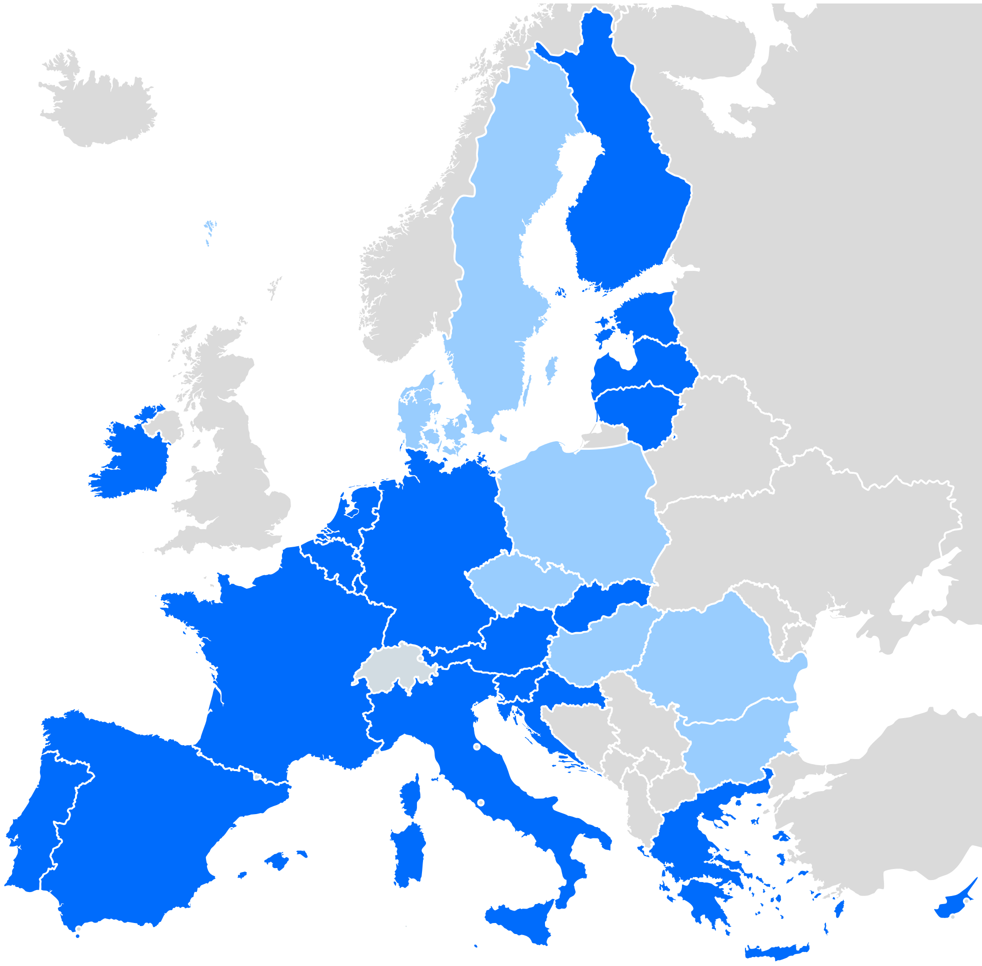
An important argument for or against the adoption of the euro is its perception by citizens. Surveys conducted by the European Commission show a very high support for the euro in countries that have adopted the single currency, even exceeding 80% in Lithuania, Latvia and Estonia. On the other hand, support for the euro is much lower in EU countries that have not joined the third stage of the EMU. In Poland, there has been a marked increase in support for the adoption of the euro in 2022 compared to the previous year[8]. According to European Commission data from early 2023, 47% of Poles surveyed were against joining

8 According to the European Commission, the support increased from 35% (June 2021) to 49% (June 2022), Standard Eurobarometer 97 – Summer 2022, HTTPS://EUROPA.EU/EUROBAROMETER/SURVEYS/DETAIL/2693; Standard Eurobarometer 95 – Spring 2021, HTTPS://EUROPA.EU/EUROBAROMETER/SURVEYS/DETAIL/2532

the eurozone versus 44% of those in favour (European Commission 2023), however Eurobarometer surveys also suggest that support for the common currency tends to grow in the aftermath of accession.

3. Poland, the euro and the experience of other countries: integration scenarios

The discussion on EMU membership should take place in the broader context of Poland's relations with the EU, and include not only economic issues, but also political and security aspects. Preparation for the adoption of the single currency should also be based on the experience of other countries – and these are quite diverse. A large group of EMU countries experienced serious problems stabilising their public finances after euro area accession, and several of them – including Greece, Portugal, Spain and Cyprus – required financial assistance. Basic macroeconomic data, such as GDP per capita growth between 1999 and 2022, show considerable differences in the results achieved. Comparing the experiences of other countries with regard to their euro/EU path, we identify four scenarios: the Finnish, the Italian, the blocked path and the exit ones. The countries referred to in the following scenarios differ significantly from Poland in terms of their economic structures. However, their experiences allow to identify the mistakes or challenges in how countries approach their economic and monetary policies. Crucially they show that both inside and outside of the euro area countries can fall into economic traps.



The euro area in 2023

Members of the euro area

Other EU Member States

Non-EU countries

Source: https://european-union.europa.eu/institutions-law-budget/euro/countries-using-euro_en

3.1. Successful integration despite difficulties – the case of Finland

When it comes to the path of integration into the euro area, Finland may, to some extent, serve as a model for Poland. The country's example shows that it is possible to reconcile euro membership with a highly innovative market economy, an efficient redistribution system, a high level of education and maintaining a strong military. Like Poland, Finland is located on the EU's external border, and one of the main imperatives of its foreign, security and economic policy is to defend against the Russian threat. In the case of Finland, security aspects were an important motive for closer ties with the EU through monetary integration (Etzold, Tokarski 2015).

Economic considerations also played an important role: attempts to stabilise the exchange rate in the early 1990s resulted in significant costs in the form of high interest rates, falling GDP and a banking crisis. The adoption of the euro has brought financial stability. Between 2009 and 2016, the country also faced difficulties, mainly as a result of the crisis affecting Finland's key electronic and paper sectors and unfavourable demographic changes (Liikanen 2006, Berghäll 2023). On the other hand, the Eurosystem's expansionary monetary policy supported Finland's economy during the period of downturn (Välimäki, Obstbaum 2020). Finland did not assume that euro area membership alone would be enough to further the country's economic development. Over the past 20 years, it has introduced a series of structural reforms, including comprehensive changes to the pension system, the labour market, increasing the quality of education, digital skills and innovation, and increasing the efficiency of the public sector. During the COVID crisis in 2020, Finland's recession was one of the mildest in the EU and was followed by a very rapid recovery.

Finland has a multi-party system based on a consensus culture and is characterised by high efficiency and transparency of economic institutions. The country has been at the top of press freedom and democracy index rankings for years. Finland is also characterised by a lack of complexes in European politics. The country clearly articulates its interests and is not enthusiastic about all integration ideas. Thanks to its membership in the euro area, the country has taken a stronger position in political institutions related to economic integration, holding important positions, such as that of the Commissioner for Economic and Monetary Affairs held by Olli Rehn from 2010 to 2014. The country's strong culture of respect for the rule of law also positively influences proper democratic control of new EU mechanisms, as exemplified by the country's debate on the legal basis for the EU's NextGenerationEU recovery fund (Alander, Tokarski 2021). Despite its caution with respect to fiscal integration, Finland has a reputation in the EU as a stable and predictable partner.

3.2. Problematic integration – the case of Italy

This scenario of membership in the common currency, in which the full development opportunities associated with the prospect of adopting the euro were not exploited, is best exemplified by the case of Italy. The difficulties related to functioning in the euro area are considered one of the biggest headaches for the Italian economy (Cottarelli 2018). Before joining the common currency, Italy already had serious structural problems related to bureaucratic barriers, restrictions on the growth of family-run businesses, a slow judicial system, corruption and enormous regional disparities. The weaknesses of the Italian labour market remain the low quality of education and the brain drain. These challenges, despite reform attempts, have been addressed neither in the preparation process for membership nor after the adoption of the euro (Capussela 2018). Italy's EMU membership also had a negative impact on the country's exports, as the high real effective exchange rate reduced the external competitiveness of its economy. The German economy remained much more competitive because it was able to keep labour costs low (Tokarski 2019).

Italy avoided a major debt crisis in 2011 only owing to the intervention of the Eurosystem, which began buying Italian bonds under the Securities Markets Program (SMP). To date, the Italian national debt market requires stabilisation by the Eurosystem, and its structure shows the displacement of foreign private investors in favour of domestic banks (Minenna et al. 2016). The Italian debt market remains a very serious risk factor for the euro area as a whole. The crisis of Italy's economic model is generating a permanent social crisis that is causing political instability and polarisation, as well as an inability to introduce reforms internally. On the other hand, euro area membership helped Italy during the COVID-19 crisis, when the country was the first victim of the pandemic in Europe. If it had its own currency, a health care crisis would most likely trigger a currency crisis and a national debt crisis, which would take the Italian economy years to recover from.

3.3. “Blocked path” scenario – Sweden

The following scenario assumes EU membership, but outside the euro area. There are 7 EU countries in various stages of peripherality to the euro: Denmark, Sweden, Bulgaria, Romania, the Czech Republic, Hungary and Poland.

Sweden can serve as an example for Poland on how to organise the debate on euro area membership and what mistakes to avoid in this debate. The debate in Sweden was going on for many years with the participation of many domestic and foreign economists, and its main point of reference was a report commissioned by the government in 1995 and published a year later by a committee headed by Professor Lars Calmfors, which presented a negative stance toward entry into the euro area. This culminated in a referendum held in 2003, in which 56% of voters opposed the adoption of the single currency (Tokarski and Wiklund 2013). The result of the referendum, although non-binding, has frozen the membership question in political terms for many years, which seemed the right decision during the eurozone crisis. Macroeconomic data also show faster GDP growth in Sweden compared to other EU eurozone countries.

Now, however, Sweden is facing an extensive real estate and currency crisis; the Swedish krona (SEK) exchange rate against the dollar (USD) is at its lowest level since the 1970s. This negatively affects the economic and social situation, as well as confidence in the Swedish currency and the country's financial system. Professor Lars Calmfors, who was previously sceptical of Sweden's entry into the euro area, now supports the idea (Rawet 2023). The Swedish example shows that despite the broad economic debate, its conclusions can become outdated in changing economic circumstances. Even for a highly developed, competitive economy, stabilising the exchange rate can be important in the event of internal or external shocks and inflationary pressures.

There are more countries that are “stuck” at various stages on the path to the euro, including Bulgaria, which is a member of ERM II and the banking union. Due to institutional weakness, political problems, oligarchisation and corruption, the country's entry into the third stage of the EMU is unlikely in the medium term. The Czech economy, which remains outside the eurozone, is also plagued by various structural problems, so its development model is not a suitable example for Poland either (OECDa 2023). Under this scenario, only Denmark can currently be considered a highly competitive economic model without major structural problems. However, this model is very specific and is characterised by a high degree of state interference in the economy, as manifested in 2022 by the highest level of public spending to GDP among OECD countries. Although Denmark has an “opt-out” option when it comes to integration into the eurozone, the Danish krone (DKK) is in ERM ll, which means that the exchange rate is *de facto* fixed, and the Danish central bank makes use of ECB liquidity on preferential terms.

3.4. Exit and drift scenarios – the case of the United Kingdom and Hungary

The final scenario is the process of drifting away from the EU economic integration, as exemplified by the UK. The UK's withdrawal from the EU and the internal market has created new and costly trade barriers, had a negative impact on economic growth, caused a decline in foreign investment and led to labour shortages in some industries. It can be expected that in the case of a similar scenario in Poland, the economic consequences would be much more severe due to the much smaller size of the Polish economy, a less developed capital market and the lack of the zloty's status as a reserve currency, to give just a few examples.

A Hungarian-type scenario of formally remaining within EU structures, while increasingly distancing itself in legal, political and ideological terms from the rest of the Member States and having little influence on the Union's decision-making processes, is also possible.

The main risk associated with these scenarios in the case of Poland is that there is no widespread awareness of the degree to which the Polish economy is integrated with the EU internal market. The example of the UK shows that leaving the EU does not have to be the result of a deliberate political decision. It can also be a side effect of political actions that inadvertently lead to the creation of a certain political dynamic that is difficult or even impossible to stop. In this regard, one of the most positive aspects associated with Poland's membership in the eurozone would be that it could be a factor impeding EU withdrawal.

4. Adoption of the euro as a development project: recommendations for a multi-year reform programme

The above analysis suggests that the question regarding the relationship between Poland and the EMU should not be "Should we become a member of the euro area?" but rather "How to join and be a member of the euro area in such a way as to strengthen the potential of Poland and the Union as a whole?".

In the current geopolitical context, embarking on a multi-year and multi-stage process of integration with the euro area would benefit Poland politically, economically as well as in terms of security and its sustainability transformation. This process would contribute to strengthening the country's political standing in the EU at a time when issues relevant to our country, such as institutional reforms and the prospect of Ukraine's membership in the Union, are central to the Brussels agenda. In contrast, the experiences of various countries outlined above show that the prerequisites for success are adequate preparation for the moment of accession, as well as strong institutions to co-design the framework for monetary integration in a substantive manner and in line with the public interest.

Formulation of a multi-year reform plan in response to the question: "How to join and be a member of the euro area?" requires a distinction between:

- **action levels** (national, EU, civic/social);
- **time horizon** (short- and medium-term);
- **ambition levels** (low/formal criteria, medium, high).

As regards the level of action, the process of joining the third phase of the EMU requires meeting formal criteria at both the national and EU levels. A strategic approach to a multi-year process of euro adoption requires setting short- and medium-term milestones. Different levels of ambition can also be set: ranging from one purely focused on meeting formal criteria (undesirable), through actions ensuring appropriate resilience of the economy and society in the face of change, to high ambition approach oriented at co-shaping the future of the single currency (most desirable). As the experience of other countries shows, agency of a euro area members is facilitated by economic power, but also diplomatic, personnel or research capacities (see Fig. 6 for summary).

At the national level, for adequate substantive preparation and coordination of activities, the function of the plenipotentiary for the euro area in the government should be reestablished, and the relevant unit within the NBP recreated. To ensure that the benefits of the euro area membership are felt, it is crucial to go beyond the (obviously relevant) discussion of meeting formal conditions. Legal issues (such as the need to amend the constitution or restore the credibility and the *de facto* independence of the central bank) as well as adequate supervision of fiscal policy, have been addressed in subsequent reports on convergence by the European Commission or the rich literature of Polish experts . Many authors have also pointed out that Poland's development and rapid modernisation scenario upon joining the euro area is contingent on effective policies, efficient institutions and the vitality and adaptive capacity of businesses (Orłowski 2019). In today's context, four more areas of reform should be added to this list. First, the restoration of the rule of law, also understood as a system of control mechanisms and standards of lawmaking and enforcement. Second, anchoring the discussion over Poland's new economic model and potential as a full member of the EMU in the discussion of sustainability transition. Third, strengthening market institutions including housing and labour market reforms, among others, to ensure that the currency transition is fair. Fourth, deepening the Polish financial market and strengthening its supervision, while maintaining high standards of corporate governance, investor protection and taking advantage of the opportunity for enhanced development with the trend of sustainable finance. An early entry into the Banking Union may be helpful in this regard.

At the EU and eurozone level action should be taken in three different areas.

Firstly, a diplomatic initiative is needed, as not all capitals may be immediately enthusiastic at the prospect of EMU enlargement at this juncture. Per Art. 140 TFEU, EMU enlargement requires a proposal from the European Commission, consultation with the European Parliament, the decision of a qualified majority of Member States and a positive recommendation from a majority of euro area (Eurogroup) Member States. The exchange rate is set on the proposal of the European Commission after consultation with the ECB, unanimously by the euro area Member States and the prospective new member of the EMU's third stage. This complex procedure means that securing a favourable exchange rate and other conditions will require years of work both in Brussels, Frankfurt and the individual European capitals.

Secondly, Poland needs to support, prepare and promote own personnel capable of taking key positions in the euro area institutions. In this context, the potential of the many Poles already working at the European Central Bank should be used. Since monetary institutions often operate on the transnational level, especially in the area of agenda-setting research, it is essential to support expertise exchanges of Poles and the regional cooperation.

Thirdly, Poland should actively engage – in a substantive and multi-level manner – in the debate on EMU's future. Such engagement should recognise the specific economic policy challenges, especially the sustainability transition, which requires significant financing while remaining relatively (financially) stable. The fact that the ECB is increasingly considering the impact of sustainability issues on financial stability in its supervisory and monetary policy decisions represents a huge opportunity for Warsaw, especially given the role that the European Parliament plays in holding the ECB's to account. At the same time, Poland, with its post-transformation tradition of responsible fiscal policy, is well-placed to be a credible and constructive partner in the discussion of EMU's evolving structures.

In view of the political constraints and the relatively long-term horizon associated with the process of EMU integration, scope for civil society action should not be overlooked. Civil society and academia can facilitate building awareness of monetary integration . Support for the euro in Poland has fluctuated in recent years, according to European Commission surveys. In the first quarter of 2023, more Poles opposed the euro (47% to 44%), although just a year earlier the situation was the opposite (60% of respondents in favour of adopting the single currency) (European Commission 2023). The lack of adequate knowledge makes citizens susceptible to false and populist arguments. Although, according to an EC survey, more than half of Poles consider themselves "well" or "rather well" informed about the euro, responses to factual questions reveal one of the lowest levels of knowledge about the basic elements of the eurozone's design among non-EMU countries (cf. Kurs na Euro, 2023). Another study further points to the low quality of public debate about the euro in Poland. In addition to the somewhat understandable concerns about price increases, which 57% of respondents feared in the context of currency conversion in 2022, many Poles still consider the eurozone unstable (22%) and associate it with deregulation (18%) (European Commission 2022). Experts and researchers have a special role in stimulating substantive discussion and deepening awareness of the euro also in the context of the undermined credibility of the Polish central bank as an independent institution acting in the public interest. According to recent surveys, only half of the surveyed Poles trust the information provided by the NBP, the lowest level of trust in the central bank among the non-eurozone EU countries (European Commission 2022). In the long term, raising awareness of monetary integration can also become an engine for raising Poles' financial literacy, which in turn will support the strengthening of the local capital market and citizens' long-term financial resilience (forms of savings, greater financial independence, less susceptibility to fraud) (OECD 2023b).

Fig. 5. Euro as a development project: recommendations for a multi-year programme of reforms and activities in Poland

Actor level	Ambition level			Time horizon
	Formal conditions (low ambition)	**Necessary actions (medium ambition)**	**Strengthening activities (high ambition)**	
Civic and social		▪ information and educational activities	▪ deepening financial knowledge	**Short term (1–2 years)**
		▪ inclusion of monetary integration in the core curriculum ▪ nationwide information campaign in the context of a possible referendum	▪ development of civil society in the area of economic policy	**Medium term (> 3 years)**
National		▪ restoring the role of the plenipotentiary for the eurozone in the government ▪ strengthening control mechanisms in the area of fiscal policy ▪ restoration of the rule of law ▪ financial market development; strengthening of national supervisory institutions ▪ raising the standard of corporate governance, particularly in state-owned companies ▪ ensuring a friendly regulatory environment ▪ institutional reforms (labour and housing market)	▪ strengthening of the civil service ▪ in-depth analyses of the impact of harmonisation in the area of financial law (in relation to sustainable finance and financial innovation) and the actions taken by the supervisors of the banking union within the framework of a multi-currency EU	**Short term (1–2 years)**
	▪ restoring the credibility and *de facto* independence of the NBP ▪ debt and deficit levels ▪ price levels ▪ exchange rate stability ▪ accession to the Banking Union ▪ amendment of the constitution	▪ increasing the transparency of public finances (creation of the Fiscal Policy Council) ▪ use of macro-prudential tools ▪ structural reforms (housing and labour market)	▪ emphasis on the development of innovation, digitalisation and transformation to a low-carbon economy ▪ development of institutional and expert facilities	**Medium term (> 3 years)**
EU		▪ active participation in the work on fiscal rules reforms ▪ signalling the intention to adopt a single eurozone for the capitals of the states	▪ active participation in the process of evaluating and monitoring the National Recovery Plan	**Short term (1–2 years)**
	▪ setting a favourable exchange rate	▪ future active participation in the Governing Council of the ECB ▪ cooperation with the European Commission in the context of the application to adopt the euro	▪ preparation and promotion of personnel	**Medium term (> 3 years)**

5. Conclusions

The analysis carried out in the report leads to the following conclusions:

1. In the current dynamic geopolitical context, embarking on a multi-year and multi-stage process of integration with the euro area would be beneficial to Poland politically, economically and in terms of security and sustainability transition. Such a program would also contribute to strengthening Poland's political standing in the EU at a time when issues important to our country, such as institutional reforms and Ukraine's membership prospects, are on Brussels' agenda.
2. Poland should draw lessons from the experience of other EMU members in shaping the optimal path towards membership, as well as creating an effective institutional framework for economic policy, which is necessary for thriving in the single monetary area. The greatest benefits of adopting a common currency are experienced by countries with a strong and independent market and political institutions (independent media, strong rule of law).
3. Integration with the euro area could be an important factor in restoring the rule of law, strengthening the state institutions, and creating mechanisms and institutions such as the Fiscal Stability Council that would hinder unsustainable fiscal policy.
4. Integration with the euro area would also lead to a decoupling of monetary policy from party influence, moving away from banking nationalism and strengthening the stability of Poland's banking sector by entering the Banking Union.
5. Integration with the euro area would revive the debate on structural weaknesses and growth engines of the Polish economy over the next decades. Since 2015, the discussion of economic policy has focused mainly on redistribution aspects.
6. Adopting the euro would be a means of preventing the worst-case scenario for Poland – Polexit – which could be a side effect of political infighting, a path dependent process that could potentially spiral out of political control. Nevertheless, such a scenario cannot be completely ruled out in Poland, even if the current proeuropean turn in Warsaw makes it less likely.

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