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Poland

Assessment of National Reform Programme

1. In 2006, GDP per capita is expected to reach 51% of the EU average. Between 2001 and 2006, Poland had an annual growth rate of 3.3%. Labour productivity has grown at rates well above the EU average over the last decade and labour market conditions have been improving lately. Despite the recent fall in the unemployment rate, it remains the highest in the EU (projected at almost 15% in 2006, down from 17.7% in 2005) and the employment rate (estimated at more than 54% in 2006) remains the lowest. The government deficit (pension reform costs not included) amounted to 2.5% of GDP in 2005 and is expected to reach 2.2% of GDP in 2006.
2. Poland's growth and jobs performance is constrained by a number of interconnected structural problems, including the low level of labour utilisation, slow progress in economic restructuring, underinvestment and the imbalances in government finances. Economic policy is confronted with a complex challenge of addressing these growth constraints. Removing disincentives to work and reforming the social security system could simultaneously contribute to a stronger performance of the labour market, and improve the sustainability of public finances, which are burdened by high mandatory social expenses.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified the following key challenges: consolidation and better management of public finances; developing entrepreneurship and innovation; infrastructure development; ensuring a competitive environment in network sectors; creating and sustaining jobs and reducing unemployment; and improving the adaptability of workers and enterprises by investing in human capital. In its 2006 Annual Progress Report (APR), the Commission invited Poland to pay further attention to: increasing competition; raising public sector R&D and innovation; developing a comprehensive strategy for investment in infrastructure and environmental protection; a more complete approach to raising employment and addressing regional disparities. Concerns were also expressed over the lack of targets, timetables, budgetary implications and information on monitoring and evaluation in the NRP.
4. The 2006 Implementation Report partially addresses these concerns. A timetable for implementation with expected impacts of the measures proposed together with qualitative and quantitative indicators are now presented. There is more information on the financial resources devoted to these reforms.
5. Poland has made limited progress with the implementation of its NRP. There is progress in implementing measures on redirecting state aid away from a given industry and towards horizontal support; better regulation; measures to improve the business environment (especially for SMEs), and encouraging entrepreneurship. There are encouraging signs of progress on health care reform; removing barriers in professional services; efforts to boost R&D and innovation; and environmental

protection. These measures need to be strengthened and implemented. Progress with fiscal consolidation relies predominantly on positive cyclical developments, while the implementation of expenditure reforms is lagging. Progress has been disappointing on: better budgetary planning and on restraining public expenditure; improving transport infrastructure; energy liberalisation; attracting and retaining more people in employment; improving the adaptability of workers and enterprises; and reforms of education and training.

6. Progress has been limited towards meeting the commitments made at the 2006 Spring European Council, for example on facilitating business start-ups and offering young people leaving education guarantees of employment or training opportunities within six months. Neither has a clear target for R&D investment for 2010 so far been set.
7. Ownership of the reform process has improved but more remains to be done. The Implementation Report was not discussed by Parliament before being finalised. The establishment of an inter-ministerial implementation group is encouraging, as is the decision to strengthen cooperation with social partners, via this group. Cooperation between central, regional and local governments now needs to improve. The Commission welcomes Poland's commitment to devote at least 60% of Structural Funds expenditure towards growth and jobs objectives. Although there is progress, governance of Structural Funds investment needs to be better integrated with that of implementation of the NRP. The new law on public finance will have an important impact on how well Poland is able to absorb the structural and cohesion funding available for 2007-2013. Cohesion Policy funding will amount to 3.4% of GDP in the 2007-2013 period. To enhance communication on Growth and Jobs issues, the government has set up a committee of government, members of the national and European Parliaments, regional and local authorities, business and media. Cooperation between government and the Polish Lisbon Strategy Forum to communicate with a wide range of stakeholders and citizens is encouraging.

PART II: ASSESSMENT BY POLICY AREA

Macroeconomic policies

8. The NRP identified one key challenge in the area of macroeconomic policy: the consolidation and better management of public finances. The Commission supported this choice and recommended preparing a more detailed assessment of the macroeconomic and budgetary impact of reforms.
9. The Implementation Report presents budgetary costs and target indicators. It refers to tax changes endorsed by the government in June 2006, although many of these have not been implemented. Moreover the report presents projections from the January 2006 convergence programme, yet these have been superseded by projections in the draft 2007 budget. Expenditure reforms, especially on social spending, are identified as key for public finances and employment. However, the implementation of these reforms is delayed. Implementation of the key reform linking farmers' contributions to the social security fund (KRUS) with their income is scheduled now for 2008, later than originally planned. Furthermore, it appears that the reform is limited and

will have to be continued after 2008. The projected increase in contributions is only 10%, whereas they cover less than 10% of KRUS expenditure.

10. There is no information provided on progress since September 2005 in the harmonisation of temporary early pensions (“bridge pensions”) for people working in difficult conditions. Implementation is planned for 2007. The government will decide in 2007 on the final shape of reforms in the disability benefit system (linking the level of benefit to the level of pensions in the reformed pension system), with implementation scheduled for 2008. The intention to achieve savings from reforming administration is no longer mentioned. The plan to introduce a basket of guaranteed medical services financed by the state health care fund seems promising, as it is likely to result in better targeting of public spending on health care, but implementation is not expected until after 2007.
11. The four-year nominal state budget deficit anchor of PLN 30 billion, around €7.84 billion, (no more than 3% of GDP in 2005) is not formally adopted by law and may be undermined by plans to increase social expenditure during the current favourable economic cycle. Given optimistic revenue projections, should the business cycle become less favourable, the anchor may not be met (as no sanction would be applied). According to the draft 2007 budget, implementation of multi-annual task-oriented budgetary planning for the whole state budget is scheduled only for 2011, rather than 2009.
12. The approach towards making public finances more sustainable is broad and covers the appropriate areas. Implementation however, remains incomplete. The fiscal regime in Poland has been ‘expenditure-led’ which has entailed adjusting tax revenues to the planned levels of government expenditure. As a result, the general government expenditure to GDP ratio is significantly higher than in other Member States at a comparable level of economic development. The existing national fiscal rules do not appear sufficient to contain the excessive expenditure growth in Poland. Stronger commitment to public finance reform, especially concerning expenditure, and faster implementation is needed.

Microeconomic policies

13. The 2005-2008 NRP identified as key microeconomic challenges: developing entrepreneurship; increased innovation by companies; infrastructure development and upgrading; and ensuring a competitive environment in network sectors. The Commission broadly shared this view, although recommended more emphasis on competition, on reinforcing public sector R&D and innovation, and on developing comprehensive strategies for infrastructure investment and environmental protection.
14. A range of initiatives is being implemented to improve the business environment and develop entrepreneurship. A system to measure administrative costs, and simplification of the tax system, are useful steps. However, the start of a “one-stop-shop” system for the registering of new businesses has been repeatedly postponed. There are no measures mentioned to reduce the time and costs of registration and to facilitate the recruitment of the first employee. A comprehensive ICT strategy and speeding up of governmental ICT projects would help in this area.

15. The adoption of the regulatory reform programme is a major step forward but will require considerable implementation efforts. Since access to finance is a chronic problem for SMEs, steps to improve it are valuable, especially those focused on technology-based start-ups and using the Structural Funds. Poland has made significant efforts to reduce its backlog in transposing EU legislation into national law, but needs to ensure the quality of transposition. The reform of commercial jurisdiction is promising. Promising work to reform the legal profession is underway and similar reforms should be made with respect to other professions. Efforts to reduce the overall level of state aid, and to increase the share of horizontal state-aid are welcome, but further efforts are required to redirect it, in particular towards R&D.
16. Poland has proposed measures to increase R&D and innovation. Law amendments and tax exemptions will help address a lack of business innovation. However, a more comprehensive strategy for attracting foreign direct investment, notably in medium and high-tech industries, is needed. The reform of public procurement rules could now stimulate innovative products and services. Pilot projects on clusters and technology start-ups are valuable and there are plans to introduce them on a much larger scale. The reform of public sector R&D with its extra focus on a limited number of large projects and on the best performing institutions is welcome, but the legislative changes still need to be adopted and implemented. A document on increasing innovation over the 2007-13 period has been drawn up: it will be important to ensure that this leads to a coherent strategic approach and prioritisation of measures, as well as the use of benchmarking and the continuous evaluation of measures. Poland should set a firm and realistic target for overall investment in R&D, given that the target originally set in the NRP is now recognised by the Polish authorities as unattainable.
17. Measures to improve transport infrastructure need to be stepped up and should be coordinated with regulatory measures. The simplification of the administrative processes for investment and a review of spatial planning are still awaited. Improving infrastructure, along with enhancing the broad business environment, should help in attracting much needed foreign direct investments. Market opening in the energy sector and in railways is not progressing sufficiently. Poland should remove obstacles to new competitors in these sectors. However, in telecommunications, recent regulatory decisions in line with EU laws are to be welcomed. The recent regulatory, institutional and other developments related to regulatory supervision in the network and financial sectors raises concerns over the functioning of such regulators and their ability to guarantee competition, and in particular, access to these markets.
18. In the energy markets, emphasis has been put on securing supply and on environmental sustainability. Less attention is devoted to the role of competition in delivering these objectives. In particular, the energy plans assume the creation of four vertically integrated groups incorporating generation, retail and distribution services prior to the unbundling of distribution services. While the commitment to unbundling is welcome, this sequencing could delay it until after the 1 July 2007 deadline and make the process more difficult. There is progress on encouraging environmental reform but this now needs an integrated environmental strategy.

19. The micro-economic measures, implemented or planned, could boost the business environment, innovation, entrepreneurship and infrastructure. The postponement of the implementation of some measures raises concerns that not all the necessary reforms will be completed.

Employment policies

20. Creating and sustaining jobs and reducing unemployment, and improving the adaptability of workers and enterprises by investing in human capital, were among the main employment priorities of the NRP 2005-2008. The Commission subscribed to this choice, but pointed to the need for: an appropriate policy mix to favour employment growth; further reform of the tax and social benefit systems; stronger measures to reduce regional imbalances; and a more effective approach to transform undeclared work into formal employment.
21. The implementation of measures to attract and retain more people in employment is slowly progressing. For the first time since 2001, employment growth has resumed. The government has set targets for 2010 for the employment rate (57%-58%) and the unemployment rate (12%-13%). The 2006 National Action Plan for Employment specifies in more detail reforms announced in the NRP, including timetables and budgetary implications. Expenditure on active labour market policies has increased, but with little focus on skills development (in 2005, only 5.2% of unemployed people received training). Modernisation of the public employment services is underway, but so far with few tangible effects. The low staff-client ratio remains a concern. The government plans to integrate more young people in the labour market through activation programmes, but a clear commitment to deliver specific services is missing. A law aimed at increasing the employability of people with disabilities has been presented to Parliament.
22. Progress on the implementation of measures to improve the adaptability of workers and enterprises is slow. Although Poland has the lowest employment rate of older workers in the EU, and one of the lowest average exit ages from the labour force, early retirement entitlements (initially to be phased out by the end of 2006) have been extended till 31 December 2007. Policies to promote a "flexicurity" approach focus only on one component (promoting flexible forms of employment), underplaying the role of active labour market policies, lifelong learning and social security systems. Increasing flexibility in the retirement age and equalising the retirement age of women and men has been postponed to after 2008. Although the tax-wedge in Poland is one of the EU's highest, plans to reduce charges on the wages of low-wage workers have been discontinued. A study is in progress on undeclared work, but results will be available only by the end of 2007. The government is preparing a draft programme covering access to childcare and women's participation in employment, but no information on its planned implementation is presented. The need to reduce regional disparities, in particular through more occupational and geographical mobility is addressed only partially.
23. To improve and increase investment in its people, Poland is developing a lifelong learning strategy but implementation is scheduled only for 2007-2008. Although the Commission in the 2006 APR expressed concern about the lack of a fully-fledged strategy for vocational training, no concrete steps are presented to address this. Increasing participation in education and training, in particular for low-skilled

workers, remains a challenge. The mismatch between the education system and the needs of the economy has contributed to a very high rate of youth unemployment.

24. Labour market reforms envisaged in the NRP, and then specified in the National Action Plan for Employment, are in general appropriate and respond to Poland's challenges. However, they may not prove sufficient and implementation of some of the reforms, for example lowering the tax burden on labour, is delayed or abandoned,. Determined action and strong commitment are needed to implement reforms urgently through an appropriate policy mix encompassing making work pay, activation, prevention of unemployment, and improving skills.

PART III: CONCLUSIONS

25. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
26. Poland is making limited progress in the implementation of its National Reform Programme. There are signs that Poland is beginning to move ahead strongly in the micro-economic area, even though implementation of many measures is still in the early stages. Implementation of the macro-economic and employment reforms is so far insufficient. There is a limited policy response to the commitments made by the 2006 Spring European Council.
27. Among the most promising reforms being undertaken by Poland are simplifications to the tax system, the introduction of systematic impact assessments for legislation and steps to increase SME's access to finance.
28. The policy areas in the Polish National Reform Programme where weaknesses need to be tackled with the highest priority are: fiscal consolidation; improving competition in network industries and financial sectors; increasing the quantity and quality of R&D; making active labour market policies more extensive and more effective; and improving human capital and incentives to work. Against this background Poland is recommended to:
 - pursue its action to step up fiscal consolidation and supplement the nominal state budget deficit "anchor" (deficit ceiling) with an expenditure rule, in order to contain overall expenditure growth;
 - improve competition in network industries and in the financial sectors, including through a review of the role of regulators;
 - in order to boost R&D and innovation, pursue the reform of the public research sector and introduce policies to better attract and maximise the benefits of medium and high-tech foreign direct investment;
 - complete the reform of public employment services in order to increase the level and efficiency of active labour market policy to cover a larger share of unemployed, especially older persons and youth;

- lower the tax burden on labour and review benefit systems in order to improve work incentives, while developing policies to increase adult participation in lifelong learning and to modernise education and training systems in view of labour market needs.

29. In addition, it will be important for Poland over the period of the National Reform Programme to focus on: upgrading transport infrastructure; improving environmental protection; further reducing and redirecting state aids; the full liberalization of energy markets; speeding-up the business registration process; and ensuring that cohesion policy instruments underpin the structural measures highlighted in the Implementation Report with a view to contributing to boosting growth, competitiveness, employment and social cohesion. A firm and realistic target for overall investment in R&D by 2010 should be set.

PART IV: STATISTICAL GRAPHS AND DATA

POLAND

	PL							EU25				
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target	
GDP per capita in PPS	46.8	46.1	46.3	46.9	48.8	49.8	1.65 (2008)	100.0	100.0	100.0	70.0	
Labour productivity per person employed	58.0e	50.3	51.5	59.5	62.1	63.1		100.0	100.0	100.0		
Employment rate								62.4	63.3	63.8		
Total	55.0	53.4	51.5	51.2	51.7	52.8						
Women	48.9	47.7	46.2	46.0	46.2	46.8		53.6	55.7	56.3		
Men	61.2	59.2	56.9	56.5	57.2	58.9		71.2	70.9	71.3		
Employment rate of older workers								36.6	41.0	42.5		
Total	28.4	27.4	26.1	26.9	26.2	27.2						
Women	21.4	20.4	18.9	19.8	19.4	19.7		26.9	31.7	33.7		
Men	36.7	35.6	34.5	35.2	34.1	35.9		46.9	50.7	51.8		
Gross domestic expenditure on R&D	0.64	0.62	0.56	0.54	0.56	0.57		1.86e	1.86e	:		3.0
Youth education attainment level								76.6	77.1	77.5		
Total	88.8	89.7	89.2	90.3	90.9	91.1						
Women	91.7	91.8	91.9	92.8	93.1	93.3	79.5	80.1	80.3			
Men	85.8	87.7	86.5	87.9	88.7	88.9	73.7	74.2	74.7			
Comparative price levels	56.3	62.9	59.5	53.4	52.4p	59.6p	100.0	100.0p	100.0p			
Business investment	21.4	17.3	15.3	14.9	14.6	14.7	18.3	17.1	17.4			
At-risk-of-poverty rate after social transfers							16.0e	16.0e	:			
Total	16.0	16.0	17.0	17.0	:	:						
Women	16.0	15.0	16.0	16.0	:	:	17.0e	17.0e	:			
Men	16.0	16.0	17.0	17.0	:	:	15.0e	15.0e	:			
Dispersion of regional employment rates							13.4	12.2	11.9			
Total	6.9	7.2	7.3	7.2	6.4	5.6						
Women	8.7	8.9	9.2	8.7	7.6	7.0	20.5	17.3	16.9			
Men	5.8	5.9	6.3	6.4	6.0	5.1	9.9	10.2	9.7			
Long-term unemployment rate							3.9	4.1	3.9			
Total	7.4	9.2	10.9	11.0	10.3	10.2						
Women	9.1	10.8	12.3	11.7	11.0	11.4	4.8	4.7	4.5			
Men	6.0	7.8	9.7	10.3	9.6	9.3	3.3	3.6	3.5			
Total greenhouse gas emissions	68.2	67.7	65.5	67.7	68.4	:	90.7	92.7	:			
Energy intensity of the economy	680.2	673.5	654.2	623.1	596.6	:	208.8	204.9	:			
Volume of freight transport relative to GDP	81.8	79.9	80.5	81.9	88.7b	89.6	100.1e	104.6be	104.7e			

PERFORMANCE COMPARED TO EU-25

