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Financial security of a small open economy in conditions of globalization as a requirement for economic growth

Abstract

In the conditions of the globalization of economies the issue of financial stability, which is a condition for the economic security of the state, has acquired a special significance. The aim of the article is to determine the importance of the role of financial stability for maintaining economic security and economic growth and to validate the role of the Safety Network Institution in maintaining stability.

Keywords: financial security, economic security, national security, globalisation, safety network

JEL Classification Codes: H56, F52, F62, F63, G00
Introduction

The issue of broadly understood national security has always been very important for the functioning of a state. Along with the development of statehood, economy and geopolitical relations, the issue of security also evolved from being clearly understood as an ability to defend against military aggressors towards the high importance of its economic angle. Currently, the economic reality is largely shaped by the globalization process. In the conditions of the unification of economies, as well as the entire financial systems, the issue of financial stability, which is a condition for the economic security of the state, has acquired a special significance. Especially due to the fact that the globalization process brings various opportunities and threats, but the latter are particularly important in conditions of a bad economic situation, in particular during a crisis.

The aim of the article is to determine the importance of the role of financial stability for maintaining economic security and economic growth and to validate the role of the Safety Network Institution in maintaining stability. Regarding the methodological framework, the article was composed on the basis of a review of the relevant literature.

The article consists of 4 main parts. The first defines the importance of security for the functioning of a state. The second highlights the importance of financial stability for maintaining economic growth. The third part focuses on the process of globalization that is a major factor shaping today’s economic reality. In the fourth part, the aim is to underline the role of the Safety Network in maintaining financial stability in the conditions of globalisation.

The scope of national security as the highest value for a modern society

The term ‘security’, according to Oxford Dictionary, is defined as ‘the state of being free from danger or threat’ [Oxford Dictionaries, 2018]. This definition can be understood as a situation where a particular subject in the face of various difficulties, problems, perturbations, weaknesses and challenges does not feel threatened, and therefore feels safe [Delumeau, 1998, pp. 9–20]. The application of this term is currently very broad and may refer to the safety of individuals, social groups and whole societies, business entities, the financial sector, ecology, energy, economy, the state, etc.

Historically, the concept of security of a state, increasingly referred to as national security, was mainly related to the ability to defend against military aggressors. The closer to the present, the economic dimension of national security becomes more and more important [Ronis, 2011, p. 11; Alting von Geusau, Pelkmans, 1982, pp. 3–10]. The purpose of this article is not detailed, theoretical considerations on this subject, but only an overview of the most important aspects of this subject.
Financial security of a small open economy in conditions of globalization as a requirement for economic growth

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**Table 1. The historical development of the definitions of security**

<table>
<thead>
<tr>
<th>Year</th>
<th>Author</th>
<th>Definition of security</th>
</tr>
</thead>
<tbody>
<tr>
<td>1943</td>
<td>Walter Lippmann</td>
<td>A nation has a sense of security when it does not have to sacrifice its legitimate interests to avoid a war and is able, if questioned, to maintain them by war.</td>
</tr>
<tr>
<td>1962</td>
<td>Arnold Wolfers</td>
<td>Security, in an objective sense, is the lack of threats to acquired values and in a subjective sense, is the lack of fear that these values will be attacked.</td>
</tr>
<tr>
<td>1968</td>
<td>International Encyclopaedia of Social Sciences</td>
<td>A nation's ability to protect its internal values against external threats.</td>
</tr>
<tr>
<td>1981</td>
<td>Amos Jordan, William Taylor</td>
<td>National security has a broader meaning than protection against physical harm, it also means protecting, through various means, important economic and political interests whose loss could jeopardize the basic values and vitality of the state.</td>
</tr>
<tr>
<td>1990</td>
<td>Charles Maier</td>
<td>National security is an ability to control national and international conditions that the general public considers necessary to enjoy self-determination or autonomy, prosperity and well-being.</td>
</tr>
<tr>
<td>2011</td>
<td>Sheila R. Ronis</td>
<td>National security is societal, political, and economic strength. In today’s world, national security for a superpower is meaningless without a strong military capability as well.</td>
</tr>
<tr>
<td>2016</td>
<td>Ammerdown Group</td>
<td>National security may be understood as a shared freedom from fear and want, and the freedom to live in dignity. It implies social and ecological health rather than the absence of risk and is a common right.</td>
</tr>
</tbody>
</table>

*Source: own concept based on Romm (1993), pp. 5–6.*

The definition of state security can vary depending on its framework and purpose, as the category of the security of state is a very complex and multidimensional phenomenon. In this context, national security [Kitler, 2011, p. 27]:

- is a superior value among other national (state) goals, and at the same time determines the success in their implementation;
- concerns goals that include values (and as a consequence, needs, interests):
  - life (key) – values decisive for the stability of the state, national prosperity and development, its national identity and a sense of certainty (security of survival);
  - important – values that have no direct impact on the fate of the state and the nation as a whole, historically, situationally, objectively and subjectively variable, the implementation of which affects the safe national existence and development of the state;
  - other (secondary) values that from the point of view of national existence and development of the state do not have much influence on them;
- defines the level of freedom in achieving these goals;
- as a process includes: various treatments in the area of international and internal relations as well as protective and defence projects (in the broad sense), aimed at creating favourable conditions for the functioning of the state on the international and internal arena and countering the challenges and fears of national security;
- is to ensure the security of the state as a political institution (sovereignty, integrity, inviolability of borders);
- is the protection of society, its goods and the environment in the face of threats that limit its functioning in a restrictive way or are compatible with national values subject to special protection;
• concerns the opposition to the challenges and threats of values, goals and national interests;
• it concerns ensuring favourable conditions for the implementation of national goals – national development (material and cultural) in a world filled with fierce competition and rivalry, including the political, economic, cultural and military background.

National security is the most important value and national need and maintaining it is especially challenging in the conditions of a small open economy. It is the goal of the state, individuals and social groups, and at the same time a process involving various means, guaranteeing a lasting, disruptive existence and state development. This includes defence of the state as a political institution and protection of individuals and society as a whole, their goods and the environment, against threats that significantly limit its functioning or harm property that is subject to special protection [Kitler, 2011, pp. 22–31].

**Financial stability as a mandatory condition for growth**

Economic security, which is part of total welfare of a nation, can be defined as a state of mind or sense of well-being by which an individual is relatively certain that he or she can satisfy basic needs and wants, both present and future [Rajda, 2015, p. 7]. Another view regarding economic security defines it as a state of development of a national economic system, which ensures high efficiency of its operation – through the proper use of internal development factors and the ability to effectively resist the external pressure which may lead to developmental disorders [Stachowiak, 1994, p. 189]. Another definition highlights that economic security relates to a state of uninterrupted functioning of the economy, that is, maintaining basic development indicators and ensuring a comparative balance with the economies of other countries [Księżopolski, 2012, p. 178].

A secure economic environment is arguably a key factor for promoting private investment and economic growth [Poirson, 1994, p. 4]. The main pillars of economic security consist of [Siemiątkowski, 2015, p. 37]:

• international competitiveness of the economy – a long-term ability of the national economy to cope with international competition;

• an ability of self-development and progress – the ability of an economic system to create the right amount and quality of technological innovation, providing foundations for modern production, a system for improving the qualifications of employees and creating a favourable climate for investment;

• economic sovereignty (independence) – such a state of development of a national economic system and international economic ties which ensures an ability to effectively resist external pressure that may lead to developmental disorders.

In addition, a balanced budget and a relatively low level of public debt as well as participation in international economic structures that formalize relations with the environment are important. Economic security can be considered on two levels – as national economic
security, which concerns one country, and as international economic security, which is the sum of individual states’ activities for security and relations between them. Except for this division, there is also a differentiation due to the goals the state sets for itself in creating the policy of economic security [Sojka, Waloszczyk, 2008, p. 82]. In the context of differences between the economic security of the state and other types of security, a number of features can be mentioned. Most importantly, one should mention: stability (unchangeability) and certainty, attitude to challenges arising from the external environment, relations with the external environment, connections with foreign partners, or the role of the market and the state [Kurek, 2000, p. 28]. It should be emphasized that the economic security of the state is not only a set of its specific features, but it is one of the basic elements of general state security, also revealing a certain relation with them regarding: conditions and factors of their formation and convergence of barriers that limit them, as well as common fields of threats. It also means that the economic security of every state should be considered in a similar way to general security, i.e. both at the international and national level, or in other words as external and internal security [Stachowiak, Stachowiak, 2014, p. 199].

Financial security of the state is immanently related to the general national security of the state. It is a concept narrower to the concept of economic security, although interrelated. It can be defined as a whole range of legal regulations and self-regulation aimed at ensuring financial stability and protecting the interests of market participants using financial intermediaries, as well as all institutions responsible for controlling the compliance with these regulations and self-regulation [Iwanicz-Drozdowska, 2008, p. 22].

The areas of considerations within the scope of financial security include:

- **external financial security:**
  - changes in the balance of payments;
  - foreign debt;
  - official reserve assets;

- **internal financial security:**
  - security of the financial system;
  - security of the banking system;
  - security of financial markets;
  - the appropriate level of indebtedness of entities (cash and credit security);
  - public finance safety.

In another view, financial security can be defined as a set of institutional solutions and legal regulations aimed at protecting the financial system from destabilization [Wierzba, 2005, p. 38]. This definition focuses on the condition of stability of the financial system as a factor of its security. The concept of financial security is very much related to the financial stability of the state. In a sense, state security is a broader concept than stability. The main difference is that the category of security, over the category of stability, includes the continuous trust (credibility) of its clients and the smooth operation of infrastructure, such as technology platforms, the payment system and the regulatory and supervisory framework [Pietrzak, Wasiak,
Definitions of the stability of the financial system have a common feature – they indicate that in case of shocks the financial system will be able to fulfil the functions assigned to it [Iwanicz-Drozdowska, 2014, p. 6].

To summarize, as mentioned earlier, maintaining national security is a condition for building economic growth. Since the loss of financial stability has a negative impact on the financial security of the state, and this is part of economic security and further contributes to national security, the maintenance of financial stability positively affects both, broadly understood security as well as economic growth.

The issues of security as well as financial stability are closely related to the stability of the state’s financial system. Maintaining the stability of the financial system is particularly important nowadays, in the conditions of openness of economies, financial markets and dynamically progressing globalization.

**Globalization as a factor shaping economic development**

The current shape of the world economy is to a large extent the result of progressive globalization [Ostaszewski, 2013, p. 74]. This process has gained particular importance in recent years, strongly affecting the structure of the economy, its particular sectors, the dynamics of development and business processes. Globalization can be understood as a process of economic merger of economies, consolidation of economic structures and interdependencies of phenomena that take place over the perspective of the national economy and lead to integration of domestic markets with the world market [Małecki, 2007, p. 7] and its unification [Obstfeld, Taylor, 2002, pp. 1–9, Morawski, 2009, pp. 22–32]. There are also qualitative changes understood broadly as systemic restructuring towards the economic consolidation of the world [Suszyński, 2003, p. 71].

The phenomenon of globalization can be synthetically defined as free movement of goods, services, labour, capital and knowledge between countries [Flejterski, Wahl, 2003, p. 17]. In other words, it is a global integration of economic, technological, political, cultural and social conditions between states [Hamilton, 2009, p. 10]. In the handbook issued by the OECD, globalization is defined as the progressive internationalization of markets, goods and services, the financial system, corporations and industries, technology and competition [Pomiar globalizacji, p. 17]. The course of globalization accelerates, to a large extent, the reduction of the administrative role of the state in controlling all kinds of flows across national borders, such as the flow of goods, services, capital and people.

It is said that globalization is a result of the triumph of capitalism over other regimes world-wide [Milward, 2004, p. 16]. However, it has often been noticed that its progress leads to the replacement of the old state power which was exercised by national elites with the new dictatorships of international finance and corporations [Stiglitz, 2013, p. 219].
The article addresses the subject of financial security of a small open economy. This concept is crucial for the view of its financial security in conditions of globalization. A small open economy is one that is limited in its own space and economic potential and in order to improve efficiency and well-being, based on its strengths, it must strategically take advantage of the opportunity offered by integration with the outside world [Castello, Ozawa, 1999, p. 18].

A metaphor for the functioning of an economy in relations with the environment may be the model of a medieval city surrounded by high walls and a moat, which in the conditions of danger formed a defence line and allowed isolation from external threats, while during the period of prosperity, through the system of gates, it was possible to physically bring in and export goods. In modern small open economies, it is the regulations that allow or forbid the flows of capital, goods, production factors, knowledge and technologies. But the concept of openness comes from the fact that the flow of stream is opened. A small economy is understood as an economy that cannot influence the key global macroeconomic variable and that the exogenous macroeconomic factors are primary to the endogenous [Komorowski, 2013, p. 285].

Nowadays, one can talk about the global economy as a unified world economy consisting of large and small open economies. Its links, open economies of individual countries, giving up the administrative control of flows of goods and services on the scale of individual countries, lose the possibility of influencing processes which become of global nature. This means that in times of prosperity there are no restrictions for expansive business processes, while in difficult times, there is no way to isolate itself from the impact of negative external processes. Under these conditions, economic growth is becoming increasingly dependent on the interrelations between economies [Brodzicki, 2006, pp. 4 and following]. As a consequence, the phenomena of recovery and crisis have an international context [Kindleberger, 1999, pp. 209, 213].

The international market and external determinants for a small open economy are inherently primary and have a stronger impact on the internal situation than internal factors. Under the conditions of global interdependencies, the interaction between domestic supply and demand and the impact of regulation tools is seriously disrupted. Conducting operations across national borders creates difficulties in controlling them and in an adequate risk assessment of these processes [Komorowski, 2010, pp. 248–251]. Globalization, as an inevitable and irreversible phenomenon, creates both opportunities and threats [Robertson, 2000, pp. 8 and following]. It seems, however, that the balance of these phenomena is on the side of its positive features [Kołodko, 2001, p. 191].

In the conditions of real globalization coming down to the unification of economic processes, the similarity of economies and the creation of global markets, we deal with its extensive effects on many levels leading to intellectual globalization. The phenomena are spreading with pop culture, international tourism, flows of goods and services, etc., patterns of market behaviour, dissemination of tastes and standards of products, and the flow of technology. As a consequence, the changes taking place as a result of qualitative processes cause the measurement of the degree of globalization illustrated by simple measures, such as the share of trade in GDP, to be unsatisfactory [Komorowski, 2011, pp. 343–387].
The main features of globalization are [Flejterski, P. Wahl, 2003, p. 23]:

- creation of a global financial market;
- institutionalization of international trade;
- the so-called ‘McDonaldization of society’, or in some areas limiting, not increasing freedom;\(^1\)
- increase of flows in the category of foreign direct investments, [A. Buszko, 2011, pp. 52–65];
- dominance over the global economy by multinational corporations;
- geographical disruption of the value-added chain on a global scale;
- creation of a knowledge-based economy;
- creation of the intellectual services sector;
- redefinition of the importance of the state.

The systemic foundations leading to the modern phase of globalization of financial markets were established in 1944 at a conference in Bretton Woods, creating a system of international settlements and trade credit based on the US dollar. In 1973, the system of fixed exchange rate was abolished and the dollar was released and became floating. From this moment on, we have observed the process of deregulation of international financial markets, which has gained a special dynamism in the last two decades of the 20th century, after the collapse of the Soviet bloc. At the same time, this trend was followed by the liberalization of capital requirements and prudential regulations concerning the activities of banks. Under these conditions, a continuous increase in capital flow and the integration of financial markets could be observed. The construction of real economic and financial ties through international capital investments and commercial settlements favoured the developing global financial system [Collier, Dollar, 2002, pp. 23–53].

Along with the economic development of the world and the emergence of ever stronger trade links between states, the processes taking place in the sphere of the real economy on the one hand forced the development of legal conditions. On the other hand, the sphere of legal regulations set the conditions and influenced the shape of globalization processes in the future.

The liberalization of the capital flow of the integrating Europe was initiated by First Capital Directive 60/921/EEC in 1960. It is worth noting that this fact took place even before the creation of the common European market in an institutional form. It was not until 1988 that the EEC Council of Ministers, along with the adoption of Council Directive 88/361/EEC for the implementation of Article 67 of the Treaty, decided to fully liberalize capital flows between the Member States and in relations with third countries, as of July 1st, 1990. It contains safety clauses enabling temporary protection measures to be taken by states threatened by an imbalance of the balance of payments. On this basis, the current difficulties of public finances authorize the governments of some EU members to take extraordinary measures.

Free movement of capital, in addition to the movement of goods, services and people, i.e. the freedom to migrate and settle within the EU, is one of the four fundamental freedoms

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\(^1\) In other words, social behaviour is imposed by the mass media and marketing activities of corporations on a global scale.
guaranteed in the treaties establishing the European Union [Treaty establishing the European Community, 2002]. The concept of capital flow is also specified. In EU regulations, it was restricted to the so-called independent financial transactions [Council Directive 88/361/EEC, 1988]. In the light of the regulations in force, current payments that are not self-existent are not considered to be capital flows, as they result from the implementation of the remaining freedoms [Emmert, Morawiecki, 1999, pp. 373–374]. Such operations as trade settlements or transfer of money remuneration for work done in another country, are not classified as capital flows.

The process of eliminating the barriers to capital flows has been the basic and strongest factor in economic globalization in recent decades, but not the only one. The free flow of technology and information has a significant impact on the functioning of financial systems. In the conditions of openness and complex connections on many levels, global processes are getting out of control. The destabilization of the market equilibrium, the change in the economic situation, and even the triggering of a global financial crisis may be caused by a small group of entities that focus their actions on one specific market scenario. The persistent pursuit of a scenario in essence becomes a form of concentrated speculation on a global scale. Its strength may destroy the delicate market balance, and as a consequence, sooner or later can lead to an uncontrolled reaction on many levels. It boils down to the accumulation of risk, entailing entities from a broad economic environment, not participating in the initial mechanism of speculation. This situation shows a kind of powerlessness of participants who are drawn into the game in the global market but are not able to manage from the perspective of the control of its results.2

In the conditions of openness and integration, global interdependence is expressed by the fact that events and trends in a particular field are not isolated but result in a chain of processes that induce further consequences in many other areas [Komorowski, 2011, p. 344]. These processes sometimes develop in parallel in many areas and within many countries, then they are completely strengthened in another dimension of financial relations.

The globalization process brings various opportunities and threats, but the latter are particularly important in conditions of a bad economic situation, in particular during a crisis. They mainly result from the lack of barriers to the flow of goods and services, and the openness of economies in times of economic turmoil. This does not mean, however, that despite the lack of the possibility of isolation of an economy from the global economy, states do not have internal resilience to crisis phenomena. This resistance is determined by individual institutional, market and socio-cultural conditions. There is also no doubt that the level of resistance to crisis phenomena is a derivative of the competitiveness of the economy, innovation of individual industries and the development of enterprises [Waelde, Wood, 2004, p. 15].

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2 This is what happened during the genesis of the previous global crisis and was expressed by pumping the real estate bubble and the development of financial engineering in isolation from real risk.
Ultimately, the resistance of an economy affects the functioning of the financial system, which is a kind of safety buffer for capital-related crisis phenomena, as well as for the real economy. Its condition is interdependent with the financial system’s condition and is associated with the crisis spreading through non-financial and trade related channels [Komorowski, 2012, pp. 151–152].

As mentioned, globalization is a process that affects today’s reality to a very high degree. In such dynamic conditions maintaining financial stability is key and becomes a very big challenge. It is important to analyse the factors affecting stability and institutional methods of maintaining stability.

**Challenges for maintaining financial stability in the conditions of globalization**

Functioning of a small open economy in the globalised system carries a number of opportunities, but also there are many threats which are instigated by the endogenous processes and factors. The dependence on the global macroeconomic trends is especially important for maintaining stability of the financial system in a small open economy. The financial system is a sector of public trust. Its operation is based on the undisputed principles of transparency and the acting in good faith for its clients. These rules constitute the basis for the proper functioning of the sector and they should be superior to the pursuit for earnings of intermediaries. The activity of the players of the financial sector is strongly regulated, and the credibility of entities is enhanced by:

- the need to comply with local and international legal regulations;
- strict financial supervision;
- codes of best market practice.

In regard to the stability of the financial system in a small open economy, its maintenance is especially challenging. In the system of open economies, an impulse triggering a crisis may indeed materialise risks in different spheres of the entire global economy, often not related to the initial source causally, functionally or geographically. Such a spontaneous domino effect may affect the internal stability, especially in the financial sector, during the phase of contagion. It is not possible for the government or public instructions to isolate the internal economy from the exogenous crisis factors, however, it is the resistance of the financial sector that may either absorb the shocks or let the shock through to hit the real economy. It is said that today’s regulation causes a tomorrow’s crisis. In the conditions of openness of an economy, the stability of the financial sector is primarily determined by the regulation and maintained by the supervision authority. In general, it is the Safety Network Institution that manages the internal stability of the financial system and prevents a crisis transferred into a small open economy from its environment. This institution consists of the:
• Regulatory Authority;
• Central Bank;
• Supervision Authority;
• Deposit Guarantee Fund;
• Macroprudential Authority;
• Resolution Authority.

No matter how the Safety Network will be organised (i.e. the Macroprudential Authority, or the Supervision Authority might as well be part of the Central Bank or can be separate institutions, etc.) it is important that the structure fulfills all the founded functions in the most effective way. The functioning of the Safety Network can be divided into 3 main spheres: maintenance of stability and prevention of crises, management of a crisis (once it occurs) and information and education activities. The table below shows detailed functions of each of the Safety Network entity with the functions it performs.

Table 2. The classification of the Safety Network Institution functions

<table>
<thead>
<tr>
<th>Stages of activity</th>
<th>Functions</th>
<th>Regulator</th>
<th>Central Bank</th>
<th>Supervisor</th>
<th>Deposit Guarantee Fund</th>
<th>Macroprudential Authority</th>
<th>Resolution</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Maintenance of stability and prevention of crises</td>
<td>Regulation</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
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<tr>
<td></td>
<td>Control and supervision</td>
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<tr>
<td></td>
<td>Sanctions</td>
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<td></td>
<td>Security of the payment system</td>
<td>X</td>
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<tr>
<td></td>
<td>Macropurudential analysis</td>
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<td></td>
<td>Threat monitoring system</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<td></td>
<td>Organised liquidation</td>
<td>X</td>
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<td>X</td>
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<td></td>
<td>Coordination of the functioning of the Safety Network</td>
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<tr>
<td>2. Management of a crisis</td>
<td>Control and supervision</td>
<td>X</td>
<td>X</td>
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<tr>
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<td>Sanctions</td>
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<td>Security of the payment system</td>
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<td></td>
<td>Extraordinary regulations</td>
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<td>Macropurudential analysis</td>
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<td>Threat monitoring system</td>
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<td></td>
<td>Organised liquidation</td>
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<td></td>
<td>Coordination of the functioning of the Safety Network</td>
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<td></td>
<td>Last-resort lender</td>
<td>X</td>
<td>X</td>
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<td></td>
<td>Public finance support</td>
<td>X</td>
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<td></td>
<td>Payment of deposit guarantees</td>
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<td>X</td>
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<tr>
<td>3. Information and education</td>
<td>System of public information</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<tr>
<td></td>
<td>Education</td>
<td>X</td>
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</tbody>
</table>

Of particular importance for the rapid stabilization of the financial system during a period of destabilisation is the efficient activity of the Safety Network [Szczepańska, 2008, p. 128]:

- the actions must be taken quickly and decisively by central banks;
- the Safety Network institutions should cooperate with each other;
- there must be a clear division of competences and tasks between individual Safety Network Institutions, and the role of the Central Bank must be clearly defined.

It is impossible to fully immunize the financial system against market risk, but the revision of several key aspects of the sector’s operation will certainly have a positive impact on its stability in the event of potential destabilisation:

- maximizing the security of banking sectors [Iwanicz-Drozdowska, Jaworski, Zawadzka, 2010, pp. 190–191]:
  - establishing an optimal guarantee system for bank deposits\(^3\) [Demiruguc-Kunt, Detragiache, 2000, pp. 25–27];
  - maintaining a safe level of prudent liquidity of the banking system\(^4\) [Global Financial Stability Report, 2010, pp. 57–85];
  - minimizing moral hazard for bankers, especially working for large financial players that in case of problems are ‘too big to fail’, and can count on state support [Burton, Brown, p. 243; Tapiero, 2010, pp. 194–200];
  - efficient and continuous banking supervision and effective precautionary macro regulations;
  - maintaining a balance between innovation and stability [Wyman, 2017, p. 9];

- increasing the transparency of the banking system:
  - increasing the transparency of the government’s fiscal policy;
  - cooperation between financial sector institutions in terms of building stability;
  - international coordination of activities to improve transparency;

- abandoning the protectionist policy of states, which may have destabilizing effects in the long term [Szymański, 2009, p. 164];

- revision of quantitative easing policies run by major central banks.

The transformation across the financial services system brings a number of risks which could affect system stability. These new systemic risks are driven in part by the altered dynamics many market participants are experiencing, such as increased market fragmentation, regulatory changes causing an uneven playing field, and increasing pressure from declining margins [Wyman, 2017, p. 10]. The creation of regulatory and legal conditions that would guarantee the system’s development with efficient risk management is strategically important for establishing long-term stability of the sector within the conditions of dynamic globalisation.

\(^3\) Appropriately high level of guarantees reduces the risk of mass liquidation of deposits and bank runs, at the same time triggers risk asymmetry and moral hazard.

\(^4\) Liquidity problems of banks during the crisis led to the disappearance of the interbank market and the necessity to launch public resolution programmes.
Summary

Maintaining financial stability in a small open economy is crucial for building conditions allowing economic growth. Furthermore, the loss of stability may affect the security of a nation. Thus, the issues of security as well as financial stability are closely related to the stability of the state’s financial system.

Sustaining financial stability is challenging particularly during the time of economic crisis under the conditions of globalizing economies, especially for a small open economy. It is important to build the internal resilience of the financial system to external destabilising processes. It is the role of the institution of Safety Network to shape a stable financial system and manage its stability. The most important, general factors for the functioning of the Safety Network as for maintaining stability would be:

- institutional structure of the Safety Network that would allow for an optimal arrangement of responsibilities and functions of its institutions;
- adequate regulation that would promote growth, and on the other hand, preserve against crises;
- effective maintenance of stability:
  - monitoring *ex ante*, including macroprudential analysis – avoidance of destabilisation;
  - adequate and effective response *ex post* – reaction once destabilisation occurs.

The functioning of the Safety Network can be divided into 3 main spheres: the maintenance of stability and prevention of crises, management of a crisis (once it occurs) and information and education activities. Each of the institutions performs a set of functions from the mentioned categories. In regard to the structure of the Safety Network in terms of its organigram, it is usually subject to political decisions. What is most important is to build such a structure of institutions that would fulfil all the mentioned functions, irrespectively of the view on the actual set or the number of institutions.

It is said that globalization is a result of the triumph of capitalism over other regimes world-wide [Milward, 2004, p. 16]. However, it has often been noticed that its progress leads to the replacement of the old state power which was exercised by national elites with the new dictatorships of international finance and corporations [Stiglitz, 2013, p. 219]. In such reality, the role of the state and its institutions becomes even more challenging in managing financial stability and maintaining economic security of a nation in the condition of openness of economies.
References


