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TRANSFORMATION OF ECONOMIC SYSTEM IN POLAND

Abstract

The paper studies peculiarities of market transformation in Poland. The stages of transition period are highlighted. The regularities are accentuated; likewise methods and technique for implementation of Polish practice, as well as positive and negative consequences of the chosen strategy are analyzed.

Key words:

Balcerovicz, «shocking therapy», liberalization, stabilization, privatization.

JEL: O16, O52.

The early 90-s were marked with profound changes in world environment. In many socialist countries the approaching crisis manifested itself in crashing of the world socialist economic system, thus originating the process of drastic reforms. Since the countries of Eastern Europe were afraid of the Soviet regime to be back they chose a new system of foreign political priorities, and saw their

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main objective in integration into the European Economic Community. Then the East European countries actively started to transit to a market economy. As it turned out later, rapid start of the reforms showed that political capital was used in a right way, while the delay testified to the fact that the opportunities were lost. The reform programs consisted of stabilization acts, institutional changes, and structural policy, in particular, privatization. Monetary and fiscal restrictions had to deter inflation, renovate financial equilibrium, and ensure preconditions for sustainable macroeconomic situation. And extending of external ties had to facilitate the optimal price level and fair competition on a domestic market. In addition, it was envisaged to transfer the resources from unprofitable enterprises into more profitable areas of activity performed by a privately owned enterprise. At that, the welfare rate had to increase, while expenditures – to remain limited. All those actions met the general priority of favorable climate creation for foreign investments. The direct foreign investments were expected to rapidly inflow into the countries of transition economies with low cost labor and thin markets. Expecting that investments would increase employment, export, revenues, and knowledge transfuse most of the governments introduced the programs for investment encouragement. Relatively low wages, corporate tax rates, access to the EU subsidies, and favorable investment climate could make those countries attractive to the ROW.

And though all the countries were in similar conditions, Poland intensely succeeded as against the others. Thanks to profound social and economic transformations this country can be proud now of its economy with private sector as its major part, and rapidly developing institutional infrastructure. So, what was the Polish practice peculiar with? The government set its major task to ensure inflation stability via price liberalization and limiting of nominal wages increase. To speed up the transition the method was applied which later became known as «shocking therapy». At that time the situation in Poland was disastrous, namely: the production fall, inflation increased, the commodity demands were enormous, monetary reserves were critically minor. At the same time people seemed to be ready to accept the drastic changes and understand their introduction. Therefore, the only certainty for succeeding had to become rapid and extensive movement to the market. As the author of the reforms Leszek Balcerowicz says: «I insisted on critical introduction of a packet of stabilization and liberalization of economy, start of more long-term and deep reforms of state institutions and economies. That radical strategy provided a chance for success, though it was risky. But the strategy of gradual changes was, in my opinion, doomed to failure» [1]. That plan justified itself. Firstly, as the Soviet economic and political regime was unable to be reformed in parts and step by step. Secondly, in Poland, like in other countries of the former Soviet block, a high inflation rate was observed, and it needed to be fought quickly and vigorously. Thirdly, the breakthrough that brought freedom to people was succeeded by a short period when drastic reforms were carried out easier than usual. Consequently, economic, political, and psychological arguments spoke for the benefit of sweeping reforms.

There are four following aspects of transition to a market: stabilization, liberalization (mostly of price and trade), change of institutional structures, and privatization. The «shocking therapy» included all of them. In fact, the shocking therapy can be taken for immediate stabilization (in case of necessity), rapid steps towards price and trade liberalization (avoiding complete bankruptcy of enterprises), and continuous movement towards reformation of institutions. Leszek Balcerowicz describes that scheme as «two stage transition» – first to «marketization», and on the second stage – to the economy with domination of private property [1]. Liberalization included liquidation of legislative barriers in economy, abolishment of state regulation of prices and resource distribution, use of hard currency and scopes of its convertibility**.** Stabilization was oriented at monetary restrictions, regulation of exchange rate and wages. At that, stability could be described as the state of economic system which could be kept for a long time through the respective regulation means. That definition allows understanding economic sustainability not as its state, but as a strategic process consisting in approaching to economic strength. Institutional policy embraced privatization, change of laws, taxing and banking systems. At that, initial conditions (liberalization, financial stabilization, and privatization) for market development were created by the government within the shortest term, and further the government had no right to directly intervene into economic activity. Subsequently the economic life is proceeding on the basis of self-regulation, and the state intervention is regulated by respective laws.

Reformation in Poland was carried out step by step. The first stage spread from 1990 to 1991. At that time the government sold shares of five big and four small companies. In particular, Poland succeeded in small privatization. New private businesses were set mostly in the format of Partnerships and Companies, Limited, which mainly belonged to Polish citizens. Typically they were small, but efficient enterprises, like factories, workshops, trade companies, and service firms. By the end of the 1990-s the proprietors owned about 40% of retail sail businesses, about 60% of public catering facilities, and 50% of commercial banks [3].

During the second stage (1991–1992) 13 enterprises were privatized through corporatization. Some enterprises had to be liquidated. Work collectives widely rented the enterprises, as well as they sold the latter to national and foreign firms. Among industrial enterprises small ones with up to 5 people employed were prevailing. Small businesses were connected with wood and metal working, food and garment industries. Almost half of employed labor force was busy in a private sector. In 1991 the zone of the greatest expansion became trade. Thus, in retail sails the ratio of private shops made 75% [10].

Having coped with two stages of transition period Poland approached to the third one, which was specified with encouraging of investment activity. In 1991 for improvement of investment climate Poland adopted the Law on Foreign Investments. The Law adjusted the types of enterprises to be invested; also the conditions for repatriation of profits and wages of foreign specialists, tax benefits for foreign investors, and it secured the legal protection of foreign investments in

Poland. The Law removed the restrictions, prior established to profit expatriation, and abolished restrictions to volumes of investments, as well as most of prior demands for accommodating on different levels. In 1998 the Foreign Currency Act was adopted to regulate the currency transactions of foreign investors. In 1999 the Law on economic activity was passed, which specified the type of economic activity requiring the foreign investor to have the permission of the government [14]. Those normative acts fairly facilitated attraction of foreign investments, and practically led the Polish legislation to the standards of the European Union. In addition, Poland adjusted certain areas of activities where exclusively Polish enterprises could be involved. It was fixed that the ratio of foreign property should not exceed 49% in airfreight, and 33% in national radiobroadcast [14]. It is interesting to note, that foreign affiliation can have the benefits similar to these of local company if more than 50% of added value of the product was created in Poland [14]. It sometimes makes the TNCs to increase the volume of production on the territory of Poland.

The development of normative basis intensified the investment activity. At that, private enterprises attracted more investments against public ones. Inflows of foreign investments into production area and application of western technologies greatly facilitated structural reformation of Polish industry. Though western firms, like IKEA and Rossman entered the market in 1990, big conglomerates started investing big capital into Polish economy only in 1994. In 1995 out of $5.3 bln. of total investments 3.2bln. was channeled into industry, including 1bln. – into mechanical engineering [13]. It made the basis for the development of cooperation with western countries. A number of Polish enterprises switched to assembly of products from the equipments and assemblies provided by western firms. In 1997 economic growth of Poland made 6.7%, its industrial growth – 11.2%, and production of goods for investment purpose exceeded 15%. The total volume of foreign direct investments reached $20.6bln. by 1997 against $17 bln. in Hungary, and $8.2 bln. in Czech Republic [9]. Americans were leaders among others, since by the end of 1997 they invested about $4 bln. The greatest capital volume ($505 mln.) was invested by Polish-American Fund, succeeded by Pepsi-Cola, International Paper, and Philip Morris. The most attractive for investment turned out to be a motor industry. Poland produces the cars of the leading European brands, like Ford, Toyota, and General Motors.

Nevertheless, attraction of foreign investments has also a negative side. Today many Polish enterprises completely or partially depend upon material and assemble a supply from abroad, which essentially increases the ratio of imports in the foreign trade pattern. In addition, lately the structure of industrial production also changed. Privatized Polish enterprises almost do not produce sophisticated science intensive products, though socialist Poland was known for those. Furthermore, we can not ignore the fact, that Poland has an old-fashioned heavy industry. Coal mines, metallurgical complexes, backward transport and energetic infrastructure – all those turned out to be outside the market economy. The most old-fashioned Polish enterprises remained state-owned. Incidentally, Poland tries to solve that problem through holdings or concerns made on the basis of merged enterprises of similar industries. But the pattern of the manufactured goods is the same, only the management problem is getting more complicated.

Financial solvency can also be regarded as positive result for Polish economy.

In the second half of the 1990-s the production rapidly grew. The use of western technologies and inflows of foreign investments into the production area facilitated structural reformation of Polish industry. It became the basis for cooperation with western countries. A number of Polish enterprises switched to assembly of products from the equipments and assemblies provided by western firms. In 1997 economic growth of Poland made 6.7%, its industrial growth – 11.2%, and production of goods for investment purpose exceeded 15%. Foreign direct investments grew by 10% [8]. The consequence of high rates of economic growth was public debt. Internal indebtedness exceeded 60% of GDP.

Consequently, though Poland had chosen the right direction mistakes were inevitable. The initial prognosis concerning production was too optimistic, devaluation was rather intensive, and monetary policy – extremely rigid. The perspectives to return to former property status caused uncertainty, and discouraged investors. The privatization schemes were too complicated, the possibilities of certain state-owned enterprises were underestimated, trade relations with former communist countries were ceased too abruptly, and the reduction of external debt was paid little regards to. Nevertheless, the spirit of the first reformation Polish government was rewarded. And no matter what problems and drawbacks of transition period were faced Poland can rightly be proud of its achievements. We can say that the policy of profound changes met its major task, i.e. it created preconditions for extensive development of market relations. The principal aims of that policy were to assure the relatively balanced and sustained economy. We can positively assert that the noted aim was reached. Poland having become one of the first countries to choose the way of system reformations was among the first to yield the outcomes of a market transformation. At the moment this country can offer to foreign investors a fairly safe and liberal investment climate. To sustain that strong position Poland not only has to make efforts for preserving the image of attractive economy for foreigners, but also for improving normative base, making it more transparent, to make the bureaucratic procedures shorter, and to keep on improving transport infrastructure.

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