

# Transformation in Poland

Libor Žídek

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The first part

# **DEVELOPMENT DURING THE COMMUNIST REGIME**

# Insight to long-run political development

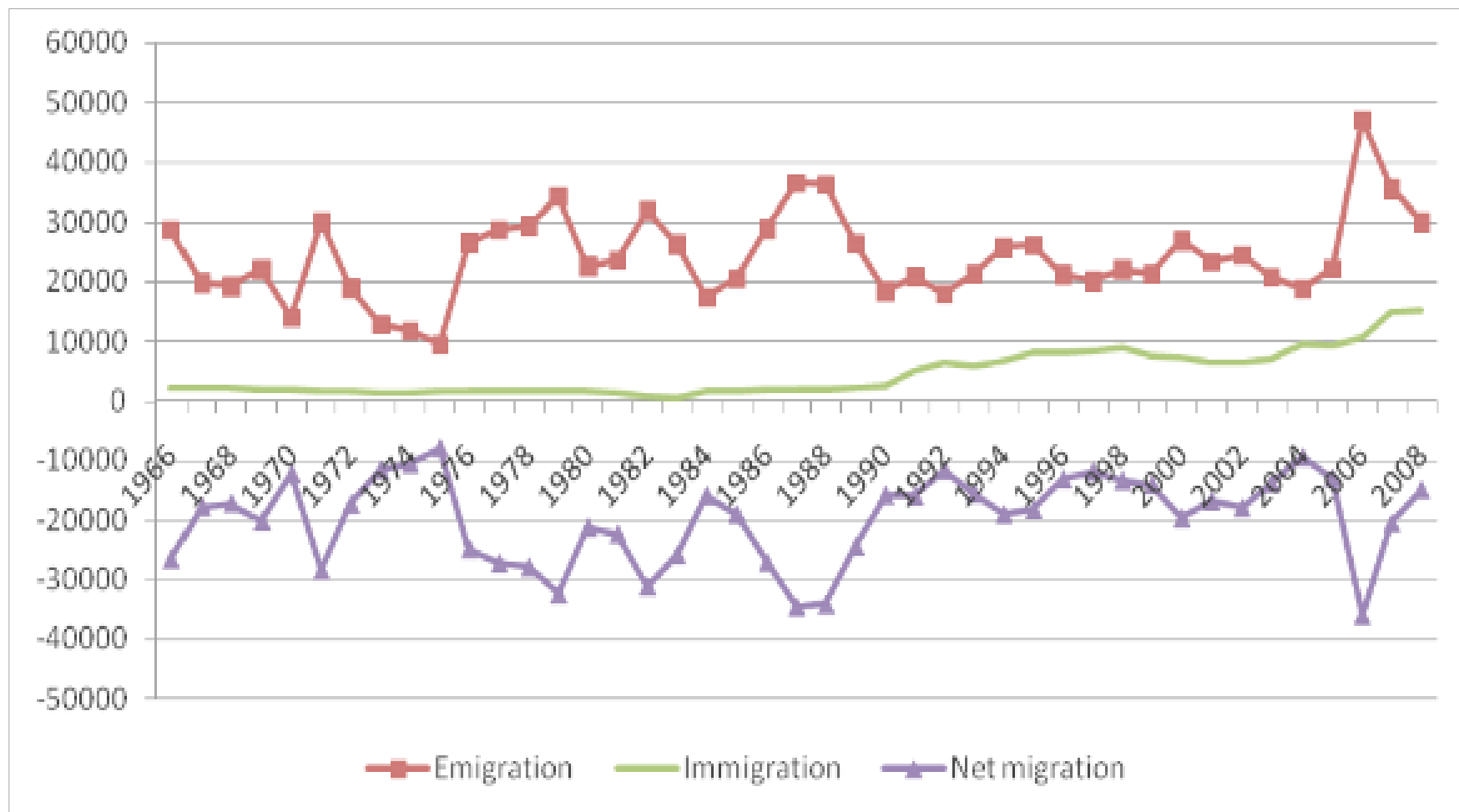
- **Poland – Russia relations before WWII**
- **Member of the communist block after WWII**
  - **prickly relations** with Russia -> effect on attitude towards socialism
  - problems with the regime + bad economic situation -> **protests** (1956, 1970)
  - attempts for reforms -> **Gomulka** (1956), **Gierek** (1970)
  - **Jan Pavel II** (1978)-> symbol of Polish opposition against the communist regime
  - lack of freedoms + economic situation -> **emmigration**

# Now you see it, now you don't, now you do

Poland's changing borders



# Chart 1: Emigration, Immigration and net migration in Poland in 1966-2008



Source: Central Statistical Pffice (GUS), [http://www.stat.gov.pl/gus/5840\\_8408\\_ENG\\_HTML.htm](http://www.stat.gov.pl/gus/5840_8408_ENG_HTML.htm), (29.12. 2010)

# Economic situation I.

- **Centrally planned system**
- Backward economy with large portion of **agriculture**
- **Measures** in 1960's and 1970's
  - Membership in **GATT** since 1967
  - Legal framework for **FDI**
- **Economic problems**
  - FDI -> overheating, inflationary pressures
  - Borrowings from abroad -> **↑** foreign debt
  - Impacts of global debt crisis (1980) -> **↓** GDP, **↑** government deficit, deficit of BoP, shortage of basic products, monetary excess

**Riots, destabilization ...**

**... martial law and reforms as solutions?**

# Table 1: Chronology of reform measures before 1990

Reform measure	Hungary	Poland	Czechoslovakia
Cancellation of obligatory plans	1968	1982	1990
Cancellation of centralized quotas	1968	1991	1990
First steps leading to liberalization of prices	1968	1957,1975	1991
Unified exchange rate <sup>1</sup>	1981	1990	1991
Admission to IMF and WB	1982	1986	1990
Free private enterprises	1982	No restrictions	1991
Bankruptcy law	1986	1983	1991, 1992
Two-stage banking system	1987	1988	1990
New income tax system	1988	1992	1993
VAT system	1988	1993	1991(sic)
Corporate Law	1989	1990	1991
Trade liberalization	1989	1990	1991
Unemployment benefit system	1989	1990	1991

Source: Kornai (1996)



# Economic situation II.

## ➔ **No improvement ...**

- Another **crisis** (1987) - > shortage of consumer goods
- Partial price liberalization -> **hyperinflation**
- **Chaotic economic policy** and **economic distortions**

## ➔ **Problems with ...**

- Polish **self-managed socialism**
- Overall **ownership structure**
- **Structure of the economy**
- Development of main **indicators**

# Self-management socialism

- **Companies controlled by workers**
  - better functioning, motivated employees, improved overall efficiency
  - self-governing (powerful) **councils** established in almost all companies
- In reality **negative impact** on companies
  - increasing wages -> **inflation**
  - no rationalisation of production processes
  - no improvement in motivation of employees

# Structure of the economy

- **Public sector**
  - large portion of GDP
  - f.e. state companies and cooperatives created 81.9% of GDP in 1988
- **Private sector**
  - smaller portion of GDP, mainly in agriculture
  - growing share since the end of 1970s
  - BUT larger than in Czechoslovakia
- **Large share of agriculture**
  - – sign of underdevelopment
- **Armament production**
  - obstacle to transformation
  - relatively high portion of industrial production
  - one of the biggest producer
  - for Warsaw Pact countries and Soviet Union

**Table 2: Exchange rates to American dollar (averages in units of national currency)**

	Czechoslovakia		Hungary		Poland	
	Official	Unofficial	Official	Unofficial	Official	Unofficial
1988	14.36	33.44	50	.	431	1979
1989	15.05	43.39	59	.	1446	5665
1990	17.39	(39.0-40.0)	63	.	9500	9570
1991	29.48	32.28	74	.	10559	10731

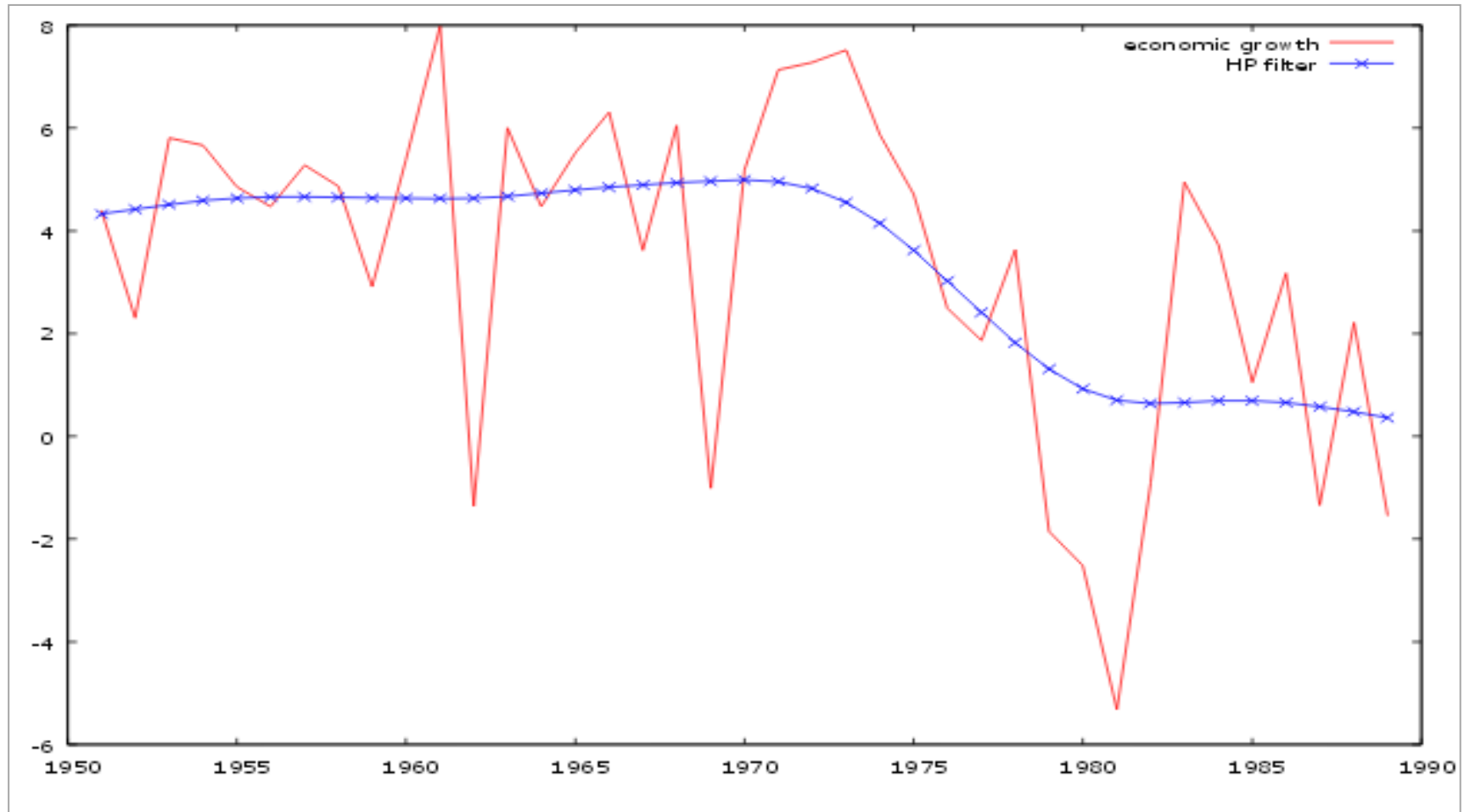
Source: Winiiecki, *Regional survey, (1993)*.

**Table 3: The share of nationalized and private sector in industrial production in Poland**

Year	Share of the nationalized sector	Share of private companies
1977	98.22	1.78
1980	97.54	2.46
1985	95.49	4.51
1989	93.4	6.6
1990	91.2	8.8

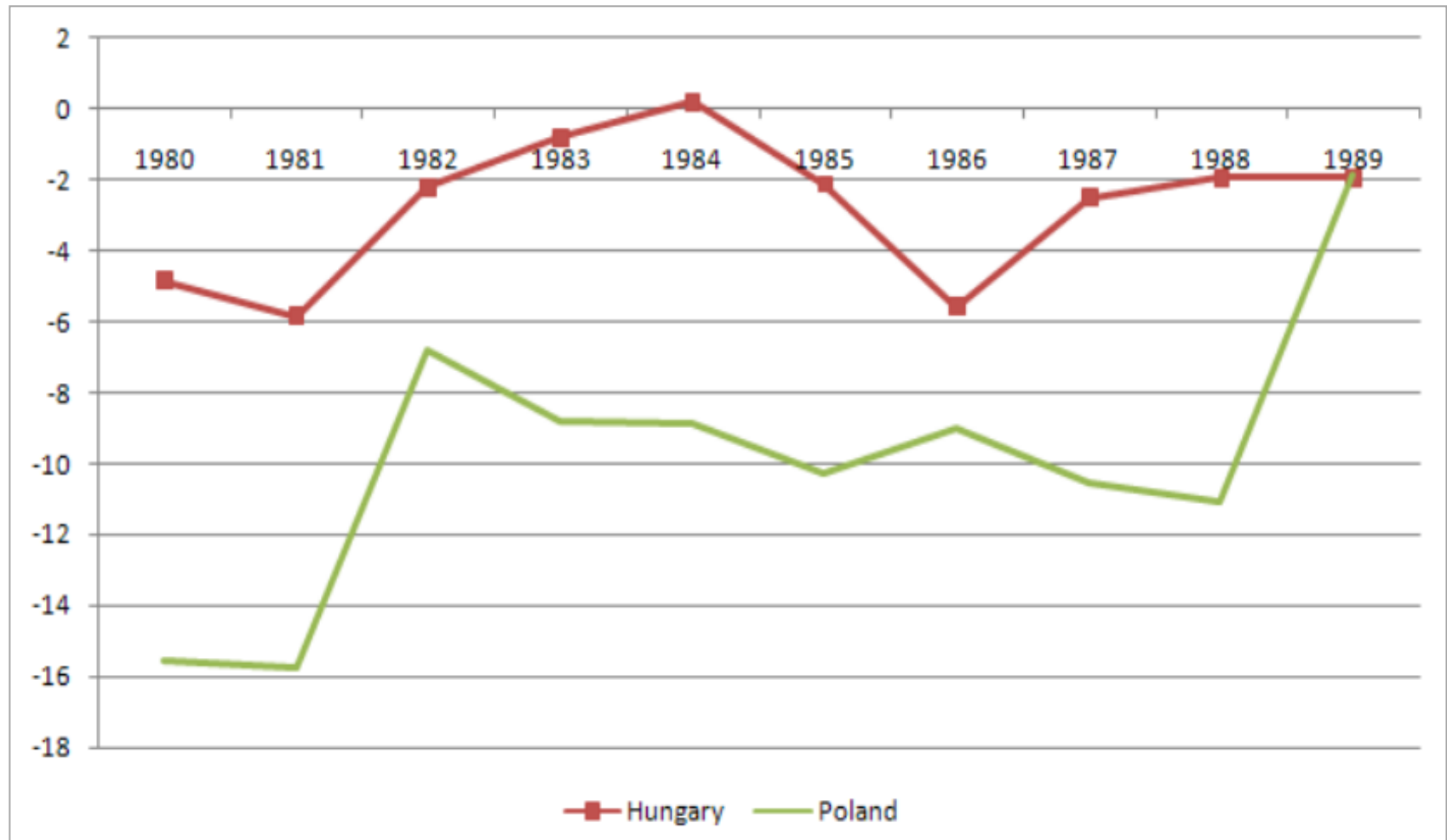
Source: Wang, Zhen (1991)

# Chart 2: Economic growth and long run trend (by HP filter) in Poland 1950–1989 (in %)



Source: Maddison, *Historical Statistics*, Retrieved October 11, 2010 from <http://www.ggdcc.net/MADDISON/oriindex.htm>

### Chart 3: Current account balance % of GDP



Source: International Monetary Fund, World Economic Outlook Database, October 2010, <http://www.imf.org/external/pubs/ft/weo/2010/02/weodata/index.aspx> (1.12.2010)

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The second part

# **POLITICAL DEVELOPMENT**



# Political development I.

- **Pseudo-democratic system**
  - Consequence of negotiations with **Solidarity**
  - First non-communist government in 1989 -> Solidarity (high support)
  - Walesa – president (1989)
- **First free elections in 1991** -> 29 parties in the Parliament
  - fragile political situation
  - weak and changing coalition governments
  - **associate agreement** with EC in 1991
  - new **constitution** -> stronger position of president
  - **protests** -> early elections

# Political development II.

- Elections in **1993** → post-communist party (**DLA**) as winner
  - slowdown of the transformation process
  - emphasis on social aspects
  - leader of the party → next president
- Elections in **1997** → right wing parties (**SEA**)
  - 40 political groups without uniform position
  - membership in NATO (1999)
  - unpopular steps → collapse in 2000
- Elections in **2001** → left wing parties (**DLA**)
  - coalition with the Polish People's Party
  - collapse in 2003
- **Membership in EU** (2004)

 **Unstable political situation** regardless of +/- economic situation

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The third part

**TRANSFORMATION PERIOD**

# Economic reforms after 1990 I.

- **„Big Bang“ reform** (shock therapy)
  - Consequence of catastrophic economic situation
- **Public opinion**
  - In favour of reforms
  - No sense about the function of market economies
- **Balcerowicz plan (1990)**
  - Liberalization of markets and prices
  - Inner convertibility of the zloty
  - Restrictive monetary policy
  - Devaluation + fixing of the zloty to the dollar
  - Wage regulation
  - Fiscal restrictions (limiting subventions)
- **Jeffrey Sachs**
  - key economic adviser of the Polish government

# Economic reforms after 1990 II.

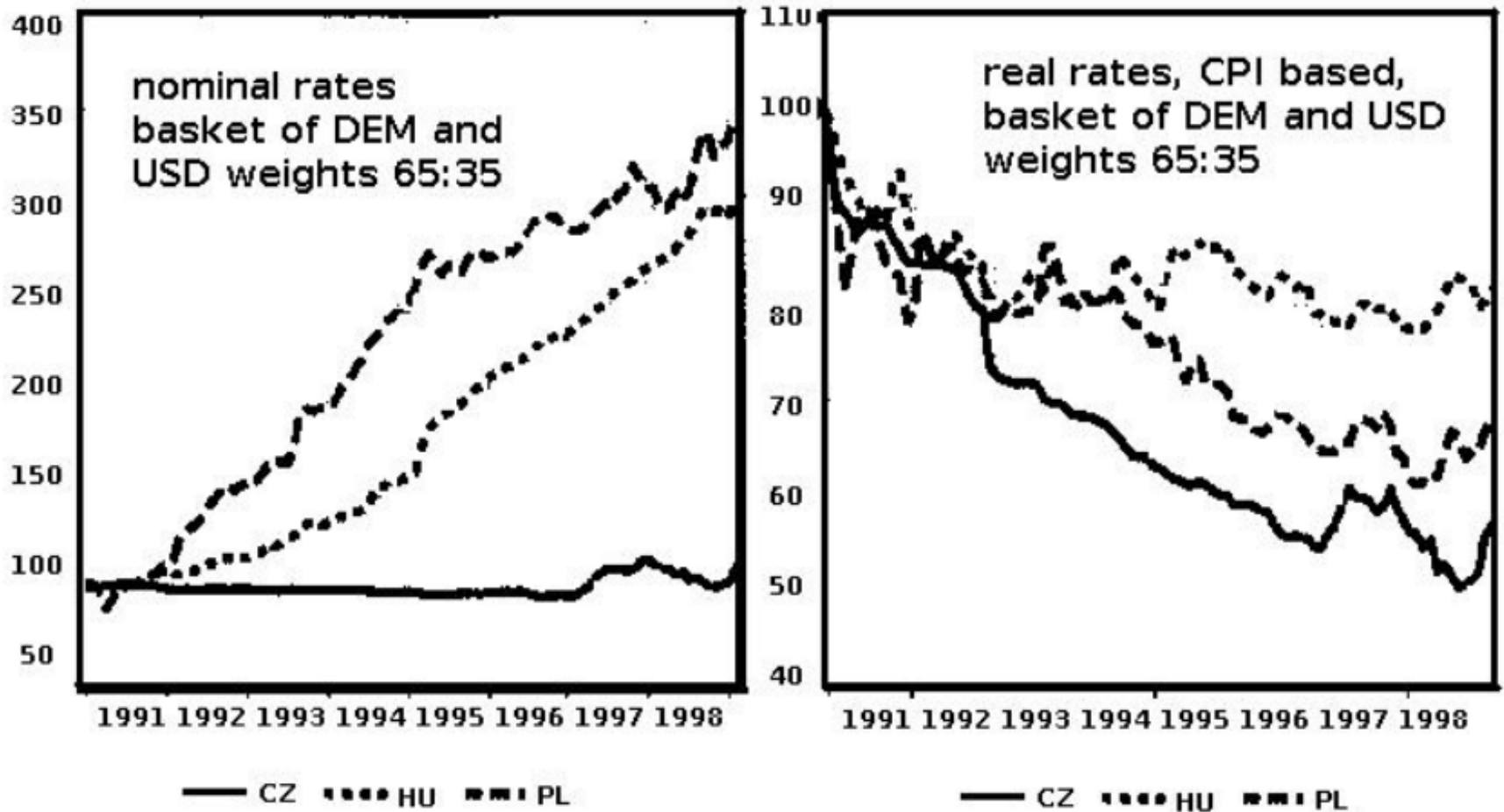
- **Transformation recession**
- **Development in foreign sector**
  - Decline in trade with COMECON
  - Support from the West
    - PHARE
    - Remitting polish debts
    - IMF (stabilization program and loans)
- **Devaluations of the zloty + fixed to a basket of 5 currencies + crawling pegg**
- Poor economic conditions still in 1993 -> **Strategy for Poland**

**Table 4: Development of the main economic indicators in Poland 1990-1993**

	1990	1991	1992	1993
Real GDP	-11.6	-7	2.6	3.8
Inflation (CPI)	585.8	59.4	45.3	36.9
Unemployment	6.5	11.8	13.6	16.4
Public budgets (% of GDP)	0.7	-6.4	-6	-2.8

Source: Holman (2000)

# Chart 4: Nominal and real exchange rate in Central Europe



Source: Frait, Kotlán (2000)

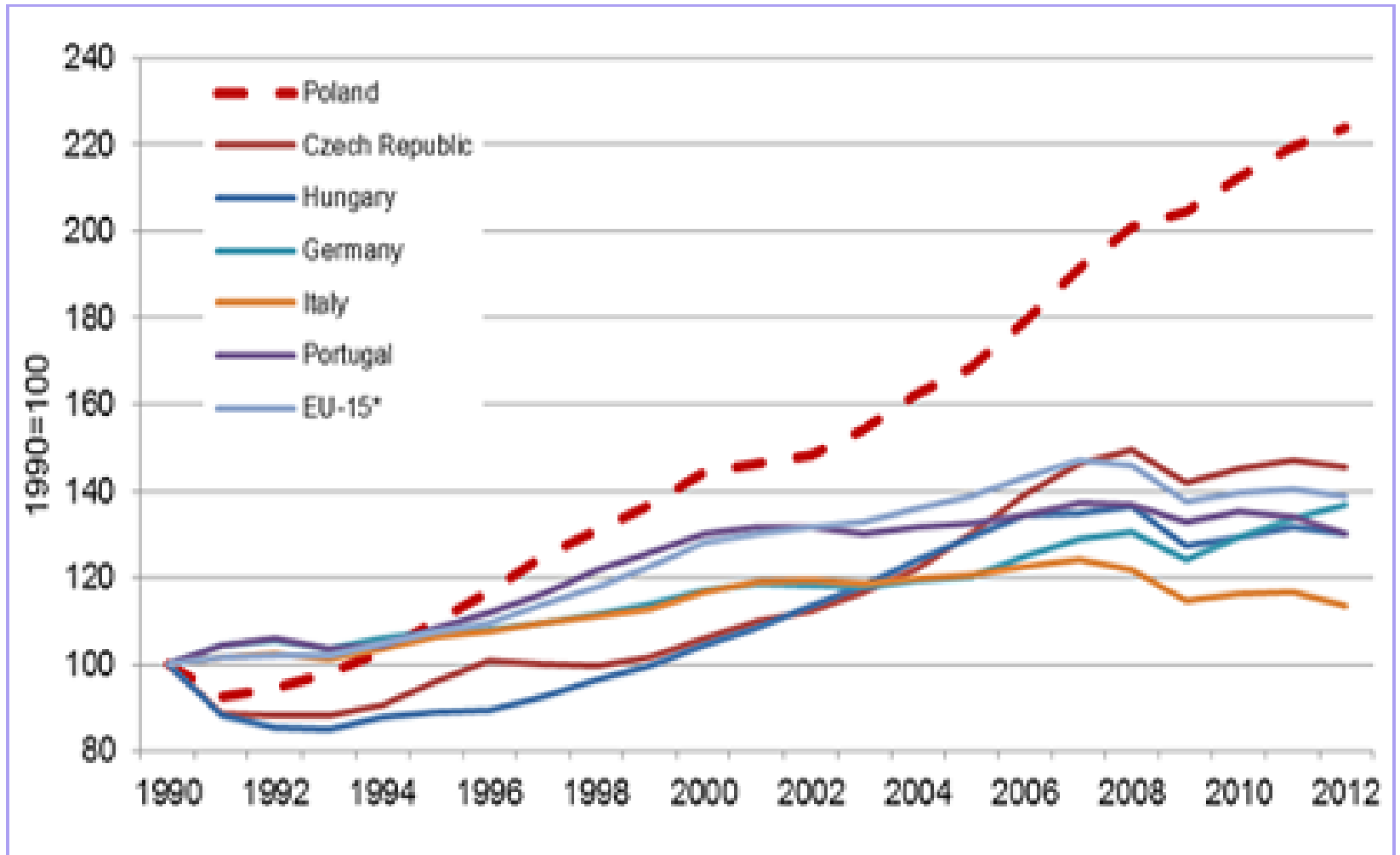
# Table 5: Development of Gini coefficient 1994-2004

	Czech Republic	Hungary	Poland
1989	19.3	21.3	25.0
1990	19.7		26.8
1991		20.3	23.2
1992	20.3		24.0
1993	21.5	22.6	31.5
1994	22.0	23.0	32.6
1995	21.5	24.3	32.2
1996	22.9	24.4	32.9
1997	22.6	24.5	34.0
1998	22.6	24.3	32.6
1999	23.8	23.7	33.1
2000	23.8	25.0	34.2
2001	22.8	25.7	34.0
2002	23.2	24.6	34.9
2003	22.8	25.2	35.2
2004	23.5	27.4	36.6

Source: United nations university - UNU Wider - world institute for Development Economics Research, [http://www.wider.unu.edu/research/Database/en\\_GB/wiid](http://www.wider.unu.edu/research/Database/en_GB/wiid), 22. 12. 2010



# GDP per person 1990=100



Source:

# Economic reforms after 1990 III.

- Relatively **high economic growth** -> budget deficit under control
- Monetary policy -> **targeting money in circulation**
- Agreements with **London and Paris creditors clubs** (1994)
- **Re-denomination** of the zloty (1995) -> 10 000 PLZ for 1 PLN
- **Liberalization of transactions on the financial account**
  - Massive inflow of foreign capital
  - Appreciation and increase of foreign reserves to keep the exchange rate
  - Periodic devaluation, wider fluctuation zone, basket of 2 currencies
- Membership in **OECD** (1996)
- Government vs. Public debt
- Direct **inflation targeting** (1999)
- **Free floating** since 2000

Table 9: General government balance as % of GDP (1990-2000)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	Average
Czech Rep.	-0.2	-1.9	-3.1	2.6	-1.2	-1.1	-3.3	-3.8	-5.0	-3.7	-3.7	-2.2
Hungary	0.0	-2.9	-6.1	-6.0	-7.5	-6.7	-5.0	-5.9	-8.0	-5.5	-3.0	-5.1
Poland	3.1	-2.3	-5.3	-2.8	-2.8	-3.1	-3.3	-4.6	-4.3	-1.8	-3.0	-2.7

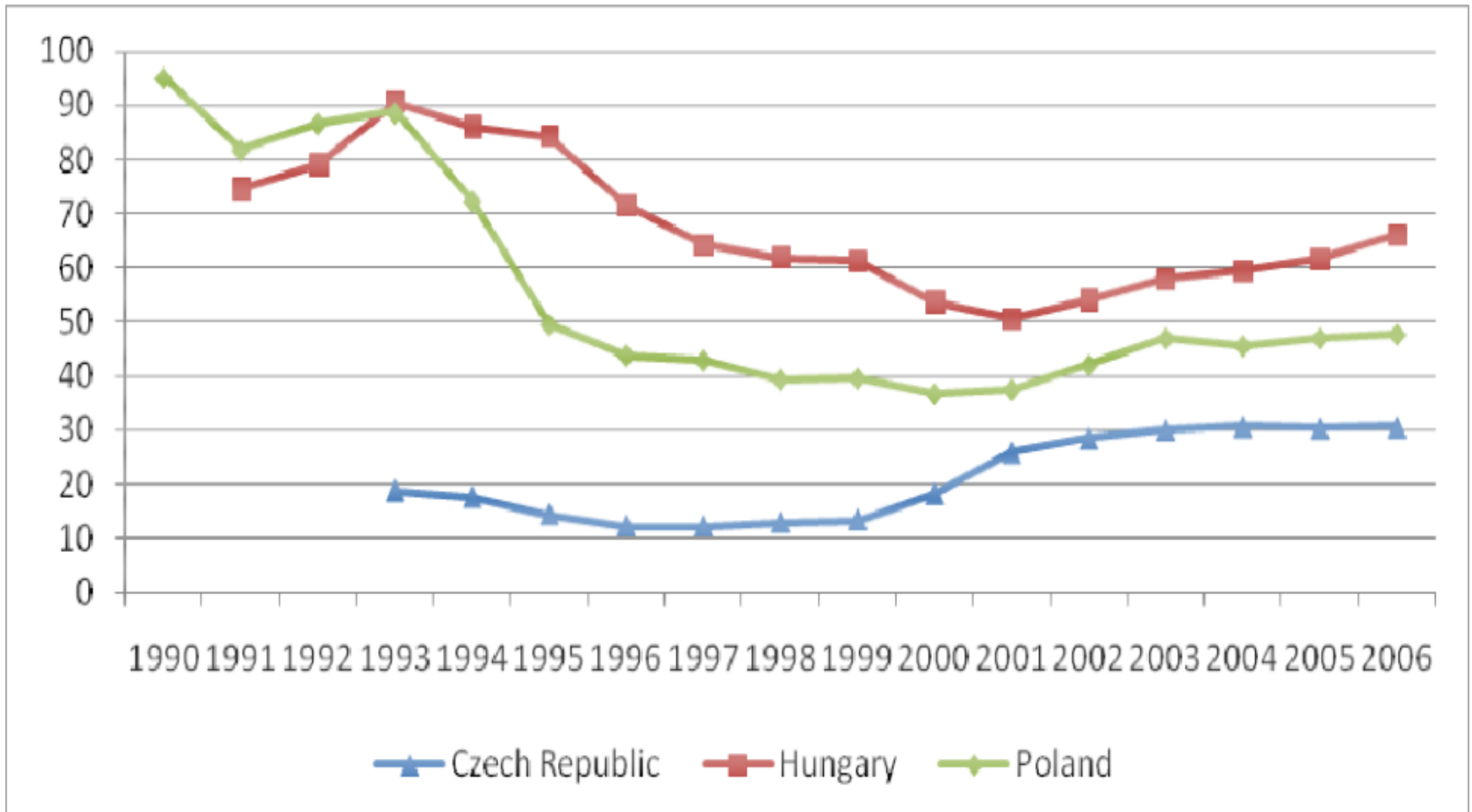
Source: EBRD: Selected economic indicators data, 26. 11. 2007.

Table 9: General government balance as % of GDP (1990-2000)

	1998	1999	2000	2001	2002	2003	2004	2005
Government balance	-3.2	-3.3	-3.3	-5.2	-6.1	-5.6	-5.9	-3.9
Structural balance	-4.4	-4.4	-4.1	-4.8	-4.7	-4.5	-5.2	-4.0

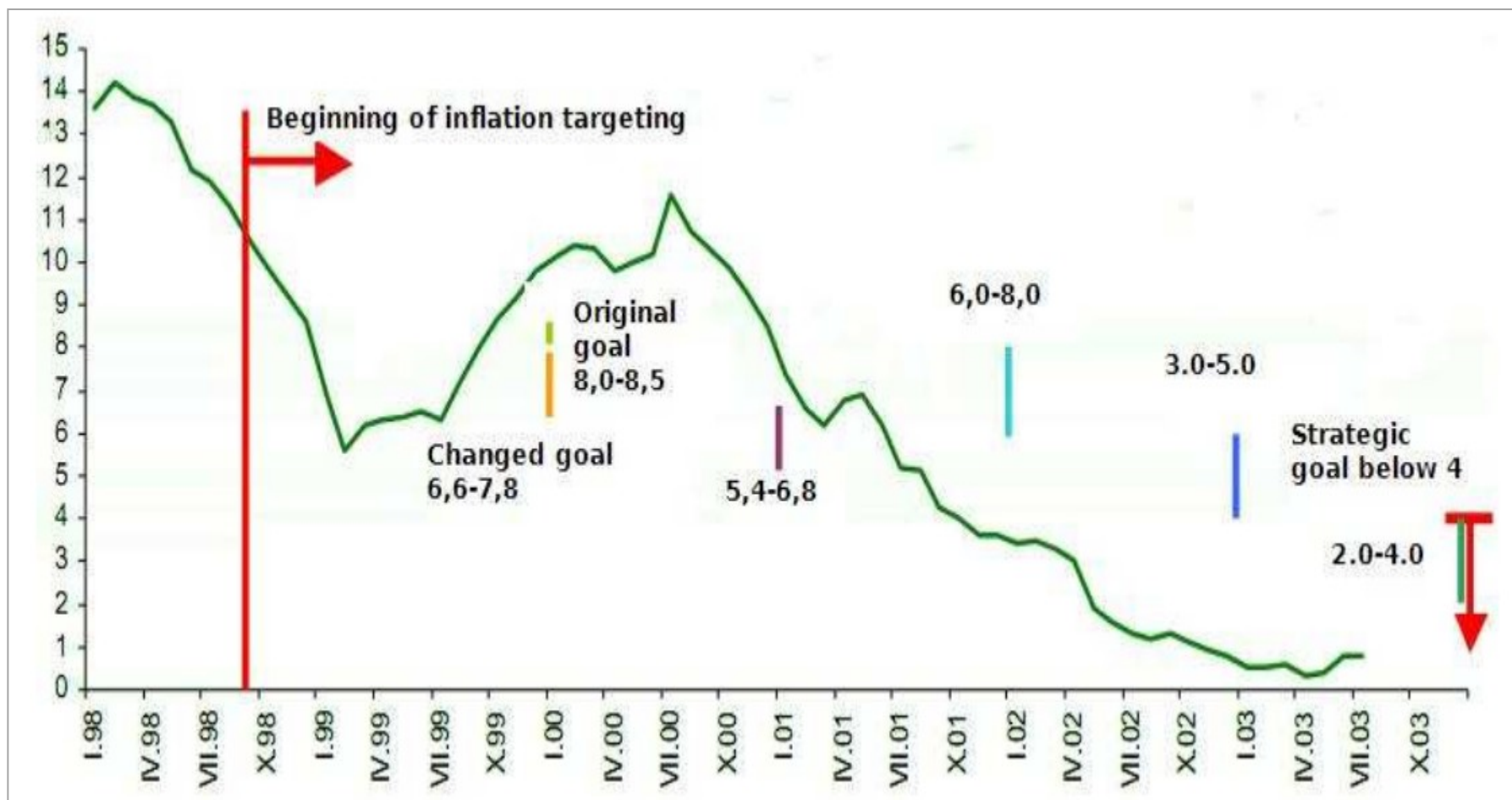
Source: IMF: Republic of Poland: 2003; IMF: Republic of Poland: 2006

# Chart 5: Public debt, % GDP



Source: EBRD: Selected economic indicators data, 26. 11. 2007.

# Chart 6: Inflation and inflation targeting in Poland 1998-2003



Source: NEWTON: Makroekonomický vývoj Polska, 2003

# Privatisation

- Lack of domestic savings but stronger **position of employees and trade unions**
- „**Spontaneous privatisation**“ at the beginning
- New forms of ownership change – **commercialisation and liquidation**
- **Voucher privatisation** – specific features
- Slow and postponed process

**Table 11: Employee Ownership Resulting from Privatisation in 1994**

Country/base group of co's. for estimation	Companies with employee control	Privatisations (percentage)	Average % held by all employees	Estimated total employment in EOs
Czech Republic (voucher priv., 1st wave)	3	1	4.4	N.A.
Hungary (self-privatisation)	187	43	42.0	36 000
Poland (priv. liquidation)	1 478	75	50.8	450 000

Source: Earle, Estrin (1996)

**Table 12: Private sector share in employment (in %)**

	1990	1991	1992	1993	1994	1995	1996	1997
Poland	47.9	50.0	54.0	57.0	59.0	61.4	61.6	62.0
Hungary	na	na	81.4	78.1	77.6	77.7	78.7	79.2
Czech Republic	7.0	18.7	31.1	47.1	53.0	57.2	58.9	59.7
	1998	1999	2000	2001	2002	2003	2004	
Poland	62.3	63.7	65.8	67.9	66.8	68.5	70.6	
Hungary	79.5	80.0	80.4	79.6	79.3	79.1	79.1	
Czech Republic	60.6	65.0	65.0	70.0	70.0	70.0	70.0	

Source: EBRD: Selected economic indicators data, 26. 11. 2007.

# Development in banking sector

- The first attempt for change in 1988 (creation of 9 state banks)
- **Impacts of transformation recession**
  - weak position of banks, ↑share of classified credits
- **Enterprise and Bank Restructuring Program (1993)**
  - recapitalization, positive effect on banking sector
  - relatively low cost on recovery
- **Privatisation of banks**
  - Slower than expected, but ↑share of foreign banks
- **Importance of state banks** vs. limited role of commercial banks and exchange stock



**Table 13: Financial sectors in European countries in 2002**

Country	Banking assets (% of GDP)	Domestic credit (% of GDP)	Stock market capitalization (% of GDP)
Czech Republic	126	61	16
Hungary	61	42	19
Poland	66	39	14
Euro area	265	135	72

Source: Gabrisch, Hölscher (2006)

**Table14: Number of IPOs in Central Europe**

	2000	2001	2002	2003	2004
Poland	11	6	2	2	31
Czech Republic	0	0	0	0	1
Hungary	0	0	0	1	1

Source: Kovanda (2005)

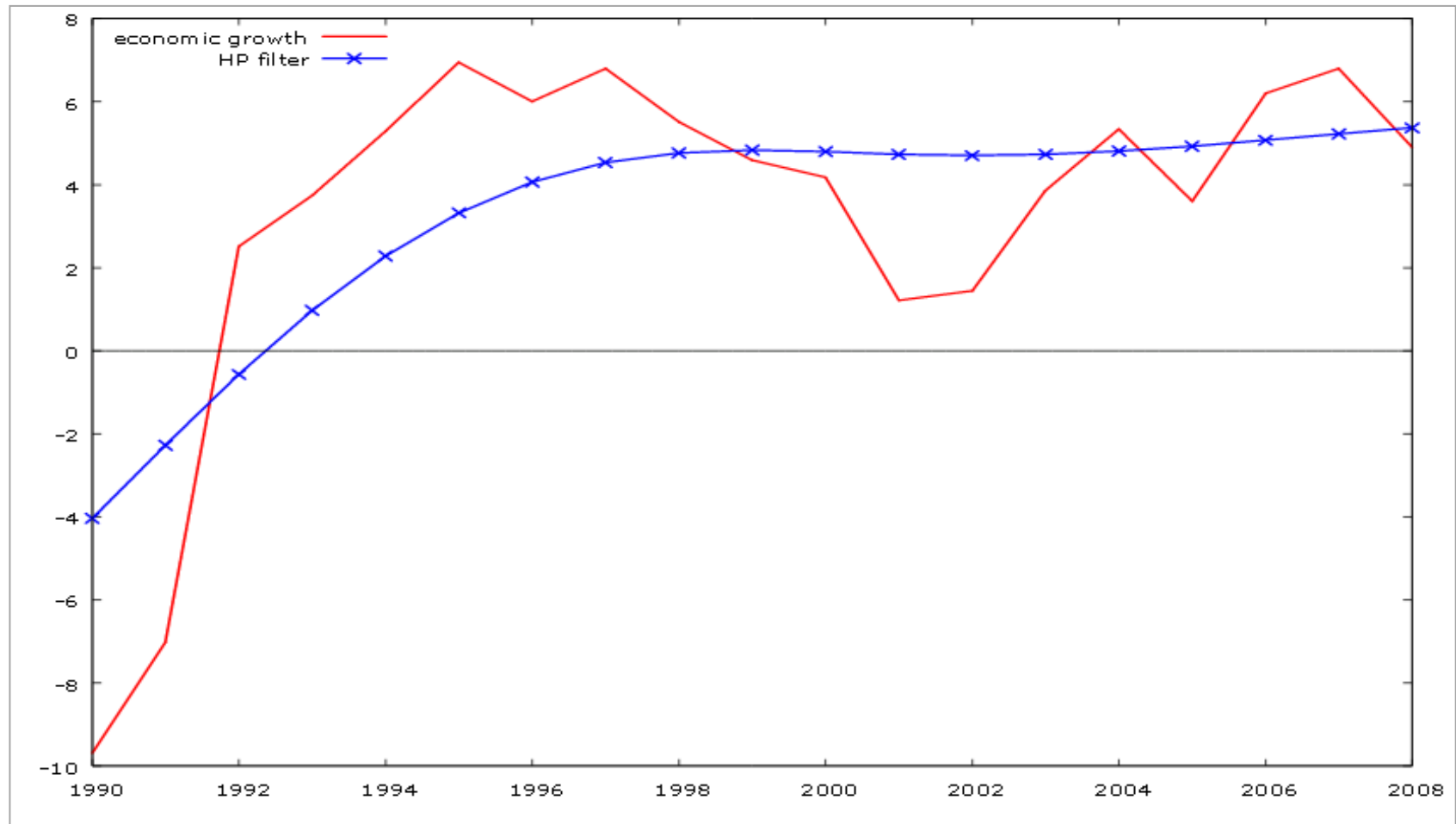
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The fourth part

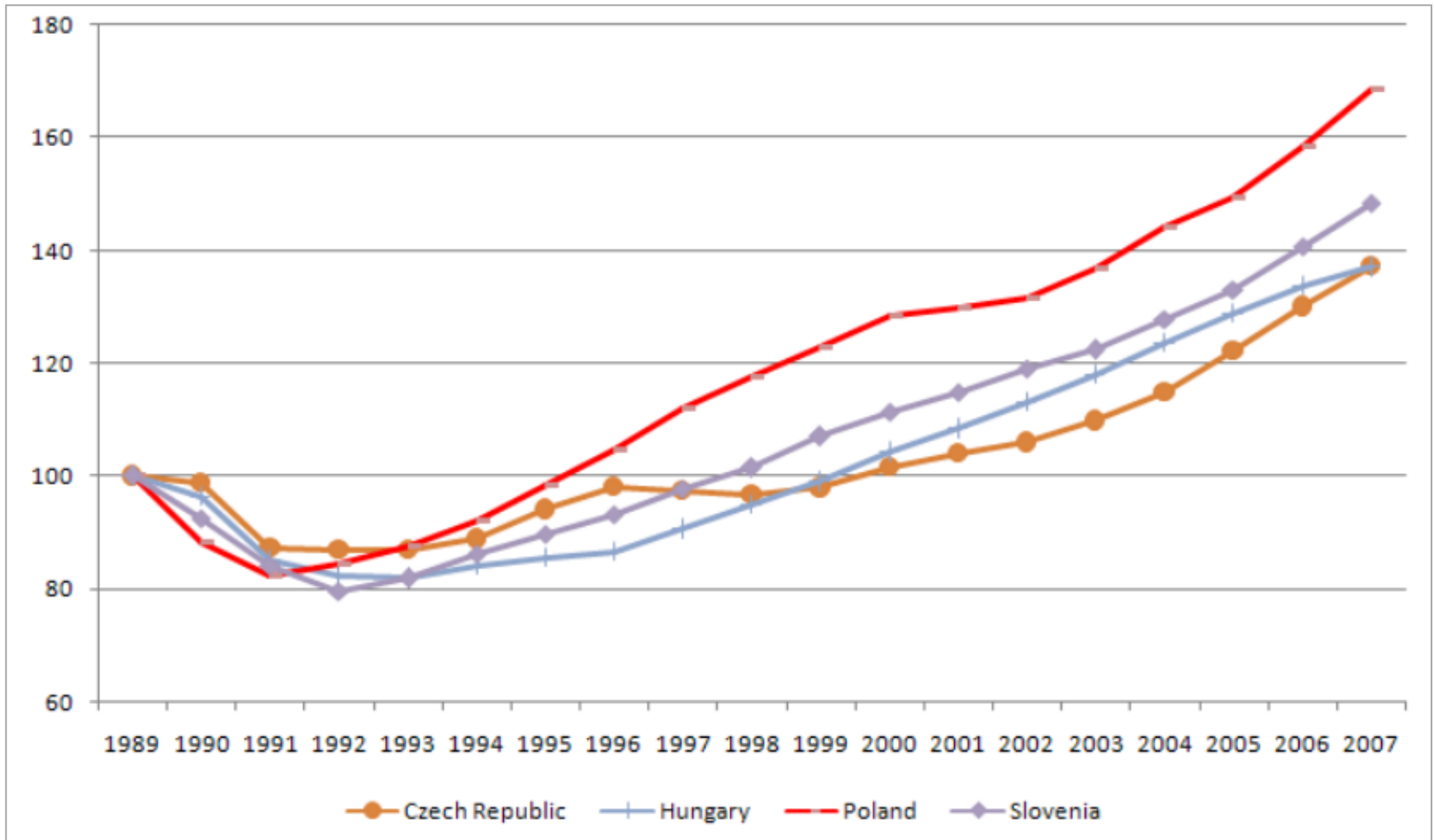
# **ECONOMIC RESULTS**

# Chart 8: Economic growth and long run trend (by HP filter) in Poland 1990-2008 (in %)



Source: EBRD: Maddison, Historical Statistics, Retrieved October 11, 2010 from <http://www.ggdc.net/MADDISON/oriindex.htm>.

# Chart 7: Cumulated GDP (1989=100)



EBRD: Selected economic indicators data, 26.11. 2007.

**Table 15: Real wages in Eastern Europe, the bottom and situation in 2005 in comparison to the pre-transformation year**

Country	Year, when real wages reached the bottom	Cumulated growth of real wages against the bottom till 2005 (in %)	Cumulated change of real wages in 2005 against the pre-transformation year (in %)
Czech Republic	1991	98	38
Hungary	1996	57	19
Poland	1993	43	2

Source: Klaus, Tomsik (2007)

**Table 16: Development of HDI in central Europe 1975-2010**

Country	1980	1990	2000	2005	2010	HDI Rank
Czech Republic	..	..	0.801	0.838	0.841	28
Hungary	0.689	0.692	0.767	0.798	0.805	36
Poland	..	0.683	0.753	0.775	0.795	41
World Average	0.561	0.602	0.638	0.658	0.678	

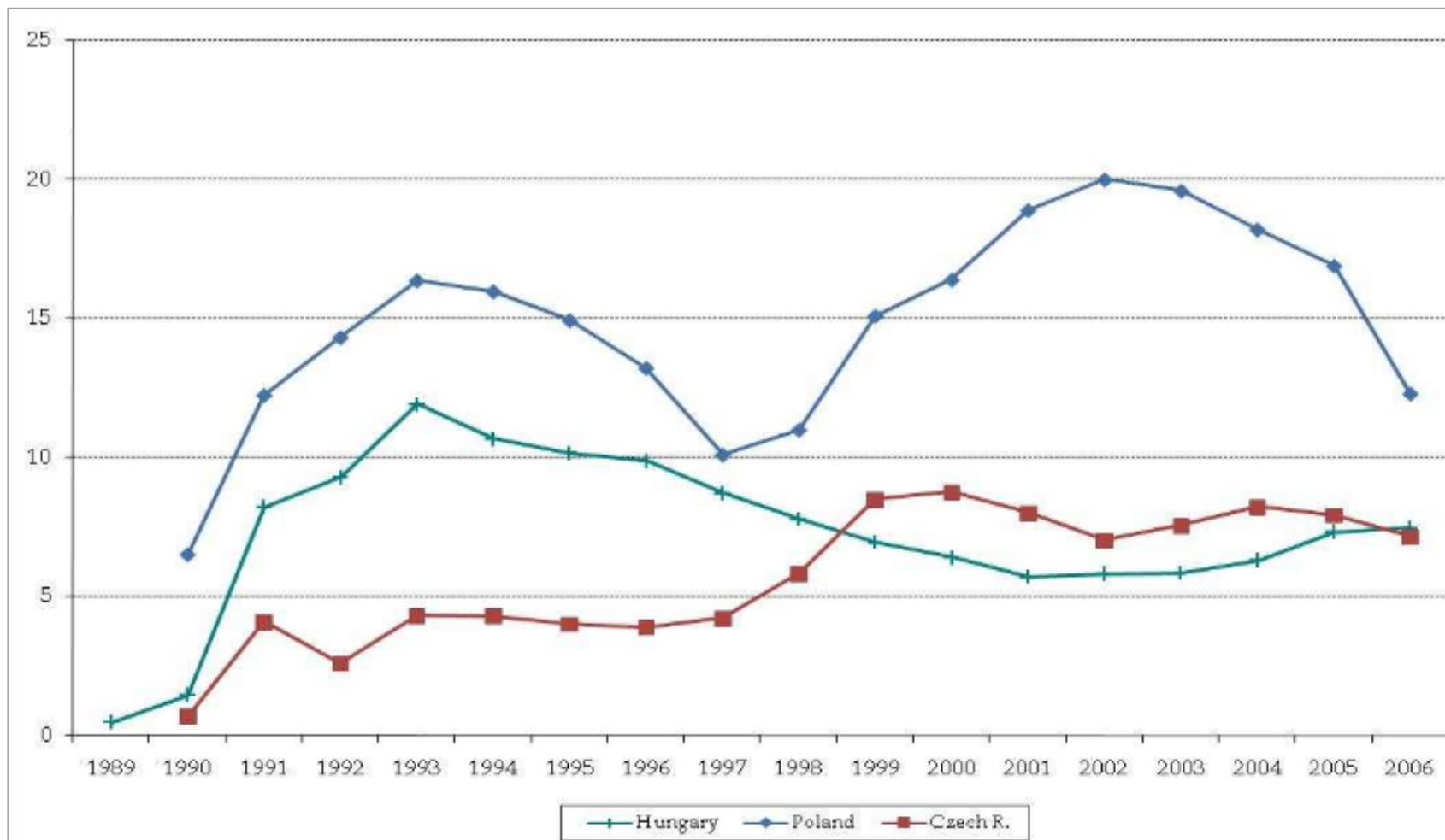
Source: UNDP: International human development indicators Retrieved December 22, 2010 from <http://hdrstats.undp.org/en/indicators/49806.html>

Table 18: Employment by sectors (% of total employment)

	Czech Republic			Hungary			Poland		
	Agriculture	Industry	Services	Agriculture	Industry	Services	Agriculture	Industry	Services
1990	n.a.	n.a.	n.a.	18.2	36.8	45	25.2	37	35.8
1991	n.a.	n.a.	n.a.	16.1	36.1	47.8	25.4	36	38
1992	n.a.	n.a.	n.a.	11.3	35.1	53.4	25	34.6	39.8
1993	7.7	42.9	49.3	9.1	33.8	56.9	n.a.	n.a.	n.a.
1994	6.9	42.2	50.9	8.7	33	58.1	24	31.9	43.9
1995	6.6	41.8	51.5	8	32.6	59.3	22.6	32	45.3
1996	6.1	41.5	52.3	8.3	32.6	59	22.1	31.7	46.2
1997	5.8	41.1	53	7.9	33.1	58.9	20.5	31.9	47.6
1998	5.5	41	53.5	7.5	34.2	58.2	19.2	32.1	48.7
1999	5.2	40.1	54.6	7.1	34	58.9	18.1	31.3	50.6
2000	5.1	39.5	55.3	6.5	33.7	59.7	18.8	30.8	50.4
2001	4.8	40	55.1	6.2	34.2	59.5	19.1	30.5	50.4
2002	4.8	39.6	55.5	6.2	34.1	59.6	19.3	28.6	52
2003	4.5	39.4	56.1	5.5	33.3	61.2	18.4	28.6	53
2004	4.3	39.2	56.5	5.3	32.8	61.9	18	28.8	53.2
Change 2004/ 1990	-3.4	-3.7	7.2	-12.9	-4	16.9	-7.2	-8.2	17.4

Source: World Databank - World Development Indicators (WDI) & Global Development Finance (GDF); Retrieved December 10, 2010 from <http://databank.worldbank.org/ddp/home.do?Step=12&id=4&CNO=2>

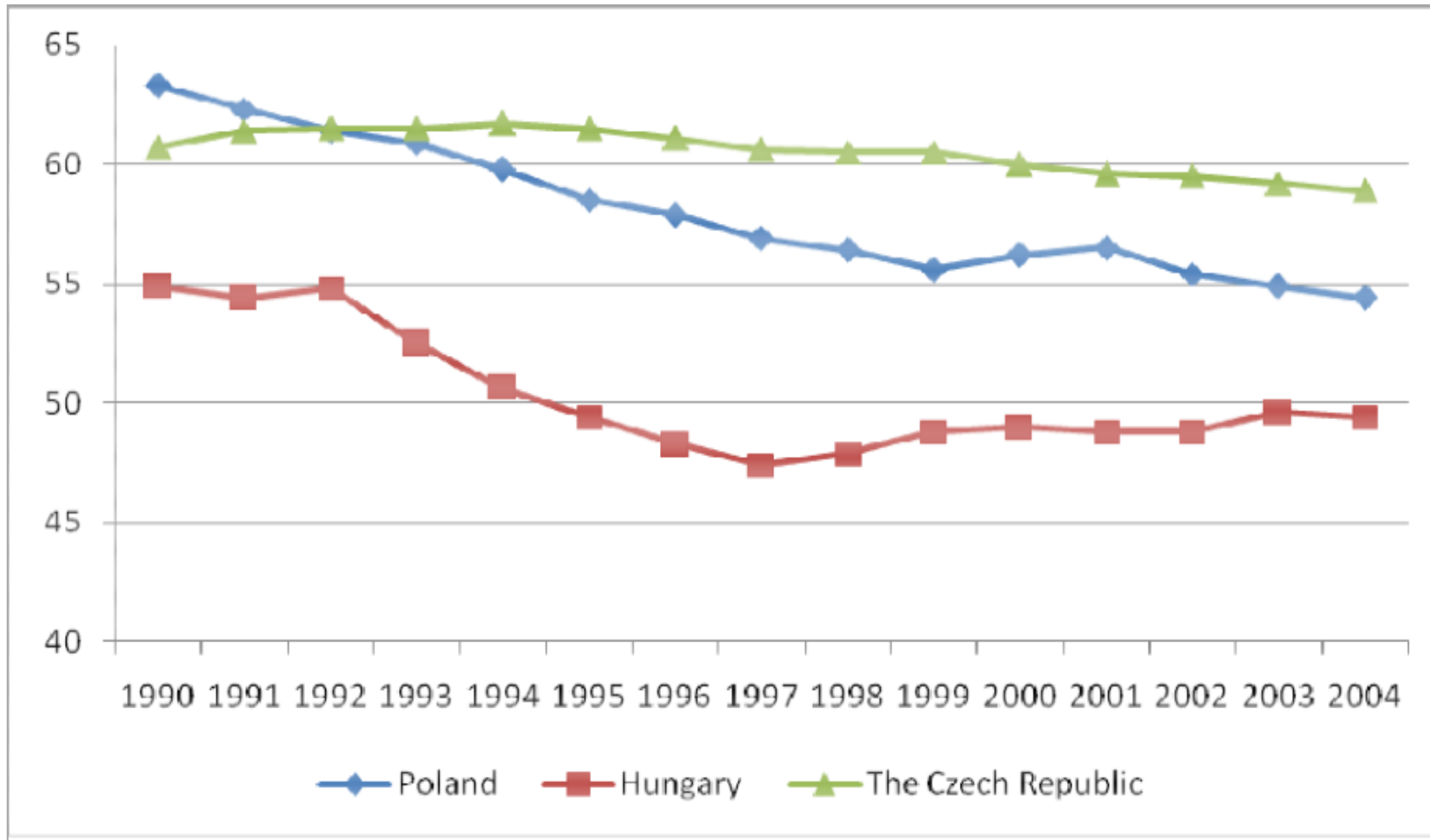
# Chart 9: Development of unemployment in Poland, Hungary and the Czech Republic between 1990 and 2006 (in %)



Source: EBRD: Selected economic indicators data, 26. 11. 2007.



# Chart 10: Labour participation rate, total (% of total population ages 15+)



Source: World Databank - World Development Indicators (WDI) & Global Development Finance (GDF); Retrieved December 10, 2010 from <http://databank.worldbank.org/ddp/home.do?Step=12&id=4&CNO=2>

Table 19: Development of consumers prices annual average (%)

	The Czech Republic	Hungary	Poland	Bulgaria	Rumania	Slovakia
1989	1.4	17.0	251.1	6.4	1.1	2.3
1990	9.7	28.9	585.8	26.3	5.1	10.8
1991	52.0	35.0	70.3	333.5	170.2	61.2
1992	11.1	23.0	43.0	82.0	210.4	10.0
1993	20.8	22.5	35.3	73.0	256.1	23.2
1994	9.9	18.8	32.2	96.3	136.7	13.4
1995	9.6	28.2	27.8	62.0	32.3	9.9
1996	8.9	23.6	19.9	123.0	38.8	5.8
1997	8.4	18.3	14.9	1 082.0	154.8	6.1
1998	10.6	14.3	11.8	22.2	59.1	6.7
1999	2.1	10.0	7.3	0.7	45.8	10.6
2000	4.0	9.8	10.1	9.9	45.7	12.0
2001	4.7	9.2	5.5	7.4	34.5	7.3
2002	1.8	5.3	1.9	5.9	22.5	3.3
2003	0.2	4.7	0.8	2.3	15.3	8.5
2004	2.8	6.8	3.5	6.1	11.9	7.5

Source: EBRD: Selected economic indicators data, 26. 11. 2007.

# Comparison of inflation in the CR, selected transition economies (1989 = 100)

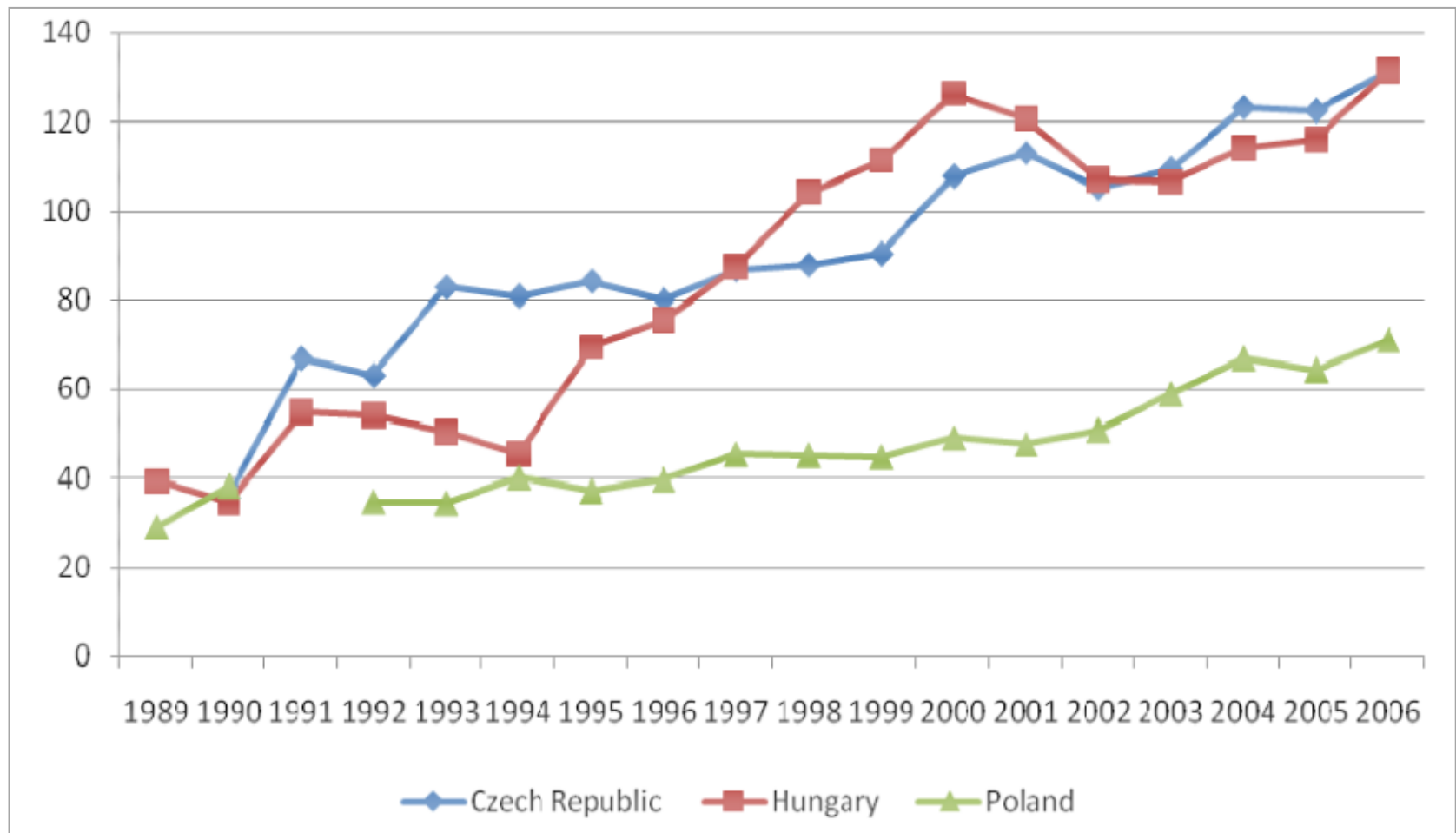
	1990	1991	1992	1995	1997	2000	2002	2004
Bulgaria	100	434	789	4 341	114 410	154 751	175 923	190982
Rumania	100	270	839	9 353	33 077	111 816	184 164	237609
Czech Republic	100	152	169	246	290	341	364	374
Hungary	100	135	166	310	453	625	719	804
Poland	100	170	244	557	767	1 013	1 089	1136
Slovakia	100	161	177	272	306	404	448	522

Table 21: The main Polish trading partners 1929-2004 and their share in Polish trade (in %)

		The 1st Partner	% share	The 2nd Partner	% share	The 3rd Partner	% share
1929	Imports	Germany	27.3	USA	12.5	U.K.	8.5
	Exports	Germany	31.2	Czechoslovakia	10.5	Austria	10.5
1938	Imports	Germany	14.5	USA	12.2	U.K.	11.4
	Exports	U.K.	18.2	Germany	14.5	Sweden	6
1950	Imports	USSR	28.8	Czechoslovakia	13.2	DRG	11.5
	Exports	USSR	24.3	DRG	13.9	Czechoslovakia	9.2
1960	Imports	USSR	31.2	DRG	12.5	Czechoslovakia	8.5
	Exports	USSR	29.4	DRG	9.4	Czechoslovakia	8.5
1970	Imports	USSR	37.7	DRG	11.1	Czechoslovakia	8.6
	Exports	USSR	35.3	DRG	9.3	Czechoslovakia	7.5
1980	Imports	USSR	33.1	FRD	6.7	DRG	6.6
	Exports	USSR	31.2	FRD	8.1	Czechoslovakia	6.9
1985	Imports	USSR	34.4	FRD	9	DRG	6.1
	Exports	USSR	28.4	FRD	8.7	Czechoslovakia	6.2
1990	Imports	Germany	20.1	USSR	19.8	Italy	7.5
	Exports	Germany	25.1	USSR	15.3	U.K.	7.1
1995	Imports	Germany	26.6	Italy	8.5	Russia	6.7
	Exports	Germany	38.3	Netherlands	5.6	Russia	5.6
2000	Imports	Germany	23.9	Russia	9.4	Italy	8.3
	Exports	Germany	34.9	Italy	6.3	France	5.2
2004	Imports	Germany	24.4	Italy	7.9	Russia	7.2
	Exports	Germany	30.1	Italy	6.1	France	6

Source: Central Statistical Office, Yearbook of Foreign Trade Statistics 2007, 2007.

# Chart 11: Trade openness (exports plus imports to GDP in %) in Poland, Hungary and the Czech Republic



Source: EBRD: Selected economic indicators data, 26. 11. 2007.

Table 23: The share of the current account balance to GDP between 1990 and 2004 (in %)

Country	1990	1991	1992	1993	1994	1995	1996	1997
Czech R.						-2.5	-6.7	-6.3
Hungary	1.1	1.2	0.9	-10.8	-9.5	-3.6	-3.8	-4.3
Poland	1.9	-0.4	1.0	-1.3	5.3	0.6	-2.1	-3.7
	1998	1999	2000	2001	2002	2003	2004	
Czech R.	-2.1	-2.4	-4.7	-5.3	-5.7	-6.3	-5.3	
Hungary	-7.0	-7.7	-8.5	-6.0	-7.0	-8.0	-8.4	
Poland	-4.0	-7.4	-6.0	-3.1	-2.8	-2.5	-4.0	

Source: IMF: World Economic Outlook Database, Retrieved October 9, 2010 from <http://www.imf.org/external/pubs/ft/weo/2010/02/weodata/index.aspx>

Table 24: Cumulative inflows of FDI in absolute terms and per capita in Eastern Europe 1989-2004

Country	Cumulative FDI inflows 1989-2004, in million US\$	Cumulative FID inflows per capita, 1989-2004, in US\$
Czech Republic	41 704	4 045
Hungary	37 189	3 719
Poland	56 333	1 471
Total Central Europe and Baltic countries	161 255	2 313

Source: Berend (2009)

Table 25: The share of foreign companies in industry at the end of the 1990s

	Employment	Investment	Sales	Exports
Czech Republic	27	53	42	61
Hungary	47	82	73	89
Poland	29	63	49	59

Source: Berend (2009)

# Conclusions

- Dramatic **changes in economic conditions** through the analysed period
  - **Economic catastroph** before the fall of communist regime
  - **Transformation recession** and hyperinflation due to „shock therapy“
  - **Improvement** of economic situation in medium-term
- **Outcomes**
  - Establishment of **growing trend**
  - **Catching up** with developed countries

**... the main goal of transformation was fulfilled !**



Thank you for attention !