CHAPTER 2

สำนักงานวิทยทรัพยากร จุฬาลงกรณ์มหาวิทยาลัย

Balcerowicz Plan

2.1 Balcerowicz Plan - The "Shock Therapy"

Although, the free trade program for the entrepreneurship was initiated during the period of communist government in 1982 under Rakowski's government, it was not successful implemented as planned, mainly due to the lack of budgetary discipline. Government expenditures were not appropriately spent to improve the market economy. The country deteriorated rapidly and inflation ran highest at the rate of 700% per year. These situations led to the Round Table Talks between the communist government and the Solidarity that culminated in the first non-communist government to seek remedial solution in 1989.[23]

The formation of a non-communist government in Poland in September 1989 under the administration of Tadeusz Mazowiecki's government, opened the floodgates of reforms and revolution in East-Central Europe. The new Minister of Finance, Leszek Balcerowicz, appointed a Harvard University economics professor, Jeffrey Sachs, economics advisor, to assist him in Poland's economic planning.

The government implemented a two-stage program under its economic plan which was aimed first at stabilizing the economy by curbing the hyperinflation and ending shortages of consumers goods, and then attempting to speed up to a market economy through privatization and deregulation to transform Poland into a modern European country. In the beginning of 1990, upon being approved by

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[23] Ibid., p. 33

the IMF, the introduction of radical reforms was a precondition of Poland's survival. The "shock-therapy" program designed in late 1989 by the Deputy Prime Minister/Finance Minister Laszek Balcerowicz, aimed to abolish all centralized economic planning mechanisms, eliminate inefficient enterprises, the improvement of overall effectiveness of the economy, and the enhancement of the competitiveness to reach the stage of free market economy as soon as possible. The program consisted of :

2.1.1 Price liberalization
2.1.2 Establishment of free trade
2.1.3 Restructuring of banking and financial sector
2.1.4 Privatization

2.1.1 Price liberalization

During the communist period, the pricing of goods and services was controlled by the State which was regarded as an artificial pricing. The controlled prices have been liberated in almost all sectors with an important exception of the energy sector. Upon implementation of the free pricing method, it then caused side effects. Liberalization of prices allowed them to rise in response to market forces, inflation running 600% in 1990, declined to 44% in 1992, 35%in 1993, 30% in 1994 and 27% in 1995. This was according to the rules of demand and supply. Virtually all government subsidies were eliminated. A new currency law ended the previous artificial exchange rate for the Zloty and full domestic convertibility was introduced. Foreign trade transactions were liberalized and trading monopolies abolished, initiating a dramatic rise both in exports and imports.[24]

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[24] UNIDO, "Foreign Investors' Guide to Poland", Warsaw, May 1996. p. 11

The radical implementation of the pricing liberalization under the "Shock Therapy" program first caused the country to experience a deep recession. The GDP declined at least 20% over three years from 1989. Industrial production fell by a quarter in 1990 alone and by further 12% in 1991, while real earnings declined by 35%. Unemployment has been on the rise throughout the period to the peak at almost the 3 million mark early in 1994, then started to decline.[25]

With decentralized price, shortages and queues disappeared. The free trade regime had helped bring the structure of domestic prices closer to the world market price. A labor market also emerged in a peculiar manner. On the one hand, where there were jobs, the workers demanded their pay at real market prices. On the other hand, unemployment rose high because of the cut in government subsidy.[26] Interestingly, the reduction in employment was observed only in the public sector, while in the same period (1992-1995) the private sector recorded a 600,000 job increase in employment.[27]

The recession was deep but relatively short-lived. In fact, Poland was the only country in the region to record growth in GDP in 1992. The recovery gained momentum in 1993 with GDP growing 3.8%, which at that time was the highest growth rate in Europe. In 1994 and 1995 a further acceleration of growth was recorded and the GDP went up 5.2% and 7.0% respectively. Forecasts for the future continue to predict this growth trend.[28]

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[25] Ibid., p. 12
[26] Op. Cit., pp. 34-35
[27] The Foreign Trade Research Institute, "Poland Your Business Partner", (Warsaw:1996), p. 52
[28] Op. Cit., p. 12

The government is committed to encourage the free competition necessary for the proper working of a free market economy by which a program for competition development has been implemented. The program also aims at anti-monopolistic business activities and practices. The Anti-Monopoly Office has been established to study price tendencies, supervise companies which take majority market shares in Poland and impose sanctions. The Office is also involved in developing the competition law to comply with EU requirements for possible future integration.[29]

2.1.2 Establishment of free trade

Along with the implementation of pricing liberalization, the government had eliminated trade that were mainly conducted by the State which unrealistically ignored the basic rule of demand and supply. The quotas system on import of foreign goods was replaced by the tariff based system. The private sector has also been allowed to engage in foreign trade together with the establishment of the non-restricted foreign exchange in order to boost the foreign trade transactions. The government has refocused its foreign economic policy. Priority has been given to relations with the European integration structure, and particularly, with the EU. [30]

Major trade partners of Poland in OECD countries are Germany, Netherlands, Italy, United Kingdom and France and major trade partners in Central and Eastern Europe are Russia, Ukraine, Czeck Republic, Slovak and Austria. These countries are both the

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[29] UNIDO, "Foreign Investors' Guide to Poland", Warsaw, May 1996, p. 40.

[30] Vajrasthira, Prathoomporn, "The European Union's Assistance to the Visegrad Countries", February 1995, p. 35.

principal exporters to Poland and also the principal importers of Polish products.[31]

Poland is a member of several international trade and financial organization. It is a member to GATT, WTO, OECD, Europe Agreement, CEFTA, EFTA, IMF and the World Bank. The trade turnover regulated by the trade agreements accounted for 75% of the country's total foreign trade in 1995.

UNIDO office has also significantly contributed to the promotion of cooperation with foreign partners among Polish business community, particularly through extensive information and training. Many projects with the participation of foreign capital were initiated or supported at a certain stage by the UNIDO office.

Poland has also been granted most favored nation status (MFN) by the United States.[32]

2.1.3 Restructuring of banking and financial sector

The development of a banking system is embodied in the Banking Law and the Law of the National Bank of Poland (NBP) in January 1989. The role of the National Bank was modified to correspond to that of an independent central bank in the West with responsibility for monetary policy and banking supervision. It controls most of the banking system in Poland. The Ministry of Finance is working with the NBP to update the rules and regulations which govern the banking operations in Poland.[33]

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[31] The Foreign Trade Research Institute. "Selected Data on Polish Foreign Trade", Warsaw, 1996, pp. 16-17.

[32] The Foreign Trade Research Institute, "Poland: Your Business Partner", Warsaw, 1996, pp. 56-58.

[33] Price Waterhouse. "Doing Business in Poland". USA, 1998, p 48

Amendments to the 1989 legislation adopted in 1991 and 1992 are expected to complete the transformation of the Polish banking system to meet the requirements of a market economy; to prepare its integration with EU legislation; and to encourage foreign investors participation in the development of the banking sector. The government believes that the entry of foreign banks into the Polish market is a desirable step in the development of a free market economy. The intention is to create a level playing field for both domestic and foreign financial organizations.

Foreign banks were invited to establish branches in Poland. Financial support from the World Bank had been provided which engaged Western financial institutions to the provision of technical advice and personnel training in return for an opportunity to take 20% holding in the Polish bank once it is privatized.[34]

Privatization of the banking system was initiated and implemented since 1992 with the sale of a listed state owned bank as well as the entering into cooperation agreement with overseas banks. As of 1 May, 1992, nine commercial banks have been transformed into corporations owned by the State Treasury. In addition, 50 private banks and 14 foreign owned banks have been formed and 6 banks have formed joint ventures with foreign businesses. Two foreign banks have established branches and 1,600 cooperative banks also operate in Poland[35].

The re-establishment of capital market in Poland was introduced by the Law on Public Trading in Securities and Trust Funds of 1991. The

[34] Vajrasthira, Prathoomportn, "The European Union's Assistance to the Visegrad Countries", February 1995, p. 35.

[35] Op., cit., pp. 45-47.

Law provides the regulatory framework for operations on the capital market, agents, the Securities Commission, the Securities Exchange and stock brokers.

The Warsaw Stock Exchange was opened on 16 April 1991. It is a joint stock company with the State Treasury as the major shareholder.

The number of companies listed on the Stock Exchange in 1996 was 73 companies which has been increased from 12 in 1991. At the end of October 1997, shares in 130 companies were being traded on the main floor and parallel market of WSE.[36]

2.1.4 Privatization

The concept of private owned property and privatization of state owned enterprises is the main foundation and fundamental factor for Poland in becoming an efficient economy. Privatization will rapidly improve the country's productive efficiency and increase competitiveness in the world market. Privatization is considered as one of the most important components of the economic transformation together with stabilization and liberalization program. Poland has regulated three legal acts in 1990 to facilitate the privatization process, namely:[37]

- The Statute on the Privatization of State-Owned Enterprises of July 1990
- The Statute on the Management of the Agricultural Land of the State Treasury and on amendments to certain statutes.

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[36] Price Waterhouse, "Doing Business in Poland", USA, 1998, p. 53.
[37] Op., cit. p. 54

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- The Statute on National Investment Funds and their Privatization of April 1990, as well as by some provisions of the Statute on State Enterprises of September 1981

However, the privatization process is governed by the Act on Privatization and Commercialization of State-Owned Enterprises of August 30, 1996.

The laws structure the methods and manner in which ownership of economic entities may be transformed from the State to the private sector which are set forth in two methods: **the Capital Privatization Method and Direct Privatization Method**.

Capital Privatization Method is primarily applied to the privatization of large state-owned enterprises which are in good commercial and financial status. It involves the transformation of a state enterprise into a single person company, either a joint stock company or limited liability company, and to be wholly owned by the State Treasury or a privatization agency. The transformation will transfer the state enterprise from the Register of State owned Enterprise to the Register of Companies, under the Commercial Code. The assets and liabilities of the transformed state enterprise upon being removed from the Register and being evaluated independently will be transferred into the new company.

The transformation may be initiated by the enterprise itself through the Manager of Workers' Council, or by the founding organ; or ex officio of the enterprise or by the Prime Minister at the request of the Minister of Privatization or one of its regional office.

Shares in the transformed company must be offered and sold to investors within two years after incorporation unless it is extended by the Council of Ministers. The sale may be through an auction, public offer or negotiations initiated by public invitation or as specified by the Council of Ministers.

Employees of the company can acquire shares under preferential circumstances (i.e., at discount price or freely) upto certain percentage of the capital in total and up to number of months' wages in the transformed enterprise per person. In the course of privatization, foreign investors is however restricted to buy shares upto certain maximum percentage of the shares in each enterprise. It should be noted that state enterprises however, cannot take shares in other companies unless a permission has been given by the Minister of Finance.

By the end of 1995, 958 state enterprises underwent the transformation under this method. There were 160 companies successfully privatized. The number was increased by the end of 1996, 1,479 state enterprises underwent the transformation and 40% of it was successfully privatized.[38]

Direct Privatization Method applies to privatize small and medium sized state enterprises whose number of employees does not exceed 500 and whose annual volume of sales does not exceed ECU 6 million. While being initiated by the relevant founding authority (Ministry of the Economy and the State Treasury and the regional government representative), the enterprise itself, or at the request of the Workers

[38] UNIDO, "Foreign Investors' Guide to Poland", Warsaw, May 1996, p. 36.

Council submitted to the Ministry of Privatization, the enterprises be liquidated by ways of:

- sale of the enterprise (assets)
- in-kind contribution of the enterprises (assets) to a company, or
- Transferal of the enterprise to its creditors

The sale of assets involves the sale of state enterprises to other investors in the private sectors. Contribution of assets involve investment in other existing company set up by the State Treasury and a foreign investor by using of assets in exchange of the shares capital as an in-kind shares investment. Creditors buy-out involves other existing company, set up by creditors of the state enterprise, leases assets from the liquidated enterprise with an option to purchase such assets in the future. Creditors include employees of such state enterprise.

It is however possible that the combination of the above three methods can be made for privatization.

In 1995, there were 1,358 state enterprises being liquidated. However, only 396 state enterprises have been privatized.[39]

It should be noted that in 1990, when the process of privatization was just starting, there were about 8,440 state owned enterprises and communual enterprises in Poland. As of mid 1997 about 4,000 enterprises had been privatized or were in the process of being privatized under both methods.[40]

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[39] Ibid., p. 37.
[40] Price Waterhouse, "Doing Business in Poland", USA, 1998, p. 19.

Mass Privatization Program

Following the introduction of the law on National Investment Funds and their Privatization on April 30 1993, Poland embarked on a massive privatization program (MPP) in its commitment to economic reforms designed to build a market economy. In December 1994, 15 national investment funds (NIFs) were established to assist in the restructuring of state-owned enterprises by holding shares in 512 companies that took part in the MPP. In each of the 512 enterprises only 1 NIF holds a lead stake of 33%, and each of the other NIFs holds minority stake of 1.93%. Of the remaining 40% of each enterprise, 15% is distributed free of charge to employees, and 25% is retained by the State Treasury.

Nearly all NIFs have appointed a firm or consortium to manage their portfolio. Fund regulation is closely supervised by the Polish Securities Commission. Governing bodies of the NIF include a management board, a supervisory board and a general shareholders' meeting.

Resident Polish citizens are entitled to participate in the MPP by purchasing share at nominal value. The shares are currently freely traded. The shares in the NIFs were listed on Warsaw Stock Exchange in June 1997.[41]

[41] Ibid., p. 21