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**DEPARTMENT OF STATE**  
**BRIEFING PAPER**

Poland: Economic Problems and Prospects

What Are the Problems?

- o Poland is undergoing a wrenching transformation from an economy based on central planning to a market system. This change has come at the expense of growth. According to official (and incomplete) statistics, GDP declined 12 percent in 1990 and real incomes fell 30 percent. Unemployment has increased to 6 percent.
- o Meanwhile, loose wage and credit policies of the second half of 1990 threaten a return to high inflation and resulted in a suspension to Poland IMF's agreement.
- o Poland has been unable to attract foreign investment due to the slow pace of its privatization program and the overhang of a \$45 billion foreign debt.

What Has Been Done?

- o Poland's performance under the agreement it concluded with the IMF in February, 1990 was mixed, as the GOP exceeded its wage increase and credit growth targets. Two IMF drawings were thus forfeited.
- o A March, 1990 Paris Club obviated the need for Poland to make any debt payments to official creditors until March 31, 1991. This, combined with \$1 billion in G-24 contributions toward a currency stabilization fund, helped bolster Poland's 1990 balance of payments.

What Needs To Be Done?

- o Poland must now carry forward its reforms in a 3-year arrangement with the IMF, concentrating on consolidating its stabilization gains and giving emphasis to structural measures.
- o To attract foreign investment, Poland must transform its ownership and production patterns, demonopolize industry, and undertake privatization. Polish ratification of the Treaty Concerning Business and Economic Relations will be key to this effort (the U.S. ratified it on Nov. 30, 1990).
- o The authorities must hold to a tight fiscal stance, restrain money and credit growth, and keep wage increases from accelerating to avoid a damaging bout of inflation.
- o For the long-term viability of the Polish economy, official creditors must agree to substantial debt reduction, and Poland must reach a similar agreement with its commercial creditors. The Paris Club is expected to act on official debt once Poland's 3-year IMF agreement is concluded.

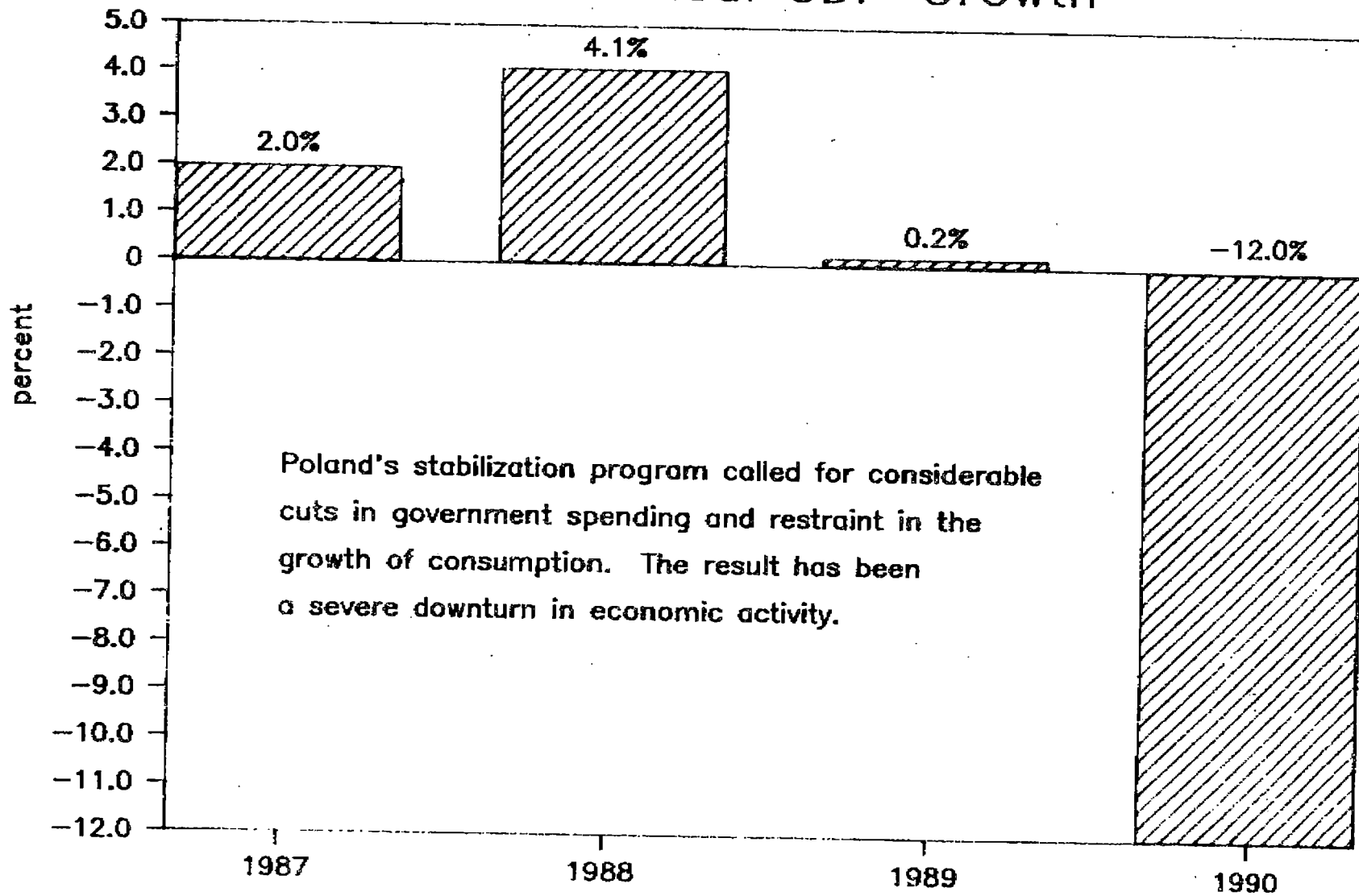
**Economic Fact Sheet - Poland**  
(US\$ billions unless otherwise stated)

	1987	1988	1989	1990
=====				
<b>1. Socio-economic Indicators</b>				
-----				
Population (millions)	37.7	37.9	37.9	37.9
Pop. growth rate	0.5%	0.5%	0.0%	0.1%
Life expectancy (years)	72	72	72	72
Adult literacy	94%	94%	94%	94%
Infant Mortality (per 1000)	16	16	16	16
<b>2. Economic Indicators</b>				
-----				
GDP (billion 1988 US\$)	69	70	71	62
GDP per capita (1988 US\$)	1,833	1,860	1,863	1,642
Inflation rate (CPI)	25.2%	60.2%	245.3%	31.2%
Real GDP growth rate	2.0%	4.1%	0.2%	-12.0%
Real GDP growth per capita	3.6%	1.5%	0.2%	-11.9%
Unemployment rate	n/a	0.3%	0.6%	6.0%
Investment/GDP	22.6%	22.5%	16.4%	n/a
Govt. expenditures/GDP	41.0%	37.7%	37.0%	29.5%
Govt. budget balance/GDP	-3.5%	-1.4%	-6.1%	1.2%
<b>3. Balance of Payments</b>				
-----				
US Exports to Poland	0.18	0.25	0.18	0.19
US Imports from Poland	0.27	0.36	0.36	0.24
US-Poland trade balance	-0.09	-0.12	-0.18	-0.05
Total merchandise exports*	12.0	13.8	12.9	13.9
Total merchandise imports*	11.2	12.8	12.8	8.7
Trade Balance*	0.8	1.1	0.0	5.1
Current Account Balance*	-0.4	-0.1	-1.4	4.0
<b>4. External Finance</b>				
-----				
Foreign exchange reserves	3.3	5.1	10.0	14.5
Exchange rate (zloty/US\$)	265.1	430.5	1439.2	9500.0
Total external debt	39.7	39.1	40.6	45.9
Annual debt service	6.2	6.8	5.1	6.8
Debt service ratio	91.0%	85.0%	62.0%	58.0%
<b>5. U.S. Assistance</b>				
-----				
U.S. Economic Assistance (FY)				
Stabilization Fund	0	0	0	200
Agricultural Assistance	0	0	0	97
Technical assistance	0	0	0	30

SOURCES: International Financial Statistics, Direction of Trade Statistics, Embassy Reporting, EB Calculations

\* Trade/current account figures combine convertible and non-convertible data Prepared by:EB/IFD/OMA:JPReid 3/6/91

# Poland - Real GDP Growth





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## Economic Issues in the Presidential Campaign

Louisa Vinton

*The best path to a market economy is at the heart of the conflict between Poland's two major presidential candidates. Prime Minister Tadeusz Mazowiecki stands unambiguously for continuity in the government's economic policy. Solidarity leader Lech Walesa's position is less clear. Critics have argued that Walesa's call for "acceleration" misleads voters, because it implies that economic progress can be achieved both more rapidly and at less cost. Walesa's campaign statements have at times seemed to dismiss key elements of the government's anti-inflationary strategy. Walesa's intention, however, may be not to reject the current government's policy but rather to implement it more rigorously.*

**T**he bluster of the Polish presidential campaign has tended to exaggerate the differences on economic policy between the two major candidates. Judging from their published programs, Solidarity leader Lech Walesa and Prime Minister Tadeusz Mazowiecki share a common vision of Poland's future economy: a market system based on private ownership in which foreign capital functions as an engine of change. Moreover, both candidates are in basic agreement as to the methods necessary to achieve this transformation. The real source of conflict, then, is the feasible tempo of economic change and, most important, its psychological and social context.

The central argument of Walesa's campaign seems to be that he alone can ensure the proper social and political climate for the sort of drastic

economic change Poland requires. By inspiring and coaxing the Polish public to view the market economy as a chance for prosperity rather than a painful burden, only Walesa, his campaign statements have suggested, can inspire the motivation and discipline necessary to see the public through the hardship that still lies ahead. In contrast, the Mazowiecki camp has argued that Walesa's efforts to win the public over endanger the very cause he claims to serve, the success of the economic transformation, by pandering to the public's wishful thinking about the costs and the duration of economic upheaval.

### **Mazowiecki: Stay the Course**

Walesa's persistent demands for "acceleration" have forced Mazowiecki not only to defend the government's economic achievements of the past

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year but also to explain why more could not have been accomplished in the same period. The repeated elucidation of the difficulties encountered and the challenges yet to be faced has given the Mazowiecki presidential campaign its sober tone. Mazowiecki's opening remarks in his first campaign radio spot were typical: "This country's problems will not come to an end on November 25 . . . regardless of who wins."<sup>1</sup> The prospect of any rapid change in the nation's economic fortunes, Mazowiecki has argued, is illusory, and "it is better to promise what is possible."<sup>2</sup>

Mazowiecki advocates the continuation of the government's economic program under the leadership of Finance Minister Leszek Balcerowicz. The "Balcerowicz plan" aims at this point to carry out systemic changes—privatization, demonopolization, a new banking system, a new tax structure, a coherent legislative framework to govern foreign investment—as rapidly as possible, without wasting the gains achieved so far.<sup>3</sup> This year's achievements, which include drastically reduced inflation, a stable and convertible zloty, a balanced budget, market equilibrium, and a huge hard-currency trade surplus, are the result of the "stabilization" plan of tight fiscal policies and strict wage controls introduced on January 1, 1990. The price for these gains has been a deep recession and a drop in living standards.

Balcerowicz has argued for a realistic assessment of these costs. Outdated statistical methods, he notes, overstate this year's 15% to 16% drop in production as a 30% decline.<sup>4</sup> In addition, there have been some recent signs of economic recovery: production has been rising slowly since July, the output of private firms has grown dramatically, and the market has begun to sort out the good firms from the bad. But at the same time, government officials have warned of new threats: the Gulf crisis, the shift to hard-currency trade with the Soviet Union, and the disappearance of the East German market.

In the face of criticism from some economists<sup>5</sup> and widespread pressure from workers for higher wages, Balcerowicz has argued that only structural changes, not a new influx of money into the market, can generate increased production. Yielding to the temptation to relax wage and budgetary controls at this point, Balcerowicz has said, would merely encourage a new explosion of inflation. Instead, the government should strive, on the one hand, to continue its economic stabilization program and, on the other, to transfer state firms to private owners as quickly as possible. In the transitional period to full privatization, the government should strive to "commercialize" firms, that is, create a healthy market environment that will force state

firms to operate efficiently and to maximize their profits. Only the rational hiring and wage policies that would result from the private ownership of firms would enable the government to remove the wage controls currently in force.

The response of state firms to market pressures has so far been uneven. While some have sought new markets or improved efficiency, many others have simply continued the old strategy of raising prices to cover all higher costs. For this reason, as well as public pressure for more rapid change, the government has condensed its privatization timetable. Mazowiecki's election platform, like the government's recently adopted economic strategy of "swift continuation" for 1991,<sup>6</sup> envisages the privatization of 50% of state firms within three years. While thus accepting a faster pace of change, the government has warned that this necessarily entails greater hardship—higher unemployment, in particular—and greater risks. As Mazowiecki has put it, "I am in favor of acceleration, but safe [acceleration]: if excess speed causes the cart to overturn, we will arrive at our goal even later."<sup>7</sup> Balcerowicz has also asked that the public keep its aspirations "out of the realm of illusions" and use as a standard for comparison living conditions in Portugal, not western Germany.<sup>8</sup>

#### Walesa: Balcerowicz but . . .

Although Walesa has criticized the government's economic performance, it is unclear how fundamental his objections are or what alternative course he would suggest. Walesa's statements have for the most part endorsed the general direction of the Balcerowicz plan while at the same time suggesting generally undefined revisions. While his electoral program calls for "radical change" in the implementation of the government's economic policy,<sup>9</sup> Walesa has also said that the Balcerowicz plan provides "the only way out of the crisis," provided that "a few corrections" permitting swifter privatization are introduced.<sup>10</sup> Walesa's supporters and closest advisers have likewise suggested that Walesa would want Balcerowicz to stay on as the government's economic chief, or even to serve as Prime Minister, should he win the election.<sup>11</sup>

Walesa's remarks on the campaign trail have, however, at times seemed to conflict with the basic tenets of the Balcerowicz plan. Walesa's tone varies depending on his audience; the mood of his listeners at election rallies tends to influence the way he speaks, encouraging exaggeration and imprecision. On November 10 Walesa complained that "reform has not really begun; this is just correcting socialism, not building something new."<sup>12</sup> Walesa

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has also said that he does not believe in unemployment, although he has called limited unemployment a form of "economic hygiene." He has argued that Poland's huge, unproductive factories should be shut down only when new jobs have been created for displaced members of the work force. He has encouraged foreign investment but demanded guarantees to prevent Western capital from turning Polish workers into "white slaves."

Remarks such as these have caused concern that, for all his appreciation of the Balcerowicz plan, Walesa is undermining its chances of success by making easy promises that he will be unable to fulfill should he win the election. Mazowiecki has caricatured Walesa's manner of speaking as "I'm in favor, and what's more, I'm opposed."<sup>13</sup> Other critics have charged that Walesa says exactly what the crowds at election rallies want to hear and thus frequently implies that there are less painful ways to achieve prosperity than those proposed by the government. For this reason, critics say, Walesa's "acceleration" would, in fact, slow down the process of change. Others point to the contrast between Walesa's statements at election rallies and those intended for Western consumption. Ernest Skalski of *Gazeta Wyborcza*, for example, has charged that "there are no principles to Walesa's economics; in his economics you can have something for nothing."<sup>14</sup>

One of Walesa's campaign assets has been his ability to muster the support of numerous, quite varied groups (from the right-wing Christian National Union to Tadeusz Fiszbach's Social Democratic Union) without having to pledge anything in return. This has complicated the task of clearly assessing Walesa's economic intentions. Three different bodies that support Walesa—the Center Alliance, the Citizens' Committee, and the advisory team led by Andrzej Micewski—have drawn up economic guidelines in preparation for a Walesa Presidency, but Walesa has identified none of them as his own.<sup>15</sup> Moreover, these plans differ. Stefan Kurowski, who helped write the Center Alliance's program and belongs to the Micewski team, has urged the prompt repudiation of Poland's debt and the lifting of wage controls,<sup>16</sup> proposals that Balcerowicz would most probably reject out of hand. But other economists on the Micewski team have expressed approval for the government's course. Aleksander Mueller, for example, has even argued that "ousting Balcerowicz from the posts of Finance Minister and Deputy Prime Minister responsible for economic matters would mean a catastrophe."<sup>17</sup>

Balcerowicz has not taken part in the election campaign, although he has expressed his admiration for Mazowiecki's "calm determination" in

pursuing a difficult economic program. Asked by *Polityka* about the suggestion that he would remain in his post if Walesa became President, Balcerowicz said that for him "the most important question was the possibility of continuing the economic program."<sup>18</sup> At the same time, he warned that introducing the "corrections" proposed by some of his critics would mean a different economic program altogether, one that would lead to prolonged stagnation rather than genuine structural change.

## Taming the Populist Horse

Even Walesa's harshest critics have admitted that the confusion surrounding Walesa's economic program stems more from the way the public chooses to interpret it than from its explicit content. Walesa's message on the campaign trail is not designed to win voters over to a specific program but rather to inspire in them a change of attitude. Walesa's presidential campaign can, in fact, be reduced to a single, central message: the importance of self-reliance and individual responsibility in reversing Poland's economic fortunes. Assuming that the gravest threats to reform in Poland are apathy and passivity, Walesa has demanded that his listeners take the initiative and solve local problems themselves. These remarks from a recent election rally are typical:

Many people think that if they vote for Walesa and then go off to drink beer, he'll take care of the rest. He'll take care of the *nomenklatura*, he'll take care of business, and there will be more [of everything]. Well, my dear friends, the worst thing that could happen would be if I really won and you went off and left me to build Poland by myself. I can't do it. The chance [of success] of our reforms is directly proportional to your participation [in them].<sup>19</sup>

As the pro-Mazowiecki daily *Gazeta Wyborcza* observed in an article entitled "What They Are Applauding,"<sup>20</sup> Walesa's standard addresses are full of unwelcome homilies about the individual effort necessary to achieve Poland's economic transformation. In explaining Poland's need for small family businesses, for example, Walesa has said that "the father will be the director, the mother the trade union, and the son and daughter the proletariat." The crowds that come out to see Walesa, however, heed only a part of his message. His audience applauds when Walesa criticizes the government, says "you've been cheated," demands a "settling of accounts" with the *nomenklatura*, or calls for an "airing out" of Warsaw; but its response to the central message of self-reliance is chilly.

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A regional Solidarity leader warned in a recent interview that many workers "were passive, waiting for a leader who would shorten the path to Western prosperity."<sup>21</sup> The surprisingly strong showing in recent pre-election polls by Stanislaw Tyminski, a wealthy businessman born in Poland who also holds Canadian and Peruvian citizenships, confirms this impression. Tyminski is the author of a book called *Sacred Dogs*, which he claims contains a 21-point economic program designed to cure the Polish economy. He returned to Poland to run for President. Early in the campaign, he was accused of "buying" the 100,000 signatures necessary for registration by offering free copies of his book to anyone who submitted a supporting petition with at least 20 names. The polls show that Tyminski has moved into third place (with 17%), behind Walesa and Mazowiecki, and has outdistanced the other three candidates.<sup>22</sup> Tyminski's startling popularity seems to stem almost entirely from his apolitical aura and what could be called the "rich uncle" syndrome, the popular notion that a wealthy Pole who made his fortune in the West might have the key to painless prosperity.

Tyminski has also played on public fears that Western economic aid and foreign capital investment (German, in particular) pose threats to Poland's sovereignty. Other candidates have used this issue as well. Peasant Party candidate Roman Bartoszcze has charged that the Balcerowicz plan is "not a Polish plan" and was imposed on the nation from outside by foreign advisers determined to destroy Polish farming.<sup>23</sup> Tyminski's charges have been the most extreme, however, and his tone the most shrill. "We are in a state of war and occupation no less threatening than World War II," he claimed at a rally in Zakopane on November 17. In remarks that prompted the prosecutor's office to open a slander investigation, Tyminski accused Mazowiecki of "treason" for selling "our economy's most beautiful pearls" to foreign investors for next to nothing. He also claimed that the government had falsified

statistical data to conceal the true magnitude of inflation. When Tyminski held a press conference to present the "secret" documents he said would prove his charges, however, it turned out that he had mistaken yearly turnover figures for sales prices in a widely available government document.<sup>24</sup>

Although Walesa in fact promises very little, his campaign appears to have harnessed some of the same sentiments that have made Tyminski an unexpectedly strong challenger. Walesa's supporters have insisted that this is a conscious tactic on his part. All campaign rhetoric aside, they argue, Walesa is a confirmed advocate of rigorous, market-oriented economic policies. But because he is recognized as an authority by precisely those groups most threatened by economic change and most likely to rebel against it, they say, Walesa alone will be able to ensure the social climate necessary to carry out far-reaching structural change in the economy.<sup>25</sup> Walesa has said that "when I stand before a stormy crowd, I must yield to the storm in order to calm it." He has also explained his approach in a parable:

Let's imagine that a horse is running away from me. I want to stop him. But if I try to block his path, then he'll trample me. So what can I do? I have to pursue him, jump into the saddle, and rein him in.<sup>26</sup>

This approach is, of course, a risky one. Indeed, Mazowiecki's supporters have pointed out that by raising unreal hopes and arousing expectations for a quick economic transition, Walesa's approach could result in even greater public disappointment than exists at present and in far more bitter outbursts of dissatisfaction. As the enthusiasm generated by his campaign has suggested, however, Walesa alone seems to have grasped the importance of building a social and political architecture within which the Balcerowicz plan can work.

PO0494.90R

November 22, 1990

## Notes:

1 Radio Warsaw, October 29, 1990, 7:25 A.M.

2 *Ibid.*, October 30, 1990, 7:25 A.M.

3 On the Balcerowicz plan, see RAD Situation Report/16, *Radio Free Europe Research*, November 14, 1989, item 1.

4 See Balcerowicz's address to the Sejm on October 11, 1990, excerpted in *Gazeta Wyborcza*, October 12, 1990.

5 Economists affiliated with the Center Alliance, including Stefan Kurowski, argued earlier this year that the government should relax wage controls to counter

recession. Reaching the same conclusion, the government decided in July to ease somewhat the tax on excess wages. Recent renewed inflation of over 4% per month, largely the result of higher oil prices worldwide, seems to have moderated the Center Alliance's demands. The government's plan to privatize 50% of state firms in three years has brought its timetable in line with the Center Alliance's. Balcerowicz's most vocal critic is the economist Rafal Krawczyk, whose economic program the Polish Peasant Party and its presidential candidate, Roman Bartoszcze, have adopted as their own. Krawczyk

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has appeared together with Bartoszcze in most of his radio and television campaign spots. For Krawczyk's views, see his book *Wielka przemiana. Upadek i odrodzenie polskiej gospodarki* [The Great Transformation: The Collapse and Revival of the Polish Economy] (Warsaw: Oficyna Wydawnicza, 1990). For a summary, see the interviews in *Gazeta Pomorska*, August 24, 1990, and *Tygodnik Gdanski*, September 30, 1990. One of *Polityka's* economic writers has dismissed Krawczyk's program as "noisy, verbal opposition that changes nothing and has nothing new to offer Poland's economy . . . with the possible exception of the author himself" (Jerzy Baczynski, "Main and Incidental Sins," *Polityka*, September 29, 1990). Krawczyk's statements reveal a great personal bitterness towards Balcerowicz. See the responses to Krawczyk's *Tygodnik Gdanski* interview by the economists Jan Mujzel and Stanislaw L. Bagdzinski, along with Krawczyk's own comments, in *Tygodnik Gdanski*, November 11, 1990.

6 On the government's plans for 1991, see Piotr Aleksandrowicz, "The Strategy of Swift Continuation," *Rzeczpospolita*, November 6, 1990.

7 Quoted in *Rzeczpospolita*, October 26, 1990.

8 In an interview with *Polityka*, November 3, 1990.

9 Walesa's election program was summarized as "Lech Walesa: New Beginning," in *Rzeczpospolita*, November 13, 1990.

10 In an election broadcast, Radio Warsaw, November 14, 1990, 8:25 A.M.

11 Walesa adviser and sociologist Jadwiga Staniszka has recommended a "Walesa-Balcerowicz tandem" to push through economic reform (Radio Warsaw, October 30, 1990, 7:25 A.M.). Center Alliance leader Jaroslaw Kaczynski reported on October 23 that Balcerowicz was on Walesa's list of candidates to head the government (*Rzeczpospolita*, October 24, 1990); and Citizens' Committee Chairman Zdzislaw Najder told a US audience that Balcerowicz would remain in his post should Walesa win (Radio Warsaw, October 30, 1990, 7:00 P.M.).

12 Quoted in Marian Strzelecki, "Five Government Concepts," *Rzeczpospolita*, November 12, 1990.

13 In an interview with *Gazeta Wyborcza*, published in full on November 3-4, 1990.

14 "Don't Burn the Last Bridge," *Gazeta Wyborcza*, November 12, 1990.

15 For more on the Micewski group, see Louisa Vinton, "A New Team for Walesa," *Report on Eastern Europe*, no. 41, October 12, 1990.

16 For Kurowski's proposals, see Tomasz Roguski, "A Program for Walesa," *Rzeczpospolita*, October 29, 1990; "Center Alliance—Draft Economic Program," *Rzeczpospolita*, July 16, 1990; and "Center Alliance," *Gazeta Wyborcza*, July 23, 1990.

17 In *Konfrontacje*, November 1990. See also the interview with another economic adviser on the Micewski team, Wladyslaw Balicki, in *Slowo Powszechne*, October 12-14, 1990.

18 *Polityka*, November 3, 1990.

19 Radio Warsaw, November 9, 1990, 7:25 A.M.

20 Pawel Smolenski, "What They Are Applauding," October 31–November 1, 1990.

21 Zdzislaw Malinowski, Solidarity leader in the Kujawy region, in an interview with *Zycie Warszawy*, November 14, 1990, quoted by Radio Warsaw, November 14, 1990, 7:00 A.M.

22 The last state polling service poll conducted before the elections (November 19 and 20) showed that 38% of those planning to vote intended to cast their ballots for Walesa; 23% for Mazowiecki; 17% for Tyminski; 6% for "leftist" candidate Wlodzimierz Cimoszewicz; 5% for Peasant Party leader Roman Bartoszcze; and 2% for Confederation for an Independent Poland (KPN) chief Leszek Moczulski (PAP, November 22, 1990).

23 At election rallies in Wloclawek on October 27 and Kalisz on November 12, as reported by Radio Warsaw, October 27, 1990, 7:00 P.M.; and PAP, November 12, 1990.

24 For Tyminski's remarks in Zakopane, see PAP, November 17, 1990. On the press conference, see PAP, Reuter, and AP, November 20, 1990.

25 See, in particular, the interview with Jaroslaw Kaczynski in *Frankfurter Rundschau*, October 29, 1990.

26 Quoted in Jagienka Wilczak, Marian Turcki, "Always on the Attack," *Polityka*, September 29, 1990.

# The Economy a Year after Price Liberalization

Nancy J. Cochrane\*

*One year after price liberalization in Poland, the lines in front of food shops have disappeared and food supplies seem adequate. Institutional rigidities continue, however, to hamper Poland's transition to a fully functioning market economy. The agricultural sector faces a particularly serious situation, with low procurement prices, mounting surpluses, and real difficulties in marketing those surpluses. One of the reasons for the surpluses is reduced consumer demand, but an equally serious problem is the lack of developed, private marketing channels.*

Some profound changes have taken place in Poland in the year following the liberalization of retail prices in August 1989. Lines in front of stores have disappeared, and small private businesses are springing up everywhere. While real income has dropped significantly from its January 1990 level and gross output may have declined by as much as 20%, there is little evidence of dire poverty. People appear well-fed, and their mood is generally optimistic.<sup>1</sup>

Although supply seems to have met demand in the retail trade, the same cannot be said for primary agricultural production. The agricultural sector is now characterized by low procurement prices, mounting surpluses, and angry farmers. If these conditions persist, there could well be a severe contraction of the farming sector. It may be that market forces will dictate some contraction, as the agricultural share of Poland's national income (15% in 1988) is much larger than it is in the developed West. But, because of continuing institutional rigidities in the Polish economy, there is a danger that this contraction will be more severe than it would be under better conditions.

What has emerged in Poland could be described as "petty capitalism." Establishing a fully functioning capitalist system will be far more difficult, and several factors threaten the process. Some of these are beyond the Polish government's control: the Gulf crisis and the deepening chaos in the Soviet Union, for example. Furthermore, the social dislocations the economic reforms will cause are only beginning.

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## The Emerging Market

There is abundant evidence of private economic activity on the streets of Warsaw. Fruit and vegetable stands have sprung up on any sidewalk large enough to hold them. The square in front of the Palace of Culture is crowded with vendors selling all manner of goods—clothing, shoes, radios, watches, small appliances, tires and other automobile parts, tools, and even fur hats from the Soviet Union. At one end of this square is a row of trailers loaded with sides of meat ready to be carved at the customer's request. These trailers are apparently sufficient to meet recently imposed regulations requiring that meat be sold from structures with four walls, running water, and a nonporous cutting surface.

What one does not see are privately run butcher shops. Private shops are appearing everywhere in Warsaw, but these tend not to be food stores, which in fact are still controlled by the same cooperatives and state enterprises that ran them in the past. Although the long lines and barren shelves of two years ago are gone, these stores still offer only a poor selection of goods and rather indifferent service.

Plenty of opportunity seems to exist for entrepreneurs wishing to open food shops that could compete with the state-run enterprises, offering lower prices and better service. So far, however, people have not availed themselves of this opportunity. Approximately 30% of the pork that is sold at present is marketed through private channels,<sup>2</sup> but almost all of that 30% is sold directly by farmers in markets like the one at the Palace of Culture. There is currently little interest in investing in such enterprises as private meat-packing plants and butcher shops.

Two reasons for this are Poland's underdeveloped banking system and the fact that the program launched by Minister of Finance Leszek Balcerowicz

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in 1990 has imposed strict credit limits. Major investments are, of course, very difficult without functioning capital markets. But there is evidence of discretionary income in Poland that is being invested in luxury items such as large houses and new Mercedes. The problem appears to be mobilizing this money for investments such as small private food concerns.

It may be that what is needed most is time. Under communism, government attitudes toward private economic activity were unpredictable at best; and would-be entrepreneurs were reluctant to undertake large investment projects, fearing that the government might seize the profits. Money was therefore spent on consumer items and private economic activity was limited to those areas in which start-up costs were minimal, including open-air food markets, service-oriented businesses such as automobile or tractor repair, shoe repair shops and tailors, or small boutiques selling jewelry or knitwear. Habits formed over 40 years are hard to break, and it will certainly take time for people to develop enough trust in the new government to be willing to make investments that could take a year or more to begin to pay off. Institutions are also needed: capital markets, an effective communications system, a better developed legal system, government regulations, and the bureaucracy for implementing those regulations. Much of the necessary legislation is still being debated in the parliament.

#### Problems in the Agricultural Sector

In the meantime, the situation confronting Poland's farmers is rather serious. Despite all adversities, Poland had another record grain crop this year, of 27,000,000 tons. But 2,000,000 tons of that remain in storage because there are no buyers. The state-run purchasing agencies, citing the "demand barrier" at the retail level, have curtailed purchases. Dairy farmers are suffering worse problems. The dairy cooperatives in charge of purchasing are themselves in severe financial difficulty and have been unable in some cases to pay farmers for milk already delivered.<sup>3</sup> There are mountains of unsold potatoes, as traditional marketing channels have collapsed. Now farmers and ministry officials are worried about similar problems with the sugar beet harvest.<sup>4</sup>

The government has so far resisted farmers' demands for higher minimum price levels. It has introduced limited subsidies for improving soil fertility and developing high-quality seeds and breeding stock. Low-interest credit is also available for the purchase of farmland. But all this support goes to the larger, more efficient farms. Officials of the Ministry of Agriculture and agricultural

research institutes maintain that the real problem with Polish farming is high production costs. They argue that many farms are too small to be economically viable and are very inefficient. They advocate the consolidation of these small farms into larger units. The hope is that the less successful small farmers will be pressured into selling out and leaving farming altogether.

To an extent, this reasoning is valid. Some of Poland's farms are clearly too small to be viable. The clearest case is the one- and two-cow dairy farm, where one can see a farmer milking his two cows by hand in the field and transporting the cans of milk on his bicycle to the procurement center. No consumer is willing to pay the higher price it would take to make the farm profitable. Other small farms are doing well, however, such as some of those specializing in fruit production. Furthermore, some of the larger farms, which the government has been encouraging, are also in trouble. The small hog farmer, for example, can bypass the state purchasing system and sell his hogs directly on the streets of Warsaw. But it is more difficult to sell 100 hogs that way. Particularly hard hit are those farmers who recently invested heavily: interest rates for credit were as high as 48% a month at the beginning of 1990.

There is a danger under the current conditions that the wrong farmers will be forced out of business. There is no reliable evidence on which to evaluate the efficiency of farms. Although Polish researchers have conducted numerous studies on production costs and concluded that they were too high, they based their research on conditions under communism. Those costs were calculated using distorted prices and cannot be used as accurate indicators of efficiency.

Furthermore, if small farmers are going to give up their farms, they need some alternative source of livelihood. With industrial unemployment rising, part-time farmers see their farms as their sole source of economic security. Government officials are aware of this problem and plan to emphasize the development of nonagricultural rural industry. They also hope that many of those leaving farming will be able to earn a living by providing badly needed services to those remaining in the sector. But it will take time to develop alternative sources of employment.

It is not clear whether Polish experts have focused on the most serious problem. The market will ultimately identify the efficient farms. At present, however, the market that is providing negative signals to so many farmers is still an imperfect one. One of the most serious impediments to the advancement of Polish agriculture is the lack of developed, private-marketing channels.

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Approximately 80% of marketed food products are still sold through state channels. Available evidence suggests that these state enterprises are still acting like monopolies.<sup>5</sup> The central apparatus that controlled the activities of these organizations has been dismantled, but what has emerged instead is localized monopolies. They are reacting to high processing costs and the elimination of government subsidies by cutting back on production to preserve their profit margins and are therefore purchasing less from the farmers. At present, a farmer's only alternative is to sell his produce himself, directly off the back of his truck. The costs of this type of marketing (in terms, for example, of the farmer's time and the cost of fuel to transport the produce) are obviously quite high.

#### The Comparative Advantage of Polish Agriculture

Despite this year's exportable wheat surplus, Polish economists generally agree that Poland's comparative advantage lies in livestock production rather than grain production. Because of the poor quality of most Polish farmland, the general belief is that Poland should not be striving for grain exports. Polish analysts also note that there is a potential for developing the pork sector.

In the short term, however, the development of an internationally competitive livestock sector is constrained by the lack of good-quality feed. Through the 1980s there was a shortage of protein in feed rations. All soy meal must be imported, and imports have been limited by the shortage of hard currency. The rapeseed crop offers some potential, but in recent years Poland has ended up exporting large amounts of rapeseed because of a shortage of crushing capacity. This year, the protein deficit is even more acute. Because the price of feed concentrates is no longer subsidized, demand on the part of farmers has fallen precipitously. This year's soy meal imports are down considerably. One estimate from the Institute for Agricultural and Food Economics in Warsaw places 1990 soy meal imports as low as 300,000 tons, down from more than 1,000,000 tons in 1989. Farmers are feeding their livestock grain (grain supplies are more than adequate), potatoes, and skimmed milk—commodities whose prices on domestic markets are depressed.

For this reason, Polish economists place greater hope (at least for the short term) in more labor-intensive lines of production. Examples given include fruit, vegetables, and other specialty items, together referred to as "boutique agriculture." Analysts also suggested that Poland could specialize in "healthy foods," that is, produce grown without chemicals; this would turn the shortage of agricultural

chemicals into an advantage. They have been quick to point out that despite the notorious pollution in the southwestern part of Poland, two-thirds of Poland's agricultural land is virtually free of any pollution.

But the question that always comes up is where to find foreign markets. The lack of foreign markets has been considered the greatest limiting factor in the potential development of Poland's pork production. The largest market at present for Polish pork is the United States, which accounts for most of Poland's sales of canned ham. The other major market is the Soviet Union. No one seems to believe that there is much chance for growth in the US demand for ham. And the Poles are truly worried about the growing economic chaos in the Soviet Union. There is real doubt as to whether the Soviets will have the means to pay for imports.

The most serious obstacle to expansion, say Polish experts, continues to be the barriers erected by the European Community (EC), which is the main market envisaged for the "boutique agriculture." Despite the economic aid that has been provided by the EC and the recent trade agreement between the EC and Poland, EC markets are as difficult to penetrate as ever. Polish strawberry exports to the EC are illustrative. Polish strawberries are said to be of better quality and cheaper to produce than those produced in the EC area. But the EC has decided to implement a minimum price of \$2,000 a ton for imported strawberries, compared with the EC price of \$1,500.

#### The Future of Polish Agriculture

Most productivity indicators show Poland lagging behind the EC by between 30% and 50%. Model results obtained in this branch were based on the assumption that Poland could close this gap by at least half by the mid-1990s.<sup>6</sup> Because of the poor quality of Polish soil, grain yields may never reach EC levels. Livestock productivity could, however, certainly increase enormously. The limited subsidies recently introduced by the Polish government are specifically aimed at boosting productivity.

However, with procurement prices as low as they are, Polish farmers have no incentive to strive for such productivity gains. The efficiency of feeding practices, for example, will almost certainly be lower this year, because farmers do not find it economical to use high protein feed concentrates and are relying instead on traditional feeding practices. As long as procurement prices remain low, one cannot hope for much gain in productivity. The depressing effect of the "demand barrier" on prices will not disappear in the near future; consumer demand will continue to be constrained by

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falling real incomes and the penetration of foreign markets will continue to be a problem.

Despite these difficulties, the agricultural and food production sectors of the Polish economy are in far better shape than those of Bulgaria and Romania. There are ample food supplies in Poland, which cannot be said of those two countries. Poland's situation could improve still more with the demonopolization of the processing and distribution sector. If intermediate costs could be

lowered, then demand could be stimulated at the retail level, as more goods were offered at lower prices. At the same time, competition should help increase the prices paid to producers, giving them an incentive to raise productivity. Otherwise, Poland's agricultural sector will shrink and its products will be competitive only because of cheap labor.

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November 12, 1990

## Notes:

1 The conclusions reached in this paper are based on interviews with Polish government officials and researchers and the author's personal observations on a recent visit to Poland.

2 This is a rough estimate by economists at the Institute for Agricultural and Food Economics in Warsaw. No one knows exactly how much is being marketed through private channels.

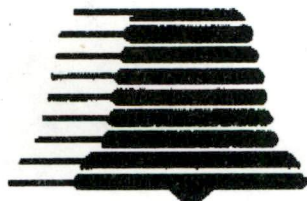
3 For further discussion of the problems of Polish dairy farmers, see Karen Lemiski, "The Settlement of the Agricultural Protests," *Report on Eastern Europe*, no. 37, September 14, 1990.

4 *Gazeta Wyborcza*, no. 214, September 14, 1990, p. 2.

5 As evidence of the continued monopolistic status of these enterprises, results of research conducted at the Institute for Agricultural and Food Economics in Warsaw shows that overall profits in the food-processing sector actually rose during the first half of 1990, even

given the elimination of subsidies and falling consumer demand. Also, there are huge variations in prices from one region to another. For example, procurement prices for milk in the month of July ranged from 461 zloty to 694 zloty a liter.

6 This is the conclusion reached in Nancy J. Cochrane, *Trade Liberalization in Yugoslavia and Poland*, Agricultural and Trade Analysis Division, Economic Research Service, U.S. Department of Agriculture. Staff Report No. AGES 9058. This study presents the results of a model that simulated the effects of economic reform on Polish agriculture. The results suggested that with the removal of the barriers insulating Polish producers and consumers and productivity gains averaging around 20% for all commodities, Poland could become a significant net exporter. According to the results, the country would be exporting large amounts of pork but would continue to import grains and oilseed products.



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## Mazowiecki's Year in Review

Anna Sabbat-Swidlicka

*Poland began 1990 with an established and popular Solidarity-led government intent on implementing an ambitious program of political, economic, and social reform that was to lay the foundations for an independent, democratic state and a functioning market economy. In spite of its many notable achievements in both of these areas, the government gradually lost touch with a significant part of its supporters among the political elite and the broader public. Solidarity leader Lech Walesa's challenge to the government he had originally helped to power resulted in new presidential elections by general suffrage and Walesa's accession to the Presidency with a pledge to speed Poland's transition to democracy.*

**I**n 1990 Poland left communism behind and began to implement a complex program of building democratic institutions and a market economy on the ruins left in its wake. The country entered 1990 with its precommunist name and coat of arms and a rump constitution that had discarded most vestiges of the communist system. Although it was still burdened with a head of state who represented the forces of the old system and a parliament whose composition reflected a prearranged distribution of seats that guaranteed the Communists and their allies a majority, Poland could boast a Solidarity-led government that enjoyed broad public support. This government, led by the Catholic intellectual and former Solidarity adviser Tadeusz Mazowiecki, had taken over from the Communists in September 1989. By the beginning of 1990 it had already been able to restore respect for human and civil rights, take over the economy, draw up plans

to combat inflation and create a completely new economic infrastructure, and define policies and priorities in all branches of government.

### **Mazowiecki's Achievements**

In the course of 1990 Mazowiecki's government made much progress on the road to democracy and economic rationality. Mazowiecki conceived of his government as a team that would pull together in order to put the country on the right track rather than having each minister pull in his own direction in defense of particularist interests, as had all too often been the case in the communist past. While each minister was responsible for defining policies and priorities within his own sector, they were all bound to proceed in accordance with three cardinal rules: the rule of law, gradual change, and the primacy of economic reconstruction in determining government priorities. Despite the fact that the

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government included some political appointments. Mazowiecki was able to create a disciplined and professional institution whose smooth functioning and efficiency made it a credible part of the new democratic order.

**Building a Market Economy**

The government's first priority was to halt inflation and lay the legal and institutional foundations for a market economy. The Government's Program for Changing the Economic System, devised by Finance Minister Leszek Balcerowicz with the support of the International Monetary Fund and the World Bank, went into effect on January 1. It prescribed a quick but painful leap into a market economy. Within the first two months Balcerowicz had succeeded in stabilizing and achieving the full convertibility of the Polish currency; reducing the monthly inflation rate to single figures; balancing the budget; and eliminating shortages on the domestic market. These successes were achieved at the cost of a sharp drop in the public's purchasing power, a drop in production, and the appearance of, and then increase in, unemployment.

By May the government was ready to proceed with long-term economic restructuring. All efforts were focused on the privatization of state enterprises. There was general agreement on the need for speedy privatization in order to transfer economic responsibility from the state to identifiable owners and create a capital market to ensure efficient use of the country's economic resources. The plan entailed the "small privatization" of local shops, restaurants, and service outlets that were part of large state concerns, as well as principles for the privatization of large industrial plants, which included a preliminary stage of "commercialization." The passage of the government's legislative package was delayed in the Sejm, however, because of objections raised by the workers' self-management lobby, which called for special privileges for workers of privatized enterprises, such as greater emphasis on employee ownership of entire enterprises. The package was finally passed in July. It included the establishment of a Ministry for Ownership Transformations, which has been identifying and preparing state companies for privatization. Shares for the first five companies went on sale on November 30 and there has been lively public interest in the acquisition of shares.

Among the 117 laws initiated and drafted by Mazowiecki's government in 1990 were several important pieces of economic legislation. In addition to the budget and privatization packages, the government laid the legal foundations for a stock exchange; liberalized customs regulations; introduced amendments to the bankruptcy law, the commercial code, the

banking system, and the legislation governing expropriation; and transferred part of central government resources to local government bodies.

**Foreign Policy**

The government's greatest achievement in foreign policy was the successful conclusion of a Polish-German border treaty in which a united Germany recognized the finality of the Oder-Neisse border and renounced claims to former German territories that have belonged to Poland since the end of World War II. The treaty, which was signed on November 14 but must still be ratified, safeguards Poland's security interests and creates good prospects for future cooperation between the two neighboring countries.

In 1990 Poland continued the policy begun by Mazowiecki's government immediately after it took office of introducing some balance into relations with the Soviet Union by basing them on genuine mutual interests, respect for human rights, and international law. Although establishing a workable partnership with Poland's neighbor to the east proved difficult, not least because of internal political and economic problems in the Soviet Union, some progress has been made. By the end of the year talks on the withdrawal of Soviet troops stationed in Poland had begun and Poland had joined with Hungary and Czechoslovakia in lobbying for the dissolution of the Warsaw Pact's military structures. Bilateral economic negotiations have served to redress the terms of trade at least partly to Poland's advantage, although inequities remain. The Soviet authorities finally admitted that atrocities committed on Polish officers at Katyn and other places had been perpetrated by the NKVD at Stalin's orders, helping to clear the way for better mutual relations. The Poles have also taken steps to institute direct relations with some of the Soviet republics bordering Poland. Finally, Poland has opened out to the West, in particular toward West European countries and institutions. Diplomatic relations with Israel, which were broken off under Soviet pressure after the Israeli-Arab war of 1967, have been restored.

**Changes in the System of Justice**

Many changes were also made in the course of 1990 in the system of justice. Judicial independence was boosted by the removal of ideological references from the oath of office, a new system of appointments, the establishment of a National Judiciary Council and judges' conventions as self-governing institutions, and the election of a new Supreme Court. A new generation of voivodship court chairmen also replaced the old guard of

*nomenklatura* officials. The first stage of a nationwide reorganization of the courts has been completed. It included the establishment of 10 appeals courts and the takeover by the Justice Ministry of the misdemeanor courts, which had served under communist rule as a means of repressing independent democratic activity.

The central Prosecutor's Office, which had, in the past, been unofficially linked with the Ministry of Internal Affairs, was disbanded and its tasks taken over by the Justice Ministry. All voivodship and local prosecutors were subject to rehiring according to purely professional criteria. Many of the more notorious prosecutors were retired or not rehired. The prisons' administration was reformed and steps were taken at least to humanize conditions in Poland's outdated prisons and detention centers. Amendments were made to both the civil and criminal codes to remove the more glaring vestiges of communist ideology (such as the provisions meant to defend the communist political, social, and economic systems) and to bring them into line with the changed political and economic conditions.

#### **The Police and the Army**

1990 also saw the beginnings of change in the police force and army, the two redoubts that had been left in the hands of the Communists by the April 1989 round-table agreements between representatives of the communist establishment and the democratic opposition movement. The Ministry of Internal Affairs remained closed to outside influence until March, when the Catholic journalist Krzysztof Kozłowski was appointed a deputy minister to General Czesław Kiszczak. The communist-run police force was allowed to set its own house in order. In the course of this process, many police archives were secretly destroyed. In May the Sejm passed a package of laws that reorganized the police along nonideological lines. The security police was abolished and replaced by a State Protection Office. A strict screening process weeded out many, though not all, of the old regime's security forces. The regular police force was reorganized to concentrate on fighting crime, rather than defending the political order. Public criticism of the incompetence of the police in combating a rising crime wave was countered by police complaints that they are hampered by a lack of personnel and resources. It was not until July 1990 that Kozłowski took over from Kiszczak.

The process of depoliticizing the army also had a delayed start. Although the Main Political Board was abolished as early as November 1989, political party membership was banned, and ideological indoctrination was replaced by emphasis on patriotic values and traditions, the very nature of the army

as a closed institution forced the government to rely on existing structures and cadres to implement reforms. Most of the top commanding officers were retired or replaced by a younger generation of officers. Two deputy ministers from Solidarity were appointed in April 1990 to deal with educational matters and international military relations. In July, the old guard communist Defense Minister General Florian Siwicki was replaced by Rear Admiral Piotr Kolodziejczyk. After this, internal organizational changes received new impetus. The army's territorial organization is to be reorganized and units are to be redistributed the better to protect Poland's security interests. In particular, units will no longer be concentrated on Poland's western border, as had been dictated by Soviet military interests, but will also be deployed on Poland's previously largely undefended eastern border. Defense Ministry officials have begun cultivating official relations with the North Atlantic Treaty Organization as ties with the Warsaw Pact's military structures are successively loosened. Ministers of religion have returned to military units, and the military as a whole is taking a greater part in national patriotic and religious events. There are plans to institute a soldiers' rights spokesman who would help to ensure the humanization of conditions within the army.

#### **Reform of the State Administration**

Mazowiecki's government also prepared and introduced an important reform of the state administration. The state's 49 voivods were directly subordinated to the central government. In the course of 1990 most of the voivods were replaced with individuals enjoying authority and the support of their local communities. The system of people's councils that had served under communist rule as a facade concealing the real nature of "people's power" was abandoned and replaced with a system of genuine local self-government. This program of decentralization endowed the basic local administrative units with legal status, fiscal autonomy, and responsibility for ensuring local services. In May 1990, the first free local government elections since before World War II put local matters into the hands of local communities. Since then, many of them, particularly those in the underdeveloped parts of Poland, have experienced serious difficulty in coping with their new responsibilities, primarily as a result of insufficient funding, while others have exploited the new possibilities to promote local economic activity and release social initiative.

#### **Problem Issues**

In spite of the government's undeniable achievements in laying the foundations for a democratic

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political system and a functioning market economy. The substantial public support it had initially enjoyed was gradually eroded. The extent to which Mazowiecki and his team had lost the public's confidence only became apparent in the course of November's presidential elections, in which Mazowiecki won only 18% of the vote in the first round, coming third behind Solidarity leader Lech Walesa and the unknown Stanislaw Tyminski, who claimed 40% and 23% respectively. Mazowiecki's defeat appears to have been caused not by any specific errors of policy but by a general climate of disaffection aggravated by the government's inflexibility on certain politically or socially sensitive issues. This irritated a large part of the public and alienated many of Mazowiecki's former political allies.

Not all of the government's political and economic decisions were unanimously approved as the Poles began to experience both the benefits and the drawbacks of democracy and capitalism. The willingness of the public to accept sacrifices declined as living standards fell and unemployment grew. Although it was common knowledge that the move to a market economy would entail a period of hardship and the government's economic experts had predicted the high social costs involved, not all of the various social and professional groups proved to be equally resilient. Many people were concerned that the drop in production, which was steeper than had been generally expected, would prevent the hoped-for upturn in the country's economy. The fact that production in the private sector was on the rise and that the downward trend in the state sector had slackened off by the end of the year failed to dispel the growing pessimism among some sections of the population.

#### The Farming Lobby

In particular, Poland's private farmers felt that they should have had a better deal. After having successfully resisted collectivization and continued, for so long and against all odds, to supply a large proportion of the nation's food requirements, peasant farmers had hoped that the advent of capitalism would finally enable them to make a good living from their farms. They believed that agriculture should be treated as a priority sector of the economy and supported with special state subsidies, as is the case in many of the European Community member countries. They wanted preferential credits that would allow them to invest in their farms. They hoped that the old state monopolies in the procurement, processing, and distribution spheres would be instantaneously dissolved and that they would be able to sell their produce at profitable prices. Finally, they counted on a reorientation of industrial production

in order to ensure adequate supplies of the means of agricultural production at prices they could afford.

The Balcerowicz Plan guaranteed none of these things. Instead, it was content to lay the foundations for a system of economic mechanisms that would, in time, automatically begin to regulate all these problems. At the same time the Balcerowicz Plan imposed strict anti-inflationary measures in the belief that conquering hyperinflation was a precondition for any successful systemic change, and peasant farmers were expected to shoulder the burden on a par with other parts of the population. The farmers seemed to feel the squeeze particularly painfully. They pointed to their tight household budgets, which were based not on weekly or monthly incomes but on their not always predictable seasonal harvest, and to the lengthy agricultural production cycle that often made essential loans unaffordable. They stressed the crucial importance of agriculture to the economy at large. They accused the government of planning to force the small family farm out of existence in favor of "farmerization," or the creation of larger, mechanized, and more efficient farms. They lambasted Mazowiecki's team as an "antipeasant" government. Some farmers ran down or disposed of their stock. In June farmers from the Clechanow area occupied a state dairy, demanding guaranteed minimum prices, guaranteed acceptance of all milk delivered regardless of quality, and payment for the previous month's deliveries. The threat of police intervention was only averted by the timely mediation of Lech Walesa. A few weeks later farmers occupied the Ministry of Agriculture in Warsaw. This time the demonstrators were forcibly evicted by the police.

These incidents caused much bad blood. They forced the resignation of Minister of Agriculture Czeslaw Janicki, led to a political impasse over who should succeed him, and ultimately prompted the Polish Peasant Party to withdraw its support for Mazowiecki's government. Although in subsequent negotiations with farmers' representatives the government made a number of concessions to the farmers' demands, it refused to compromise on the principles of its economic policy. It earmarked some 500 billion zloty for modernizing the dairy industry and an additional 300 billion zloty to cover indemnity payments and cancel outstanding debts. It also speeded up the creation of the Agricultural Market Agency. This agency, which was operating in time for the grain harvest, was set up to stabilize prices through government purchases and sales. These positive developments failed to win the farming lobby over to Mazowiecki's policies; the damage had already been done, and they remained a resentful group.

### Other Discontented Groups

Another group that found the burdens of the transition to a market economy too hard to bear and demanded state intervention was that financed from the state budget, such as municipal service employees, teachers, and nurses. The transfer of responsibility for local services to the local government authorities caused problems in a few cases when the new authorities, required by the law to be self-financing, simply lacked the funds to pay the wages of such employees. It was only after the victims had resorted to strike action that the central government stepped in to bail out the local authorities. Other groups became dissatisfied as the government's steep tax on enterprises that paid out wage rises in excess of a certain percentage of the inflation rate began to bite. Poland's miners, who had for years enjoyed special benefits and wages well above the average on account of the hazardous conditions of their work and their important position in the economy as the country's most important source of export income, also went on strike to protest the gradual erosion of their privileges. The previously privileged skilled workers from the giant industrial plants, who had been preferred by the communist state for ideological reasons, also began to see their group interests threatened insofar as they perceived themselves as the most likely targets of future unemployment.

### The Round-table Anachronism

Perhaps the most serious political failing of Mazowiecki and his team was their apparent inability to respond to the collapse of the communist party by discarding as an anachronism the round-table agreement that was signed in April 1989 between representatives of the "constructive opposition" within Solidarity and the communist political establishment. That agreement had guaranteed the Communists and their allies 65% of the seats in the Sejm and *de facto* also the post of President in exchange for the opposition's access to official institutions. The subsequent course of events, starting with the opposition's impressive showing in the parliamentary elections of June 1989, gradually transferred the initiative to Solidarity as communism disintegrated. The Communists' cooperation with a Solidarity-led government had originally been bought with the promise that the Communists would have sole responsibility for internal and external security matters. By the time Poland's neighbors in Central and Eastern Europe had rid themselves of communism and the Polish party had dissolved, however, many people no longer saw the need to continue a purely political arrangement that had been made in a different set of domestic and international circumstances.

The fact that the discredited General Wojciech Jaruzelski was still head of state and the continued presence in the government of Kiszcak and Siwicki were particularly galling. Many people were not convinced that the reform of the police and the army was genuine. They were concerned that both institutions remained impervious to public scrutiny. Such misgivings were fueled by a number of disquieting incidents involving the Ministry of Internal Affairs, such as the clandestine destruction of police archives and the appointment to a top advisory post of an individual who was subsequently identified as the head of a group of security police provocateurs. Many people also felt it was pointless to stand by security commitments that appeared to be simply political anachronisms, such as the continued stationing of Soviet troops in Poland. The government seemed to be lagging behind developments when it finally reversed its policy in this respect in August 1990 and took the first steps to negotiate the troops' withdrawal from Poland.

### The Nomenklatura and its Assets

Mazowiecki's government was also criticized for failing to deal decisively with the old communist *nomenklatura* networks that have, in some areas, survived the collapse of communism and even seem to be thriving in the new conditions. Mazowiecki's "no witch-hunts" philosophy was applied in the government administration, the economy, education, and the media. It provided that no one should be removed from his post or deprived of his benefits on grounds of previous party affiliation alone and that everyone be given an equal chance to prove his or her professional competence and loyalty in the changed circumstances. Inevitably, this meant that the more able or shrewd of the old guard seized the opportunities available to them and made use of their resources, positions, or contacts to set themselves up in private business. In this way, so-called *nomenklatura* corporations mushroomed in the first few months of Mazowiecki's tenure. In at least one case, workers found themselves facing the prospect of being employed by discredited former communist ministers. Initially, the government's insistence on abiding by the law at all costs prevented it from dissolving such corporations unless there were strict legal grounds, such as embezzlement or undervaluation of stock, for doing so.

The public was also scandalized by the communist party's stubborn attempts to hold on to the considerable wealth that it had managed to acquire, mostly unlawfully, over its 45 years in power. The government had originally intended to allow the Polish United Workers' Party and its affiliated youth and public organizations, as well as the other satellite parties it had tolerated, to keep those of its

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assets to which it could prove a legal title. It had planned to dismember the party's vast RSW publishing concern but allow the party to keep some of its newspapers and effects. These precepts were criticized by some of Mazowiecki's own supporters and a large part of the public, whose sense of justice demanded that the party be deprived of all its assets and means of activity. Nascent independent political groups and parties, which were starting up with no funds, resources, or office space, also considered themselves to be at a disadvantage with regard to their former oppressors. It was only after the government had discovered that the party's negotiators were acting in bad faith and that new *nomenklatura* corporations were being set up behind its back even as talks were in progress that it gave way to public pressure: it liquidated the RSW empire and broke its own cardinal rule by retroactively invalidating the newly established press corporations. The government's hesitancy to resort to decisive methods in such situations caused it to lose public credibility.

#### The Media

The government was also faulted for its policy on the broadcasting media, which are still overwhelmingly under state control. Although the government's legislation on radio and television and on communications makes way for private broadcasting, this is hardly off the ground, while the government's plans for breaking up the discredited and unwieldy state-run Radio and Television Committee have been challenged by both journalists and politicians. While reform of that "Augean stable" would have been a difficult task for anyone, the intellectual Andrzej Drawicz seems to have been unable to achieve the media breakthrough that the public had hoped for after the collapse of communism. Changes in form, style, and personnel were slow and incomplete; although formal censorship disappeared, neither the old generation of journalists nor the newcomers were able to create a credible, professional, and independent, as well as popular form of communication.

#### Tactical Errors

By February 1990 calls for change were being publicly aired. There was talk of holding fully free parliamentary elections that would endow the country with a representative and respected legislative body. There were calls for the replacement of Jaruzelski, who was seen as a discredited symbol of 45 years of oppression and, more particularly, of the repressive policies of martial law that were still fresh in people's minds. The new political establishment, led by Mazowiecki and his supporters within the Citizens' Parliamentary Caucus, was not

responsive to these calls for change. It maintained that the current political arrangement was both functional and essential in order to lay the foundations for a democratic system and a market economy. It refused to consider any deviation from its chosen path of reform as a risk to the success of Poland's historic experiment. The pro-Mazowiecki Citizens' Parliamentary Caucus leadership under Bronislaw Geremek ignored critical comment from within the caucus. Warnings from Walesa in Gdansk were also rejected as interference, harmful to the joint Solidarity cause.

#### The Rise of an Opposition

The Mazowiecki-Geremek group's inflexibility in the face of criticism exacerbated latent differences within the Solidarity movement. The critical part of the Citizens' Parliamentary Caucus felt that its influence on the decision-making process was being unfairly blocked and that the political process was being monopolized by a new elite. It gradually drew closer to other dissatisfied groups: the fledgling political parties that had remained outside the round-table negotiations and found themselves outside the parliament, as well as to the social groups hardest hit by the government's economic stringencies. By May Walesa had decided to stand at the head of a broad opposition movement whose core was formed by the recently created Center Alliance coalition of political and social forces. Walesa's supporters initially believed that the removal of Jaruzelski from the Presidency and his replacement by Walesa as an activist President would provide an impetus to Poland's democratic transformations. It had not been their intention to topple the Solidarity-led government but simply to prod Mazowiecki's government in the right direction and defuse public criticism until the foundations of the new system were in place.

Mazowiecki and the supporters of his government's philosophy rejected this approach. By July they had established a rival political coalition called the Democratic Action. Both of these groups aimed to be broad social movements rather than political parties; but whereas Walesa's coalition was committed to the development of a multiparty system in Poland, Mazowiecki's group believed that, in the current circumstances, Poland required a broad public consensus rather than a proliferation of weak and fractious parties. The Solidarity union gave its backing to Walesa, but the union that emerged from its second national congress in April 1990 had already lost many of its original leaders and advisers and was no longer the national force it had been in 1980 and 1981.

### The Struggle for the Presidency

Mazowiecki's decision in October to challenge Walesa for the Presidency meant that the conflict had developed into a full-blown struggle over the best strategy to be pursued in order to attain goals that were common to both sides. It all but excluded the possibility of a Walesa-Mazowiecki tandem after the elections. The sudden appearance of the unknown outsider Tyminski and his strong showing in the first round of the presidential elections brought home to both the antagonistic camps, as well as to the other aspiring political forces, the extent of the public's alienation from the political process underway in Poland, the gulf separating the new elites from the masses, and the risks still menacing the nascent democracy. Indeed, the risk to the future of democracy in Poland was considered so great that even the Roman Catholic Church hierarchy, which had withdrawn from the front-line of politics in the course of the year and had insisted on keeping its neutrality in the first round of the elections, saw fit to warn the nation of the impending danger. Walesa's 74% victory over Tyminski in the second round suggests that the majority of the Polish public was sensitive to the dangers, but Tyminski's 25% remains as a warning for the future.

Mazowiecki treated the results of the first round as a public vote of no confidence in his policies and announced his resignation, together with that of his entire government. With hindsight it is possible to discern four reasons for his defeat. First, he and the supporters of his gradualistic and legalistic philosophy were so committed to their political program that they considered it both exclusive and untouchable. Their rejection of any compromise made them vulnerable to the charge of inflexibility. Second,

they proved unable to share power, forming a closed, narrow group that left even those who should have been cultivated as political allies largely out of the decision-making process. Third, their reaction to criticism was excessively defensive and also slow. By the time they had reacted, many of the critics had become alienated. Finally, they were very weak as far as propaganda and public relations were concerned. They seemed unable to sell their undoubtable achievements to the public as reasons for national pride and enthusiasm and to make propaganda capital out of those few issues on which they were forced to compromise by public opinion or the logic of events.

Walesa's accession to the Presidency and the appointment of a new government mark the end of an experiment in which a respected but relatively closed elite tried to implement a generally accepted reform program by appealing to the masses for total confidence and support in the name of the Solidarity ethos. The termination of this particular experiment does not signify the failure of the entire undertaking nor does it negate the considerable progress already made by today's political losers. Rather, it signifies a new approach to the same set of problems, one that would preserve the goals and programmatic principles while paying more attention to the broader public and involving its political representatives in the decision-making and opinion-forming processes. The lessons of 1990 in Poland are that democracy cannot be steered by any group, however talented and trustworthy, and that room must be left for spontaneous initiative and criticism in any attempt to create social justice, political stability, and economic prosperity.

PO0533.90R

December 10, 1990



## Walesa's First Challenge: State Workers Reject Anti-Inflationary Wage Controls

Louisa Vinton

*Protests are mounting against the Polish government's main anti-inflationary tool: the tax on excess wages, known as the "popiwek." State workers charge that the tax, from which private firms are now exempt, is discriminatory and hinders production. The government has countered that under Polish conditions higher wages fuel inflation without stimulating economic growth; moreover, only private owners have a real incentive to pursue rational wage policies. This conflict is the first test of President Lech Walesa's ability to balance the demands of economic reform with public dissatisfaction.*

Virtually from the moment of their confirmation in early January, Polish Prime Minister Jan Krzysztof Bielecki and his government have been under siege from state workers demanding wage increases. State workers' dissatisfaction has centered on the "popiwek," the tax on excess wages that the government has used to limit the flow of money onto the market and thus to control inflation. Workers in several state firms have declared strikes in an attempt to force the government to relax wage controls. The former pro-communist trade union federation (OPZZ) has made a hard-line stance on the "popiwek" its rallying point, threatening a general strike should the government fail to withdraw the tax completely. The government's negotiations with the Solidarity union, whose approach to the tax, although critical, is less confrontational, have likewise reached an impasse.

The "popiwek" conflict has expanded beyond the immediate taxation issue into a protest that calls into question the government's entire program for economic reconstruction. The government is thus defending the "popiwek" for both economic and political reasons. Wage increases cannot "artificially" improve living standards, the government has argued. Until efficiency-enforcing changes in ownership are effected, higher wages in state firms will merely foster higher prices, thus fueling an inflationary spiral that could obliterate the economic stabilization so painstakingly achieved in 1990. In political terms, the government views the state workers' acceptance of wage controls as a measure of the public's willingness to endure the disruptions required to create a working market economy.

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**The "Popiwek"**

The bill governing the 1991 tax on excess wages (the tax's formal title in Polish is *podatek od ponadnormatywnych wyplat wynagrodzen*, but popular wisdom has shortened it to "*popiwek*," whose literal meaning has the ring of "after the beer") was the last piece of legislation considered by the parliament in 1990. In introducing the bill to the Sejm, Leszek Balcerowicz, the Finance Minister and Deputy Prime Minister in both the previous and the current governments, made an urgent appeal for its rapid passage, warning that the lack of a mechanism to block wage growth would prompt a burst of renewed inflation at the beginning of 1991. Acceding to Balcerowicz's request, the Sejm approved the bill on December 22, 1990. President Lech Walesa signed it into law on January 2, 1991.<sup>1</sup>

Like the excess wages tax in force in 1990, the 1991 version of the "*popiwek*" imposes a punitive tax on firms that increase wages above a threshold set by the government.<sup>2</sup> This limit is defined as a percentage of the monthly increase in retail prices. For January and February 1991, the government set this threshold at 60% of the rise in prices. Firms that exceed this limit by more than 5% must pay a 500% tax on the sum of excess wages; by 3-5%, a 200% tax; and by up to 3%, a 100% tax. By imposing such steep penalties, the excess wages tax is designed to prevent wages from growing faster than prices, and thus to stifle inflation.

The 1991 tax has been liberalized to exclude both private firms and firms undergoing privatization in which the state owns less than half of the shares. The only exceptions to this rule are private firms enjoying a monopoly position on the Polish market. The 1991 law also extends graduated relief from the tax to "commercialized" firms, that is, those that have qualified for privatization and been transformed into treasury-owned joint-stock companies. The underlying assumption here was that only private owners have a real incentive to maximize profits and minimize costs, including wages. State firms, in contrast, lack identifiable owners. Their managers thus tend to side with the work force and yield to demands for pay raises instead of protecting their firms' financial well-being, on the assumption that the state budget will in the end provide subsidies to save them from bankruptcy. In sum, then, the 1991 excess wages tax completely exempts private firms while imposing stiff penalties on state firms that grant raises without a proportionate increase in profits. In this way, the government has designed the 1991 "*popiwek*" to give state firms a rough substitute for private owners and, at the same time, an incentive to seek privatization.

Changes were also made in the 1991 excess wages tax in response to criticism that the 1990 tax

had penalized profitable state firms by preventing them from rewarding their workers for increased output. Beginning in April, firms able to improve their ratio of profits to wages or to reduce their losses to levels below those of 1990 will be permitted to increase wages without suffering a penalty. The base sum from which permissible wage hikes were calculated in specific enterprises was also changed: from the total wages bill to the firm's average wage. This measure was designed to slow the growth of unemployment, as the 1990 tax had allowed firms to dismiss part of their work force and to use the funds thus saved to raise the wages of those who remained, without violating the restrictions imposed by the tax.

**The Economic Controversy**

The 1991 excess wages tax is an unwieldy tool at best, the government has acknowledged. However, government officials have argued that in the absence of a free labor market, which would yield real-market wages as the outcome of genuine bargaining between employees and private owners, the tax is necessary. Critics have nonetheless charged that the overall economic effect of the tax is negative.<sup>3</sup> Some economists have claimed that the tax impedes Poland's recovery from the recession that resulted from the balanced budgetary and tight fiscal policies introduced at the beginning of 1990. Affiliates of the Center Alliance, for example, pressed in mid-1990 for a relaxation of the "*popiwek*," claiming that higher wages would prompt increased demand, which, in turn, would spur enterprises to step up production. Under heavy pressure from both the labor unions and the political opposition, the government of Tadeusz Mazowiecki relaxed the excess wages tax in mid-1990, but this failed to achieve the desired result.

The "*popiwek*" has also been criticized for petrifying an inefficient employment and wage structure and for transforming local wage disputes into national conflicts to which the government must react. The provisions of the 1991 law that are intended to fight unemployment, it has been argued, discourage firms from making more rational use of manpower, because the general pool of wages that is exempt from taxation gains nothing from dismissals. The end effect is hidden unemployment. The excess wages tax may thus serve a political goal, diffusing some of the public dissatisfaction that widespread unemployment could cause, but at the cost of continued inefficiency at the microeconomic level.

Balcerowicz, the architect of the economic stabilization policy originated by the Mazowiecki government, has rejected the first argument—that the excess wages tax contributes to recession—as

inapplicable to Polish conditions. He has pointed out that wages grew very rapidly in the last half of 1990;<sup>4</sup> however, despite signs of hesitant improvement in August and September, production in state firms remained stagnant. Moreover, wages continued to rise. In contrast, the private sector demonstrated rapid and consistent growth throughout 1990. Balcerowicz's conclusion: unjustified wage increases in the state sector would reignite inflation without putting more goods on the shelf. In addition, Balcerowicz argued, such wage increases would reduce the competitiveness of Polish products on both domestic and foreign markets, force an increase in interest rates, undermine the stability of the budget, and thus deepen rather than ease the recession and promote unemployment.<sup>5</sup>

Balcerowicz's conclusion seems to be borne out by Poland's lasting inability to reduce inflation to negligible levels (although end-of-year bonuses, higher oil prices, and the shift to hard-currency trade with the Soviet Union are also at fault):

TABLE

INCREASES IN RETAIL PRICES (in percentage)		
Year	Month	Increase
1990	January	79.6
	February	23.8
	March	4.3
	April	7.5
	May	4.6
	June	3.4
	July	3.6
	August	1.8
	September	4.6
	October	5.7
	November	4.9
	December	5.9
1991	January	12.7

Sources: *Rzeczpospolita*, February 2, 1991; and PAP, February 16, 1991.

The 12.7% rise in prices in January 1991, which was more than double what the government had predicted, is particularly troubling, as it threatens to upset the calculations on which the budget for 1991 has been prepared. These unfavorable results are likely to reinforce the government's conviction that stringent wage policies are still required.

#### The Political Crisis

In a climate of political stability, these issues would perhaps have remained a source of resentment without leading to an open revolt. But the

expectations promoted by Walesa's presidential election campaign, the prolonged transition to full democracy, and the prospect of imminent parliamentary elections have combined to make the "popówek" an explosive issue. State workers have come to hold the tax responsible not only for relatively low wages but for all their discomforts and fears as well. As Labor Minister Michal Bori has put it, the "popówek" has taken the place of General Wojciech Jaruzelski as the "scapegoat of Polish reform."<sup>6</sup> The tax has also become the rallying point for criticism of the government and the Solidarity establishment on the eve of the elections.

The "popówek" issue has once again shifted the focus of economic conflict from individual enterprises to the government and the national trade union organizations, putting both the new administration and Solidarity in jeopardy. With no stake in either the Bielecki government or the new economic order that the government is trying to build, the OPZZ has rejected wholesale the government's anti-inflationary rationale and demanded the immediate and unconditional lifting of all wage controls. In a series of protests and demonstrations, the OPZZ has attempted to use the issue of the excess wages tax to build up a reputation as an unequivocal opposition, most likely with an eye on the upcoming elections.<sup>7</sup> The same motivation has led many postcommunist politicians, including the leader of the Democratic Left parliamentary faction, Włodzimierz Cimoszewicz, to echo the OPZZ's arguments.

The most emotionally-loaded aspect of the conflict over the "popówek" tax is the tax's implicit encouragement of privatization. Indeed, this issue has become the OPZZ's favorite theme, although statements by OPZZ and Solidarity union activists alike have uniformly condemned the tax as a form of discrimination against state firms. The sound economic reasoning behind the exemption of private firms from the tax has been ignored. One national meeting of Solidarity union locals even cited the current constitution's guarantee of equal protection for different forms of property as grounds for repealing the tax.<sup>8</sup> In part, this resentment may result from an identification of privatization with the parasitic joint-stock companies formed by the old *nomenklatura* on the basis of undervalued state assets and bureaucratic influence. Still, the government seems to have overestimated the public's understanding of the vital importance of ownership transformations in creating a functioning market economy. One Solidarity deputy, for example, thought it a damning accusation rather than a statement of fact to charge the government with "a lack of faith in state ownership."<sup>9</sup>

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This situation has put the Solidarity leadership under pressure from its increasingly unruly membership and in danger of being outbid and outshouted by the OPZZ. The Solidarity leadership has long had difficulty in balancing its "reformist" interest in the long-term success of economic change with its "unionist" mission to defend workers' living standards. The challenge of the excess wages tax may prove a watershed for the union, whose stance has hardened in recent weeks. Indeed, Solidarity leaders have threatened that the union would reconsider its policies and might even choose to oppose the government at Solidarity's third national congress, scheduled for February 23 and 24.<sup>10</sup> In three rounds of negotiations with the government in February, Solidarity demanded that the government abolish the tax by the end of June 1991 and replace it with "different means of fighting inflation." The union also demanded that both the minimum base sum from which tax-free wage hikes are calculated and the government-set threshold for wage increases be raised immediately. Some deferred compensation, the union proposed, could also take the form of an entitlement to shares in privatized companies.<sup>11</sup>

The government has opened negotiations on only two of these points: the minimum base wage from which permissible increases are calculated, and the idea of deferred compensation through the distribution of privatization coupons. Raising the minimum wage exempt from the tax is seen as a measure that would benefit primarily those at the lower end of the wage scale. (The government has reluctantly offered to raise this minimum from 800,000 zloty to 900,000-950,000 zloty a month, while Solidarity has reduced its demand from 1,350,000 zloty to 1,200,000 zloty a month.) Negotiations continue, although both sides have begun to present their positions with a decisive note of finality.

Solidarity's tough stance is dictated by its reading of the political situation and its assessment of the depth of popular dissatisfaction. Deputy Chairman Lech Kaczynski, the chief of the union's negotiating team, argued that a recent meeting with government officials had revealed "two philosophies" in conflict: "The philosophy of what is socially possible, represented by the union, and the philosophy of economic laws, supported by the government's representatives."<sup>12</sup> "Solidarity," Kaczynski noted, "feels that society's endurance is exhausted." The government's failure to provide partial concessions on the issue of the excess wages tax, Solidarity has suggested, could provoke the total rejection of the entire economic reconstruction program.

The government has defended its own stance with similar determination. "Lifting the 'popiwek,'"

Balcerowicz told the union during the first round of negotiations, "means the collapse of public finances, the destruction of the budget, a deepening of the recession, and an increase in unemployment."<sup>13</sup> Meeting Solidarity's demands, Balcerowicz added, was the same as "agreeing to the ruin of the government's economic program."<sup>14</sup> Many government officials are clearly frustrated by their inability to convince state workers that their demands for wage increases are, in effect, self-defeating. Prime Minister Bielecki has repeatedly stressed that higher wages for state workers can provide only the illusion of improvement. If short-term popularity were the government's aim, Bielecki has said, it would have no qualms about meeting wage demands. The government's awareness of the consequences of its actions and its overriding commitment to "honesty" means, however, that this temptation must be seen for what it really is: "A road to nowhere and a short-term swindle of society."<sup>15</sup>

## Walesa's Role

The chance for a successful resolution of this conflict between the logic of economic reform and the logic of social protest seems to rest with the President. Although Walesa played on public dissatisfaction with wage controls to win support in the presidential elections, he also stressed throughout his campaign that he would use his powers and skill as a communicator to "synchronize" the government's plans with the public's needs—to ensure that free market reforms were brought to a successful conclusion. Just who was to be synchronized with whom became clearer when Walesa insisted on retaining Balcerowicz in the new cabinet and approved the formation of a government composed of liberal economists.

Walesa's stance on the excess wages tax has not been free from ambiguity. Answering a caller's question on a radio talk show on February 4,<sup>16</sup> Walesa agreed that the tax was a "bad solution" and should be abandoned as quickly as possible. As is customary in Walesa's manner of addressing the public, however, this initial gesture of respect for his listeners' views was followed by a less popular counterproposal. Raising wages was not the answer, Walesa argued, because "for the time being, there is nowhere to get the money to make things different." Instead, firms should lower their costs and increase their output, bringing down the prices paid by consumers, so that in the end "we will have our wages and live twice as well." This working man's logic is the same as the government's.

Walesa has held several meetings with Balcerowicz and Bielecki with the explicit purpose of ensuring that the President and the government speak with a single voice on economic issues.

Walesa's remarks on the "popiwek" have attempted to bridge both sides of the issue, however, and have suggested that he is trying to keep his options open. Walesa's entourage and supporters have contributed to the confusion over the President's stance and exacerbated political tension. In a statement issued on February 18, Walesa's personal committee of presidential advisers demanded that the tax be repealed and suggested that competition and market forces would quickly destroy firms that raised wages in a reckless fashion.<sup>17</sup> Needless to say, this approach would probably undermine the budget and lead to a dramatic rise in unemployment in precisely those quarters where criticism of the "popiwek" has been strongest.

Balcerowicz and Bielecki immediately questioned both the timing and the content of the

advisory committee's statement.<sup>18</sup> Walesa telephoned the government the following day to restate his support for its anti-inflationary policy and to distance himself from the advisory committee's statement, but it was left to the government spokesman to make this fact public.<sup>19</sup> The impression of presidential temporizing and reserve with respect to the issue of the excess wages tax has thus remained, along with the sense that confusion abounds in the President's Office. The debate over the tax has escalated into a question of the viability of both the government's anti-inflationary policy and the government itself. The fate of both may depend on an unequivocal public declaration by the President on the "popiwek" issue.

PO0086.91R

February 20, 1991

## Notes:

1 For the Sejm and Senate debate on the bill, see PAP, December 21, 22, and 28, 1990; and *Gazeta Wyborcza*, December 22-28 and 27, 1990.

2 For a review of the terms of the 1991 law, see the press conference given by Deputy Finance Minister Ryszard Pazura on December 5, 1990, and reported by Radio Warsaw, December 5, 1990, 4:00 P.M. and 7:00 P.M., and PAP, January 2, 1991.

3 For examples of the economic debate on the "popiwek," see the interview with Pazura, *Rzeczpospolita*, February 6, 1991; "Popiwek," *Gazeta Wyborcza*, January 4, 1991; Waldemar Kuczynski, "The Causes and Consequences of the War over the Popiwek," *Gazeta Wyborcza*, February 6, 1991; "Popiwek," *Tygodnik Solidarnosc*, February 8, 1991; Andrzej Halicki, "Liberals on the Popiwek," *Gazeta Wyborcza*, February 15, 1991.

4 Real wages rose by 4.5% in the third quarter and by 16% in the fourth quarter of 1990. These figures are quoted by former Privatization Minister Waldemar Kuczynski in *Gazeta Wyborcza*, February 6, 1991. See also Tomasz Telma and Keith Crane, "Inflation in Eastern Europe and the Soviet Union: Price Stability in Reforming Economies Remains an Elusive Goal," *PlanEcon Report*, vol. 4, nos. 50-51, December 21, 1990.

5 For Balcerowicz's arguments, see PAP, December 18, 1990, January 30, 1991, and February 5, 1991; *Gazeta Wyborcza*, February 4, 1991; and "Balcerowicz's Diagram," *Rzeczpospolita*, February 9-10, 1991.

6 From a press conference reported in *Rzeczpospolita*, February 1, 1991.

7 Some 2,000 miners participated in a protest organized by the OPZZ in Warsaw on February 14 (*Gazeta Wyborcza* and *Rzeczpospolita*, February 15, 1991). On February 15 several thousand OPZZ supporters staged a protest march against the "popiwek" in Warsaw (*Gazeta Wyborcza* and *Rzeczpospolita*, February 16-17, 1991).

8 PAP, February 14, 1991.

9 Citizens' Parliamentary Caucus deputy Jacek Szymanderski in the Sejm debate on the law regulating the excess wages tax (*ibid.*, December 21, 1991).

10 See, for example, the remarks by Solidarity Presidium member Marian Krzaklewski reported by Radio Warsaw, February 19, 1991, 7:00 P.M.

11 The government held negotiations with Solidarity on February 8, 18, and 20, 1991. For more information, see Jacek Podgorski, "The Popiwek Stays?" *Tygodnik Solidarnosc*, February 15, 1991; PAP, February 8, 18, 20, 1991; *Gazeta Wyborcza*, February 8, 9-10, 19, and 21, 1991; and *Rzeczpospolita*, February 9-10, 1991.

12 Quoted by PAP, February 8, 1991.

13 As quoted in Podgorski, "The Popiwek Stays?"

14 PAP, February 18, 1991.

15 *Ibid.*, February 8, 1991.

16 Radio Warsaw, February 4, 1991, 8:15 A.M.

17 PAP, February 18, 1991.

18 *Ibid.*

19 *Ibid.*, February 19, 1991.



## REGIONAL TOPICS

### CMEA: The End Is Nigh

Vladimir V. Kusin

*On January 5 the member states of the Council for Mutual Economic Assistance decided to dissolve that body and to create a small consultative group in its stead. Assuming that the member countries' Prime Ministers agree when they meet in February, the new body will, among other things, attend to property and payment matters related to the dissolution of the council. Some observers believe that the new body, to be called the Organization for International Economic Cooperation, will have a short life, as Central and East European countries are seeking affiliation with the West rather than a new regional alignment among themselves.*

**A** meeting of the Executive Committee of the Council for Mutual Economic Assistance (CMEA) ended in Moscow on January 5 with a decision to wind down the Soviet-led economic bloc and replace it with a new Organization for International Economic Cooperation (OIEC). The Prime Ministers of the nine member states<sup>1</sup> will convene in Budapest on February 26 and 27 to formalize the change.<sup>2</sup>

#### From the CMEA to the OIEC

The CMEA is being disbanded because its main purpose of coordinating the command economies of its communist member states has disappeared. The five non-Soviet Central and East European countries have abolished central planning; the USSR would be incapable of enforcing it even if it wanted to; and the three non-European members (Vietnam, Cuba, and Mongolia) are too weak to

serve as models of international planning and, moreover, are in the process of implementing many changes of their own. In addition, trade by barter and the clearing of transactions in transferable rubles have given way to freer forms of commerce based on world prices and calculated in convertible currency (\$US).<sup>3</sup>

The OIEC is being created, it would seem, for three reasons: to make the abandonment of international economic centralization more palatable to the more conservative factions in the Soviet leadership<sup>4</sup>; to disentangle the economic linkage that existed between CMEA members, mainly in the form of two CMEA-sponsored banks (the International Bank for Economic Cooperation and the International Investment Bank), and dispose of the CMEA's assets and real estate (such as the 25-story headquarters building in Moscow); and to help manage trade agreements that had been

reached between the USSR and the other CMEA partners prior to the revolutions in Eastern and Central Europe. In addition, residual questions from the CMEA era exist, such as those related to customs, tariffs, quotas, and reimbursement for contributions to collective undertakings that require settlement, deregulation, or dismantling.

The OIEC will obviously not be a reincarnation of the CMEA with a new name. Its avowed purpose is to consult and inform rather than to integrate under a superior authority. Both its size and its budget will be much smaller (the latter has yet to be agreed on). Like those of the CMEA, the OIEC's headquarters will be located in Moscow; and it will be administered by a committee of delegated government officials. The OIEC's statutes at this stage are not known in much detail; but it appears that conferences at the level of government ministers, Prime Ministers, or even heads of state (all customary in the CMEA) will not take place. It is quite possible that the OIEC will be only a transitional body, pending the admission of non-Soviet European member countries into Western economic alliances.<sup>5</sup>

In the meantime, the embryonic OIEC has declared itself open to anyone who might wish to join. Germany, as the successor state to former CMEA member East Germany, Yugoslavia (previously an associate member of the CMEA), and the European Community have been or will be invited to attend the meeting in Budapest at which the CMEA will be officially wound down and the OIEC launched. On the other hand, although Romania, Cuba, and Vietnam proposed inviting Albania to join the OIEC, other member states successfully opposed the suggestion, welcoming Albania's moves toward political and economic reform but judging full membership to be premature.

#### **A Look Backward**

No one is shedding any tears over the demise of the CMEA; in fact, there has been a conspicuous absence of tribute and recognition. The CMEA will doubtless go down in history as a singularly inauspicious organization. It failed to make international communist planning work; it failed to integrate; it failed to better the achievements of normal bilateral trade agreements; it failed to bolster the economies of its less developed members; and it failed to reform itself after reforms had become politically possible. Over the years, the CMEA evolved into a huge, cumbersome, and costly mechanism through which Soviet raw materials were exchanged for East European manufactured goods.

The CMEA will be especially remembered for its inability to forge a Soviet-inspired "division of labor"

within the communist bloc. Three major attempts were made. In 1962 the CMEA adopted the "Fundamental Principles of the International Socialist Division of Labor," which subsequently came to nothing, largely because of Romania's unwillingness to serve as an agricultural underpinning for the other members' industrial potential. The "Comprehensive Program of Socialist Economic Integration," promulgated in 1971, foundered as much on skyrocketing oil prices and the failure of Poland to benefit from capitalist loans as it did on the economic self-preservation policies of the more developed members, which were unwilling to share their part of the pie with others. Finally, Mikhail Gorbachev's "Complex Program for Scientific and Technical Cooperation until the Year 2000," formulated in 1985, never really got off the ground. Nor did the policy of "direct links" between enterprises, which in the mid-1980s was seen as a step toward less regimented forms of economic interaction. When Nikolai Ryzhkov heralded yet another "collective concept of the international division of labor for the years 1991-2005" at the CMEA session of October 1987, not even the staunchest believers thought much of the prospect. By then, the popularity of the communist economic system was inexorably declining, as the appeal of the market economy inevitably increased.<sup>6</sup>

In sum, the CMEA did no service to the national economies of its member countries. Under Soviet control, CMEA member countries were taught to rely on barter rather than trade, on quotas rather than competitive trade, on artificial rather than real prices, and on bookkeeping rather than business. Under the CMEA's aegis, member countries became unaccustomed to acting as merchants and instead became clerks. What these countries' economists were conditioned to forget during the CMEA era will now have to be relearned by them in the post-CMEA age.

#### **A Look Forward**

Regional economic cooperation in Central and Eastern Europe, including the USSR or its component parts, does not run counter to the desired economic affiliation with the West. Currently, it seems that the successor to the CMEA, the OIEC, will be more of a receiver than the seed of a new regional group. Nonetheless, when bilateral trade and joint ventures among the emerging democracies develop sufficiently, and when they all acquire the attributes of market-based economies, enhancing interaction at the regional level could well help those willing to take part. The early stages of West European economic cooperation, including the removal of trade barriers, the freeing of international capital, and the promotion of multinational investment activities, might then

## REGIONAL TOPICS

serve as a model. Since the Western economic standards, structures, and procedures that the Central and East European governments have said they want to emulate or join already exist, the

task of developing market economies will be made easier.

RT004B.91R

January 8, 1991

## Notes:

1 The CMEA's members are the Soviet Union, Bulgaria, Cuba, Czechoslovakia, Hungary, Mongolia, Poland, Romania, and Vietnam.

2 For accounts of the Moscow meeting and comments, see RFE/RL Correspondent's Report (Budapest), January 5, 1991; *Frankfurter Allgemeine Zeitung*, January 5, 1991; *Die Presse*, January 5 and 7, 1991; *Los Angeles Times*, January 6, 1991; *Financial Times*, January 7, 1991; and *The Journal of Commerce*, *Neue Zuercher Zeitung*, and *Handelsblatt*, January 8, 1991.

3 Reforms of the CMEA in varying degrees were mooted for a long time. The decision to dissolve the CMEA was based on the recommendations of a commission set up by the CMEA's 45th council session in Sofia in January 1990. See Vlad Sobell, "In Search of a New CMEA," *Report on Eastern Europe*, no. 6, February 9, 1990.

4 Paula L. Green in *The Journal of Commerce*, January 8, 1991. Czechoslovak Minister of the Economy Vladimir Dlouhy was quoted after the meeting as saying: "This new organization exists for political reasons, not just to strike a blow at the internal situation in the Soviet Union" (*Financial Times*, January 7, 1991).

5 Dlouhy interviewed on Radio Prague, January 5, 1991, 6:30 P.M.

6 Vlad Sobell reviewed the CMEA's efforts to coordinate its members in his article, "The CMEA's New Scheme for an International Socialist Division of Labor," RAD Background Report/67 (Eastern Europe), *Radio Free Europe Research*, April 19, 1988. By the same author, see *The CMEA in Crisis: Toward a New European Order* (Washington: Center for Strategic and International Studies, 1990).

## CORRECTIONS

to Marvin Jackson's article, "The Privatization Scorecard for Eastern Europe," in *Report on Eastern Europe*, no. 50, December 14, 1990.

Page 24, right column, bottom paragraph should read:

Since January a different classification has been published. According to a list published in *Ikonomika* in January, there were 460 firms "with state property," 658 "with communal property" (concerned with local industry and services), 41 belonging to social organizations, 225 "societies" (taken to be joint-stock companies whose shares are not owned by private parties), and 14,041 firms belonging to citizens (of which 11,468 were individual proprietorships, 2,404 were partnerships, and 169 were societies). By May the respective numbers had changed to 501, 709, 68, 299, and 23,739.<sup>a</sup> Companies have also included banks. For example, at the end of May shares in the first commercial bank were offered to buyers.

and to Marvin Jackson's article, "The Economic Situation in Eastern Europe in 1990," in *Report on Eastern Europe*, no. 1, January 4, 1991.

In the table on page 52, the entries for the East German area should read 7.3 and 50, respectively.

We regret these errors.



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## REGIONAL TOPICS

# The Privatization Scorecard for Eastern Europe

Marvin Jackson

*In 1990 private enterprise made significant but limited inroads into the East European economies. In the region as a whole, there are probably at least 1,000,000 small businesses (mostly one-man or family operations); between 2,000 and 3,000 large firms, many of which are joint-stock companies; and some 10,000 joint ventures with foreign capital. In 1991 the pace of privatization is likely to increase in Poland and Czechoslovakia but will probably slow down in Hungary, Romania, and Bulgaria.*

**E**conomic reform in Eastern Europe has been underway for more than a year now. In each country, similar components of this process have been utilized and steps of varying length undertaken. The privatization of property rights is one of these components. All countries recognize it, in one way or another, as necessary, although there are differences of opinion over both the specific form it should take and its timing in relation to the other components of economic reform.

This paper considers, first, the alternative forms of privatization in Eastern Europe. It then discusses the extent of privatization in each country. Thirdly, the major issues concerning privatization are identified. Finally, the relative status of private and state properties over the next year or so is considered in an attempt to determine when private enterprise will become the dominant economic force in Eastern Europe.

### Alternative Forms of Privatization

Legislation in the various East European countries seems to be focusing on two forms of privatization: small-scale and large-scale. The criterion for the introduction of either form of privatization is less the size of the units under consideration than the legal status of these units, both before and after privatization. Large-scale privatization usually refers to the process of reorganizing existing state enterprises, whereas small-scale privatization refers to processes resulting in the formation of small firms. The latter are usually either individually or family-owned, but they may also be taken over by partnerships or cooperatives.

Prior to the radical political changes of 1989, small private enterprises existed in all East European countries to one extent or another. Three categories can be identified. First, units that could be considered the legal personal property of the proprietor, such as private farms in Poland and

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repair shops run from the homes of the repairmen. Second, units that are state property and subject to conditional assignment, such as plots of land farmed by members of agricultural cooperatives. Third, units operating on land, and with equipment, leased by the state or the cooperative.

Since 1989 there have been significant increases in the numbers of all three types of small-scale enterprise, a process that is sometimes referred to as "spontaneous privatization." These increases have resulted partly from measures taken to sell or lease state and cooperative property. In addition, "reprivatization" has taken place; this term refers to the practice of returning property to its previous private and corporate owners. Small-scale privatization occurs simultaneously with large-scale privatization when existing large units are broken up into small units and either sold or leased.

Large-scale privatization refers primarily to the disposal of units that have the legal status of "state enterprises." Sometimes the process also covers the disposal of large enterprises that had been organized as cooperatives. In a small number of instances where enterprises had been organized as state-owned joint-stock companies, privatization has taken the form of selling shares to individuals and organizations.

By the 1980s nearly all East European countries had permitted joint ventures between their enterprises and foreign companies. Since the foreign companies were usually privately owned, this practice of allowing joint ventures should be considered a form of privatization, indeed, perhaps the earliest and currently most important one as regards large units. At present, there are almost 10,000 foreign joint ventures in the region.

Much confusion has arisen over the two forms of large-scale privatization: the so-called unintentional or illegal privatization and the process of "conversion." The latter refers to the act of converting a legal state enterprise into a legal joint-stock company. The provisions for such conversions were made by Hungary in 1988 and by Poland only in July 1990. Since the first stage in such conversions is the creation of a company all of whose shares are state-owned, this process can hardly be regarded as "privatization." Real privatization comes later, once shares have been sold or transferred to other owners.

#### The Extent of Privatization

There are major problems in collecting statistics on privatization in Eastern Europe. The only means of accurately recording how many private firms exist in the region would be to go to each individual country and make a count using a uniform system. As shown below, figures cited in the press often

seem contradictory, especially in the case of small-scale privatization. This is partly because the normal life-expectancy of small businesses is so short that half or more do not survive more than one year. In the case of large-scale privatization, not only is the process of conversion confused with the actual transfer of ownership, but also the intentions of those responsible for the process itself are notoriously unreliable indicators of what subsequently happens.

In October 1990 Albania took the first step toward privatization by announcing that it was allowing some 100 shops employing family members only to be set up.<sup>1</sup>

In February the post-Todor Zhivkov regime in Bulgaria issued a decree allowing people in rural areas to farm under some kind of leasing arrangement as much as 20 hectares of land on the plains and 30 hectares in hilly and mountainous areas.<sup>2</sup> This measure represented a significant expansion of users' rights, although by the end of April only 138,000 hectares had been taken up under the decree.<sup>3</sup>

In December 1989 some 12,200 private firms were reported as already existing in Bulgaria.<sup>4</sup> On April 10 a law was passed providing for the establishment of private businesses in trade, tourism, and the services sector; the law contained no restrictions on the size of these businesses.<sup>5</sup> By July over 2,000 firms had reportedly been set up under the new law.<sup>6</sup>

In the case of large-scale privatization, a law already existed under Zhivkov that permitted the conversion of state enterprises into "firms" and joint-stock companies. According to this law, a "firm" was to operate as a distinct legal and financial entity and was eventually to become financially independent. Shares in joint-stock companies could originally be held only by the state, banks, or other companies. In 1989 some 1,295 "firms" were registered, some of which were probably joint-stock companies.<sup>7</sup>

According to a list published by *Ikonomika* in January 1990, 460 state enterprises and 658 cooperatives (concerned with local light industry and services) had been privatized. There were also 41 firms belonging to organizations such as trade unions, 225 "societies" (taken to be joint-stock companies whose shares are not owned by private parties), and 14,041 firms belonging to citizens (of which 11,468 were individual proprietorships, 2,404 partnerships, and 169 "societies"). By May there were 501 state enterprises and 709 cooperatives that had been privatized, as well as 68 firms belonging to trade unions and other such organizations, 299 "societies," and 23,739 firms belonging to individuals.<sup>8</sup> New banks have also been set up.

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For example, at the end of May shares in the first private commercial bank in Bulgaria were put up for sale.

How many conversions have taken place since the summer of 1989, when the law on the conversion of state enterprises was passed, and how often they have been used to disguise takeovers by the Bulgarian *nomenklatura* is not yet clear. However, it seems that such takeovers have occurred on a large scale. Shortly after becoming President, Zhelyu Zhelev suspended privatization because of "the manifestation of speculative tendencies" that, he said, were threatening to let managers in the state sector acquire state property over which they had had control at ridiculously low prices.<sup>9</sup>

Before 1988, private land holdings in **Czechoslovakia** accounted for only 4% of farm land but nonetheless provided 12% of all meat and 50% of all fruit and vegetables.<sup>10</sup> Laws enacted in 1988 and 1990 abolished restrictions on the size of these holdings. In 1990 a law was passed that gave private farms a status equal to that of cooperatives and granted members of cooperatives the right to leave the cooperatives and have their land returned to them.<sup>11</sup> However, few have apparently left the cooperatives owing to low motivation, bureaucratic hindrances, and a lack of legislation on privatization in agriculture.<sup>12</sup>

In November 1989 there were only about 15,000 private businesses in Czechoslovakia. By September 1990 some 300,000 had been set up, most of which had only a very small number of employees (although at least one was reported to employ 100 people). Prague reportedly still had only two private restaurants.<sup>13</sup> In October two laws on private enterprise were passed. The first was on the restitution of some 70,000 shops, hotels, and other small businesses that had been nationalized between 1955 and 1961.<sup>14</sup> The second, on small-scale privatization, was passed by the parliament on October 25 and was to go into effect on December 1. Under this law, enterprises are to be auctioned by republican government bodies set up to deal with privatization cases, and the successful bidders will be required to maintain services on the same premises for at least one year. Some 100,000 businesses will be up for sale in two scheduled rounds of auctioning, the first of which will be restricted to Czechoslovak citizens who are permanent residents in that country.<sup>15</sup>

On November 1 a law on large-scale privatization was introduced in the parliament, but debate on it was postponed until January 1991.<sup>16</sup> The proposed legislation stipulates that between 40% and 80% of each large enterprise be privatized on the basis of vouchers issued to all adult Czechoslovak citizens resident in Czechoslovakia. Each adult will receive

1,000 "investment points" (apparently worth 2,000 koruny); these can be either exchanged for shares in companies or sold for 50 koruny each. Vouchers cannot be purchased by foreigners or Czechoslovaks living abroad; shares not purchased with vouchers may be sold to the state, banks, or foreigners. The actual conversion of state enterprises into joint-stock companies is not expected to begin before the spring of 1991. Such conversions will be organized by the enterprises themselves and could involve the sale of stock to employees.<sup>17</sup>

In March 1990 the government of what was **East Germany** decided to reprivatize between 10,000 and 15,000 medium-sized enterprises that had been expropriated in 1972. Claims to these and other enterprises were to have been submitted by September. In the spring of 1990 there were some 150,000 small workshops in East Germany, but many were threatened by closure and part-time work. Since the economic and currency union, on July 1, about 170,000 new enterprises have been set up, most of them businesses offering services or restaurants.<sup>18</sup> The disposition of some 8,000 former state enterprises is currently being administered by the *Treuhandanstalt*, a new government agency set up for this specific purpose. By November it had sold off or found partners for about 200 enterprises and closed down about 10. It is expected that the number of closures will eventually total some 1,000.<sup>19</sup>

In 1988 the communist government in **Hungary** passed relatively liberal enterprise laws, effective as of January 1, 1989, providing for the conversion of state enterprises into joint-stock companies, the establishment of entirely foreign-owned firms with total profit repatriation in convertible currencies, and the creation of private businesses with up to 500 employees. By mid-1989 there were close to 140,000 private businesses in Hungary, an increase of 52,000 since 1982. These businesses employed roughly 7% of the labor force.<sup>20</sup>

By mid-1990 the number of private businesses had increased to about 270,000, of which 180,000 were family units specializing in services such as installation and electrical repairs as well as retail trade (40,000). These family businesses employed about 1,000,000 of the total labor force of 5,200,000.<sup>21</sup> There were also 12,159 limited companies, 3,224 small cooperatives, and 2,007 companies and trusts that are not joint-stock companies. Some 520 joint-stock companies had been established, while state-owned, limited, and public limited companies numbered 2,300.<sup>22</sup> During the second quarter of 1990, some 837 companies with foreign participation were formed, 31 of which were entirely foreign-owned.<sup>23</sup>

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Until the fall of 1990, privatization in Hungary came about largely "spontaneously" or, more precisely, as a consequence of new firms' taking advantage of relatively liberal laws on private enterprise. More rapid privatization of small enterprises is provided for by a law passed on September 18 regulating the transfer to private hands, beginning next spring, of some 10,000 shops, restaurants, and small businesses offering services. Between 2,000 and 3,000 of these businesses are already being operated by private entrepreneurs who, under an earlier law, had contracted out state-owned premises and equipment.<sup>24</sup>

In July 1990 the coalition government agreed on a proposal for a reprivatization law. Aimed at agricultural land, the proposal stipulated that those working on cooperatives or state farms would be entitled to purchase 1.5 hectares at state-controlled prices and would be allowed to buy more if land was still available once other claimants had been satisfied. The major beneficiaries of the proposed law would have been those who had lost land after 1947, since they, or their heirs, would have been entitled to buy up to 100 hectares. At the same time, foreigners would have been denied the right to purchase land. On October 2 the High Court declared the proposed law unconstitutional, claiming that it discriminated against some former owners.<sup>25</sup>

In order to exercise more control over large-scale privatization, a State Property Agency was set up in March and placed under governmental rather than parliamentary supervision after the general elections of March and April. Furthermore, several laws passed were aimed at imposing stricter control over the large-scale privatization process. In May, for example, a law was approved under which committees responsible for the disposition of state property were set up on a regional basis to prevent this property from being sold off below its real value.<sup>26</sup> In September the law on the conversion of enterprises was amended to state that the approval of two-thirds of the representatives on the council supervising the conversion process would be required for converting a state enterprise into a joint-stock company.<sup>27</sup>

In order to avoid the piecemeal approach to privatization, on September 14 the State Property Agency, after some initial delays and hesitation, announced a special program for the privatization of 20 large companies. The agency is seeking offers for these companies and, in some cases, will make floatations on the Budapest and foreign stock exchanges. Foreign purchases must be approved by the agency and will be restricted to minority holdings.<sup>28</sup> By mid-October the agency had dealt with 160 privatization cases, of which 60 had been approved. A further 28 cases had been refused; the

explanation given for these refusals was that the agency wished to protect state assets and that "poor privatization drafts" had been prepared by the companies in question.<sup>29</sup> Privatization has so far affected about 8% of assets in Hungary.<sup>30</sup> In November Lajos Csepi, the head of the State Property Agency, said that another 20 to 25 companies would be put up for sale in December and another 60 in the next round, to be completed by November 1991.<sup>31</sup>

The number of tax-paying private enterprises in Poland was 46,512 in 1988 and rose to 71,802 in 1989. By mid-1990 the number had reached 148,741, of which 70% were said to involve street trading.<sup>32</sup> Most of these private enterprises were the result of "spontaneous" privatization. The net growth in the number of private enterprises during the first seven months of 1990 was 9%, or about 87,000 (this figure takes into account closures over the same period).<sup>33</sup> By August, about 277,000 new "economic subjects" (151,000 in trade) had been set up. In October more than 40,000 private businesses were opened, the highest-ever monthly total. Altogether, some 320,000 had been opened by mid-November, while some 200,000 had been closed.<sup>34</sup> The number of small private businesses currently operating in Poland could be as many as 200,000.

No reprivatization law has yet been passed, although Minister for Privatization Waldemar Kuczynski said in September that the government planned to enact legislation that would affect, first of all, small and medium-sized companies and farms.<sup>35</sup> Property and equipment belonging to the state or local government units have already been turned over to private businesses. By August 1990 at least 15,000 shops had been privatized, which, together with those that had become private businesses before 1990, amounts to some 25% of all Polish shops. In September the government said it hoped that 80% of all retail trade would be privatized by the end of 1990.<sup>36</sup> In November it was estimated that there were 20,000 private shops in Poland.<sup>37</sup>

Licensed private enterprise is said to account for 10% of industrial sales and 27% of construction work. Licensed private output is estimated to have increased by 25% in the first half of 1990, compared with the same period last year.<sup>38</sup>

On July 7 the parliament approved a law on large-scale privatization that provided measures for the conversion of Poland's 7,600 state enterprises into joint-stock companies and their eventual sale to individuals, companies, or foreigners. Under this law, the conversion process can be initiated by either the Ministry for Privatization or the workers' council and management of the enterprise in question. The law also provides two ways in which

an enterprise can create capital: by selling up to 20% of shares to its employees at discounts of up to 50% and by distributing to the general public vouchers worth up to 20% of its assets. Such vouchers would eventually become exchangeable for shares in joint-stock companies.<sup>39</sup>

In late September seven state enterprises became the first to be converted under this new law. The sale of five of these converted enterprises to Polish banks was to begin on November 30. Some ten days earlier, on November 20, Kuczynski had announced that 15% of state enterprises would be privatized under the new law by 1991 and that the government aimed to privatize 50% within the next three years.<sup>40</sup>

Prior to the enactment of the 1990 law on large-scale privatization, at least two large companies were subject to some form of privatization. In 1984 Universal, one of Poland's three biggest trading companies, was converted into a joint-stock company under the commercial code of 1934, which was still in force in communist Poland. After the conversion, 51% of the company was owned by the Polish government and 49% by other companies. The second company was the BIG Bank, which began selling shares to the public in May.<sup>41</sup>

Of all East European countries, Romania probably had the most severe restrictions on private economic activity, and particularly that of peasant farmers. The post-Ceausescu government liberalized the sale of agricultural products and granted peasants the use of 0.5 hectare of collective land to expand private farming. Moreover, since December 1989 some 320 cooperative farms have been closed and the land taken over by individual farmers. This has resulted in an increase of almost 250% in the amount of land privately farmed by members of cooperatives. A draft law on land ownership that would allow Romanians to own up to 100 hectares is currently being considered by the parliament.

A law allowing small private enterprises with up to 20 employees was passed in February; a ceiling of 250 employees has been mentioned for the future. By July some 50,000 requests for licenses had been made; 32,000 of these had been approved and 20,000 firms accordingly set up (some 75% of which are in the services sector).<sup>42</sup> By November the total number of requests had reached 140,000; 50,000 had been approved, of which only 20% are for businesses not involved in trade. It is estimated that the number of private businesses reached 70,000 in October. On September 20, 1990, a new law on commercial companies and foreign joint ventures was passed by the parliament. Based on pre-World War II commercial codes, it allows five categories of company, ranging from simple partnerships to joint-stock companies. All enterprises formed under earlier laws are required to convert

into one of these categories within six months of the law's passage.

A proposal for a large-scale privatization law was submitted to the parliament in June and included a provision for distributing to the public vouchers to the value of 20% of the state-owned enterprises' net assets. In July the government set itself the target of converting between 30% and 50% of all state enterprises into joint-stock companies by 1995 and said that this figure would eventually rise to 80%.<sup>43</sup> The first joint-stock company was formed in May,<sup>44</sup> but it is unclear what the legal basis for this new company is (other, that is, than the precommunist commercial code). In September a law requiring state enterprises to be converted into either a new kind of state company or a joint-stock company was passed. The latter will be required to turn over 30% of its shares to a state privatization agency, which, in turn, will issue vouchers with a nominal value of 5,000 lei to each adult Romanian citizen resident in Romania. Vouchers will be either salable or transferable after one year, but only to resident Romanian citizens. The aim is to privatize in this way roughly 50% of the country's total capital within three years.<sup>45</sup>

On November 28 it was announced that since September 1990, 19 autonomous state companies in the mining and armaments industries, communications, rail transport, as well as the supply of gas and electricity had been set up. It was also announced that over the same period, more than 400 commercial companies had been formed as a result of converting the former industrial departments of state ministries.<sup>46</sup> On December 1 the first joint-stock commercial bank, the Romanian Commercial Bank, was to be set up on a nationwide scale to take over all commercial operations of the Romanian National Bank.

In June, Tanjug reported that since the beginning of 1990 some 15,000 private and partly privatized enterprises as well as 28,000 retail shops had been set up in Yugoslavia.<sup>47</sup> The next month the press agency reported that since the beginning of the year 7,200 "commercial businesses" and 28,730 private retail shops had been established, adding that the number of the former had doubled and that of the latter increased by 31%.<sup>48</sup> A Tanjug report in October gave 30,000 as the number of "private enterprises" (by which only retail shops were presumably meant). It is not known how many one-man operations, such as taxi or trucking services, are currently operating in Yugoslavia.<sup>49</sup>

In October private businesses were said to account for only 10% of national output (a figure that obviously excludes the agricultural sector). It is hoped that under the present government's program, they will account for 35% by 1995.

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The keys to attaining this goal are the establishment of new small private companies and the sale of shares to workers in the state-owned enterprises. A draft law submitted to the Federal Assembly in June stipulates that workers who had been with an enterprise for at least five years would be allowed to buy shares at a 20% discount or more, depending on how long they had been working at the enterprise. The administrators of private pension funds would also be offered shares at a discount, while the state as well as foreigners would be required to pay the full price.<sup>50</sup> By November more than 300 publically owned enterprises had been converted into joint-stock companies.<sup>51</sup>

### Obstacles to Small-scale Privatization

There seems to be a ready supply of people willing to become private entrepreneurs, despite the risks involved. However, a problem is that many of them are members of unpopular ethnic minorities, such as the Gypsies; thus, some common prejudices against the market place have been reinforced. More important, despite some Western special aid programs, the neophyte East European businessman is unable to find expert advisors and special credit facilities. Moreover, there is a common complaint that the old bureaucracy and laws are still impeding the setting up of small private businesses.

In the case of small enterprises, complaints about red tape have been most numerous. In Poland, for example, the local authorities have established a monopoly on property available for renting and are demanding excessively high rents for shops. New private businesses in Romania have found it almost impossible to secure either premises or supplies of essential materials through normal channels. In Czechoslovakia permission from 12 different offices is required before a new firm can start looking for premises.<sup>52</sup> In Bulgaria 300,000 private entrepreneurs refused to pay income tax of 70%.<sup>53</sup> No legislation aimed at reducing these taxes has been passed to date.

Three interrelated factors vital to the progress of small-scale privatization can be identified. First, the extent to which the former retailing monopolies, the state trading and cooperative networks, have been either maintained, broken up into competing units, or put up for reprivatization or sale. Second, whether pricing policy facilitates low subsidized prices. Third, whether the supply system, especially for domestically produced food and clothing, functions effectively or breaks down.

If the former network is maintained and provides reasonable supplies at subsidized prices, then private traders and producers will find it difficult to compete and will tend to specialize mostly in

high-quality goods and services. The greater the disequilibrium in the market, however, the more opportunities for private entrepreneurs. Indeed, these opportunities increase when the domestic supply system breaks down. Private traders can move quickly to find a domestic market. As demonstrated in Poland, private traders can also establish significant contacts with importers and exporters abroad who are not readily identifiable by larger organizations.

### Conflicts

Hungary's attempt to reprivatize farm land provoked considerable debate over the rights of those who at the time were working the land but had no ownership claims. Although the proposed reprivatization law would have given them a priority claim, they would have been entitled, at least at first, to buy only 1.5 hectares. The High Court's declaration that the proposed law was unconstitutional seems to have pushed the issue into the much broader context of urban property claims.

How reprivatization will progress in Poland, Romania, and Bulgaria is not yet clear; in Czechoslovakia some of the issues have been resolved. One poll suggests that there is little interest in that country in the privatization of cooperative land.<sup>54</sup> In the case of the reprivatization of retail businesses, the managers of small shops demanded first refusal when shops were sold, but this demand was rejected. Furthermore, a compromise agreement was rejected that would have allowed them to borrow from the banks up to 50% of the purchase price for as long as seven years.<sup>55</sup>

Other conflicts in the region have involved the local authorities, which under the previous regimes were largely responsible for the administration of civic and residential property. Suddenly, because of their monopoly on property, especially in urban areas, they have found themselves in control of assets of potentially great value in market conditions. Thus, it is not surprising that they are reluctant to give up this control.

In Yugoslavia the self-protective practices of local and republican officials and bureaucrats is partly disguised by nationalist garb. Ironically, such nationalism has led even liberals in Slovenia and Croatia to oppose the central government's attempts at privatization. In Czechoslovakia the issue of privatization has featured in the dispute over the respective roles of the federal and the Czech and Slovak republican governments.<sup>56</sup>

### The Workers' Role in Large-scale Enterprises

Much of the political strife over the Polish law on large-scale privatization centered on the role of workers in the new enterprise system. It took

almost six months and 13 drafts before a bill was submitted to the parliament, in March 1990.<sup>57</sup> Passing it took another four months. A major compromise was the addition of the provision, not in the government's draft, that capital vouchers be distributed. However, the bill was resisted by those wanting some form of workers' management in Poland and became an ideological issue among Solidarity intellectuals. It also reflected the recent emergence of the workers' councils as the most important decision-making bodies in state enterprises. The law stipulates that as long as an enterprise remains a state-controlled joint-stock company, 30% of its board of directors must be elected by the workers.

#### Issues Involved in the Conversion of Large State Enterprises

In Poland and Hungary, the public and not a few leading politicians have exhibited great impatience over the slow pace of converting and subsequently selling state enterprises. For example, according to a poll carried out by the Warsaw Public Opinion Polling Center, 66% of the respondents thought that privatization would be either very favorable or rather favorable, while only 9.6% said it would be either rather unfavorable or very bad. However, 44.4% thought the pace was too slow, while 33% thought it was about right.<sup>58</sup>

Before joint-stock companies can be evaluated and sold, an enormous amount of work must be done. In the case of Czechoslovakia, some 20 additional laws have had to be passed on such issues as taxation and commercial courts.<sup>59</sup> Qualified accountants and lawyers are also needed. In the former East Germany, for example, only 600 qualified lawyers could be found, compared with some 30,000 in the western part of Germany.<sup>60</sup> In the cases of Poland and Hungary, Western accounting firms and investment bankers have provided legal and financial advice.

Only after a legal framework has been erected and expert advice made available can the difficult problems of evaluating assets and taking decisions on debts (to the state and other enterprises) be tackled. Sometimes this process involves either closing down the constituent units of the overgrown state enterprises or turning them into economically viable firms. In all cases, the book values of assets dating from the communist era have been discarded as economically and financially meaningless. As far as liabilities and ownership are concerned, decisions have had to be taken on how to overcome the effects of the previous regimes' policies on taxation, subsidies, and loans. In numerous cases, for example, postcommunist governments have provided "loans" to enterprises simply because their predecessors

had taken for the state budget the bulk of profits made by enterprises. In other cases, enterprises that are uneconomic have continued to be heavily subsidized. It is therefore no wonder that it is taking such a long time to sort out this accounting nightmare.

#### The Takeover of Companies and Assets

Since the Solidarity government was formed in Poland, politicians and ordinary citizens throughout the region have been alarmed at the possibility that the *nomenklatura*, as well as communist bureaucrats and managers, would seek to make personal profit out of privatization. Such fears have certainly been justified in Poland and Hungary, although the authorities seem to have moved quickly to put a stop to the worst abuses. This has not been the case in Romania and Bulgaria, where the governments, composed of former Communists, have been supported by the *nomenklatura*.

According to a poll conducted by Solidarity, its supporters seem to be more concerned about how capable managers are rather than which party they formerly belonged to. Another important question, however, is how well people without any experience in management and administration could actually take over from these managers and efficiently run companies and banks.

#### Foreign Investment

Even though Hungary has developed its financial system further and faster than any other country in Eastern Europe, the seemingly limited ability of this system to absorb the shares of enterprises being privatized has been given as a major reason for the relatively cautious approach being adopted in that country. In November a debate was provoked when Gyorgy Matolcsy, the Prime Minister's adviser on privatization, called for faster privatization as the key to reviving Hungary's deteriorating economy. Foreign investors have criticized Hungary's approach as too bureaucratic and too suspicious of foreign capital. Criticism such as this has been dismissed by Lajos Csepi, who claimed that the program of gradual privatization was necessary to ensure the best prices for shares in state enterprises.<sup>61</sup>

It is uncertain how much foreign investment Hungary would attract under more favorable economic conditions. But at the same time, there is no doubt that foreign investors are discouraged by the government's reaction to popular fears that "the country's wealth" is being given away. For its part, the Hungarian government has not lifted restrictions on foreign participation in Hungarian commercial banks. A similar situation in Poland appears to have been one of the major reasons for the unexpected outcome of the first round of the presidential

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election. Indeed, in every East European country, popular notions about the potential wealth of the nation seem to be at odds with the investors' calculations of the profitability of national assets.

### The Distribution of Capital

One way in which Hungary could have increased the absorption capacity of its financial markets would have been to introduce some scheme for the distribution of capital claims, such as vouchers, among the general public. Apparently, the government decided not to implement a low-cost loan scheme for financing stock purchases, despite the fact that such loans would not be inflationary. And unlike other East European countries, Hungary has no voucher scheme and has not offered discount shares to employees at enterprises.

The question is whether Hungary or Poland could speed up large-scale privatization and have less recourse to foreign investment if more emphasis were to be placed on developing a voucher scheme. In Poland a working group has been considering various schemes for several months. Czechoslovakia's voucher scheme has not been explained in detail, although it is said to have been developed with the help of a London investment bank.

Finally, it remains to be seen how workers in Poland will react to the chance to buy shares in their enterprises. Recently, the value of liquid assets held by Polish citizens has risen. Will they become willing investors in the face of considerable uncertainty, especially when demands for better housing and more durable goods have not been satisfied for so long?

### Conclusion

Under the Communists, private enterprise in farming, the marketing of food, and services was barely tolerated. Today, Eastern Europe can boast at least 1,000,000 small operations (mostly in trade and services), between 2,000 and 3,000 joint-stock and limited companies, and as many as 10,000 joint-ventures with foreign participation. However, private businesses account for only a small part of nonagricultural production, at most between 10% and 15%.

Major obstacles to privatization remain. Declining aggregate demand, for example, might discourage risk-taking and make the accumulation of private capital more difficult. Small firms lack both experience and access to premises and equipment, supplies, advisory services, and credit. Moreover, they have to contend with existing trade monopolies. The privatization of large enterprises is a lengthy process when done carefully, as in the cases of Hungary and Poland. It can, however, be carried out very quickly when the authorities are not forced to take the electorate's wishes into consideration, as in Romania, where in November alone some 400 joint-stock companies emerged.

In 1991 the privatization process in Eastern Europe is likely to be carried out under difficult economic and political conditions. Moreover, political reaction to the first wave of privatization could complicate matters. In Poland, privatization is likely to be accelerated if Walesa is elected President. In Romania and Bulgaria, it might slow down if people are able to voice their opposition to takeovers by the former *nomenklatura* and communist bureaucrats. Even in Hungary, where privatization is at its most advanced, public discontent is growing and the government is becoming increasingly unsure of its own policies.

It is doubtful whether any country in the region will be able to privatize 30% of its large enterprises by the end of 1991. Moreover, it would be surprising if as much as 50% of all state enterprises were privatized in the next five years, by which time the pace of change is likely to have slowed down. The state is likely to continue for some time to own 30% of the shares and production units of the large enterprises. Should this be the case, it will be attributable partly to the vested interests of the state and partly to the fact that a large number of enterprises are too inefficient to warrant being privatized. The state, however, might keep them operating in order to reduce regional unemployment, a policy that could result in the institutionalization of state subsidies.

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November 30, 1990

### Notes:

- 1 AFP, October 31, 1990.
- 2 *Durzhaven Vestnik*, February 9, 1990.
- 3 *Duma*, May 4, 1990.
- 4 *Rabotnichesko Delo*, December 23, 1989.
- 5 *Durzhaven Vestnik*, April 21, 1990.
- 6 *Duma*, July 7, 1990.
- 7 *Trud*, January 18, 1990.
- 8 *SS*, June 29, 1990.
- 9 BTA, August 19, 1990.
- 10 *The Journal of Commerce*, May 1, 1990.
- 11 Radio Prague, May 3, 1990.
- 12 Czechoslovak Television, September 1, 1990; and *Die Presse*, October 12, 1990.
- 13 *Die Presse*, September 22, 1990.

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- 14 Radio Czechoslovakia, October 22, 1990.
- 15 *Hospodarske Noviny*, October 11, 1990; CTK (in English), October 25, 1990.
- 16 Radio Czechoslovakia, November 9, 1990.
- 17 AFP, November 1, 1990; *Die Presse*, November 3, 1990; and *Sueddeutsche Zeitung*, November 6, 1990.
- 18 AFP, August 10, 1990.
- 19 *Die Tageszeitung*, August 20, 1990; *International Herald Tribune*, November 9, 1990; and statements made by the chief economist of the Dresdner Bank, at the *PlanEcon* conference in Frankfurt, November 14, 1990.
- 20 *MTI Econews*, August 1 and 18, 1989.
- 21 *Die Presse*, September 21, 1990.
- 22 *MTI* (in English), September 13, 1990.
- 23 *Ibid.*, September 13, 1990.
- 24 See Karoly Okolicsanyi, "Privatization: Two Cautious Steps," *Report on Eastern Europe*, no. 42, October 19, 1990.
- 25 *Financial Times*, July 24, 1990; *East European Markets*, June 27, 1990; Karoly Okolicsanyi, "Agricultural Privatization and the Smallholders' Party," *Report on Eastern Europe*, no. 31, August 3, 1990; Radio Budapest October 2, 1990.
- 26 Radio Budapest, June 4, 1990.
- 27 *Ibid.*, September 11, 1990.
- 28 *MTI* (in English), September 14, 1990.
- 29 *Ibid.*, October 18, 1990.
- 30 Radio Budapest, October 18, 1990.
- 31 *MTI Econews*, November 7, 1990.
- 32 *The Independent*, November 2, 1990.
- 33 *PAP* (in English), September 20, 1990.
- 34 *Reuter*, November 16, 1990.
- 35 *AFP*, September 30, 1990.
- 36 *PAP* (in English), September 25, 1990.
- 37 *The Washington Post*, November 3, 1990.
- 38 *The Independent*, November 2, 1990.
- 39 *Rzeczpospolita*, July 23, 1990; *The Chicago Tribune*, July 23, 1990; and *Radio Warsaw* July 14, 1990.
- 40 *dpa*, November 20, 1990.
- 41 *Reuter*, May 18, 1990.
- 42 *Rompres*, May 22, 1990; and *Romania Libera*, July 21, 1990.
- 43 *AP*, July 26, 1990.
- 44 Radio Bucharest, May 26, 1990.
- 45 *Monitorul oficial al Romaniei*, August 7, 1990.
- 46 *Rompres*, November 28, 1990.
- 47 *Tanjug*, June 29, 1990.
- 48 *Ibid.*, July 10, 1990.
- 49 *Ibid.*, October 8, 1990.
- 50 *Ibid.*, July 17 and 31, 1990.
- 51 *Ibid.*, November 8, 1990.
- 52 *Die Presse*, September 22, 1990.
- 53 *East European Markets*, July 27, 1990.
- 54 According to a survey reported in *Die Presse* of October 12, 1990, 93% of agricultural cooperative workers questioned expressed either grave doubts about, or absolute opposition to, a division of the land into private farms.
- 55 *AP*, October 2 and 25, 1990; and *Financial Times*, November 19, 1990.
- 56 *CTK* (in English), November 12, 1990.
- 57 Louisa Vinton, "Privatization Plan Prepared," *Report on Eastern Europe*, no. 14, April 6, 1990.
- 58 *PAP* (in English), November 8, 1990.
- 59 Jiri Pehe, "Rebuilding the Legal System," *Report on Eastern Europe*, no. 46, November 16, 1990.
- 60 *The Guardian*, August 24, 1990.
- 61 *Reuter* and *MTI Econews*, November 7, 1990.



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# The International Economic Situation and Eastern Europe

Marvin Jackson

*The managers of foreign trade and finance in Eastern Europe faced an amazingly complicated situation in 1990: the internal economic and political rules of the game changed just as the international environment called for major adjustments as a result of the collapse of the Council for Mutual Economic Assistance's trading system and the direct and indirect effects of the Gulf crisis. Foreign trade shifted from rubles to hard currency. To what extent this change was a result of moving away from former markets and how far it was a consequence of "dollarization" is unclear. In the process, Poland generated a record high hard-currency trade surplus, followed by Hungary, yet both countries' national debt increased. In fact, only Czechoslovakia and Yugoslavia managed to avoid increasing their debts. There will be major pressure next year to reduce trade deficits unless significant new, low-cost credits are made available.*

**C**ould more challenges have been placed before those involved in the management of foreign trade and financial balances in Eastern Europe? Internal management systems were dismantled and only partly replaced by market controls. The arrangements for bilateral state trade in rubles fell apart this year and will all but disappear in 1991. Underwriting of energy supplies by the Soviet Union was abruptly reduced in mid-1990, often without notice. The Gulf crisis added direct losses in trade and payments of debts, as well as further indirect losses in terms of trade through higher oil prices. These losses have only been partially offset by Western and international assistance and by an increase in direct foreign

investments. Some of the main dimensions of these changes will be reviewed before turning to the measurable impact on the trade and debt balances of each country in the region.

### Changes in Management Systems

The old system of centralized allocation has either fallen apart or been deliberately dismantled in every country except Albania. In Poland a few export controls remain, but any firm can now register to conduct trade, and those wishing to export or import are free to choose from among the available channels. The number of licensed foreign traders in Hungary increased from 35 only 10 years ago to 360 in 1987; at present there are an estimated

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10,000 to 12,000. Almost 90% of Hungary's import trade is reportedly conducted without prior government approval, quotas remaining only on foodstuffs and pharmaceuticals.<sup>1</sup> Deregulation in Czechoslovakia has led to the establishment of some 3,000 companies with foreign trade rights.<sup>2</sup> Even in Romania, as early as in April this year, more than 250 private foreign trading firms had been approved by the government.<sup>3</sup> But Romania and Bulgaria have both resorted to specific export exclusions. The latter, for example, banned the export of some 16 food and nonfood items in an attempt to cope with the growing disorganization in distribution networks.

Mechanisms to replace the old system—for example, programs for macroeconomic adjustments, marketization, and privatization—have only been partially implemented in the best cases (Poland and Hungary); in other countries they have either just been issued (Czechoslovakia and Romania) or only talked about (Bulgaria, Yugoslavia, and the Soviet Union). Besides becoming increasingly concerned over the money supply, most countries have introduced exchange-rate policies leading to internal convertibility. Strictly speaking, however, only Poland and Yugoslavia have actually achieved internal convertibility; Hungary and Czechoslovakia plan to do so early in 1991. In Hungary, the black market in hard currency was still offering rates about 15% above the official rate, suggesting the need for devaluation; the black market was being used by Hungarians to build up private hard-currency accounts.<sup>4</sup> Even though Romania and Bulgaria have devalued their currencies, exporters are required to turn over quotas of foreign-exchange receipts at rates far below the official ones, while access to foreign-exchange supplies is still restricted by the authorities.

The political authority to implement domestic economic reform is based on fragile coalitions in Hungary and Czechoslovakia, a weak majority in Romania, collapsing central authority in Yugoslavia and the Soviet Union, and it does not exist in Bulgaria. For those who must make the decisions and find foreign partners, the rules are unclear and uncertain. To make matters worse, the international environment has lost some of its old, established political and economic structures and become more unpredictable and unmanageable.

#### **Scrapping the System of Bilateral State Trade in Rubles**

First, the system of bilateral trading arrangements established by the Council for Mutual Economic Assistance (CMEA), which comprised half or more of each country's trade, was undergoing internal

reforms and being bypassed by its members in 1989; in 1990 it completely disintegrated and will be replaced in 1991 by a confusing mixture of state trading with a clearing agreement in dollars and direct market transactions.<sup>5</sup> Also, debt balances in rubles are being converted at bilaterally renegotiated rates from rubles to dollars.

The CMEA system, already in a state of disintegration because of its internal inadequacies, collapsed under the combined pressure resulting from German unification and the failure of all its members to honor commitments. Especially significant was the Soviet Union's failure to deliver promised oil supplies. How much of a shortfall there was is still being debated. One study suggests that Soviet deliveries in the first half of 1990 were as much as 20% below those of the previous year and that there were reductions of up to 30% of promised deliveries in the second half of the year.<sup>6</sup> Cuts have also been made in promised deliveries for 1991.<sup>7</sup> In addition, the state of Soviet politics has led to increasing confusion about who can or should be negotiating foreign trade in the country that remains the single most important trading partner in the region.

#### **The Economic Impact of the Gulf Crisis**

Just as the smaller East European partners were receiving the Soviet Union's bad news that they would either have to make do with much smaller quantities of oil delivered at subsidized prices or buy oil on world markets at world prices, the Gulf crisis broke out. The direct costs have been in the form of disrupted trade, broken contracts, and lost oil supplies, which Iraq had been shipping as part of debt payments (incurred by previous imports of arms during its war with Iran).<sup>8</sup> In addition, there are indirect costs from the Gulf conflict, especially the price of all oil imported at world market prices, including most Soviet deliveries. The total costs, both direct and indirect, to Yugoslavia and Czechoslovakia have been estimated at \$1.2 billion and \$1.4 billion, respectively.<sup>9</sup> Romania's total figure came to \$3 billion, Poland's to \$2.9 billion, and Bulgaria's to \$2 billion (including projected losses in 1991, as well).<sup>10</sup> The estimated cost to Hungary as a result of higher oil prices and lost exports alone was some \$155,000,000 in 1990 and \$1.1 billion forecast for 1991.<sup>11</sup> Hungarian Prime Minister Jozsef Antall said in October, for example, that the losses to Hungary in 1990 arising from the Gulf crisis were some \$500,000,000.<sup>12</sup> The problem with most of these figures is that they do not clearly identify either the methods of estimation or the component parts of the estimates, which should identify separately first, canceled contracts on which no expenditures have yet been made, second, lost

future exports, third, payments on already delivered exports or contract work, fourth, payments in kind or money on debts due, and, fifth, additional costs for substitute imports (especially important for promised oil deliveries).

One Western expert estimated the added costs of oil in the region at \$2 billion in 1990 and \$7 billion in 1991, in addition to \$6 billion in 1991 for the cost of "dollarizing" CMEA trade.<sup>13</sup> An estimate by the World Bank put the combined impact of the Soviet and the Gulf problems at \$15 billion for the region, or an average drop of about 5% in the gross national product, the largest drop occurring in Bulgaria (15%) and the smallest in Hungary and Czechoslovakia (both 1%).<sup>14</sup> A further impact may yet be felt if world export and financial markets are disrupted as a result of higher oil prices worldwide.

#### Western and International Assistance

According to a recent report of the Organization for Economic Cooperation and Development, lending by Western banks to Eastern Europe declined by \$6.4 billion in the second quarter of 1990 and is described as having "dried up."<sup>15</sup> At the same time, the Gulf conflict and the deterioration of the economic and political situation in the Soviet Union might reduce or disrupt the single most positive item on the East European countries' external economic account. The developed capitalist countries, including the European Community (EC), were in the process of opening channels to achieve more normal levels of East-West trade and finance by means of trade agreements, integration with the General Agreement on Tariffs and Trade, and facilitating membership in the International Monetary Fund (IMF) and the World Bank. In addition, significant economic assistance has already been mobilized for Poland and Hungary and is being considered for Czechoslovakia, Romania, and Bulgaria. Among the commitments being coordinated by the EC are \$15 billion in aid pledged to Hungary and Poland through 1992 and \$3.8 billion in aid to Czechoslovakia, Bulgaria, and Yugoslavia from the Group of 24.<sup>16</sup> The World Bank plans to increase its loans to Eastern Europe from only \$540,000,000 in the 1988-1989 fiscal year and \$1.8 billion in the 1989-1990 fiscal year to \$7.5 billion over the next three fiscal years.<sup>17</sup> Although internal political problems in Romania and Bulgaria had already disrupted programs for foreign assistance and for opening trade and financial markets, their continuation has been further delayed by the intrusion of larger issues. For example, food and other assistance programs to the Soviet Union might at present take precedence over helping the smaller countries.

#### The Growing Importance of Direct Foreign Investment and Joint Ventures

While there no reliable compilations yet of the amount of direct foreign investments, it seems that these sums are still rather modest. But the reported number of joint ventures that have been set up, estimated at 10,000, indicates a growing interest and potential response to the general liberalization of the laws governing commerce, foreign investment, and banking.

It was reported in August<sup>18</sup> that some 2,800 joint ventures, 95% with West German firms, had already been set up in what used to be East Germany. About 2,500 joint ventures with a total investment of \$750,000,000 were reported for Hungary as of October, compared with the June figure of 1,800 (and the June 1989 figure of only 280). Half the companies are in manufacturing; 70% of the joint ventures are with Austrian or German partners; and some 40% of the investment capital is from US firms.<sup>19</sup> Poland reported that, of the 1,700 foreign and joint-venture companies granted investment licenses, 949 were conducting business in the country at the end of 1989. Poland's agency for foreign investment, which was set up this year, announced in the fall that it had issued about 2,000 permits for joint ventures, of which about 800 had started operating. That figure suggests that joint ventures currently operating in Poland total at least 1,500.<sup>20</sup> Some 2,069 contracts for joint ventures were signed in Yugoslavia between January and September 1990.<sup>21</sup> By November Romania reportedly had 570 joint ventures, and a total of \$66,000,000 had been invested by foreign firms since December 1989.<sup>22</sup>

#### The Impact on Foreign Trade Balances

Caution should be exercised when working with the foreign trade statistics of all the East European countries.<sup>23</sup> It has long been known that statistics on total exports and imports as well as on the division of trade by region or by socialist and nonsocialist countries have been distorted because trade figures were aggregated using different price systems and because official rates of exchange were meaningless. For example, it could only be said that total exports had increased if exports both to socialist and nonsocialist countries had increased. And if the value of exports to socialist countries fell while the value of exports to nonsocialist countries rose, one could be relatively sure that a shift of exports from the socialist to the nonsocialist countries had occurred. But the events of 1990 further reduced the possibility of obtaining accurate statistics. Increasingly large portions of trade between the socialist countries shifted to hard-currency accounting. Thus it is no longer safe to assume that

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a reduction in soft-currency trade constitutes a shift of trade from socialist to nonsocialist countries.

The figures compiled for each country clearly indicate a shift from trade in rubles to trade in hard currency. To what extent this constitutes a regional shift of trade will not be clear until more is known about how rapidly trade within the CMEA is being "dollarized." Only Czechoslovakia seems to have managed to maintain a current account surplus in hard currency. The relatively large trade surpluses being generated in hard currency by Poland and Hungary are not enough to generate positive current accounts. Bulgaria, which could hardly afford it, and Romania, which was in a better position to do so, generated hard-currency trade deficits. With only one out of five East European countries generating a positive current balance this year, next year's terms-of-trade losses will either force significant restrictions on imports or bring about a general increase in foreign debts.

Bulgaria's total exports (adding rubles to hard currency at an unknown exchange rate) fell 28% in the first 10 months of 1990 compared with the same period in 1989.<sup>24</sup> At least part of this decline was accounted for by a diversion of goods for black-market export in exchange for hard currency, an activity that probably involved Bulgarian firms seeking means to pay for imported supplies.

In recent years, the ruble value of Bulgarian exports and imports with socialist countries has tended to decline. Since imports have fallen faster than exports, larger surpluses have been generated: some 1.6 billion rubles with the Soviet Union alone in 1989. The overall trade balance with socialist countries is expected to change from a large surplus in 1989 to a small deficit in 1990 because of limits placed on Bulgarian exports.

Bulgaria's trade with nonsocialist countries has been a sad tale. Imports rose while exports remained constant or fell, so that the balance of trade in 1989 showed a deficit of \$1.8 billion. Both exports and imports fell in 1990 as a result of disorganized export production (and probably significant diversion for black-market exports) and growing credit restrictions. The first-quarter deficit of \$150,000,000 was expected to rise to between \$600,000,000 and \$700,000,000 by the end of the year, despite Bulgaria's moratorium on debt payments announced at the end of March.

Czechoslovakia's trade has shifted from the East to the West. In the first half of 1990, exports to the West rose by 10% and imports increased by 28%. Contrary to the hard-currency current account deficit projected by PlanEcon, however, it was reported that the balance through October was still \$300,000,000 in the black.<sup>25</sup> In contrast, both

exports and imports with the Soviet Union fell by between 14% and 15% in real terms, and large reductions in exports to other socialist countries were also reported. In the first nine months of 1990, the estimated total trade deficit was about 5 billion koruny.<sup>26</sup> In 1991, rising import costs and falling export prices could cost the country an estimated \$1.8 billion in declining terms of trade.<sup>27</sup>

It had been expected that by the late summer Hungary's ruble exports would have declined even more sharply than its ruble imports, turning the ruble trade surplus of 1989 into a deficit. By the end of October the recorded deficit was 201,000,000 rubles.<sup>28</sup> Hungary's trade was clearly shifting to hard currency, although to what extent this was based on a regional shift is not yet known. Hard-currency exports rose sharply in real terms and imports in real terms declined slightly. This resulted in a strong increase in the balance of trade, which was recorded at \$890,000,000 in the first 10 months of 1990. That figure did not, however, include \$170,000,000 in oil purchases in October and November.<sup>29</sup> Thus, the trade balance, contrary to PlanEcon's early optimistic forecast, will probably not be large enough to balance Hungary's current account. This will add to Hungary's debt in 1990.

Hungary's most recent discussion with the IMF began on a sour note, owing to the expected loss of \$1.5 billion in its terms of trade that accompanied the changeover to the dollar in CMEA trade. According to the Vice President of the National Bank of Hungary, "The IMF has to realize that we will not be able to bring the affected 30% of our foreign trade into balance between January 1 and January 2."<sup>30</sup> But if Hungary does not do something soon, it might not be able to service its large foreign debt. In addition, with the switch to trade in dollars, the government stands to lose between 50 billion and 60 billion forint in import duties.

Poland is also sharply reducing its ruble trade and expects to cut more than 10% in the real volume of its exports and more than a third in its real volume of imports. The result is a huge ruble trade surplus, large enough to pay off completely Poland's debts to the Soviet Union. A further decline of 30% in total trade turnover with the Soviet Union has been forecast for 1991.<sup>31</sup> Although imports of goods paid for in dollars are also expected to drop by a quarter, exports in exchange for dollars have increased by a quarter. The result is a record dollar trade surplus, which is reported to have reached \$3.7 billion by the end of October 1990.<sup>32</sup>

At official rates of exchange, convertible currency exports in the first nine months of this year accounted for 81.4% of Poland's total exports, a slight increase over the 77.6% recorded over the same period last year. The percentage of convertible

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currency imports fell slightly.<sup>33</sup> In 1991, the rate of convertible-currency trade should soar as Soviet trade is "dollarized." If the commodity composition of Soviet-Polish trade remains the same, however, Poland will face deficits of between \$1.2 and \$2 billion.<sup>34</sup>

In the first eight months of 1990, Romania reported a trade deficit of over 1.1 billion rubles and \$908,000,000, which, combined with the deficits in September and October, totals almost \$1.2 billion and about 1.4 billion rubles.<sup>35</sup> PlanEcon did not predict anything close to the latter figure, which was the result of Romania's exports for rubles falling faster than its imports for rubles. The latter were 14% lower in the first nine months of 1990 than last year. Thus, the ruble trade deficit is not necessarily a sign of significant Soviet willingness to support Romania. According to official statistics, hard-currency imports rose by 54% in current values in the first nine months of 1990 compared with the same period last year. By contrast, ruble imports dropped in value by 14%. With exports in both directions falling by more than half, the result was a hard-currency deficit of nearly \$1 billion.<sup>36</sup>

In the first half of the year, Yugoslavia was exporting at a rate that would have resulted in a rise of almost 24% in its annual total exports, had it continued. The rate of imports increased even faster and was almost 34% higher than in 1989. Part of the increase in imports can be attributed to trade liberalization and part to the legalization of trade in the convertible dinar.

Some 80% of Yugoslavia's trade in 1989 was conducted in convertible currency. Nevertheless, the Soviet Union remained the single most important trading partner, even more so since its trade was scheduled for "dollarization" in 1991. Yugoslavia generated a trade surplus of \$2.2 billion with the Soviet Union in the first seven months of 1990. This raises the problem of which rate of exchange will be used when Yugoslavia begins settling Soviet debt balances through actual payments.

#### The Effects on Debt Balances

The net result from "dollarizing" Bulgaria's debt balances in rubles has yet to be determined. Its net hard-currency debt of \$9.2 billion at the end of 1989 was calculated on the basis of assets including Third World debts of \$2.3 billion. Bulgaria had an agreement with Iraq that its debt would be repaid in the form of oil deliveries. That and other parts of such assets are probably no longer collectible.

Bulgaria's suspension of debt payments in March initially covered only \$3 billion of principal due in 1990, but in June this was extended to \$1.8 billion of interest also due in 1991. In order for Bulgaria's creditors to work out a rescheduling

plan, Bulgaria must first conclude an agreement with the IMF, of which it is now a member. Such an agreement would not only provide IMF credits but would serve as a condition for receiving help from the World Bank. However, the IMF has no reliable government partner in Bulgaria with whom to work out an agreement. Meanwhile, Bulgaria received help in the form of oil and electricity, as well as \$50,000,000 in trade and \$25,000,000 in investment credits, from a surprising source, Turkey, that it can pay back next year.<sup>37</sup> PlanEcon was projecting a mild rise in both gross and net debts on the basis of estimated hard-currency trade deficits of between \$600,000,000 and \$700,000,000.

While Czechoslovakia's gross foreign debts rose to over \$7 billion in 1990, by mid-year its hard-currency debts were already exceeded by its hard-currency assets, leaving it on net an international creditor. PlanEcon expected the balance in net assets to reach \$3.2 billion by the end of 1990. There are two forces at work in addition to those stemming from the Gulf crisis and the revaluation of Soviet trade. First, balances are being cut by reducing the value of debts from the Third World that are not collectible. At the same time, according to PlanEcon, debts owed by the Soviet Union are being revalued in dollars at a favorable rate of 1 ruble to \$1.25. Czechoslovakia will also be under pressure in 1991 because of the introduction of internal convertibility. In order to be ready to supply the expected demand for hard-currency balances, the government plans to ask the IMF for at least \$1.5 billion in stabilization funds.<sup>38</sup>

Despite having generated a significant hard-currency surplus in 1990, Hungary does not appear to have available the \$1.6 billion in interest and the \$2.2 billion in principal due on its debts in 1991, even if the latter were refinanced.<sup>39</sup> Hungary will probably have to increase its net debt by a modest amount in 1990 and by more in 1991. Just how much this increase will be depends on the extent to which the debt is rebalanced.

The expected effects of "dollarizing" Soviet trade could push the current account balance for 1991 almost \$1 billion into the red. According to PlanEcon, the true debt situation would be worse (a net hard-currency debt of well over \$18 billion by the end of 1990) if Hungary were to take the correct approach and reduce the value of debts owed by Third World countries. How much effect the conversion of Soviet debts will have on this debt is unclear. Hungary is attempting to settle what it claims is the Soviet Union's debt of \$1 billion. The Soviet Union reportedly offered to pay the balance over a five-year period.<sup>40</sup>

Poland's record trade surplus allowed it to move from a significant deficit on its current account

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in 1989 to a significant surplus, estimated by PlanEcon at \$2.5 billion in 1990. Its hard-currency reserves, virtually nonexistent at the beginning of the year, grew to \$3.5 billion by October 1990. As a consequence, it did not draw on the \$1 billion stabilization fund that had been provided by Western countries. Even so, its gross debt grew to \$45.2 billion, of which \$2 billion resulted from a declining dollar and \$2.5 billion from the accumulation of unpaid interest.<sup>41</sup>

In 1991 Poland will have payments due on its debt of \$7.2 billion, which will consist partly of postponed debts and partly of new credits. Poland will be unable to postpone any of its debts, however, until it reaches new agreements with either the commercial banks, which together are carrying about \$10.2 billion of the debt, or the Paris Club of Western governments, which is carrying the bulk: \$30.6 billion. The banks are waiting for the club, which had sought to assist Poland by postponing payments of interest and principal until March 1991, to make the first move.<sup>42</sup> What Poland would like and badly needs is for club members to follow Germany's example. In November it canceled roughly \$500,000,000 of Poland's debt to it.<sup>43</sup> Despite repeated rumors that it planned to do so, the USA has still not moved to help Poland in this way.

From nearly zero, Romania's gross debt in hard currency is expected to increase by about \$3 billion in 1990; the country will change from being a net creditor to being a (small) net debtor. Romania probably shares with Czechoslovakia the distinction of suffering less from its inability to borrow than from the lack of effective management and knowledge of how to invest properly the funds it has been loaned. But Romania's international image is far worse than Czechoslovakia's.

In 1989 and the first four months of 1990, Yugoslavia's net foreign debt in convertible currency fell by an estimated \$4.7 billion, partly because the new, overvalued dinar encouraged Yugoslavs to repatriate hard currencies owned abroad. PlanEcon had expected a net debt reduction of only about \$1.4 billion for the whole of 1990. In 1991 Yugoslavia will probably not be able to reduce its net debts any further, but the political situation makes any prediction highly uncertain.

#### Summary and Conclusions

Amid the internal and external confusion of foreign-trade decision making in 1990, only Czechoslovakia and Poland seem to have generated a current-account surplus in hard currency, and in the case of Poland, this happened only because of the deferment of some interest payments. Yugoslavia got by because significant amounts of hard currency were repatriated. The others added to their debts, although in the case of Hungary the increase was small. Adverse terms of trade will generate major deficits next year unless steps are taken to reduce import demand by deflation or specific measures are implemented to reduce energy consumption. Also, Poland's example in 1990 suggests that others could generate significant increases in hard-currency exports if they were willing to make tough decisions about economic reforms. Otherwise, all countries will need special credit assistance and, in the cases of Poland, Hungary, and Bulgaria, possible debt relief. A recession in the West would probably force Eastern Europe to resort to major cuts in imports.

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#### Notes:

1 AFP, November 23, 1990; and *The Guardian*, November 26, 1990.

2 CTK (in English), November 19, 1990.

3 Rompres, April 14, 1990.

4 *MTI Econews*, November 9, 1990.

5 Marie Lavigne, "The CMEA's Transition from the Transferable Ruble," *Report on Eastern Europe*, no. 44, November 2, 1990, pp. 34-47.

6 Estimates of the Vienna Institute for International Economic Comparisons, cited in *Die Zeit*, November 23, 1990.

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15 Reuter, November 20, 1990.

16 *Ibid.*, November 20, 1990.

17 *Ibid.*, September 23, 1990.

18 *Financial Times*, August 24, 1990.

19 Reuter, July 3, 1990; and *The Journal of Commerce*, July 25 and October 23, 1990.

## REGIONAL TOPICS

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31 *Handelsblatt*, November 23, 1990.

32 Reuter, November 16, 1990.

33 PAF (in English), October 12, 1990.

34 *Handelsblatt*, November 23-24, 1990.

35 Rompres, October 1 and November 13, 1990.

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37 BTA (in English), October 26, 1990.

38 *The New York Times*, November 17, 1990.

39 *Financial Times*, November 8, 1990.

40 *The Guardian*, November 26, 1990.

41 Reuter, November 16, 1990.

42 *Financial Times*, November 6, 1990.

43 Reuter, November 8, 1990.

The Weekly Record of Events for December 14-21, 1990, will appear in issue 1, on January 4, 1991.

Frederick I Barbarossa and, later, as imperial administrative secretary, experienced the looting conquest of Constantinople and its art in 1204 by the French-led forces. Forced to flee Constantinople and aided by a Venetian merchant, Nicetas moved to the outlying area of Nicaea, site of the emperor Theodore I Lascaris' Byzantine court-in-exile, and wrote the 21-volume "History of the Times," a record of the rise and fall of the 12th- and 13th-century Byzantine dynasties through the combined devastations of Western Christian and Eastern Seljuq and Ottoman Turkish armies, beginning with the Greek emperor John Comnenus (1118-43) and concluding with the intrusion of the first Latin Eastern emperor, Baldwin I of Flanders (1204-05).

A fervent Greek Byzantine nationalist acutely resentful of European designs on the Christian East, Nicetas nevertheless, as actor and spectator, at times incorporating other reports, as with the Norman pillage of Thessalonica, Greece, produced a generally objective and concrete, although rhetorical, account of the Crusades' campaigns in Byzantium, which counterbalanced the leading Western version by the French crusader Geoffroi de Villehardouin.

In the theological sphere Nicetas composed the "Thesaurus of Orthodoxy," a collection of doctrinal and polemical tracts to serve as source material for responding to contemporary heresies, particularly the dualist Bogomil sect that advocated the principle of matter as evil, and to document the 12th-century Byzantine philosophical movement. The "Thesaurus" included notable texts of Nicetas Stethatos, a Byzantine theologian involved in the schism of 1054, and decisions of Eastern Church councils. Much of the content and style, however, derive from and supplement the "Dogmatic Panoply" drawn up by the 12th-century Greek Euthymius Zigabenus.

·Byzantine historiographic literature 8:951c

**chōnin**, class of townsmen that emerged in Japan during the early years of the Tokugawa period (1603-1867) and became an influential and prosperous sector of society.

So named because of their residence in city wards (*chō*), the *chōnin* were generally merchants, though occasionally craftsmen and artisans were included in their number. In spite of compulsory loans, property confiscations, and legislation designed to restrict their wealth, the *chōnin* multiplied rapidly during the Tokugawa, and their prosperity contrasted greatly with the financial straits of the peasant and samurai classes, who became heavily indebted to the *chōnin*. This resulted in considerable resentment and discontent, for which the government was often blamed.

Under *chōnin* sponsorship advances were made in the fields of astronomy, agronomy, medicine, and civil engineering in Japan. Moreover, a distinct *chōnin* culture developed in the major Japanese cities, especially during the Genroku (1688-1703) and Bunka-Bunsei (1804-29) periods. Characterized by conspicuous consumption, this culture led to the development of new art forms such as haiku poetry, Kabuki and *jōruri* theatre, and erotic novels and short stories. It also involved the extensive use of female entertainers and courtesans, such as geisha girls, who first came into prominence at this time.

Unlike their Western contemporaries the *chōnin* never emancipated themselves from dependence on government sponsorship. When freed of governmental interference and allowed to develop independently after the Meiji Restoration, the 1868 overthrow of feudal rule, the *chōnin* class gradually declined. Samurai entrepreneurs generally replaced *chōnin* as leaders of the business community.

·Kabuki theatre design development 10:368b  
·styles produced 10:1070e

**Chōnju**, city and provincial capital, Chōlla-pukto (North Chōlla Province), southwestern South Korea. One of the oldest cities in Korea, from the Three Kingdoms period (c. 57 BC) it was a strategic point of local civil and military administration. It is 21 mi (34 km) east of the Yellow Sea coast and surrounded by steep hills with fortified castles. Known as the cradle of the Yi dynasty (1392-1910), it has many historical remains. Although the population is large, the city is still calm and rural with 80 percent of its land containing green vegetation. It is connected by rail and highway with Seoul north through Taejōn and with two other big port cities by rail, west with Kunsan, and south with Yōsu. After the construction of a big paper mill in 1968, Chōnju became an industrial city. Other industries are textile and canning. Chonbuk National University and three minor colleges are located there. Pop. (1970) 262,818.

35°49' N, 127°08' E  
·map, South Korea 10:524  
·urban location map 10:526

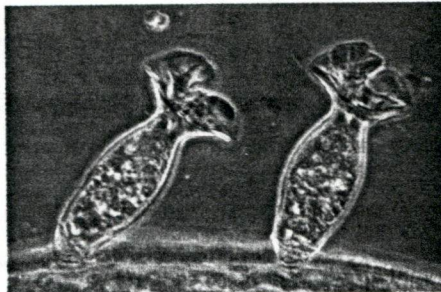
**Chon languages**, group of languages of Argentina that belong to the Macro-Pano-Tacanan language family.

·classification and location table 17:107  
·grammar, phonology, and vocabulary 17:110d  
·*passim* to 112b

**Chono**, South American Indian people who became extinct in the 19th century. In aboriginal times they inhabited the southern Chilean archipelago from Corcovado Gulf to the Gulf of Peñas. Like the Yámana and the Alacaluf (*qq.v.*), the Chono were canoe-using people who lived by gathering shellfish and catching seals and birds. They were able, however, to supplement their hunting and gathering activities with sporadic farming. Their culture was probably very similar to that of the Alacaluf, but it is not known whether their language was the same.

·cultural and economic patterns 17:112f *passim* to 116b  
·geographic distribution and socioeconomic structure 17:116e; map 117  
·geographic distribution map 17:113

**chonotrich**, any small, vase-shaped, sessile (nonmotile) member of the protozoan order Chonotrichida. Usually marine, they belong to subclass Holotrichia. As adults chonotrichs have no minute hairlike projections (cilia) for



*Spirochona* on gill cover of crustacean (*Gammarus*)  
M. Walker from the Natural History Photographic Agency—EB Inc.

independent locomotion. Instead, they attach themselves to aquatic arthropods either directly or by means of short stalks. Chonotrichs produce swimming larvae by asexual budding, and some forms reportedly reproduce sexually by conjugation. *Spirochona*, with a winding funnel-shaped collar, is a common genus.

·protozoan features and classification 15:129c

**Chontal**, Mayan Indians of Tabasco in southeastern Mexico. The Chontal are linguistically closely related to the Chol (*q.v.*), their neighbours to the south, and to the Chorti (*q.v.*), of eastern Guatemala. Chontal, Chol, and Chorti are all mutually intelligible languages. The Chontal and Chol also share a similar environment and culture. Rainfall is

heavy and the climate humid. The Chontal grow corn, beans, and squash as staple crops and weave palm-leaf fibre into strips to be used for making hats. The making of hats is of great economic importance to the region. Other crafts have for the most part died out. Clothing is factory-made; men wear trousers and shirts, and women wear cotton dresses and, on special occasions, shoes. Houses are built of poles or lumber with palm thatch roofs, sometimes plastered with mud or covered with lime.

Religion is Roman Catholic, centred on the worship of patron saints. Annual fiestas celebrate saints' days. The church also serves as a sort of community centre. Elves or dwarves are also venerated; these appear to correspond to pagan mountain and forest deities.

·linguistic affiliation 11:954g  
·Meso-American Indian distribution map 11:955

**Chontales**, department, central Nicaragua, bounded on the southwest by Lake Nicaragua. The 1,910-sq-mi (4,947-sq-km) department stretches eastward from the lowlands bordering the lake over the Sierra de Amatique, the continental divide. Until 1949 Chontales included the territory in neighbouring Río San Juan department. Agriculture is important, particularly in the north: the principal crops are sugarcane, coffee, bananas, beans, and corn (maize), and livestock raising and cheese production are significant. Forest products—timber, hardwoods, chicle, and rubber—provide additional income, as does gold and silver mining. No railroads serve Chontales, but the highway linking Managua, the national capital, with the Caribbean lowlands passes through Juigalpa (*q.v.*), the departmental capital. Pop. (1971 prelim.) 69,059.

·area and population table 13:59  
·map, Nicaragua 13:60

**Cho Oyu**, one of the world's highest mountains (26,750 ft [8,153 m]), in the Himalayas on the Nepalese-Tibetan (Chinese) border about 20 mi (30 km) northwest of Mt. Everest. The Nangpa La, a glacier saddle (pass) 19,050 ft high lying south of the peak, forms part of the trade route between Tibet (China) and the valley of Khumbu. Glaciers and a bitter climate delayed the climbing of Cho Oyu until Oct. 19, 1954, when the summit was reached by an Austrian party including Herbert Tichy, Sepp Jöchler, and Pasang Dawa Lama, a Sherpa (an inhabitant of the Himalayas).

28°06' N, 86°39' E  
·Great Himalayan peaks 8:883c; map 882  
·map, Nepal 12:952  
·mountaineering record and data table 12:585

**Chopin, Frédéric** 4:439 (b. March 1, 1810, Zelazowa Wola, Pol.—d. Oct. 17, 1849, Paris), composer who although his total output was small and practically limited to solo pianoforte was distinguished for creating within this limited framework a vast musical and emotional range. A Romantic, he found himself and the tragic circumstances of his native Poland the chief sources of his inspiration.

*Abstract of text biography.* Chopin, a prodigy, started piano lessons at the age of seven and first played in public at the age of eight. He went to the Warsaw Conservatory at the age of 16, studying piano and composition. After visits to Vienna, he settled more or less permanently in Paris when he was 21. There he formed a liaison with the famous novelist George Sand, with whom he went on a journey to Majorca that undermined his health. His time at Sand's country home at Nohant in France was more happy, and it was there that he produced much of his most searching music. After the revolution of 1848, he fled to England for the better part of the year. By the time he returned to Paris, his frail health—he suffered from tuberculosis—had worsened, and he died in October of the following year.

Chopin's long list of solo pieces for the

piano, his piano concertos, and his songs injected a new strain of poetic fancy into those genres. Critics marvelled at the way he reconciled startling originality and exquisite craftsmanship.

REFERENCES in other text articles:  
·concertos for piano 4:1072f *passim* to 1073a

·folk music influences 14:636d  
·harmony's colouristic use 8:653e  
·style and technical factors 2:133b

**chopper**, device for interrupting an electric current at regular intervals.

·electronic control of alternating current 6:683g *passim* to 685d

**Chopper chopping-tool industry**, generic name for certain stone tool traditions of Asia, probably of the late Pleistocene, characterized by roughly worked pebble chopping tools (see pebble chopper). These traditions include the Choukoutienian industry of China (associated with Peking man), the Patjitanian industry of Java, the Soan industry of India, and the Anyathian industry of Burma.

Stone with good fracture qualities, such as flint, jasper, and chert, was not as readily available in Asia as it was elsewhere in the world. Asian populations, therefore, depended on coarse-grained quartz, volcanic tuff, and petrified wood, none of which lends itself to fine tool manufacture. The lack of good materials may explain why stone toolmaking did not evolve in Asia. Choppers and chopping tools were still being made, for example, by Solo man of Asia, while Neanderthal man, his European contemporary, was able to manufacture the more advanced hand axes, borers, and knives, as well as choppers.

The characteristic tools of the Chopper chopping-tool industry were the chopper, with a single straight or curved cutting edge flaked from a pebble or from a chunk of stone; the chopping tool, with a bifacial cutting edge flaked, again, from a pebble or chunk of stone; and the hand adze, shaped from a block of stone, with a rounded butt and a single-bevel straight or curved cutting edge. Stone scrapers, cleavers, and points were also fashioned, and some tools were made of bone.

#### Anyathian industry

·Burmese ancient social patterns 3:510e  
·geographic and technical characteristics 2:204a  
·hominid fossil sites and culture 8:1051a  
·geographic sites and related traditions 2:203g  
·Homo erectus cultural advances 8:1033g  
·Pleistocene stone tool cultures. 14:840b; illus. 839  
·toolmaking technique and tool use 8:607d; illus. 608

**Choquette, Robert-Guy** (1905– ), French-Canadian writer, whose freedom of expression and disregard of syntax influenced the younger generation of Canadian poets. His *Oeuvres poétiques* ("Poetical Works") appeared in two volumes in 1956.

**choragic monument**, large, freestanding pedestal that forms the display base for an athletic or choral prize awarded in ancient times at a Greek festival. Although the only surviving example is the choragic Monument of Lysicrates (335/334 bc) in Athens, literary evidence of the existence of this type of monument may be found in Virgil's *Aeneid*.

The Lysicrates monument has a square base of 9.5 feet (2.9 metres) on which rests a circular structure surrounded by six Corinthian columns. The entablature of the monument supports a shallow dome, which, in turn, is the base of three scrolls intended to hold the tripod trophy (now missing). Although hollow, the interior of the monument was not intended for use. The choragic Monument of Lysicrates is an early example of the use of the Corinthian order. See also orders of architecture.

**chorale**, metrical hymn tune associated in common English usage with the Lutheran Church in Germany. From early in the Reformation, chorales were to be sung by the congregation during the Protestant liturgy. That they were called chorales does not imply that they were designed for singing in harmony; unison singing was the rule of the Reformed churches, both in Germany and in other countries.

Early polyphonic (multivoiced) versions may have been intended for the choir, which possibly sang only the melody, while the full version was played on the organ. In polyphonic arrangements the melody shifted only gradually to the treble line from its original position in the tenor. Likewise, the organ was established only over a period of time as the most commonly used harmonic base for congregational singing.

The words of the Lutheran chorales were often Latin plainsong hymn texts translated into the vernacular. The melodies were often borrowed from secular song and therefore displayed great melodic and structural simplicity; Luther's own versions were often more irregular than the polished versions that later predominated.

The earliest large collection of such melodies was the *Geystliches Gesangk-Buchleyn* (1524), edited by Johann Walther with a preface by Luther. From that time, the technique of chorale writing expanded and many collections were published. Luther's own compositions include "Ein feste Burg" ("A Mighty Fortress") and "Vom Himmel hoch" ("From Heaven High"), of which he certainly wrote the words and almost certainly wrote or adapted the music.

Prominent in the development of the chorale in the late 15th and the 16th century were Michael Weisse; Philipp Nicolai, composer of the celebrated "Wachet auf!" ("Wake, Awake"); and Melchior Vulpus. Active in the 17th century were Johann Hermann Schein and Johann Crüger. Crüger edited the first editions of *Praxis Pietatis Melica*, a collection of tunes first published in 1644.

More complex chorales came from Johann Eccard, Michael Praetorius, and Heinrich Schütz. Eccard's chorale settings are virtually brief motets; Praetorius was one of the first systematic arrangers in polyphonic style of tunes from earlier sources (*Musae Sioniae*, 1610); Schütz's contributions, many of which foreshadowed the more sophisticated and lyrical style adopted by the later Pietist composers, are collected in his *Psalmen Davids* (1628). See hymn, the music of.

In the passions and cantatas composed by J.S. Bach, the chorale appears as a richly harmonized hymn tune in which the congregation is expected to join with the choir. Bach's chorales are strictly choral arrangements of well-known hymn tunes, adorned with elaborate harmony; he never composed an original chorale.

**chorale cantata**, a cantata in which a chorale text (and, as a rule, chorale melody) is used for a movement other than the final one, which is nearly always a harmonized chorale.  
·variation forms in Baroque music 19:29b

**chorale prelude**, musical form most closely associated with organ music, in which a chorale, or German hymn melody, is made the basis of a brief introductory instrumental piece that decorates or varies the chorale. The organist in Lutheran churches traditionally introduced congregational hymns not by playing an introductory phrase of the melody but by extemporizing briefly on the tune (hence the term prelude), and these extemporizations became known as chorale preludes. The form was invented well before J.S. Bach's time, and since his death most organ composers have attempted it. Even when the cantus firmus, or basic melody, is not a German tune, the piece is often still called a chorale prelude. In addition to Bach, the most eminent exponents of

the chorale prelude form for organ included the composers Dietrich Buxtehude, Johannes Brahms, and Max Reger.

·musical form types 12:727b  
·organ musical composition history 13:680d

**chorale variations**, series of different harmonic versions of a hymn originally designed for congregational singing.

·strophic form in instrumental music 12:727a  
·variation forms in Baroque music 19:29b

**choral lyric**, poetry intended to be sung by a chorus, particularly associated with the Greek poet Pindar (5th century bc). See also ode; Pindaric ode.

·Greek literary style and development 10:1091f  
·Pindar's style and surviving works 14:465c

**choral music** 4:442, strictly defined, music sung by a choir with several voices assigned to each part. Much of the music sung by a choir today, however, was originally intended for a group of soloists, with one voice assigned to each part.

The text article covers the emergence of a choral tradition; sacred choral music—the mass, motets, anthems, and oratorio; occasional pieces for chorus; secular chorus works; and madrigals with their related forms.

REFERENCES in other text articles:

·African song formula and function 1:244e  
·Brahms's influence on Vienna 3:108b  
·concerto evolution from polyphonic choral music 4:1066b  
·drama rebirth in Middle Ages 18:221g  
·Franck's 19th-century style 7:688g  
·fugue for chorus and orchestra 7:769h  
·Middle Ages, Renaissance, and Baroque 12:705e *passim* to 709e  
·Monteverdi's madrigal style 12:403d  
·opera's ancient and medieval precursors 13:579c  
·operatic influence in Classical era 12:712d  
·original function and later development 12:741b  
·Purcell verse anthem development 15:298b  
·singing group's reflection of inter-group relations 16:791d  
·sonata's evolution 17:7a  
·variation of melody in variation sets 19:27h  
·vocal range and combinations 13:645c

RELATED ENTRIES in the Ready Reference and Index: for

*monophony*: see antiphon; kanon; kontakion; plainchant; psalmody; psalm tone; responsorial singing; responsory; sequence; troparion; trope

*polyphony*: anthem; antiphonal singing; cantata; chorale; chorus; national anthem; oratorio  
*monophony* and *polyphony*: canonical hours; church music; hymn; mass, music of the; Passion music; Te Deum Laudamus  
*performance mode and groups*: choir; schola cantorum

**Chorasmia** (region): see Khwārezm.

**Chorasmian language**: see Khwārezmian language.

**Chorcaigh** (county, Ireland): see Cork.

**chord**, in music, the combination of several tones sounded at once. In the analysis of harmony, chords may be consonant, implying repose, or dissonant, demanding movement to another chord. The triad, which underlies the Western system of harmony, is a chord composed of three tones that form two intervals of a third and one of a fifth; for example, e-g (a third) superimposed on c-e (another third) becomes the triad c-e-g (which includes the fifth c-g).

Superimposing an additional third upon a triad forms a seventh chord (for example, c-e-g-b or c-e-g-bb; c-b and c-bb are sevenths); still another superimposed third forms

**Copernicia cerifera** (plant): see carnauba wax.

**Copernicus**, a crater on the surface of the Moon that is the centre of an extensive system of bright surface rays. The diameter of the crater is roughly 100 kilometres (60 miles), and it lies at about 10° north latitude, 20° west longitude.

·thermal anomaly 12:427a; illus. 422

**Copernicus 5:145**, in full **NICOLAUS COPERNICUS** (b. Feb. 19, 1473, Toruń, Pol.—d. May 24, 1543, Frauenburg, East Prussia, now Frembork, Poland), astronomer famous as the proponent of the view of an Earth in daily motion about its axis and in yearly motion around a stationary Sun, a position that had profound effects on the science and philosophy of succeeding centuries.

*Abstract of text biography.* Copernicus received his university education at Cracow (1491–94?) in Poland and at Bologna and Padua in Italy (1497–1503). In 1503 he returned to Poland and took up residence in Frauenburg, where in 1497 he had been elected a canon of the cathedral, a post ensuring lifelong financial security. In 1497 he also made the first of his few recorded astronomical observations. Becoming increasingly dissatisfied with Earth-centred ideas of the universe, he spent many years developing the theory that Earth and the other planets revolved about a point in space near the Sun. From 1510 to 1514 Copernicus circulated the *Commentariolus*, a manuscript summary of his theory. Not until 1540 did he consent to the publication of his complete work, *On The Revolutions of the Celestial Spheres*. A finished copy is believed to have been brought to him on the last day of his life.

REFERENCES in other text articles:

- Aristotelianism and science 1:1160c
- astronomy and religious cosmology 1:872h
- Bradley's proof of orbital theory 3:101a
- history of calculatory device and table 11:650b
- Kant's Copernican Revolution 10:392g
- planetary model development 11:757e
- Ptolemaic system advanced 18:1013c
- science development in Renaissance 16:369e
- scientific revolution in astronomy 14:386c

**coperta**, in ceramics, an Italian term for a clear lead glaze sometimes applied over the tin glaze of Italian maiolica at a second firing to intensify the gloss and colour.

·Italian pottery decorative techniques 14:905g

**Cophes River** (Afghanistan–Pakistan): see Kabul River.

**Copiapó**, capital of Atacama province, northern Chile, lies 35 mi (56 km) inland from the Pacific coast in the fertile Río Copiapó valley, an irrigated oasis (usually regarded as the southern limit of the Atacama Desert) that has been farmed at least since the Inca period prior to Spanish settlement in 1540. The community was elevated to *villa* (town) status in 1744, when it became San Francisco de la Selva de Copiapó. The discovery of gold and silver deposits in the 19th century resulted in Copiapó's becoming a significant mining and political centre, its position being exemplified by the construction (1850–51) of the Caldera and Copiapó railway, one of the first in South America. After a period of decline from 1875 to 1925, the town's economy was revived by the development of copper mines, and a smelter was completed (1950) at nearby Paipote. The railway and all-weather roads connect Copiapó to the port and resort of Caldera, 50 mi (80 km) northwest, to Santiago, and to the adjacent provinces. A road also crosses the Andes into Argentina. Pop. (1970) 39,942.

27°22' S, 70°20' W

·map, Chile 4:248

**Copiaux, Les**, French theatre group founded in 1924 by Jacques Copeau. It was succeeded in 1930 by the Compagnie des Quinze under the direction of Michel Saint-Denis

and continued until 1936, when it was disbanded.

·productions, techniques, and ownership 18:231a

**coping**, the covering course of a wall or parapet, usually slanted, to protect it from the weather and to give it a finish. Although stone is the material most commonly used, brick, lead, or composition are also used; in the north of England the top of a wall is often pantiled, and in Shakespeare's time walls were surmounted with thatch.

·Maurya period stūpa construction 17:173f

**Copland, Aaron 5:147** (b. Nov. 14, 1900, Brooklyn, N.Y.), composer who achieved a distinctive musical characterization of American themes in an expressive modern style.

*Abstract of text biography.* Copland exhibited an early interest in music and in 1921–24 went to France for study. Returning to the U.S., he began his career as a composer with the performance of his *Symphony for Organ and Orchestra* in 1924. During the late 1920s and 1930s, Copland worked with jazz rhythms and was influenced by Stravinsky, producing *Piano Variations* (1930) and *Short Symphony* (1933). He turned in the 1940s to the use of American folk material, producing three ballets (*Billy the Kid*, 1938; *Rodeo*, 1942; *Appalachian Spring*, 1944), orchestral pieces, and film scores. Also typical of this period is *Lincoln Portrait* (1942) on a text from Lincoln's addresses. Important works of the postwar years include an opera, *The Tender Land* (1954), *Twelve Poems of Emily Dickinson* (1950), and *Nonet* (1960).

REFERENCES in other text articles:

- chamber music for various instruments 4:28f
- harmony obscured by chromaticism 8:651f
- music for films 12:667g

**Copland, Henry**, 18th-century English draftsman and engraver employed by Thomas Chippendale (*q.v.*) in the design of furniture. His *New Book of Ornaments* (1746) is a pattern book for Rococo ornamentation.

·Chippendale pattern book designs 7:801h

**Copland, Robert** (fl. 1508–47), English author and printer, whose *Introductory to Write and to Pronounce Frenche, Compyled by Alexander Barclay* (1521) contains an appendix on contemporary continental dance.

·contribution to Western dance history 5:460e

**coplas**, Spanish for COUPLETS, term referring in varying contexts to the strophe (stanza) of a Spanish song. Normally it means a simple, lyric folk song of one stanza. As such it exhibits features characteristic of Spanish folk music: preference for triple metre ( $\frac{3}{4}$  or  $\frac{3}{8}$  time), recitative singing with elaborate ornamentation of the melodic line, and sweet, consonant harmony resulting from singing the melody in thirds (such as C–E) and sixths (such as C–A). *Coplas* are also improvised between competing partners in various Spanish-speaking countries.

The *seguidilla* (*q.v.*), a Spanish folk dance, is danced with verses called *coplas*, which are sung to instrumental accompaniment. Each verse is followed by an *estribillo*, or refrain. Similarly, *copla* and *estribillo* are the strophe and refrain of two historically important forms of secular art song, the *cantiga* of the 13th century and the *villancico* (*q.v.*) of the 15th century through the 17th.

**Copley, John Singleton** (b. July 3, 1738, probably in Boston—d. Sept. 9, 1815, London), painter of portraits and historical subjects, generally acclaimed as the finest artist of colonial America. He developed within a flourishing school of colonial portraiture, and it was as a portraitist that he reached the high point of his art. His Boston portraits reflect his intimate knowledge of his New England subjects and milieu and convey a powerful sense of physical entity and directness—real people seen as they are. His brushwork is as-



"The Copley Family," oil on canvas by John Singleton Copley, 1776–77; in the National Gallery of Art, Washington, D.C.

By courtesy of the National Gallery of Art, Washington, D.C., Andrew Mellon Fund

sured, his forms are solid, and his colours are bold and scintillating.

From his stepfather, the limner and engraver Peter Pelham, Copley probably gained some familiarity with graphic art as well as an early sense of vocation. To the Rococo portrait style derived from the English painter Joseph Blackburn he brought his own powers of imagination and a technical ability surpassing anyone painting in America at the time. Copley, in his portraits, made eloquent use of a Rococo device, the *portrait d'apparat*—portraying the subject with the objects associated with him in his daily life—that gave his work a liveliness and acuity not usually associated with 18th-century American painting.

Although he was steadily employed with commissions from the Boston bourgeoisie, Copley, aware of his superior talent, was eager to test himself against more exacting standards than those of provincial New England. In 1766, therefore, he exhibited "Boy with a Squirrel" at the Society of Artists in London. It was highly praised both by Sir Joshua Reynolds and by Copley's countryman Benjamin West. They both urged him to go to England, which he did in 1774. He was elected to the Royal Academy in 1779.

Copley's ambitions in Europe went beyond portraiture; he was eager to make a success in the more highly regarded sphere of historical painting. His first important work, "Watson and the Shark" (1778; National Gallery of Art, Washington, D.C.), was commissioned by Brook Watson, who, as a boy, had lost his leg to a shark in Havana Harbour. In this painting Copley used what was to become one of the great themes of 19th-century Romantic art, the struggle of man against nature. In his historical paintings Copley achieved immediacy by portraying his figures in modern dress—an innovation of Benjamin West's.

Though he remained in England, Copley was unable to duplicate his American success. Although his paintings grew more academically sophisticated and self-conscious, they lacked the extraordinary vitality and penetrating realism of his Boston portraits.

·Adams' oil portrait illus. 1:80e

·Mansfield oil painting illus. 11:460

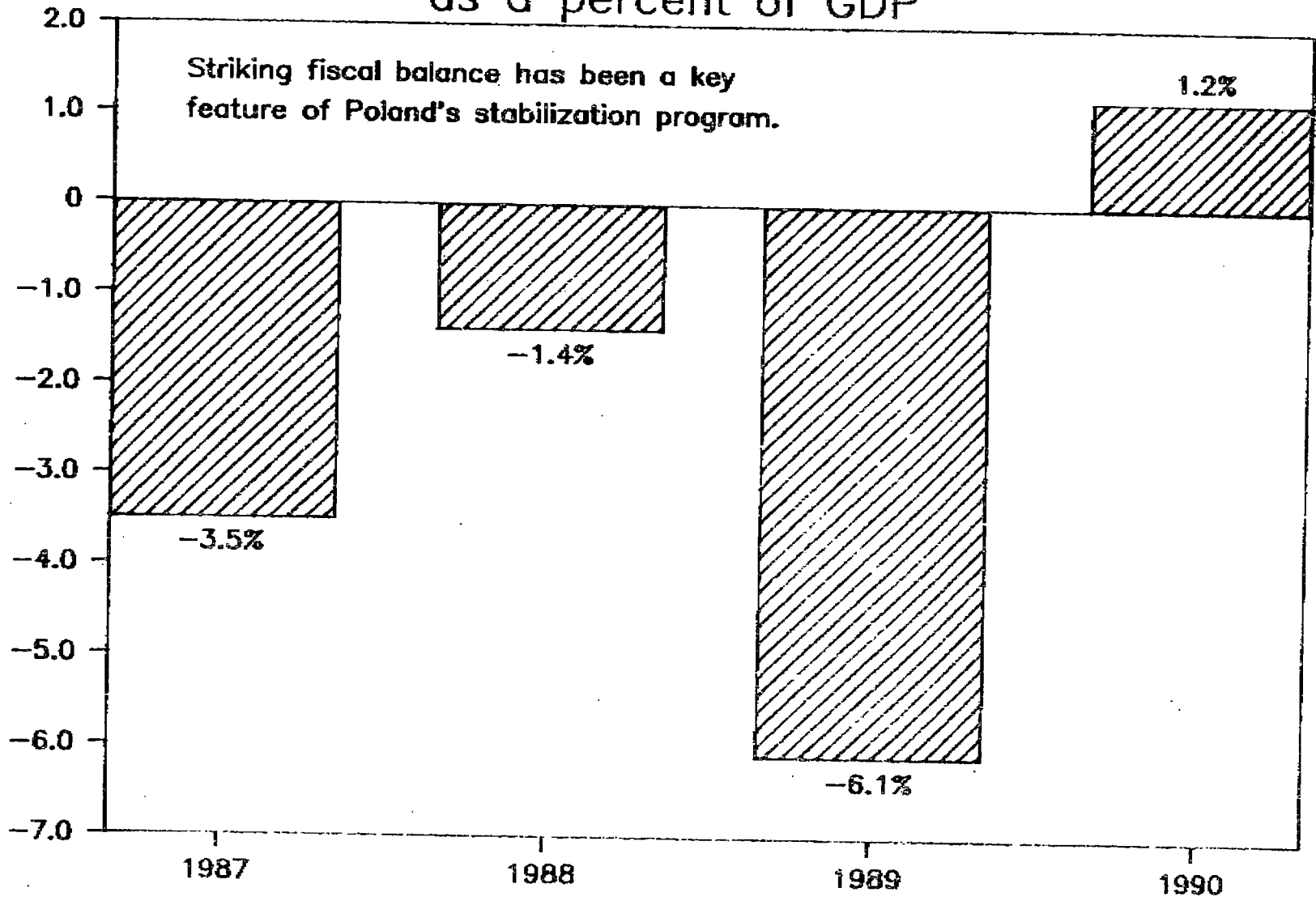
·Theodore Atkinson, Jr., portrait illus. 5:1030

**Copodontiformes**, order of extinct fishes of the class Holocephali.

·era and classification 7:341f

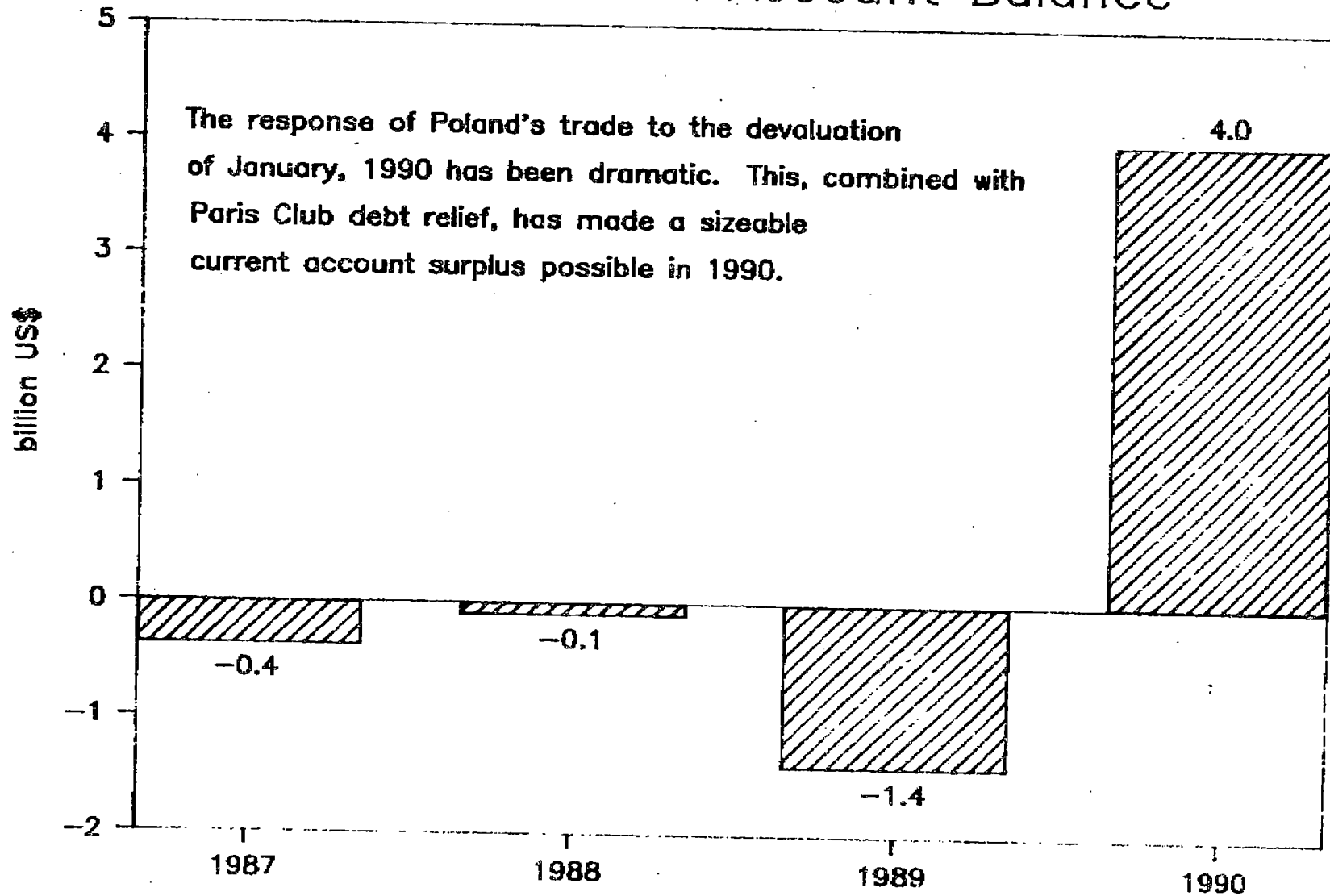
**copolymer**, any of a diverse class of substances of high molecular weight prepared by chemical combination, usually into long chains, of molecules of two or more simple compounds (the monomers forming the polymer). The structural units derived from the different monomers may be present in regular alternation or in random order, or strings of several units of one kind may alternate with strings of another.

# Poland — Fiscal Balance as a percent of GDP



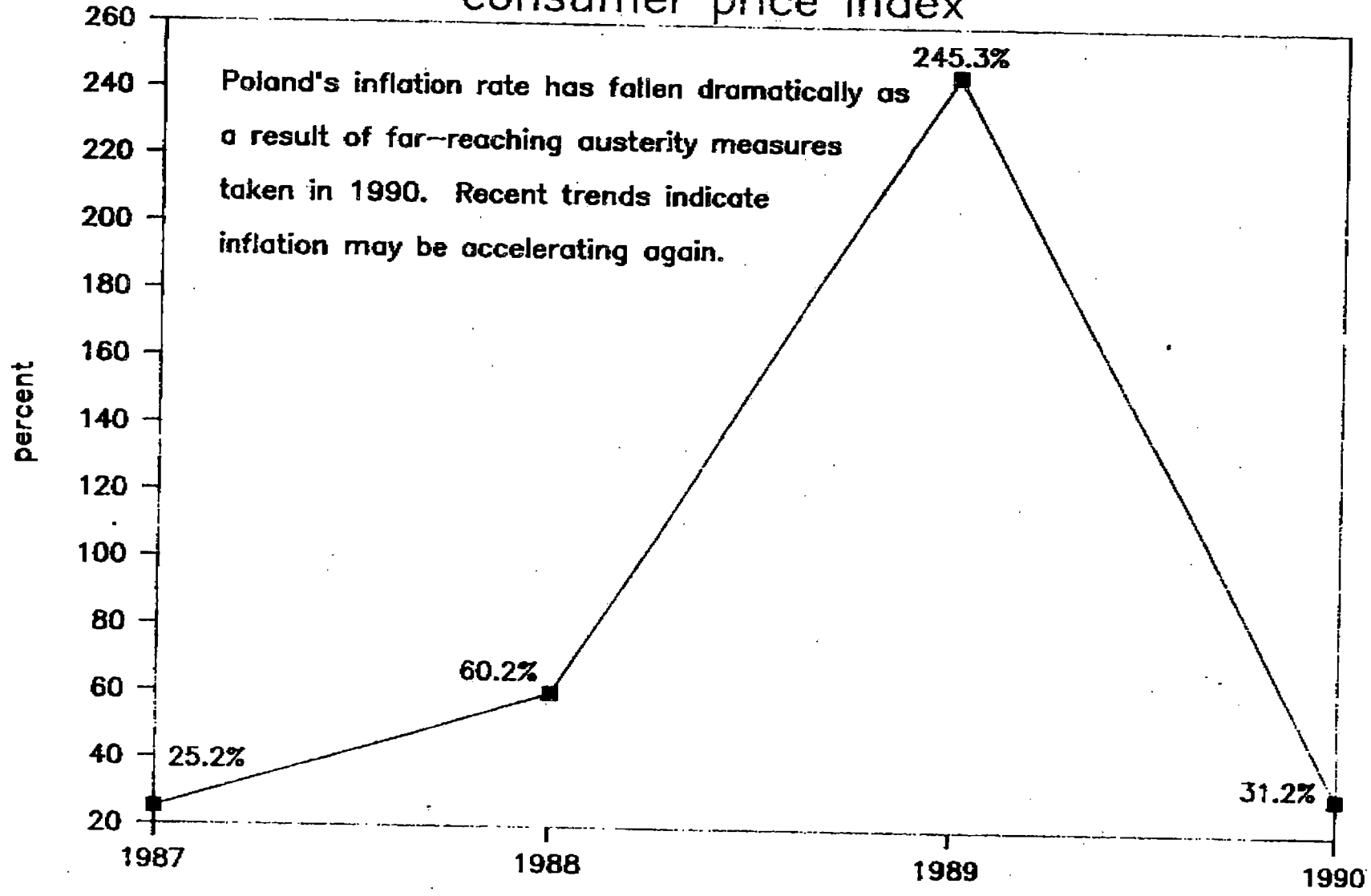
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# Poland - Current Account Balance



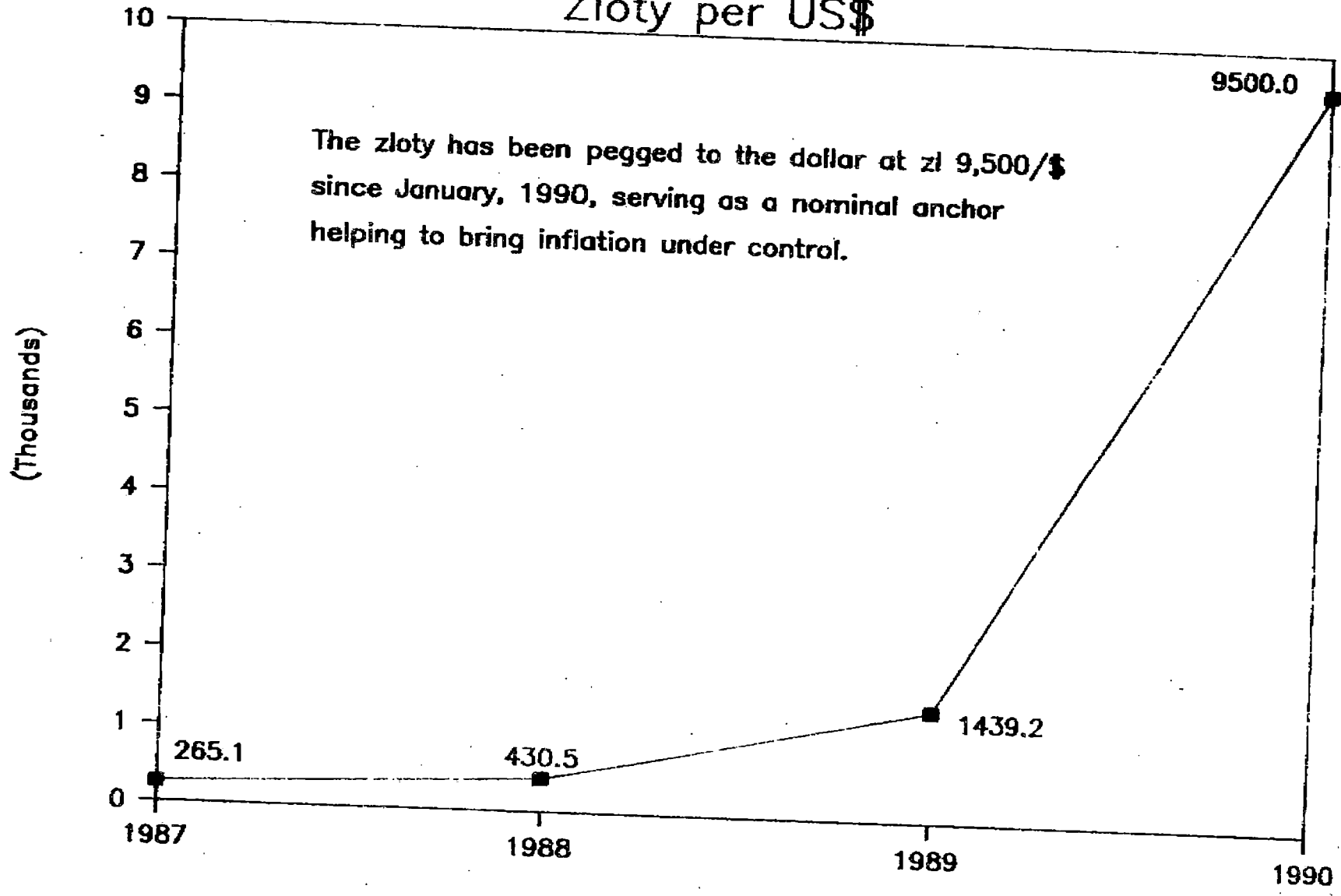
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# Poland - Inflation consumer price index



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# Poland - Exchange Rate Zloty per US\$



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