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FOR Communication 22/2019: Myths of economic transformation in Poland

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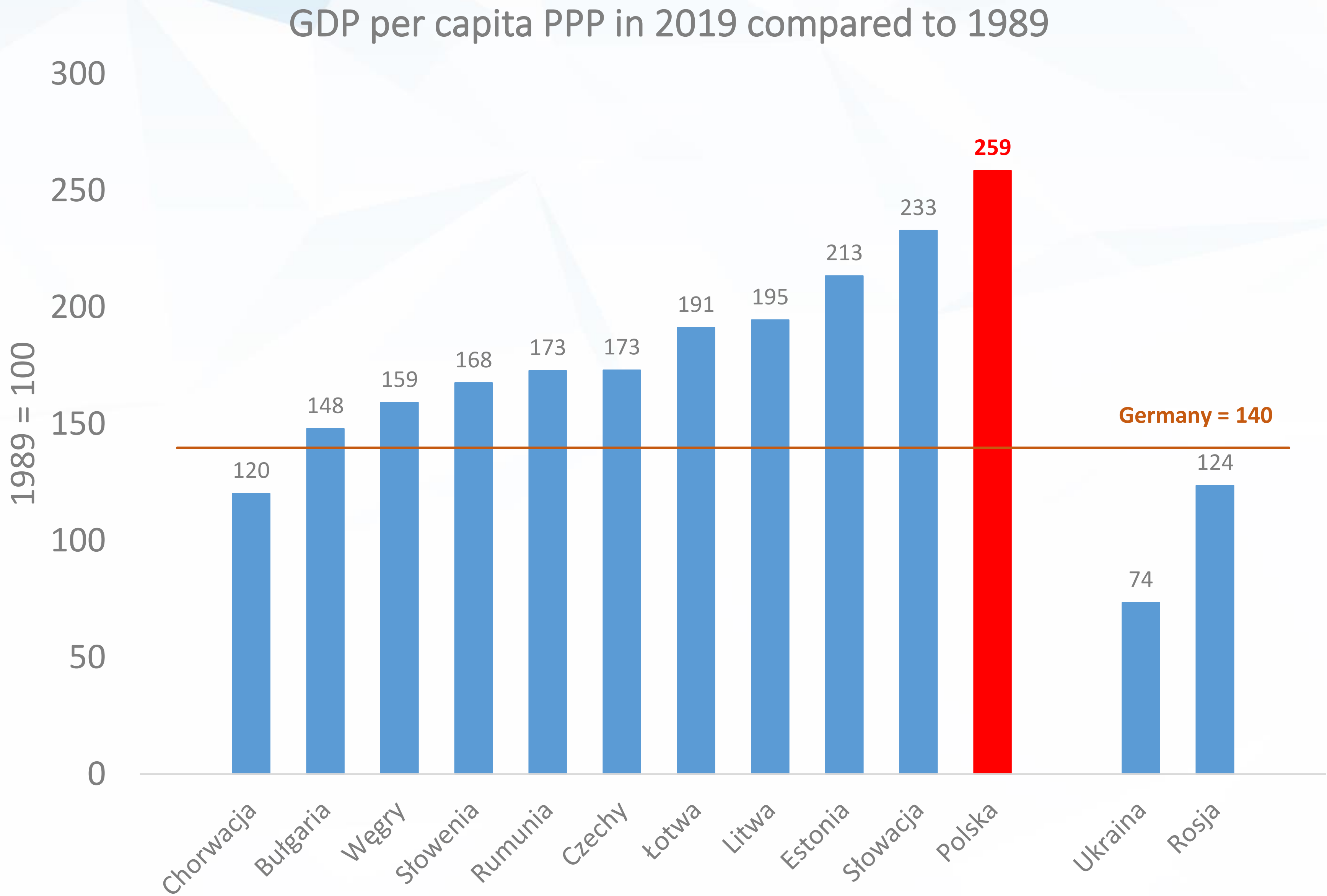
Myth 1: Poland developed poorly after 1989

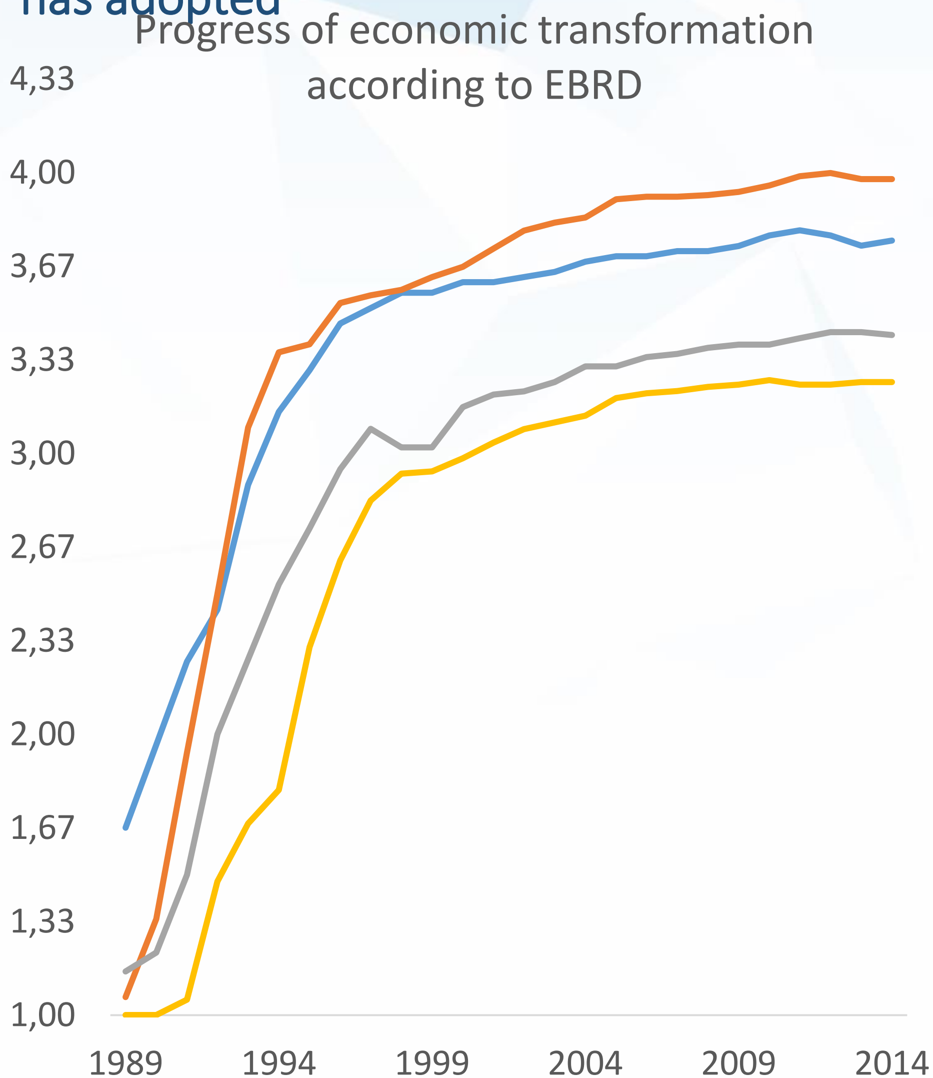


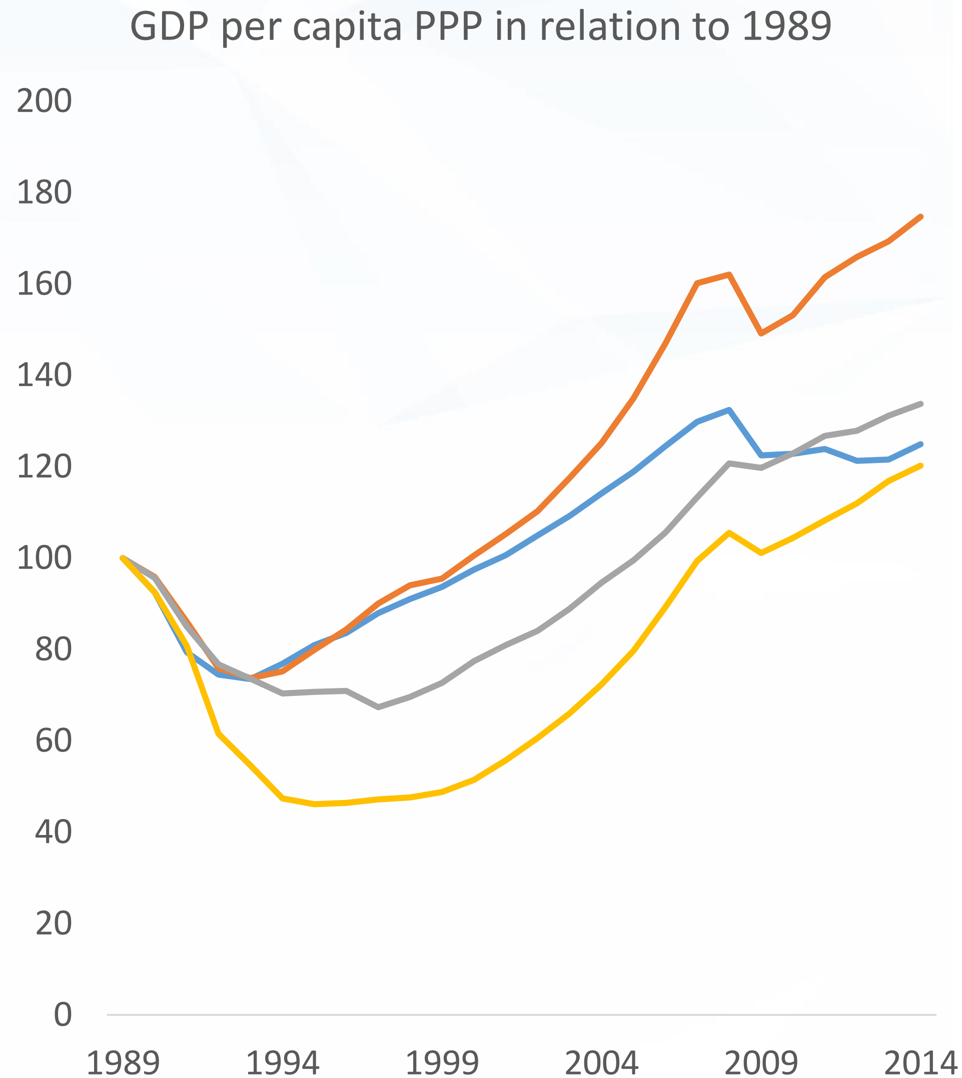
Source: Own elaboration based on Total Economy Database/ Croatia, Bulgary, Hungary, Slovenia, Romania, Czechia. Latvia. Lithuania, Estonia, Slovakia, Poland, Ukraine, Russia

Myth 1: Poland developed poorly after 1989

- Some post-communist countries are now more developed than Poland. Therefore, it seems to some people that after 1989 Poland developed poorly, and certainly not as well as these countries.
- The fact that Poland is lagging somewhat behind these countries does not result from a weak development in the last 30 years, but from the fact that in 1989 it was a very backward country in comparison with the region. Poland was the poorest of all the countries of Central and Eastern Europe, which later joined the European Union. It was at the level of development of the then Ukraine.
- Almost three decades of dynamic development allowed Poland to overtake: Bulgaria, Romania, Croatia, Latvia and - according to most estimates - Hungary, and also to significantly reduce the distance to regional leaders: the Czech Republic and Slovenia (from about 55% to about 80% GDP per capita).
- It is also the most important period in our history of catching up with the West: Poland has significantly reduced the distance between itself and the most developed countries. For example, in 1989 the Polish GDP per capita was about 1/4 of the GDP per capita in the US. We have now reached 50% of the US level.

Myth 2: Poland's development does not result from the radical reforms it has adopted





Start z wysokiego poziomu, równomierny postęp — Croatia, Slovenia, Hungary
Radykalne reformy rynkowe, które później nie zostały odwrócone — Poland, Czech Republic, Estonia, Latvia, Lithuania, Slovakia, Poland
Radykalne reformy rynkowe, które później zostały przerwane — Albania, Bulgaria, Kyrgyzstan, Macedonia, Russia, Bulgaria
Stopniowe, opóźnione reformy — Armenia, Azerbaijan, Georgia, Kazakhstan, Moldova, Romania, Tajikistan, Ukraine, Kazakhstan

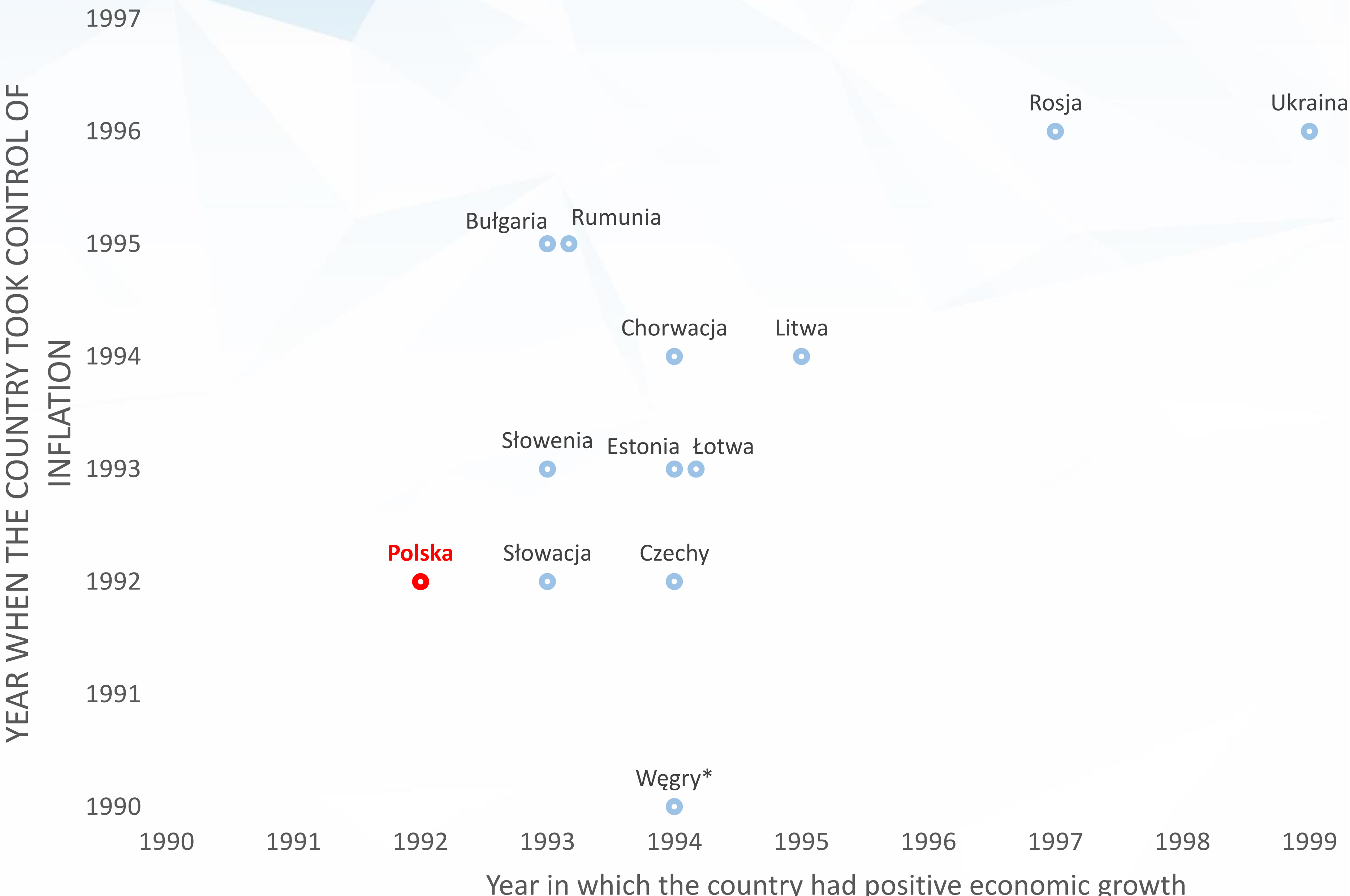
Źródło: Po lewej średnie nieważone Transition Indicators (średnia sześciu wskaźników); po prawej średnie nieważone PKB per capita na podstawie Total Economy Database; podział krajów na podstawie: Havrylyshyn, *Divergent Paths in Post-Communist Transformation Capitalism for All or Capitalism for the Few?* .

Myth 2: Poland's development does not result from the radical reforms it has adopted

- Despite overwhelming evidence in support of the radical economic reform model*, there are still voices that Poland should have introduced a market economy gradually.
- The countries that decided on radical reforms and did not reverse them later, quickly emerged from the crisis in which all the economies of the Eastern bloc found themselves as a result of decades of state ownership of the means of production and a residual market.
- The argument in favour of radical rather than gradual reforms was the desire to create a critical mass of change, in order to prevent reforms from being reversed by the interest groups associated with the former elite. However, not all countries have succeeded in doing so.
- Sometimes China is used as a model for gradual reforms. However, the conditions prevailing in China at the beginning of the reforms (1978) were significantly different from those in the countries of the former Soviet Union and its satellites. China was at the beginning of the reforms much less developed, and its economy was based on agriculture (about 70% GDP), had no problem with hyperinflation and retained control of the bureaucratic apparatus. In addition, the so-called Chinese model is incompatible with democracy

** See Hawryłyszyn, Meng, Tupy, 25 years of reforms in post-socialist countries,* https://for.org.pl/pl/publikacje/raporty-for/raport-25-lat-reform-w-krajach-

Myth 3: Balcerowicz's plan pushed Poland into a long-term crisis



*Hungary, as the only country in the region, did not have inflation throughout the

Source: Own elaboration based on Total Economy Database and EBRD reports

Myth 3: Balcerowicz's plan pushed Poland into a long-term crisis

- The beginning of the 1990s was a difficult period for all the countries of the former Eastern Bloc. Socialism went bankrupt, revealing the distortions caused by decades of central planning.
- Poland began reforms as early as in 1988 with the so-called Wilczek Act, which, however, did not solve the main problems of the centrally planned economy, i.e. the lack of market prices and the related inflationary tendencies, the inexchangeability of the Polish zloty, the state monopoly in foreign trade and the domination of the state sector in the economy. These problems were addressed only by the Balcerowicz Plan of the end of December 1989.
- The objective of the program was to free up prices (thereby closing shortages) and achieve macroeconomic stabilization by combating hyperinflation. Thanks to decisive reforms, the crisis in Poland was mild in comparison to other countries in the region and quickly ended.
- Poland was the first country in the region to achieve a positive growth rate and was one of the countries that gained control over inflation at the earliest, bringing it below 50%. Poland, together with the Czech Republic and Slovakia, is one of the first countries to reach the level of GDP per capita in 1989.

Myth 4: In the 1990s foreign investors only bought state-owned companies

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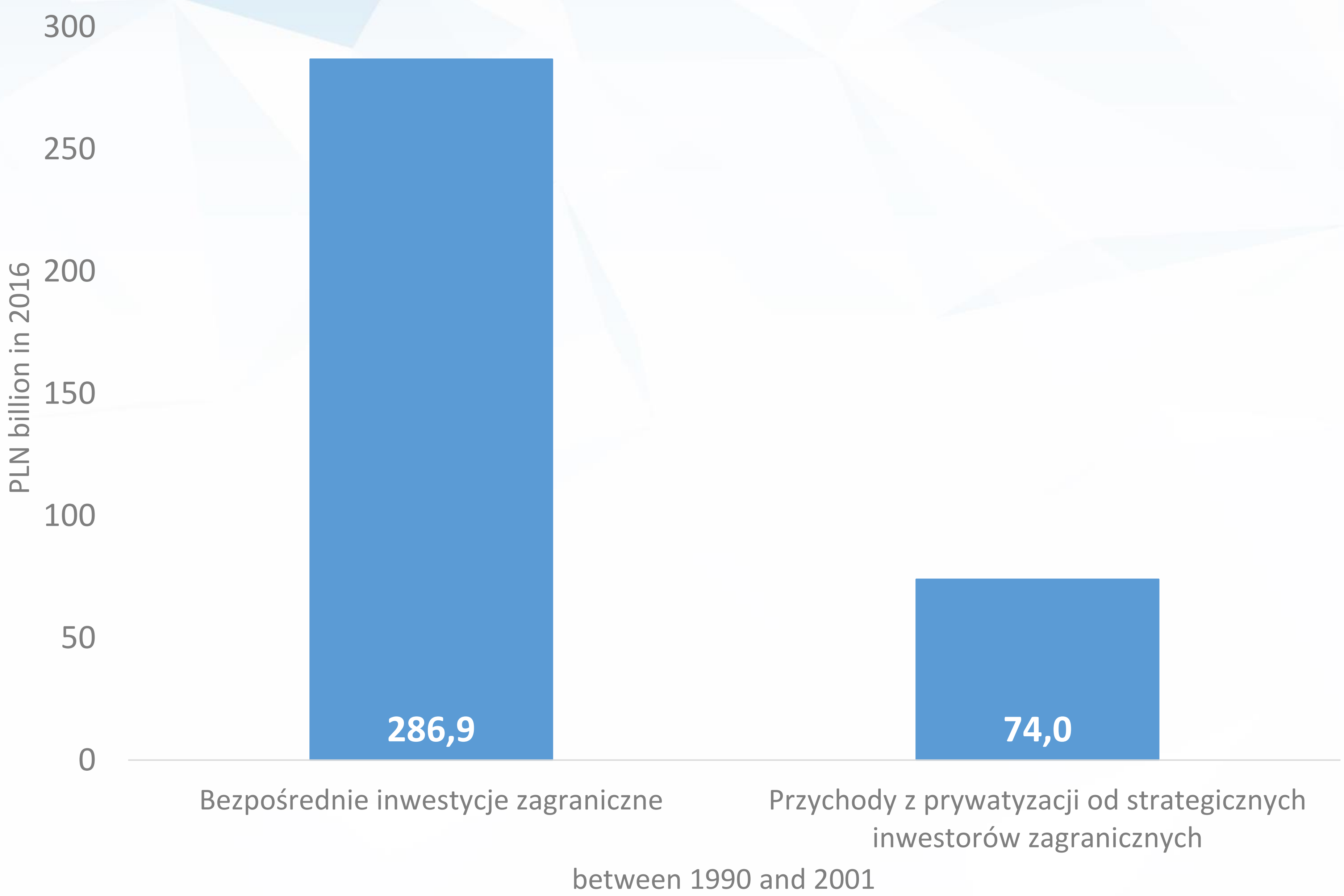
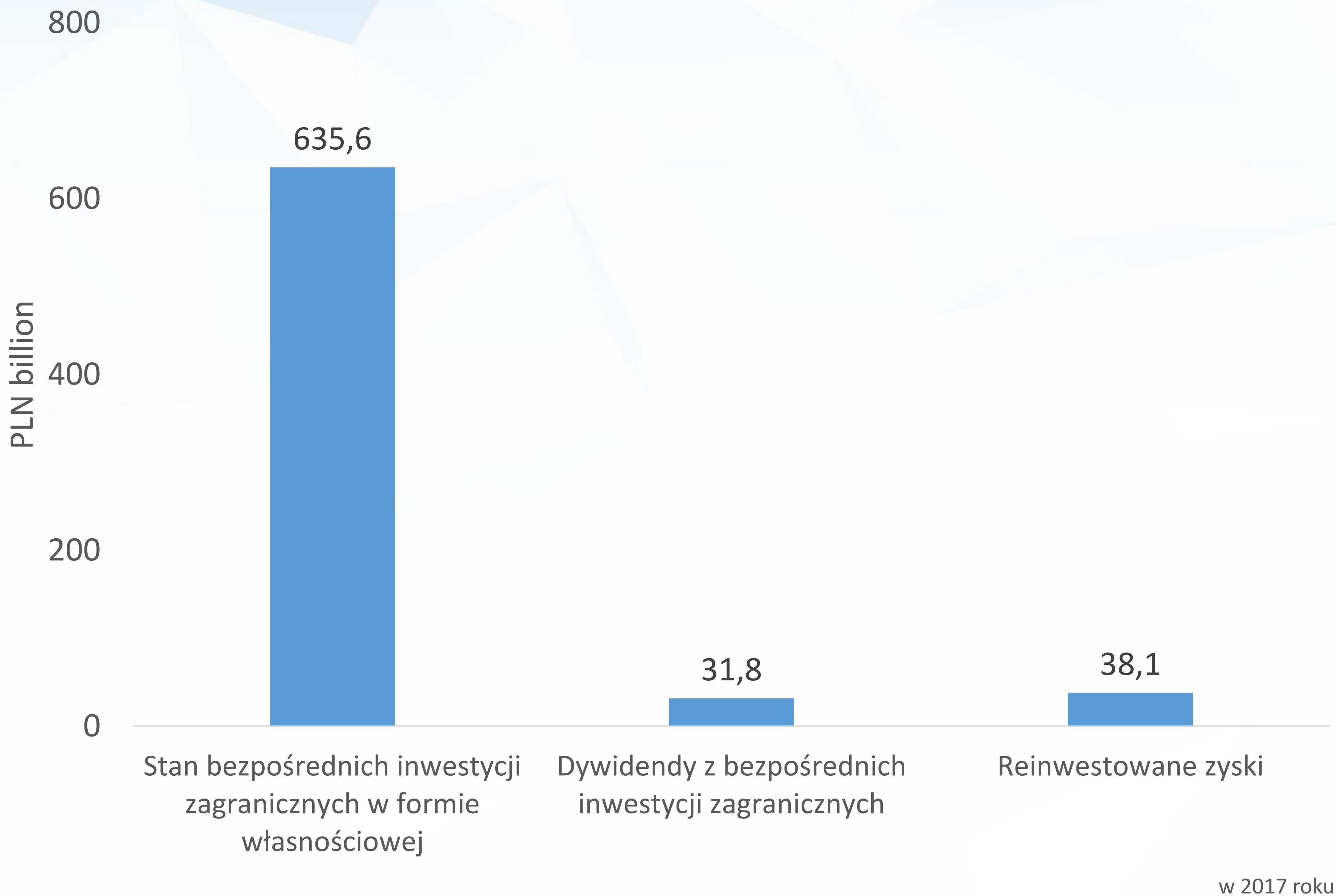


Source: Own elaboration based on NBP (BIZ) and SME (privatization revenues) data, supplemented with privatization transactions of WBK and Bank Śląski, the sale of which was the responsibility of the MF

- Foreign investments arouse a lot of emotions in Poland, and as a result many myths have grown around them.
- In the second half of the 1990s, when it was already known that Poland would not turn back from the path of economic reforms, our country became a very attractive place for foreign investors. This is very good, because it allowed us to use the best Western standards.
- The fact that a wide stream of foreign investments was flowing into Poland led Mateusz Morawiecki to make an insinuation that the current income of foreign investors is actually the profit of "capital from privatization, which bought out our industry very cheaply here".
- That's obviously not true. In Poland, foreign investors did not often participate in privatisations. Instead, they built greenfields, purchased plants from private companies or developed existing ones.

Source: https://www.pap.pl/aktualnosci/news%2C1413377%2Cpremier-panstwo-ma-wspierac-przedsiebiorcow-w-ich-ekspansji.html

Myth 5: Foreign corporations drain Poland from capital



Source: Own elaboration based on National Bank of Poland data.

Myth 5: Foreign corporations drain Poland from capital

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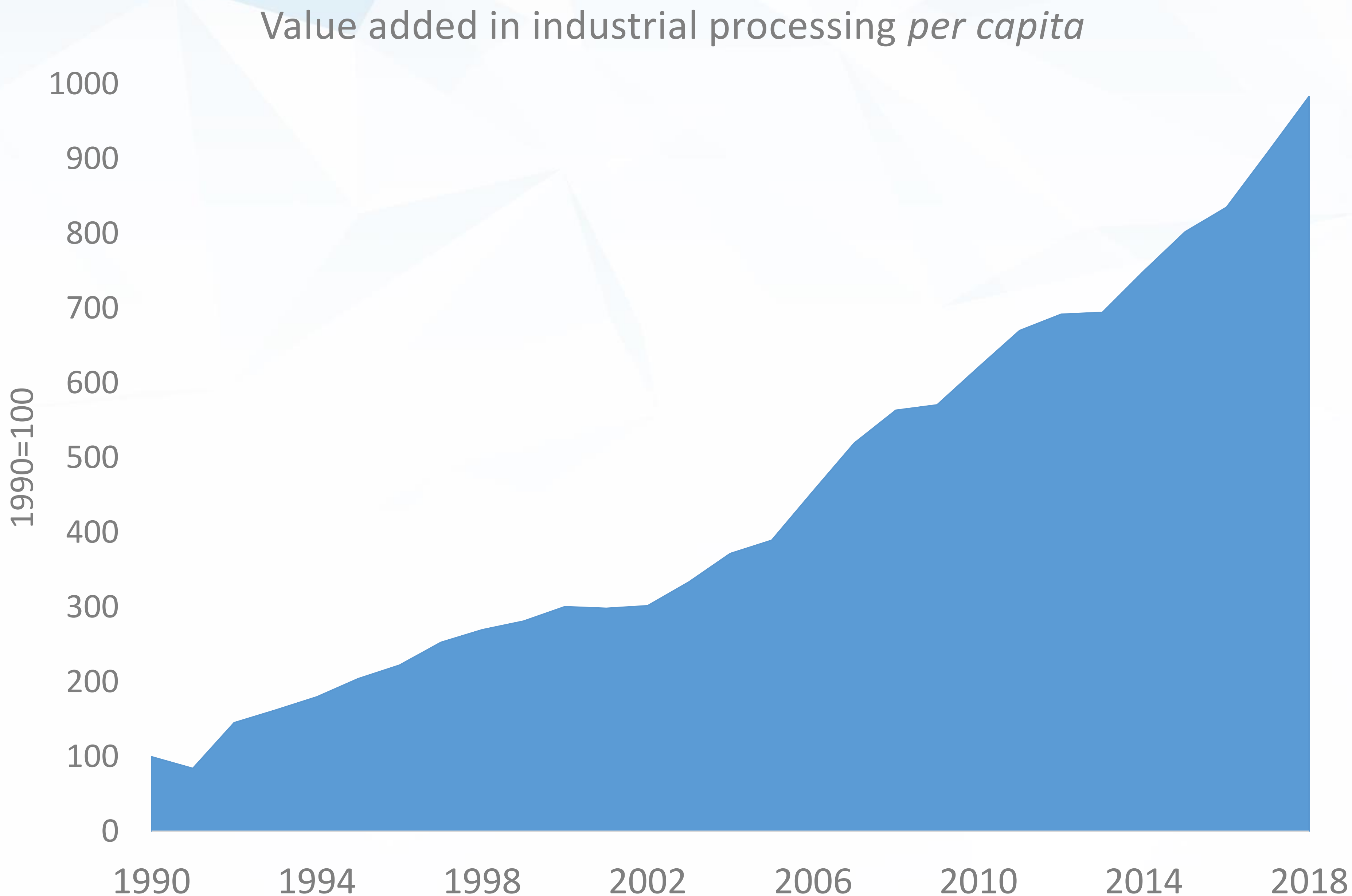
- Some politicians and publicists exaggerate the amounts that foreign investors earn from investments in Poland. They believe that because of these amounts, Poland is becoming a net payer of capital to foreign countries. Mateusz Morawiecki even stated that the dividends drawn by foreign capital in Poland amount to about PLN 100 billion annually.
- That's obviously not true. PLN 100 billion is the total amount of income of foreign investors from foreign direct investments and portfolio investments. Revenues from foreign direct investments in 2017 amounted to approximately PLN 70 billion.
- However, when we compare this amount with the value of the investment (PLN 636 billion), it turns out that the rate of return is not overstated at all - it amounts to 11%. But only a part of this income was paid to foreign investors in the form of dividends. They reinvested 55% of their income. This is not an isolated case - the same has happened in previous years.

Źródło: https://www.pap.pl/aktualnosci/news%2C1413377%2Cpremier-panstwo-ma-wspierac-przedsiebiorcow-w-ich-ekspansji.html



Source: Own elaboration based on UNCTAD data

Myth 6: Polish industry collapsed as a result of the transformation

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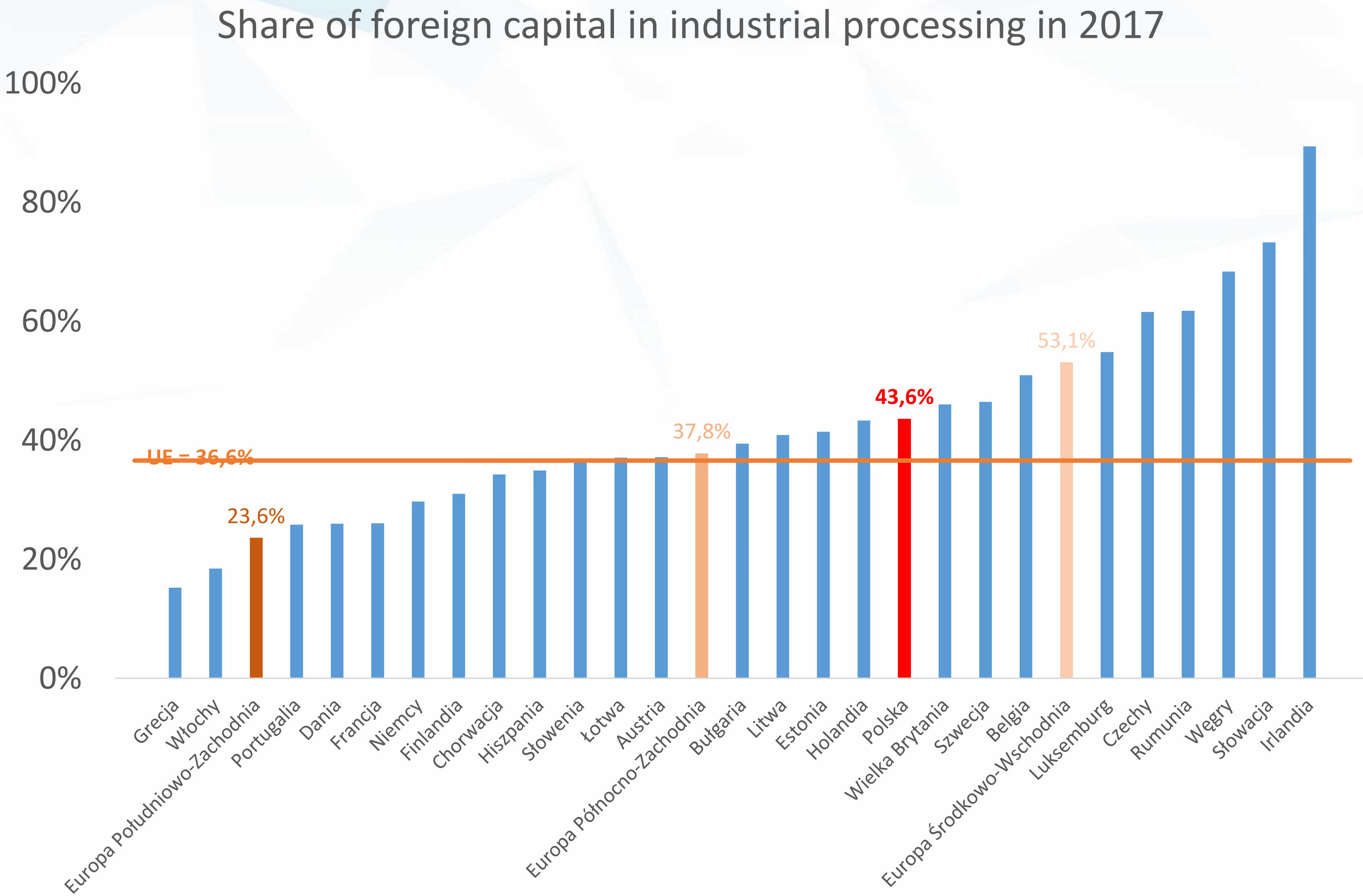
- The collapse of industry is one of the most popular myths about the economic transformation in Poland. We can often hear that so many dynamically operating industrial plants from the times of the People's Republic of Poland have been closed down.
- In fact, after 1989, Poland undertook an impressive industrialization. Since the beginning of the transformation, the value added in industrial processing has increased by almost 900% per capita. This was possible thanks to the adaptation of the Polish industry to market conditions and its integration into global value chains.
- Perhaps the popularity of this myth is due to the fact that industrial plants are now established in the suburbs, not in city centres - but the lack of a view of factory chimneys from the window cannot be a sign of collapse and alleged deindustrialisation after 1989.

Myth 7: Industry in Poland is in foreign hands

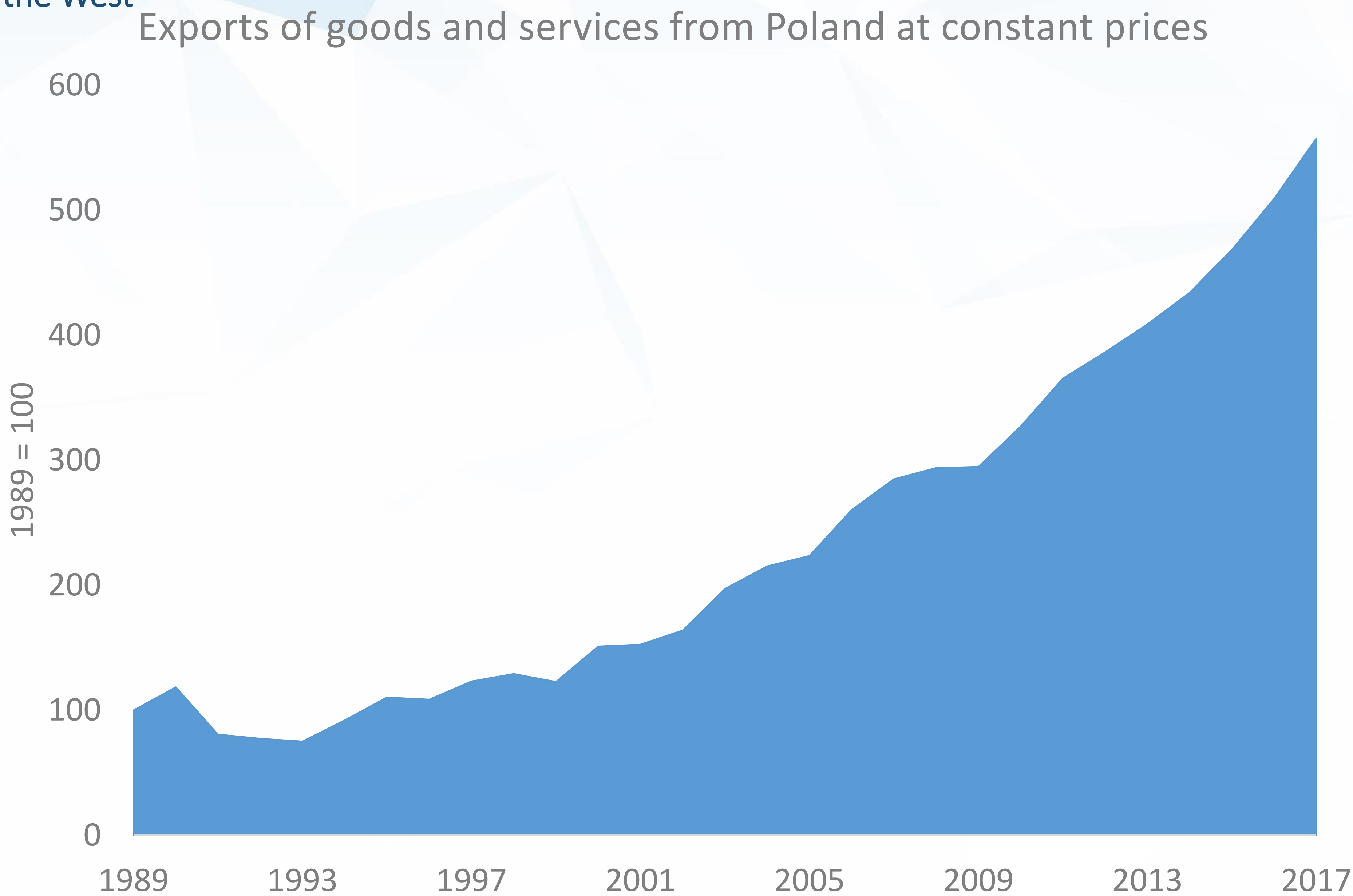


Źródło: Opracowanie własne na podstawie danych Eurostatu

Myth 7: Industry in Poland is in foreign hands

- It is not enough to show that Polish industry is developing, because such a statement - in line with the facts - immediately encounters an objection that it is not "Polish industry", but "industry in Poland".
- Poland, like other countries of our region, bases its growth to a large extent on received foreign investments. This does not mean, however, that Polish companies are not developing. We should also remember that foreign companies in Poland employ mainly Poles.
- In 2017, companies controlled by foreign capital generated 43.6% of added value in industrial processing. This is 7 percentage points more than the EU average, and at the same time 9.5 percentage points less than the average for Central and Eastern Europe.
- Greater importance of foreign capital in industry than in Poland is characteristic of highly developed economies: British, Swedish, Belgian, Luxembourgian or Irish. On the other hand, a small share of foreign capital in industry is a characteristic feature of stagnating South-Western Europe.

Myth 8: As a result of the transformation, Poland has become a market for the West



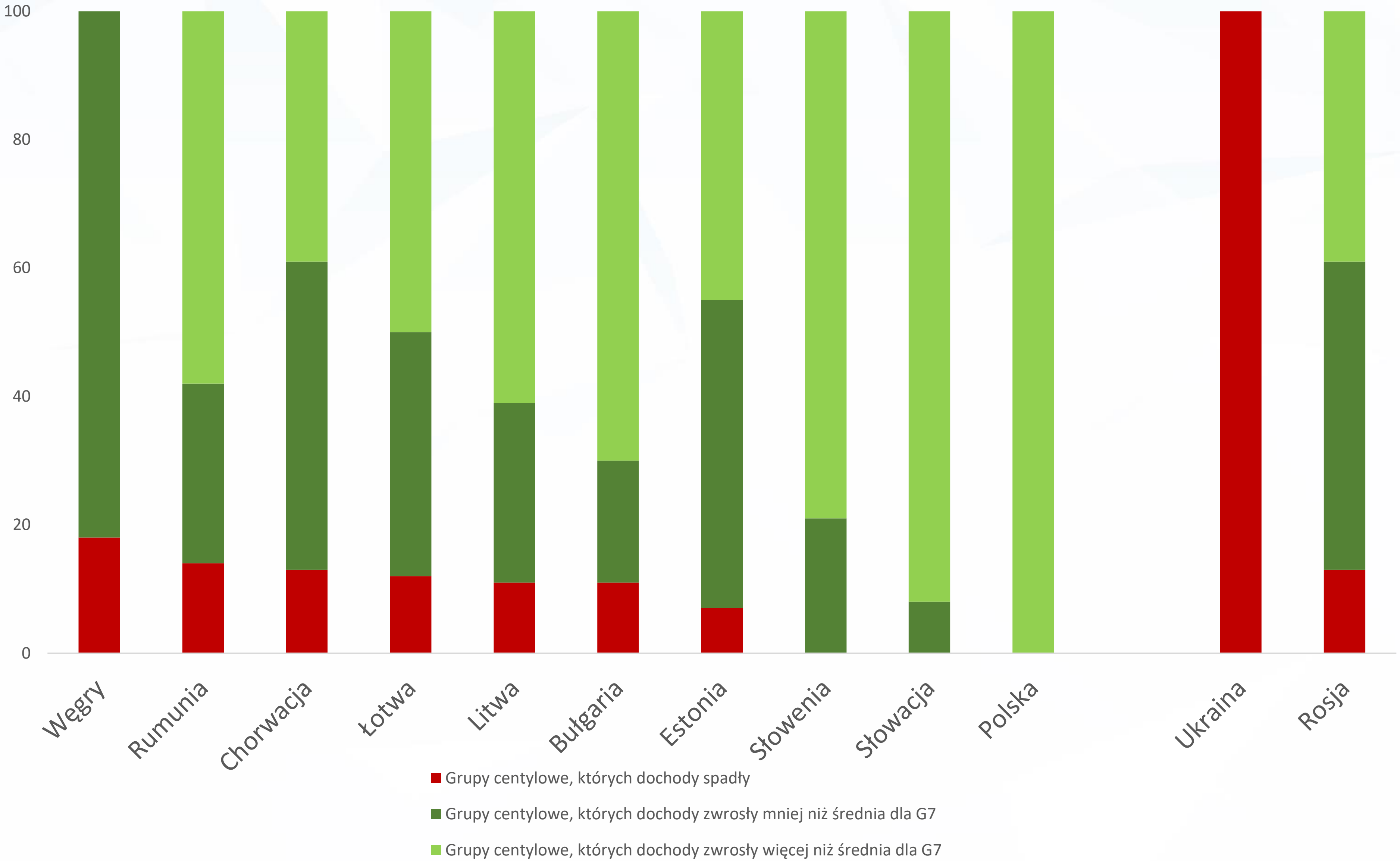
ŹSource: Own elaboration based on data from the World Bank and IMF

Myth 8: As a result of the transformation, Poland has become an export market for the Westd

- "Poland has become an export market" - it's a bizarre accusation, but it's also quite popular. Sometimes we hear that EU funds are a kind of bribe for opening our market to Western products.
- The accusation is bizarre, because consumption is the ultimate goal of production. That's why we produce, to consume. So if we have a wider choice of goods, it is better for us, not worse. If so, no one has to give us anything extra to make it profitable to open the market to imports.
- However, in order to import, you usually also need to export something - at least in the long term. During the times of the People's Republic of Poland, Poland exported processed products mainly to other countries of the Council for Mutual Economic Assistance. After the fall of socialism, it turned out that most of these products, due to their poor quality, could not be sold in the West. Hence the temporary, in the early 1990s, collapse of exports.
- Later, however, Polish producers managed to develop goods and services that foreign buyers would like to buy. The export potential of the Polish economy has also increased its accession to the European Union in 2004.

Myth 9: The Polish transformation was burdened with a large number of victims

Increase in revenue between 1989 and 2016



Source: EBRD, Transition Report 2016-17

Myth 9: The Polish transformation was burdened with a large number of victims

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- Very often, we hear about the victims of the transformation - the workers of the former state farms, the factories that are closing down, etc. - who are the victims of the transformation. In reality, however, they are not victims of transformation, but of economic distortions resulting from decades of central planning.
- According to the European Bank for Reconstruction and Development, income in Poland increased in every percentage of income groups by at least 40% (average for G7 countries). However, it has to be admitted that measuring income by different groups is quite a difficult task. However, even according to much more conservative estimates by Bukowski and Novokmet, revenues in 96 centile groups increased after 1989.
- It is true that after 1989 the officially measured income inequalities increased, although it would have been better to say that these inequalities had been revealed. In the People's Republic of Poland, consumption was determined not so much by the salary earned by the employee as by his privileges and accesses: to konsums (shops by the committees of the Polish United Workers' Party) or black market salesmen. The volume of individual consumption was also limited by the stamps system of rationing goods. Thanks to market reforms, people can freely dispose of their incomes, so that the measurement of income inequalities finally makes sense.

Source: Bukowski, Novokmet, Inequality in Poland: Estimating the whole distribution by g-percentile, 1983–2015