# HOW WORLD BANK BAILOUTS AID EAST EUROPEAN REGIMES

**by Jacek Kalabinski**

The World Bank's country report on Poland, which was published in September of 1987, is a virtual mine of information about the Polish economy. There is a wealth of data, and most of it accurate. The report is very widely used by Western correspondents in Warsaw and by Polish economists and journalists. However, when I read the conclusions and the recommendations of the report, I feel a certain uneasiness. I am reminded of an early science-fiction story by Polish writer Stanislaw Lem in which he describes how aliens from another planet came to earth to analyze a Stradivarius violin. They collected millions of data regarding thickness and length, but they never learned just how the violin plays: They never understood the idea of a violin. No wonder. And as this report is concerned, it also lacks the fiddle. You cannot understand how the violin works if you don't analyze the fiddle.

Let me emphasize that there are three fundamental elements of the Polish economy which are missing from, or glossed over in, the report — obviously for political reasons. These are Poland's military expenditures, trade with the Soviet Union, and the tax system. First, military expenditures. According to the U.S. Arms Control Agency, Poland in 1983 was the world's eighth biggest arms spender. In that year — a year of economic collapse — Poland spent $12.6 billion on its military, more than Japan and more than Iraq, which was waging a war. There was no mention of the military in the report. Not a single sentence. Nor is there a single sentence on expenditure on the internal security forces, which Polish economists believe even exceeds military expenditures.

**Draining Poland's Economy.** A second issue is Polish trade with the Soviet Union and the other Comecon countries. Many experts believe that expanded trade with the Soviet Union and other Comecon countries is virtually draining the Polish economy, particularly now that the Soviets are asking Poland to increase deliveries and make available higher quality goods. Less is available for Poland's Western-bound exports, which are badly needed to repay — or at least service — the nation's $40 billion foreign debt. Let me quote a critical paragraph from the report:

> There is also direct competition between convertible and nonconvertible trade. ["Convertible" meaning dollar-denominated and "nonconvertible" meaning intra-Comecon.] Which raises the question not so much of the feasibility of the revised projections but of whether faster convertible export growth can be achieved by diverting some exports from the nonconvertible area. Poland appears to have little flexibility to do this. Decisions about socialist trade are incorporated into the five-year plan and concluded as

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> inter-governmental agreements,. . . there is probably little prospect of changing the planned nonconvertible trade balance. . . . Even without the agreements, the margin for diverting some hard exports away from Comecon trade to convertible trade [with the West], to Poland's additional benefit, is very small.
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> Imports from the U.S.S.R are generally thought to be "harder," i.e. more readily sold in world markets than Polish exports, and Poland now faces considerable pressure to harden its export mix to the U.S.S.R. . . . This may be a valuable stimulus to the efficiency of Polish enterprises, which will no longer be able to rely on easy profits from an undemanding Comecon market, but it increases the potential competition between exports for convertible and nonconvertible. markets.

I will pay a huge prize to someone who can explain to me what this means. I believe the point is that Poland's technological backwardness is in a way dictated by or imposed on Poland by trade with the Soviet Union.

**Complex, Incoherent Tax System.** The third issue is the analysis of Polish taxes. The World Bank report emphasizes the fact that the Polish government subsidizes a number of factories, and that the tax system is complex and is incoherent. Let me quote again from the report:

> A serious and disheartening adverse feature of the Polish fiscal system is the overabundance of tax rebates at variable rates, sometimes subject to negotiation as a reward to enterprises for fulfilling diverse central objectives including investment, quality improvements, production goals. . . .

In Poland, the enterprises — all state-owned enterprises — pay nine different taxes. There is a turnover tax, there is a profit tax, there is a payroll tax. And the more payroll tax that an enterprise pays, the more the measure of the tax base on which other taxes are calculated grows. This means that some enterprises pay as much as 96 percent of their earnings in taxes — subsidizing other enterprises which are not efficient, not productive. However, I did not find a mention about this in the World Bank report.

**56 Percent Inflation.** The Polish government's "second stage of economic reform" consisted, first of all, of massive price increases. The Polish government claimed this was needed in order to reduce government subsidies. As a result of this, the inflation in the first two quarters of this year was 56 percent. The subsidies, however, were reduced only by 5 percent because, predictably, the government had to pay compensation to employees for the higher cost of living.

One World Bank official who works on Poland, Eugenio F. Lari, does not grant press interviews in Washington, but gave two interviews recently to Polish news agency correspondents. Those interviews were prominently publicized by the government media in Poland. As reported, Mr. Lari remarked that if he were a Pole, he would vote "yes" in the

Polish referendum concerning the second stage of the reform. The result of the referendum, despite Mr. Lari's publicized call, was that only 37 percent of the Poles voted "yes" for the reform. Curiously, when I asked Mr. Lari for an interview afterward, the answer I was given from his press spokesman was that Mr. Lari cannot grant an interview on Poland because that would violate the World Bank principle of non-interference in the political affairs of member countries.

**Justifying Price Increases.** All this is to say that the World Bank report on Poland, which I have quoted extensively, was used in Poland by the government to justify price increases without really doing anything about the structure of the economy itself.

Publicly, the World Bank does not state which kind of projects it is going to finance in Poland. However, Poland's official government daily, *Rzeczpospolita*, quotes a Polish national bank official responsible for relations with the World Bank as saying: "We are expecting two export-related loans for industry with an overall value of $250 million and an export-related loan for investment in the food processing industry amounting to $75 million."

Now, the journalist then asked him a question. "Does this mean that the World Bank no longer demands, as a precondition, that Poland begin an adjustment program with the IMF?"

"No," Mr. Andrej Olechowski says, "the World Bank demands only that we prepare such a [IMF] program with the prospect of activating it soon. And this demand is basically fulfilled already."

**Ignoring IMF Adjustment.** World Bank behavior vis-a-vis Poland would appear to contravene the World Bank's charter. Activation of an IMF adjustment program is a precondition for any World Bank loans. With this said, since we know so little of the emerging World Bank program in Poland, I would like to make a few remarks about the Bank's experience with Poland's neighbors in Eastern Europe. Romania joined the IMF and the World Bank in 1972, Hungary in 1982. Petra Pissulla, a West German specialist in Eastern bloc economies, writes that for Hungary – and even more so for Romania – the World Bank has always been a more important partner than the IMF. In its first three years of membership, Hungary received World Bank commitments totaling almost $1.5 billion, of which some $1 billion was in the form of the World Bank's share of "cofinancing with the private sector." Of course, the "private sector" in this case does not mean the private sector of the Hungarian economy, but Western commercial banks which were encouraged by the World Bank loans to Hungary to cofinance certain projects in the Hungarian economy. What are those projects? They were generally infrastructure projects, for example, improving the country's energy transmission grading (which is not a bad way to go of course), but also toward generating more electricity by building lignite-fired electric power stations, which generate enormous amounts of atmospheric pollutants. These latter are probably the most environmentally harmful way of generating electricity with the environmental situation in Eastern Europe already fairly bad. In Romania, a very similar project was financed by the World Bank.

Another problem is that World Bank energy-oriented projects in Eastern Europe seem to perpetuate energy overconsumption in those countries. In one World Bank study on Eastern Europe concerning ways of calculating GNP per capita, the emphasis is on energy consumption; however, the efficiency of energy use in Poland, for instance, is three times less than that in Holland or West Germany. Almost the same goes for Czechoslovakia.

**Uprooting Peasants.** In Romania, World Bank agriculture programs have the dubious distinction of having financed the groundwork for the present forced villagization policy. A World Bank project, originated in 1979, included building 27 pig fattening farms, 25 breeding farms, modernization of 37 breeding and fattening units, as well as, the World Bank handout stated, credit to agricultural cooperative members and private individuals. Now, there is virtually no private agriculture in Romania. The private agricultural sector in Romania is just 6 percent of agriculture, and none of these private Romanian farmers received any help from this project. To the contrary, the pig breeding project — together with a project for the mechanization of Romanian agriculture by creating "tractor and machinery stations" — was a prelude to the forced resettlement program being conducted right now. By using the World Bank assistance to concentrate the means of production in the hands of state-owned machinery stations, the Romanians put in place the infrastructure of today's "new villages." The whole idea of the "new villages" is to uproot the peasants from their original farm and centralize them in apartment buildings where they will be under the strict control of the government — both economically and politically. This means doing away with the private plots of land which the Romanian peasants up to now have been able to keep. They are not big plots — the maximum which a Romanian peasant may have is 250 square meters (2,691 square feet). Still, many people just survive because of them.

Finally, I would like to point out one large curiosity regarding World Bank data in the region. As Hungary was accepted to the World Bank in 1982, the official World Bank atlas was listing per capita GNP in Hungary as $4,100/year. And suddenly, in the next year's report, Hungarian GNP per capita was calculated at $1,900/ year. Why so? Because countries with per capita GNP below $2,170 qualify for the World Bank's no-interest loans ("IDA" loans) targeted at the most underdeveloped countries. In the following years, then, Yugoslavia's and Poland's per capita GNP were also recalculated quietly. Today, the official data from the 1988 World Development Report of the Bank gives per capita GNP for Poland at $2,070, Hungary $2,020, and Yugoslavia at $2,300. While it is evident to any tourist who goes to Eastern Europe that Hungary has a per capita income much, much higher than Poland has, just homogenizing those incomes was the easiest solution. So much for the World Bank's attitudes toward centrally planned economies.

**Teaching Western Business Techniques.** There is one World Bank project in Hungary, however, which probably does merit some praise. It is the so-called Hungarian retraining project. Retraining managers of Hungarian industry is financed by the World Bank, and Hungary is setting up in Budapest its first business management school with Western professors and Western ways of teaching business management. I hope, however, that the professors are not recruited from the World Bank staff.