Poland's alternative to IMF shock medicine

by William Engdahl

Over the Christmas weekend, Poland's Solidarnosc Minister of Finance Leszek Balcerowicz signed a controversial Letter of Intent with the International Monetary Fund (IMF). But rather than releasing the hoped-for flood of Western funds and investments, judging from initial reactions from West European bankers, the draconian IMF "shock treatment," a slightly rewarmed version of that demanded last autumn by Harvard Prof. Jeffrey Sachs, is actually increasing Western pessimism over Poland's future economic prospects. Nowhere is the contrast in view clearer than by comparing the IMF treatment afforded Poland with the non-IMF prospects developing for the East German (G.D.R.) economy.

On Dec. 18 the finance and economics ministers of the 12 member states of the European Community approved the outlines of a French proposal which will create a European Development Bank to finance economic reconstruction projects in Eastern Europe. The new European bank will have initial capitalization of 10 billion European Currency Units (roughly $10 billion) and will be used to funnel West European economic investment into the economies of Poland, Hungary, and East Germany, which are now being reformed.

"This is the European Development Bank idea of [French President François] Mitterrand," stated a senior Bonn Finance Ministry official privately. "The French idea is for a majority voting control to be held by the governments of West Europe. Select Eastern European countries will be invited to join the board, as will Japan and the U.S.A. But it will not be another IMF. Voting will be controlled by Western European governments." In off-the-record remarks, a Bundesbank source added, "This bank will not be subject to the straitjacket of IMF conditionalities. That would be absurd. It will channel funds to infrastructure projects in Eastern Europe, things such as the Paris-Warsaw rail project, rebuilding of telecommunications and highways."

The rapid progress on the European bank underscores an extremely crucial element of economic stabilization for the volatile economic and political situation in Eastern Europe. As well, the attitude of the Bonn government toward East German reform suggests an extremely important new element of flexibility regarding customary IMF austerity demands. "The IMF issue is definitely not a precondition for our cooperation with the G.D.R. on economic projects," emphasized the Bonn Finance Ministry official. "Our only precondition is that the process of economic reform go in a direction of freer market economy. We demand no specific preconditions."

Following the historic trip of West German Chancellor Helmut Kohl to Dresden, East Germany in late December, West German Research Minister Heinz Riesenhuber announced that he will give "serious consideration" to a proposal by Lower Saxony Minister President Ernst Albrecht to construct a high-speed rail line between Hanover and Berlin, using Thyssen's experimental Transrapid magnetically levitated train, which could carry passengers along the 300 km corridor at speeds above 400 km, or roughly 250 miles, per hour. At the same time, West German firms, including Volkswagen of Wolfsburg, have initiated talks with East German companies about joint industrial production.

Sachs's Polish shock

But the laudable progress of economic talks between West European governments and the G.D.R. stands in stark contrast to the terms being demanded of Poland. On Dec. 17 Poland's Minister of Finance Leszek Balcerowicz announced to Parliament his government's emergency economic program. The drastic austerity scheme is in fact the lunacy of Harvard Prof. Jeffrey Sachs's "shock treatment," and includes cutting Polish real incomes by 25% on Jan. 1, throwing some 400,000 Poles into unemployment, and devaluing the zloty by 66% against the dollar. Balcerowicz's program, which he calls a "deep surgical operation," is a precondition demanded by the IMF in its Letter of Intent with Poland, before it will release urgently needed short-term funds intended to relieve Poland's external balance of payments problem. The IMF demands that Poland slash its government deficit and privatize large parts of state-owned industry in order to supposedly bring its current hyperinflation, presently estimated at 30-40% per month, under control.

Such savage "anti-inflation" austerity will do nothing but aggravate Poland's economic misery, just as it has for the past seven years in African and Ibero-American debtor countries. The IMF is an Anglo-American creation of the 1944 Bretton Woods era, whose explicit mandate is not to foster national economic growth or to raise living standards, but rather to impose "equilibrium" conditions to the accounts of nations. A victim country gets IMF "stabilization" loans to do that. But the cost is almost invariably savage, self-destructive austerity for developing country economies.

The IMF medicine is the demand made by all West European governments, Bonn included, as the precondition for further assistance. If Poland signs with the IMF and agrees to the severe austerity, it is promised a paltry $700 million of IMF "standby credit," as well as another perhaps $1 billion European Community "stability fund," and perhaps another $500 million from member central banks of the Basel, Switzerland-based Bank for International Settlements. That pool of cash is intended to be a foreign exchange reserve backing to stabilize the devalued zloty. Not a penny will go to investment in tractors, rails, roads, ports or industrial infrastructure which are so urgently needed.

Such economic policy demands are just the reverse of the nation-building economics of Friedrich List which formed the basis for the astonishing 19th-century German economic miracle, or that of the postwar economic miracle after 1949. The IMF policies can be likened to an executioner telling his victim, "First cut off one arm and one leg, then we can discuss whether you qualify to receive any bandages." The Bonn Finance Ministry official admitted as much when he stated, "We think that the IMF must be expedient with Poland, but not lenient, though we would never say so publicly. The shock treatment places a heavy burden on the Poles. Poland, however, has itself chosen to impose Sachs's shock medicine."

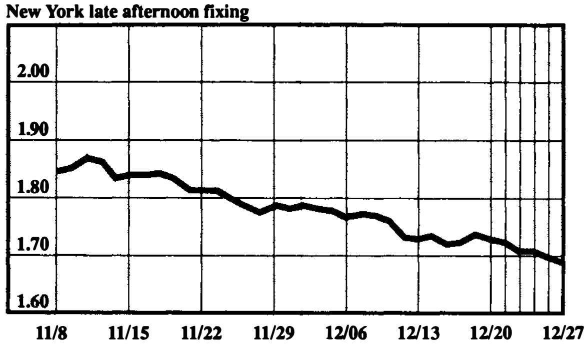
Bonn publicly rationalizes its stance on the IMF demand by pointing out that Poland, unlike the G.D.R., is a voting IMF member, therefore subject to the rules of that game, as is Hungary. Bonn officials further point to the promise of future assistance once the IMF medicine is swallowed by the Poles, including small debt forgiveness of a $1 billion credit from the 1970s and postponement of Paris Club Western government debt burdens due in 1989-90 of some $7-8 billion, 25% of which is owed to Bonn. But the reality is that this is still sadly insufficient. The popular backlash against Solidnarosc is likely to destroy the possibility for serious economic reconstruction of that nation's potentially enormous economy for decades to come.

A new 'London Accord' from Bonn and Paris?

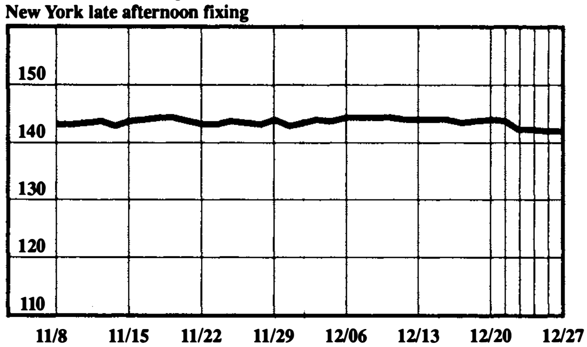
Were Bonn committed, as many in the government clearly are, to serious improvement of Poland's economic living standard as well as to the healing of the old wounds of the Second World War, Chancellor Kohl could take a positive initiative to "change the terms of the game." One obvious act would be to cite the precedent of the 1953 London Accord on Germany's pre-war debt where the Allies forgave more than 50% of monies owed them since 1919, in order to allow Germany to fully reindustrialize and rebuild its war-torn economy. More than 75% of Poland's $40 billion Western debt today is owed to the governments of the West, the vast majority to West Germany, France, Italy, and other West European states in the so-called Paris Club. France is chairman of the Paris Club creditors' committee. What better statement of Franco-German accord on real economic help for Poland than to tell the country it is simply forgiving the vast majority of that $30 billion—debt incurred under conditions which no longer pertain to the present government of Poland, including illegitimate compounding of interest arrears onto future principal owed after 1981, via so-called "interest capitalization."

Currency Rates

The dollar in deutschemarks
New York late afternoon fixing



The dollar in yen
New York late afternoon fixing



The British pound in dollars
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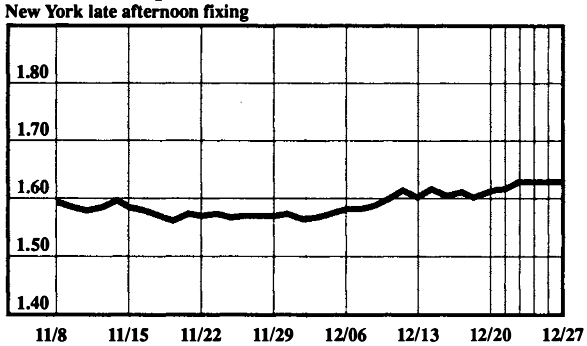

The dollar in Swiss franks
New York late afternoon fixing