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Poland at the gates of hell after four years of IMF plunder

by William Engdahl

Following four grueling years of negotiations between the government of Poland and the committee of western creditor banks, Poland early in March announced it had finally reached agreement on repayment of its $13 billion in private bank debt, part of more than $40 billion in total western hard currency debt which has accrued since the debt and political crisis of the early 1980s. Under the terms of the agreement, Poland is forgiven 45% of its defaulted $13 billion owed the banks. But far from grounds to cheer, the agreement merely signals that western bankers feel Poland has been adequately softened up by International Monetary Fund (IMF) shock therapy policies to be ready to become an eastern version of Mexican *maquiladora* cheap-labor production for western multinationals. The recent speculative frenzy on the Warsaw Stock Market by foreign investors signals anticipation of just this.

It has also been just more than four years since Poland was forced to adopt IMF shock therapy policies, the initial precondition for negotiating with western creditors and potential investors under the transition government of Tadeusz Mazowiecki. Poland's finance minister under that government was Leszek Balcerowicz, an iron-hard supporter of the shock therapy program worked out for Poland by Harvard's Jeffrey Sachs, in close cooperation with officials of the IMF. It should be noted that publicly, Sachs profiles himself as an IMF "critic," but in reality, he and the IMF work together.

At the end of October 1989, Poland became the first eastern European country to adopt IMF shock therapy. Under the government's "Program of Stabilization and Systematic Changes," measures put forward by Balcerowicz at that time included severe punitive taxes on wage increases and an end to worker bonuses; accelerated tax payments and sharp cuts in state subsidies, in order to cut the budget deficit; removal of state price controls and a cut in credit to state enterprises; and, a radical depreciation of the zloty, to allow Poland to earn more hard currency by dumping its goods onto western markets.

Poland was advised by the IMF on its economic policy, and the entire focus, it was told, was to reduce the severe inflation and increase the role of what the IMF called "market forces." What has resulted?

Not all of the elements of the Balcerowicz plan were harmful to the economy. Some, such as selective ending of subsidies, cancellation of central quotas for enterprises, and a prohibition of government borrowing from the Central Bank at a zero interest rate to cover deficits, could be desirable under any intelligent economic program. But this was not the core of Sachs's shock therapy.

Prescription for disaster

The bulk of the Sachs-Balcerowicz plan was a prescription for economic disaster. Initially, under a program to kill inflation, Poland experienced hyperinflation, much as Russia did after January 1992. The hyperinflation resulted partly from a state budget deficit financed by new unbacked money, but mainly resulted from the freeing of prices to so-called market levels, and elimination of various state budget subsidies. By January 1990, inflation reached 80% per month. Of course, one can argue that this is the cost of abandoning the unrealistic price structures of socialism, and was a one-time inflation.

But what actually resulted from the supposed anti-inflation program of the IMF beginning in 1990, was suppression, instead, of the real, physical economy of the nation. Within one month in early 1990, production fell by 31%, trade fell by over 50%, real wages fell by 30%, and prices rose by 80%. The government imposed interest rates on loans of 38% per *month*, while wages were allowed to rise only 0.3% per month, and the convertible zloty was allowed to fall to 9,500 zlotys per dollar.

Industrial firms had no capital for wages or machinery, trading firms had no money to finance inventories, and individual consumers had no money to buy goods. Predictably in this situation, state enterprises reacted by cutting production as inventories of unsold products piled up, households cut spending, and farmers were unable to sell their milk, meat, wheat, and vegetables. The first 500,000 unemployed appeared in the early months of 1990.

The madness of IMF equilibrium theory

But the IMF and Sachs were quite happy with the results. They in fact expected it, as their only goal was not the improvement of the overall production of Poland's economy and living standard of the Polish population, but only the development of what they called a Polish *equilibrium* in its external balance of payments, and only secondarily, to

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achieve internal so-called equilibrium.

Domestic equilibrium was reached, as production drastically decreased to match demand, which had decreased even more. As well, the forced export of food to the U.S.S.R. ended any chance of increasing the available domestic supply. At first, people reacted favorably to the new situation, expecting that it was a short-term sacrifice on the way to capitalist "free market" paradise. Food appeared in the shops, albeit at far higher, uncontrolled prices. People drew on their savings to live for the first months of shock therapy.

With the forced devaluation of the zloty under IMF orders, to 9,500 zlotys per dollar, three times what its actual buying power suggested, exports boomed while imports were prohibitively expensive. Enterprises exported everything possible, yielding a surplus on the national current account of $4 billion in early 1990. But this surplus only fueled inflation. Goods had been removed from the domestic market while zlotys earned by exporters were pumped into the economy, allowing more zlotys to chase fewer goods.

The main impact of the Balcerowicz shock therapy program, bizarrely enough, was directed against domestic credit, through use of drastically high bank interest rates and severe limits on credits to state enterprises. The second part of the attack was to impose a punitive tax on wage increases. This created a situation of radical economic deflation. This, in other words, was an economic depression.

But when Sachs, as an adviser to the Polish government, first announced his shock therapy program in Poland, he predicted an "economic boom" after six months of "pain." Results were otherwise. Industrial production in Poland fell by 19% between 1990 and 1991 under shock therapy. As shock therapy went into its second year in Poland, there was a violent decline of real (accounting for inflation) wages, a severe contraction of social transfer payments, and a reduction of private savings.

In 1993, a United Nations Unicef report on Polish living conditions reported that at least 20% of children in Warsaw were going hungry, and that 50% of families with three or more children were living below the poverty line. One-quarter of all families in 1992 had applied for welfare assistance to support themselves. And by late 1993, more than 8 million of a total population of 38 million were forced to live by means of a meager state pension.

As income of state enterprises was cut by IMF-dictated policy, investment levels were driven below the level needed to replace outmoded or worn-out equipment. The state budget collapsed as firms were generating no profit, and the budget deficit began to explode. Pensions were in danger, and the ability of communes to invest in anything was almost nil. Welcome to the "free market" economy.

The debt must be paid

But the only goal of the IMF policies was to create equilibrium in the foreign balance of payments of Poland, with the zloty fixed at a cheap level against the dollar. Why? So that Poland could resume honoring the illegitimate $40 billion in foreign hard currency *debt,* the great bulk of which was amassed when interest rates in London and New York suddenly rose more than 300% in 1979 under the high interest rate policies of Prime Minister Margaret Thatcher in Britain and Federal Reserve Board Chairman Paul Volcker in the United States. Poland's dollar debt was in "floating" interest rates pegged in London to the rate of interest on overnight borrowing (LIBOR). As Poland was forced into arrears on its debt service after 1980-81, the unpaid portion of interest was capitalized by western bankers and governments as added debt to be paid, despite the fact that Poland has not received a penny of new money since 1981.

Former Polish Prime Minister Hanna Suchocka, whose support for shock therapy led to the defeat of her government in the October 1993 elections.

The true purpose of the IMF in Poland or Russia should not come as a surprise. The IMF, after all, is a bankers' collection agency controlled above all by the City of London and Wall Street.

The absence of social protest in Poland was due to a general confusion as to what and who were to blame for the misery created by the IMF shock therapy. Because it was the policy of the government, and there was no clear line of responsibility evident to most citizens, the source of the evil was blamed on "market forces," or Adam Smith's "invisible hand." Previously, economic problems were blamed on Warsaw communist central planners, a clear target for the rage of the population. What a brilliant deflection!

The human toll

By the end of 1991, Polish unemployment had reached 2 million. IMF shock therapy was working. The government

defended itself by arguing it had signed "Letters of Intent" with the IMF which mandated the strict austerity measures. What did Poland get in return? Misery and collapsing production, organized crime, a growing black-market economy, criminality, social misery, and a debased population.

When Polish voters signaled their clear revolt at IMF shock therapy in January 1991 during the elections in which Lech Walesa became President, the IMF and U.S. Embassy in Warsaw delivered open threats to the Polish government, to force it to keep Balcerowicz and the IMF shock therapy program. They were told that if they did not retain Balcerowicz and his program, all western assistance to Poland would cease. Balcerowicz remained and Walesa's first choice as prime minister, Jan Olszewski, a critic of shock therapy, was forced to drop out.

By the end of 1992, after almost three years of IMF "shock," Poland's industrial production had fallen to 66% of its level of 1989, according to data compiled by the U.N. Economic Commission for Europe in Geneva, one of the few reliable economic sources of data on eastern Europe. Poland's Gross Industrial Output in late 1992 was down to the level of 1975!

Yet for all the IMF-imposed social misery and pain since 1989, inflation ran at 70% in 1991, and more than 42% in 1992 and 40% in 1993. By the end of 1993, Polish unemployment had passed 2.8 million, more than 15.5% of the active labor force.

And still, Poland has not been the beneficiary of net new foreign investment.

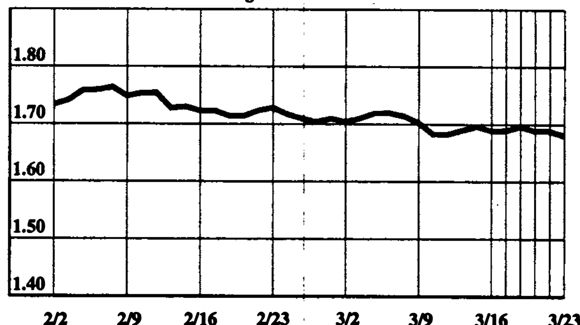
The IMF and the creditor banks, led by Barclays of Britain until very recently, have insisted on full repayment of Poland's unpayable foreign debt. In the absence of a debt restructuring agreement, Poland has been kept a pariah country. Investment has been pitifully tiny over the past four years. What "free market" economic activity exists is the most vulgar sort of small-time consumer sales. Poland has today no long-term national strategy or even government goal for where the nation's economy should go.

It will take years for Poland to undo the damage to the economy of the radical shock therapy under the best of conditions. But shock therapy has been a booming success in terms of destroying the potential of Poland to become a vibrant trade and investment partner of western Europe. In terms of increasing the overall well-being of the Polish citizen—social welfare, security in case of sickness, old age, and such—shock therapy has brought the majority of Poles to the gates of hell.

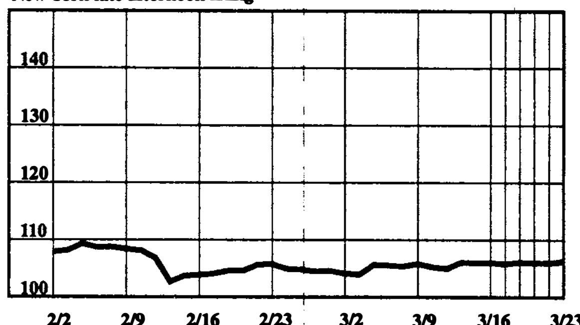
Given this history, it is little wonder that Poles, in the national elections on Sept. 19, 1993, ousted the pro-IMF regime of Hanna Suchocka and voted in a coalition of parties with direct ties to the former communists. But the tragedy is that, at least until early 1994, the government of Prime Minister Pawlak has been afraid to break with the shock therapy policy of Jeffrey Sachs and the IMF.

Currency Rates

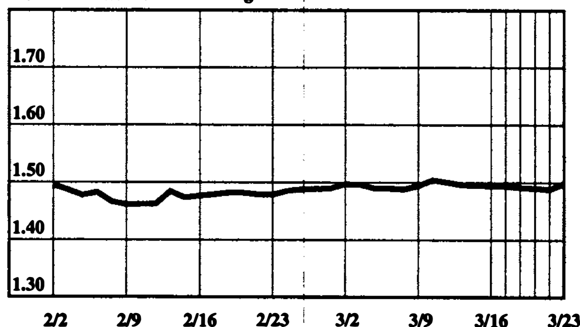
The dollar in deutschemarks
New York late afternoon fixing



The dollar in yen
New York late afternoon fixing



The British pound in dollars
New York late afternoon fixing



The dollar in Swiss francs
New York late afternoon fixing