

Poland: How To Build Capitalism and Escape Crisis

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THESES

1. We know how to build capitalism and it works
2. Institutions are not enough, good policy and heroes are needed
3. The financial crisis: overheating caused by fixed exchange rates
4. Poland has escaped the crisis through good policies

Communism, Moscow, 1991: Gray, poor, humiliating Never Again!



We Know How to Build a Market Economy

27 of 30 postcommunist
countries have become
market economies

Cure: Radical, Comprehensive Reforms

1. Quick Deregulation

2. Defeat Inflation

3. Fast, Extensive
Privatization

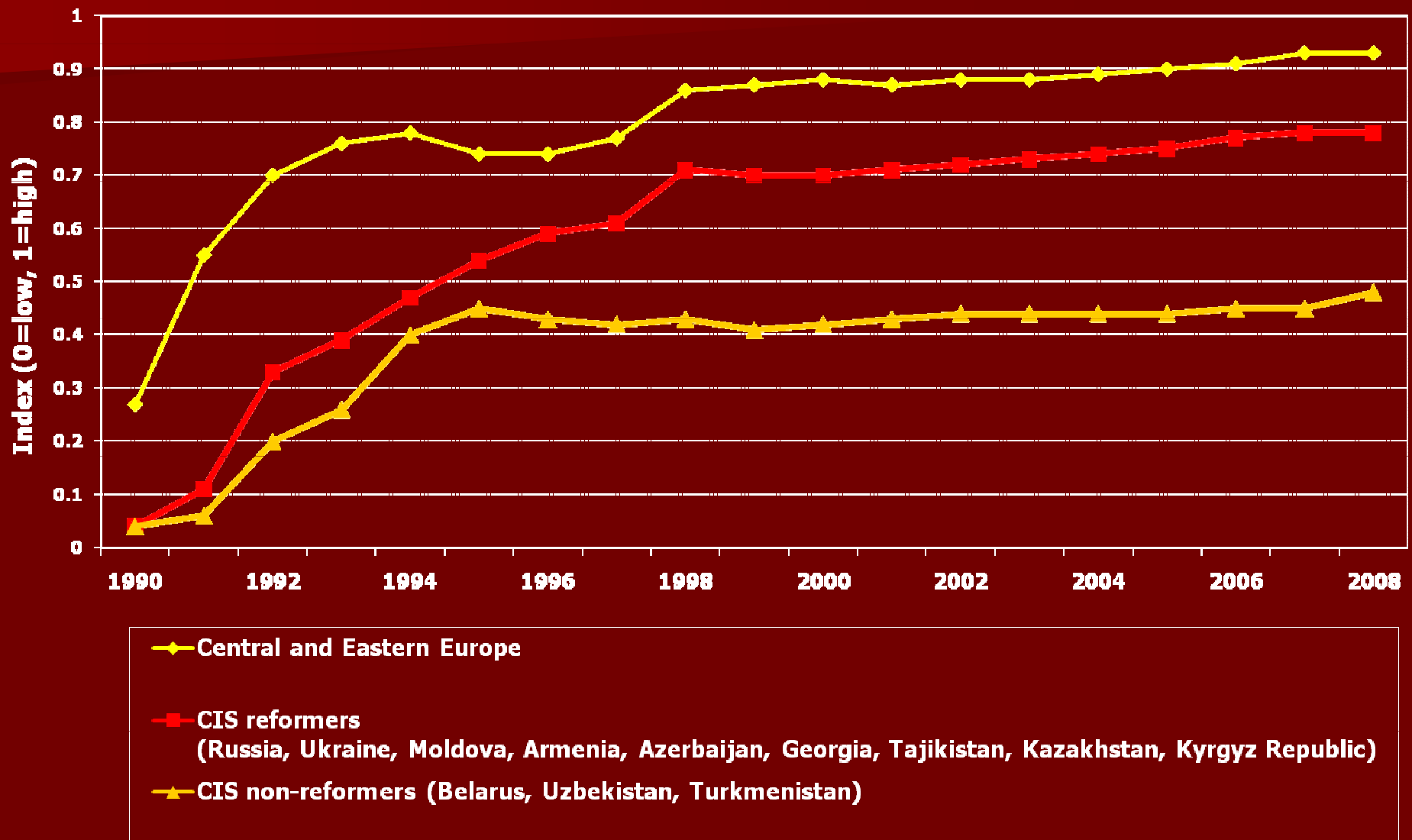
= Balcerowicz program

Speed was vital:

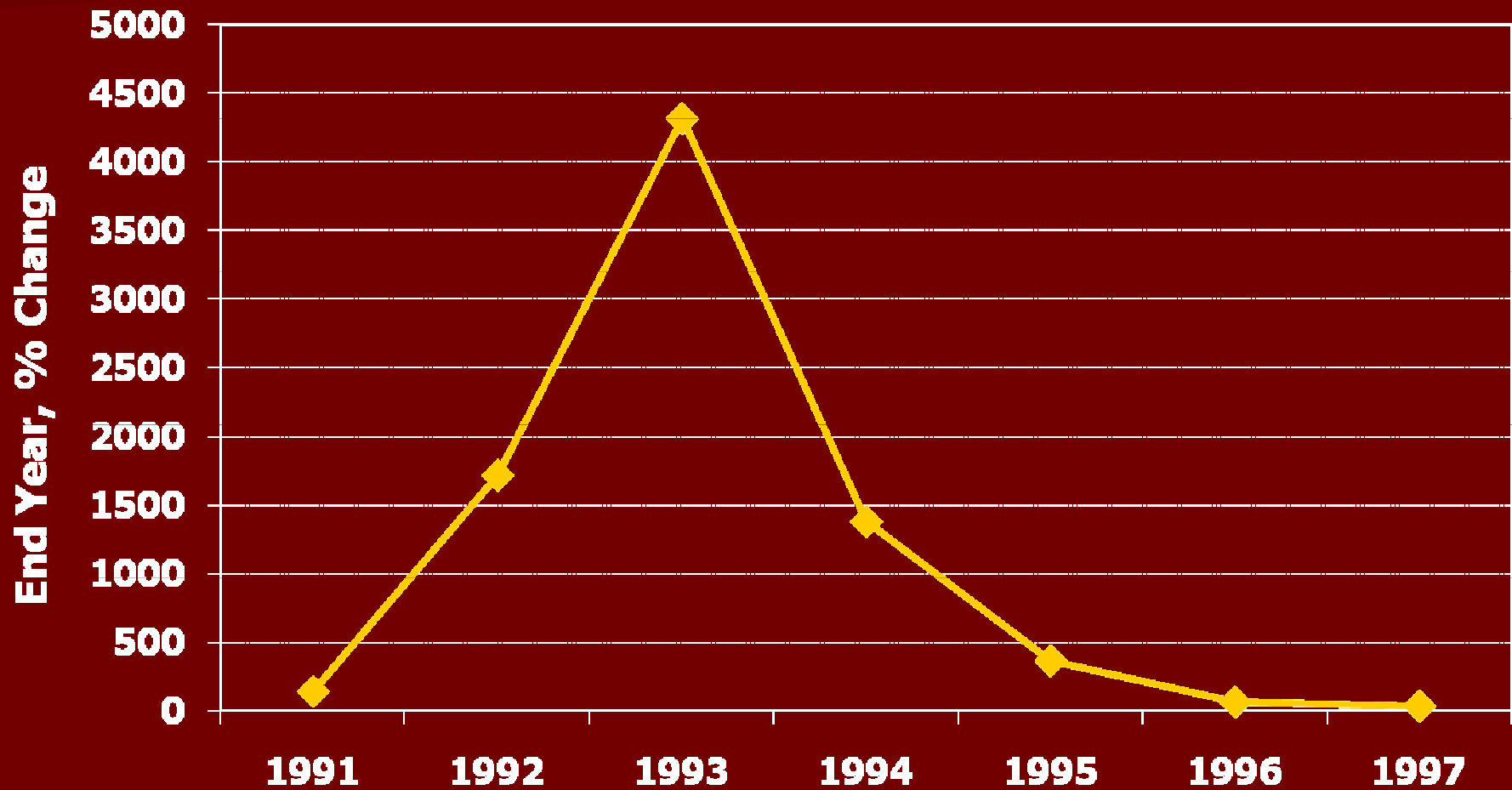
**“To wait means
to fail”**

**Mart Laar, former Prime Minister of Estonia,
1992-94 and 1999-2002**

1. Structural Reform Index: Early Reformers: Early Growth

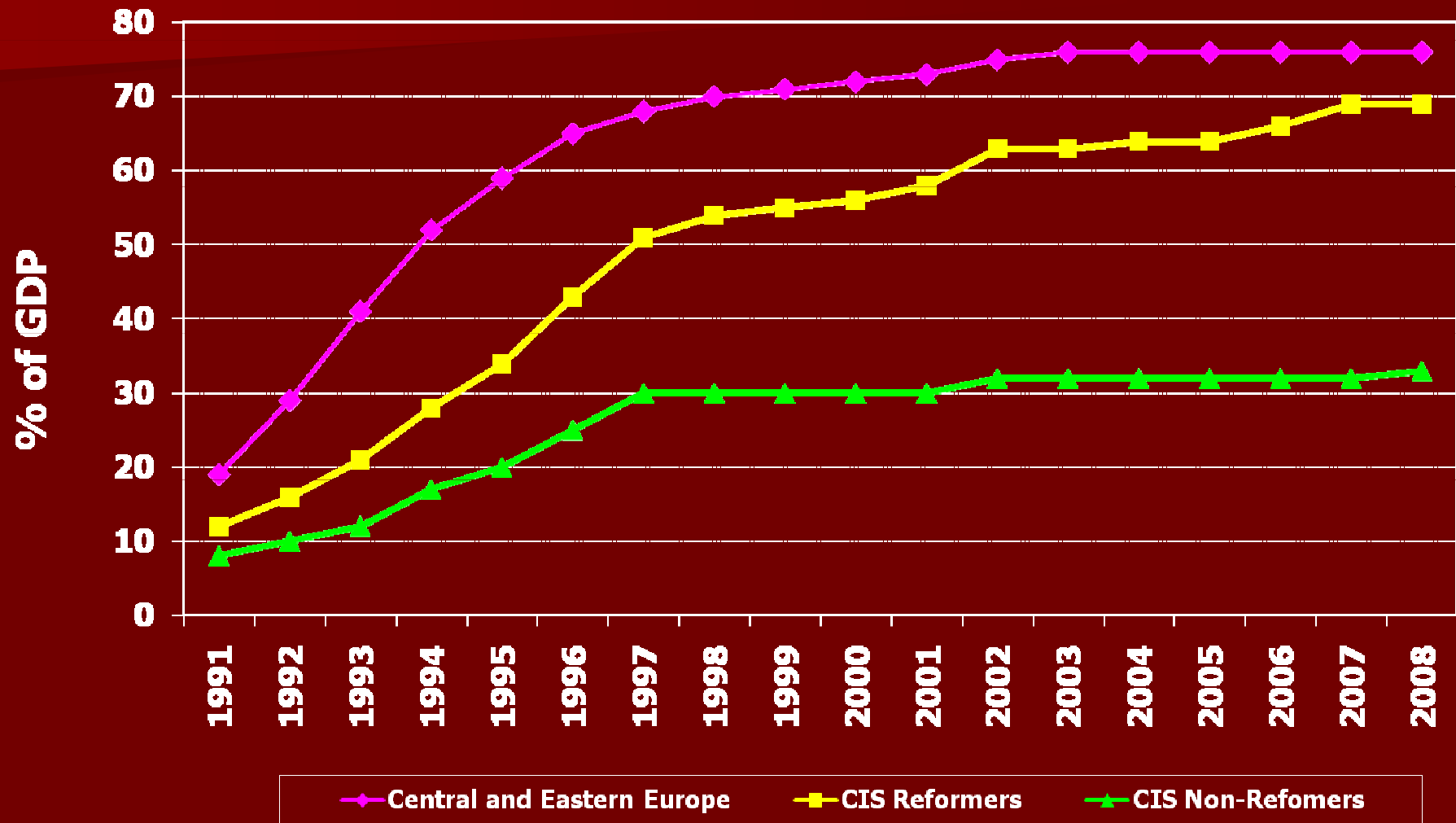


2. No Growth until Inflation under Control: Hyperinflation in the CIS



3. Early Privatization: Early Growth

Private Sector as % of GDP



Privatize As Is Politically Possible

Predominance of private sector:

- precondition for market economy
- precondition for democracy
- limits corruption

Privatize as you can!

Requirements for Success

1. Democratic breakthrough:
beat the old communist elite
2. Formulate, adopt and implement radical market reform program
3. Vital: Strong reform leader!

Poland's Contributions

1. First democratic breakthrough:
Sejm Elections June 4, 1989
2. First non-communist government
3. Balcerowicz program: original
radical reform
4. Radical small enterprise
liberalization

Heroes of Transition

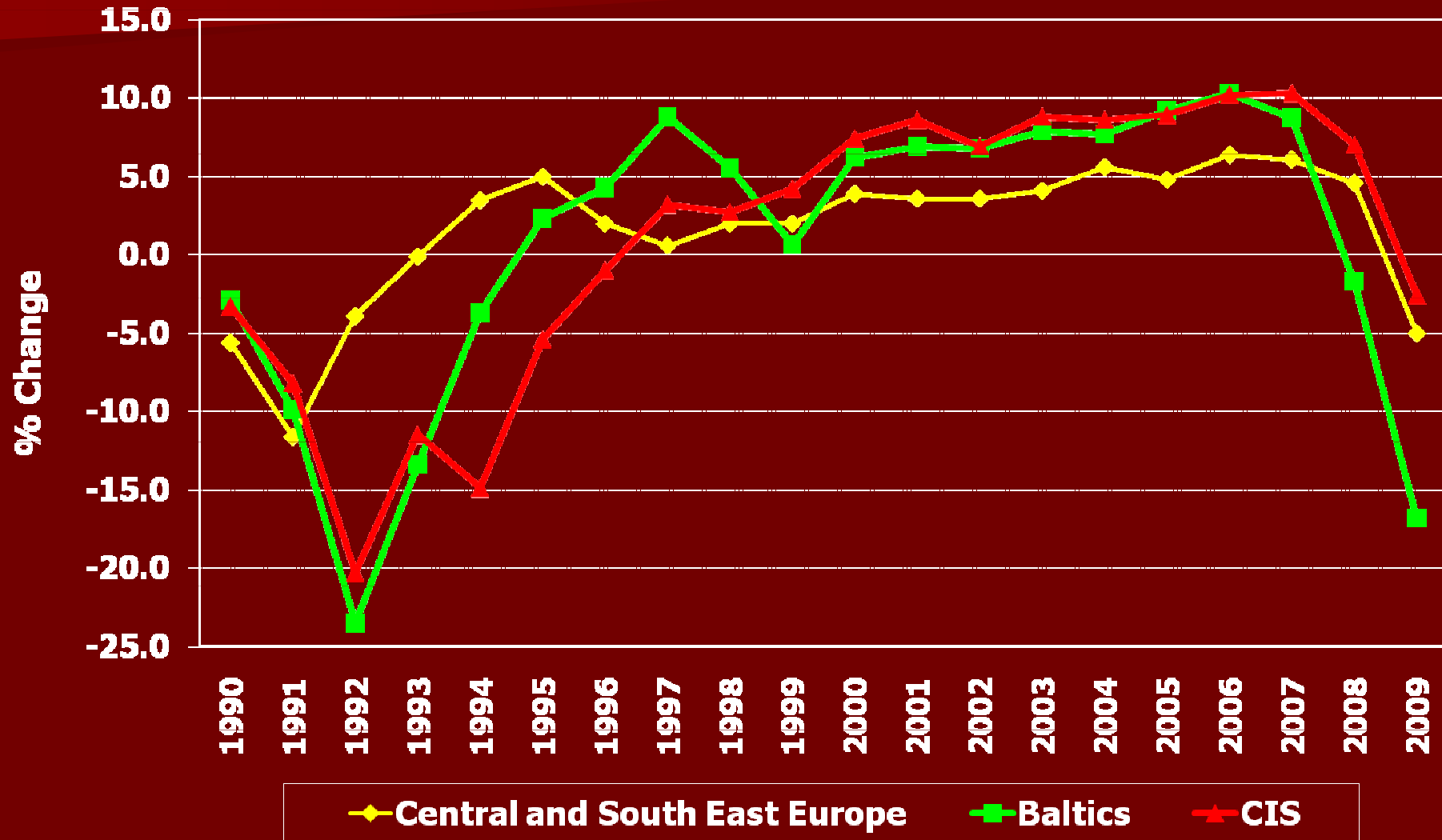
- Leszek Balcerowicz, Poland
- Vaclav Klaus,
Czechoslovakia
- Yegor Gaidar, Russia
- Mart Laar, Estonia
- Einars Repse, Latvia

Dynamic Market Economies : Reforms Worked

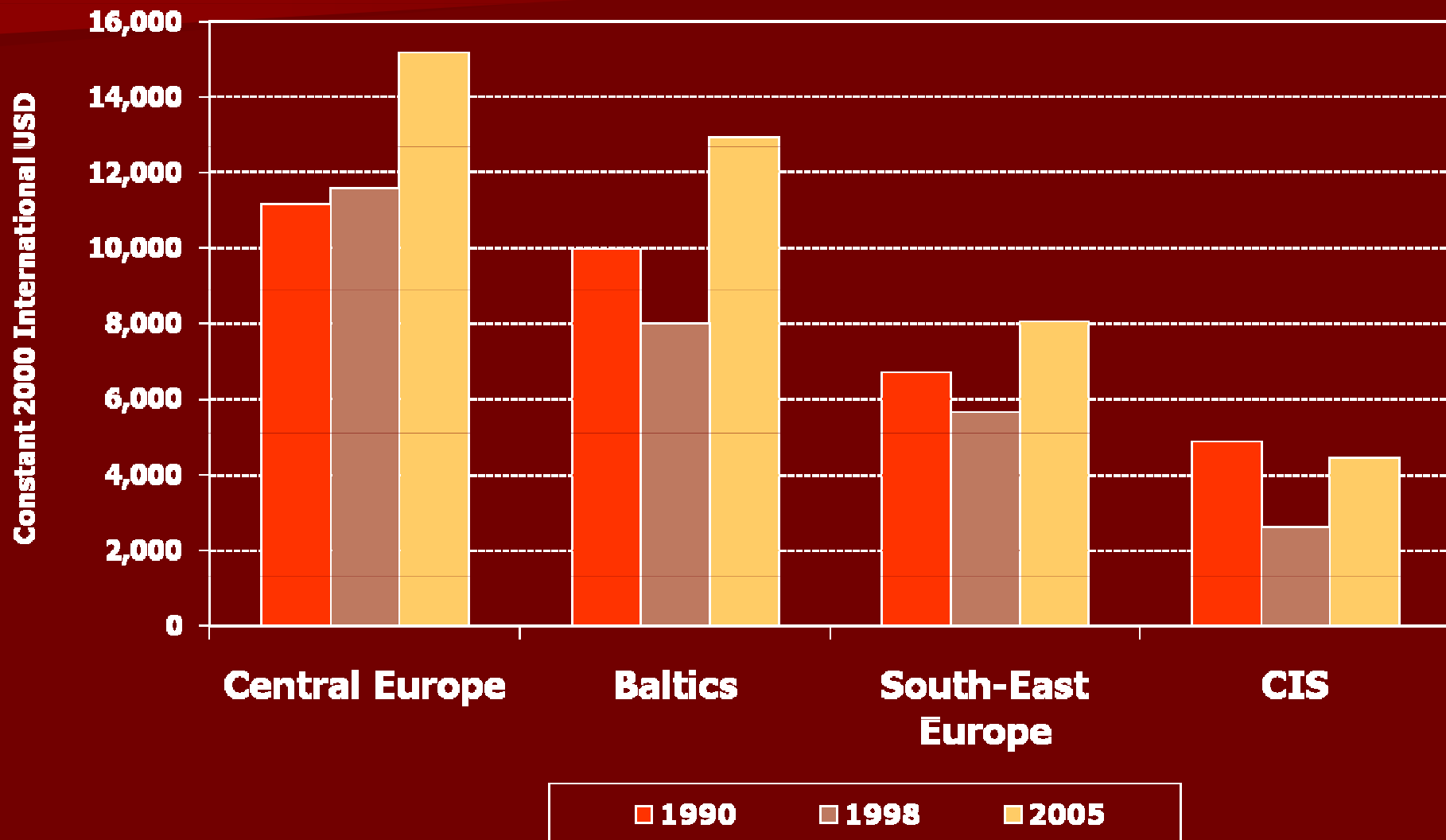
1. Critical mass of market reforms
2. ...and privatization
3. Conservative macro policy
8% GDP growth a year
2000-2008!

Official GDP Growth:

1. Collapse Bred Misery
2. Capitalism Brought Growth



GDP per Capita in PPP, 1990, 1998, and 2005

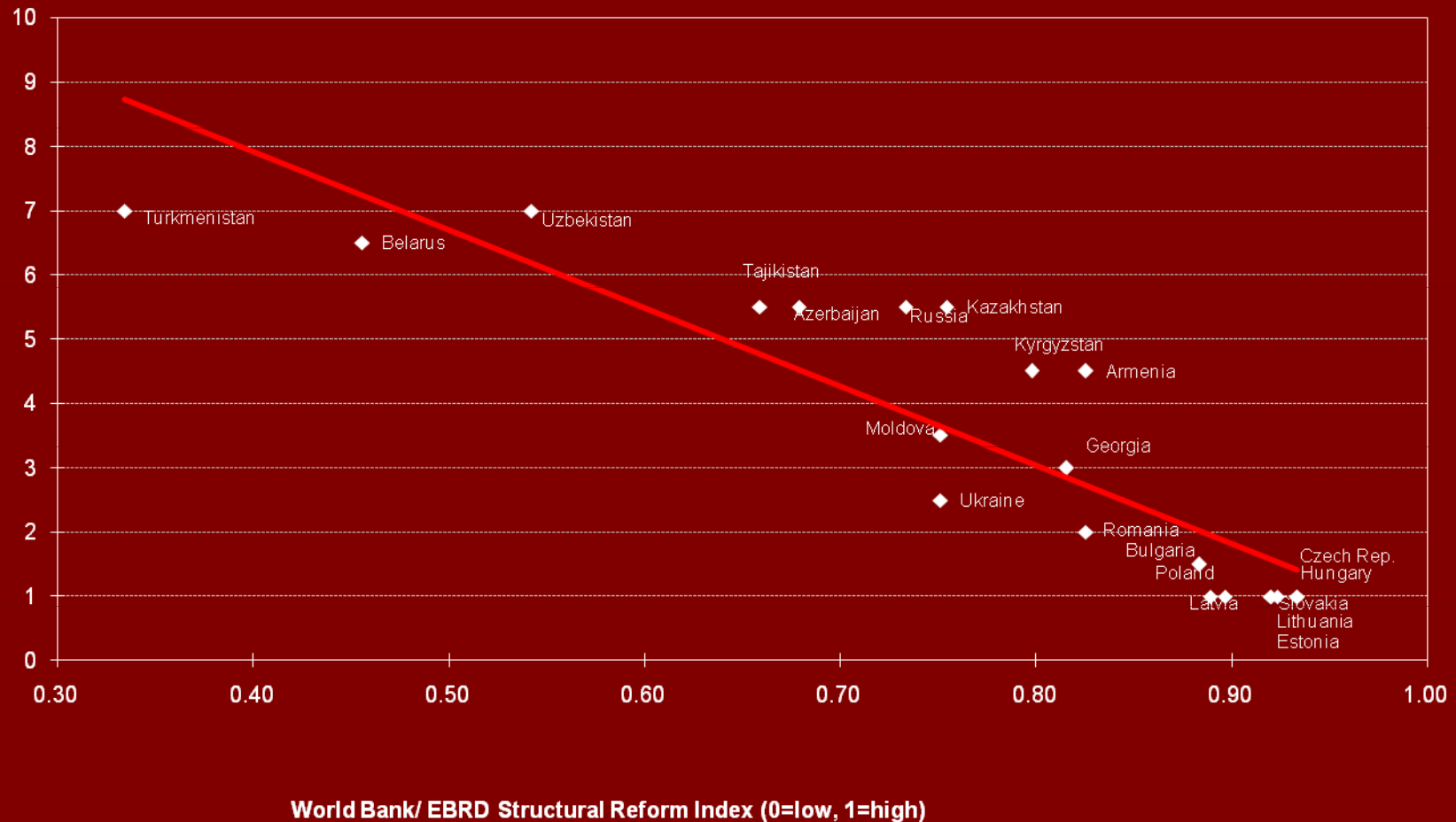


Democracy: Best Weapon against Rent-Seeking

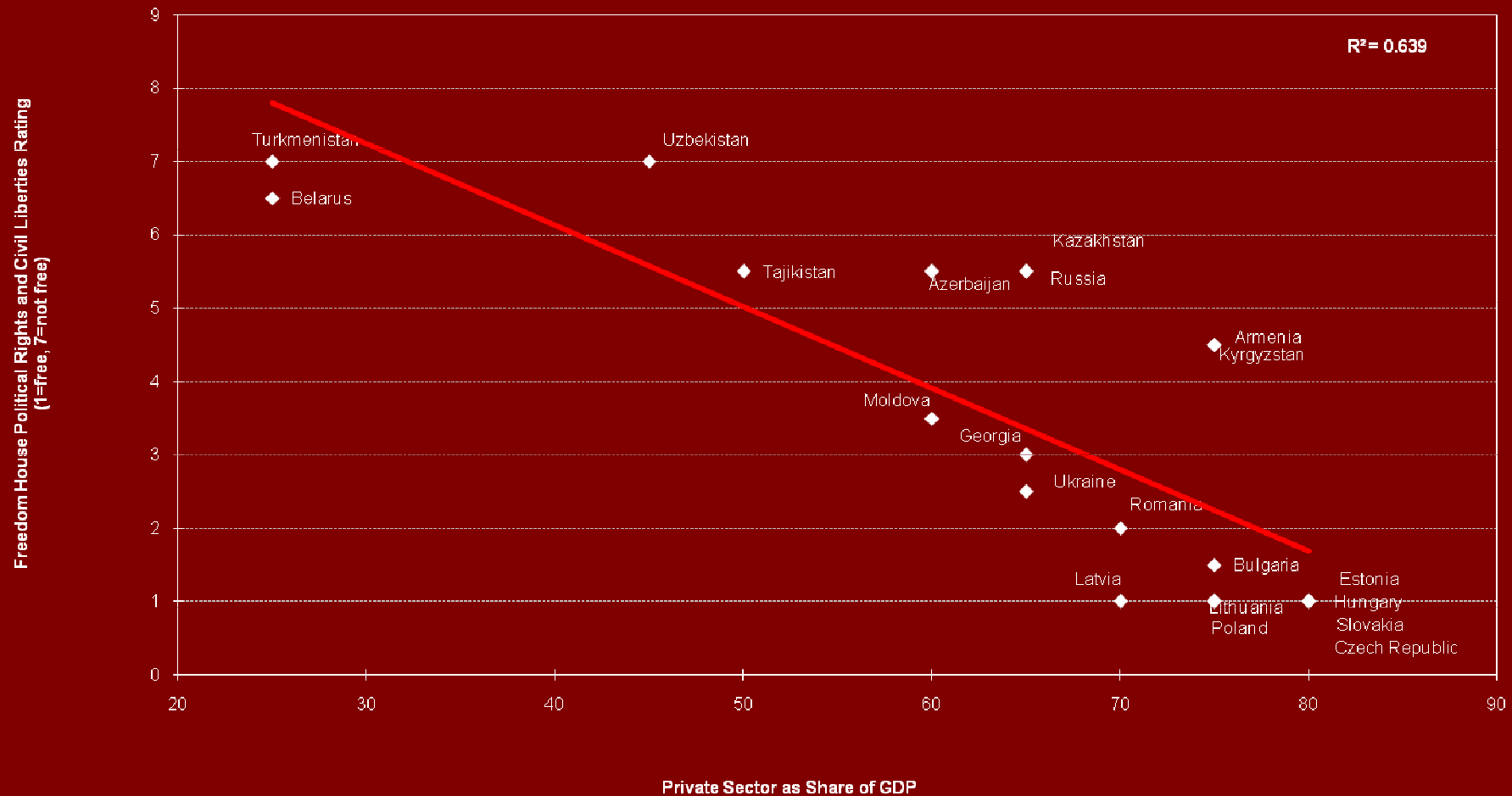
1. Democracy and market reform positively correlated
2. Democracy and privatization go together
3. Democracy & privatization reduce corruption

1. Democracy and Market Reform Go Together, 2005

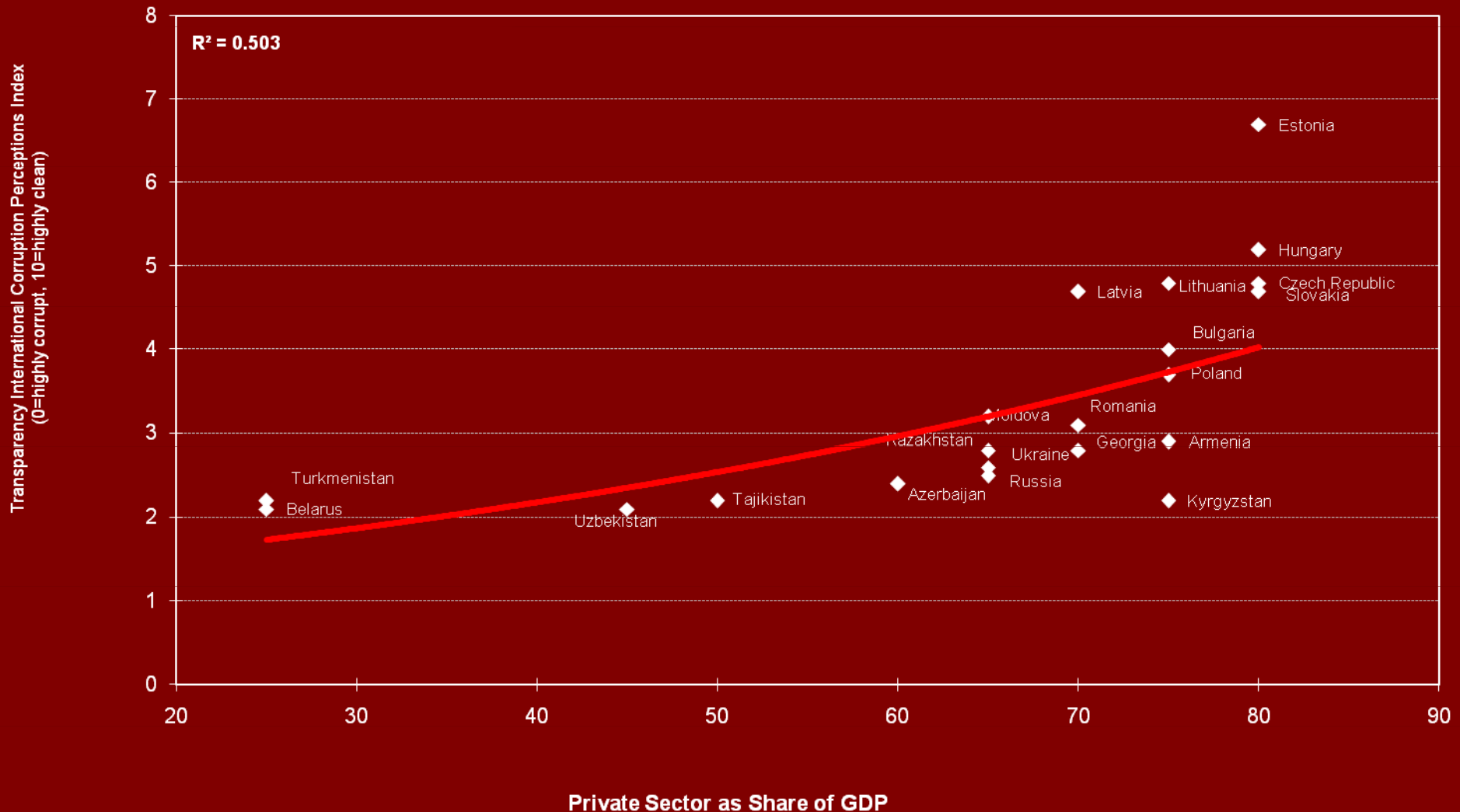
Freedom House Political Rights and Civil Liberties
(1=free, 7=not free)



2. Democracy and Privatization go together, 2005



3. More Privatization = Less Corruption, 2006



East European Financial Crisis

- Overheating: too large current account deficits, private foreign debts, and inflation
- Sudden stop & huge GDP falls
- Main cause: fixed exchange rates in Baltics, Bulgaria, and Ukraine, but not admitted to the euro
- Public finances good before crisis (except Hungary)

East European Financial Crisis (2)

- Reminiscent of East Asian crisis 1997-98
- Adequate IMF programs have been adopted with substantial financing
- Likely to end as suddenly as it started with strong recovery
- Capitalism prevails: No leftwing tendencies and amazingly few protests

Poland Has No Crisis

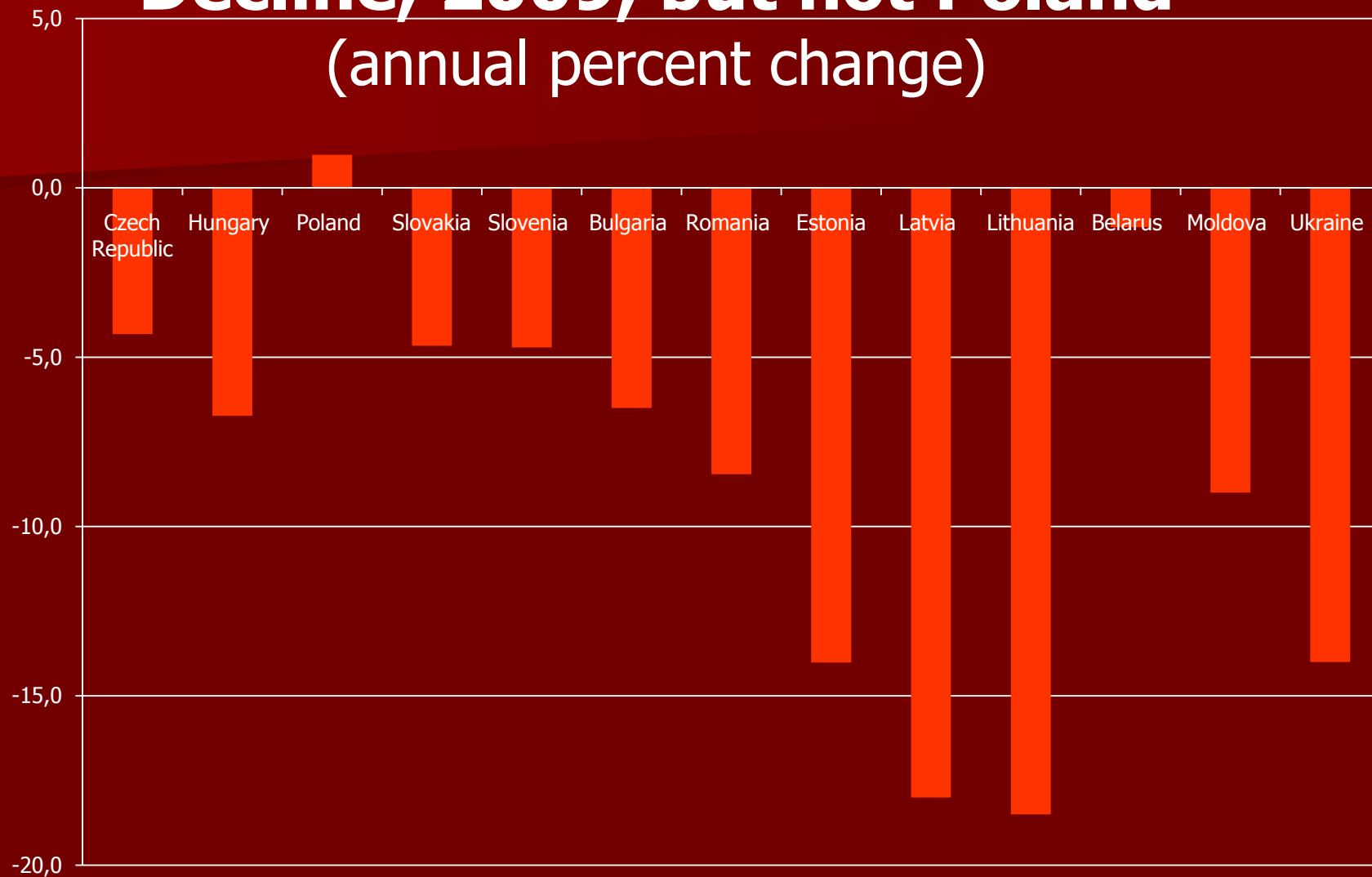
No GDP decline any quarter because of excellent Central Bank policy:

- Inflation targeting: persistent low inflation because of positive real interest rates
- Floating exchange rates impeded currency inflows
- Checked credit expansion and house prices
- Regulated away mortgages in euro

Because Leszek Balcerowicz ran the National Bank
Good institutions work only with good leadership.

Central Europe Expected GDP Decline, 2009, but not Poland

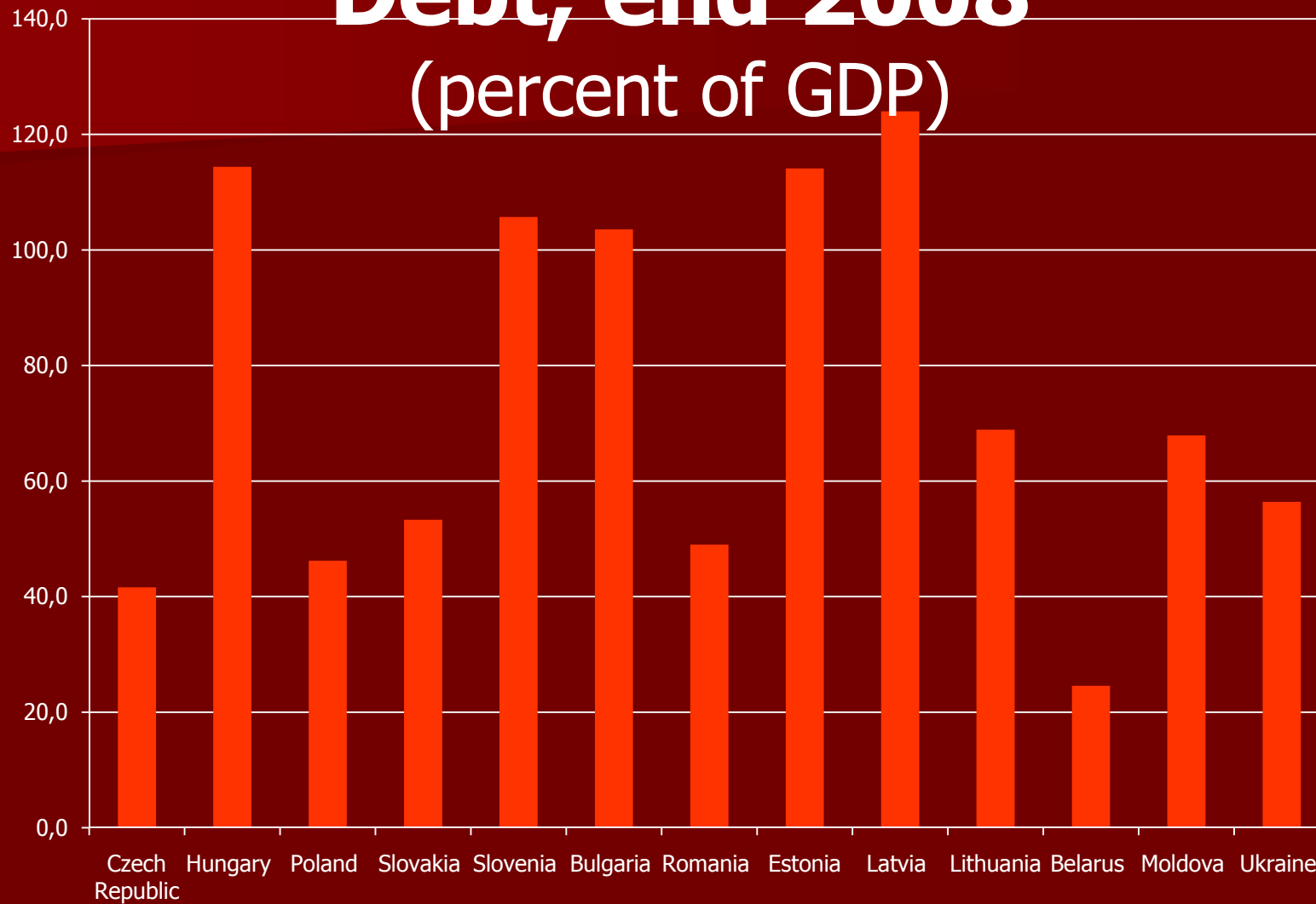
(annual percent change)



Source: IMF World Economic Outlook Database, October 2009, Accessed October 28, 2009

Poland: Little Foreign Debt, end 2008

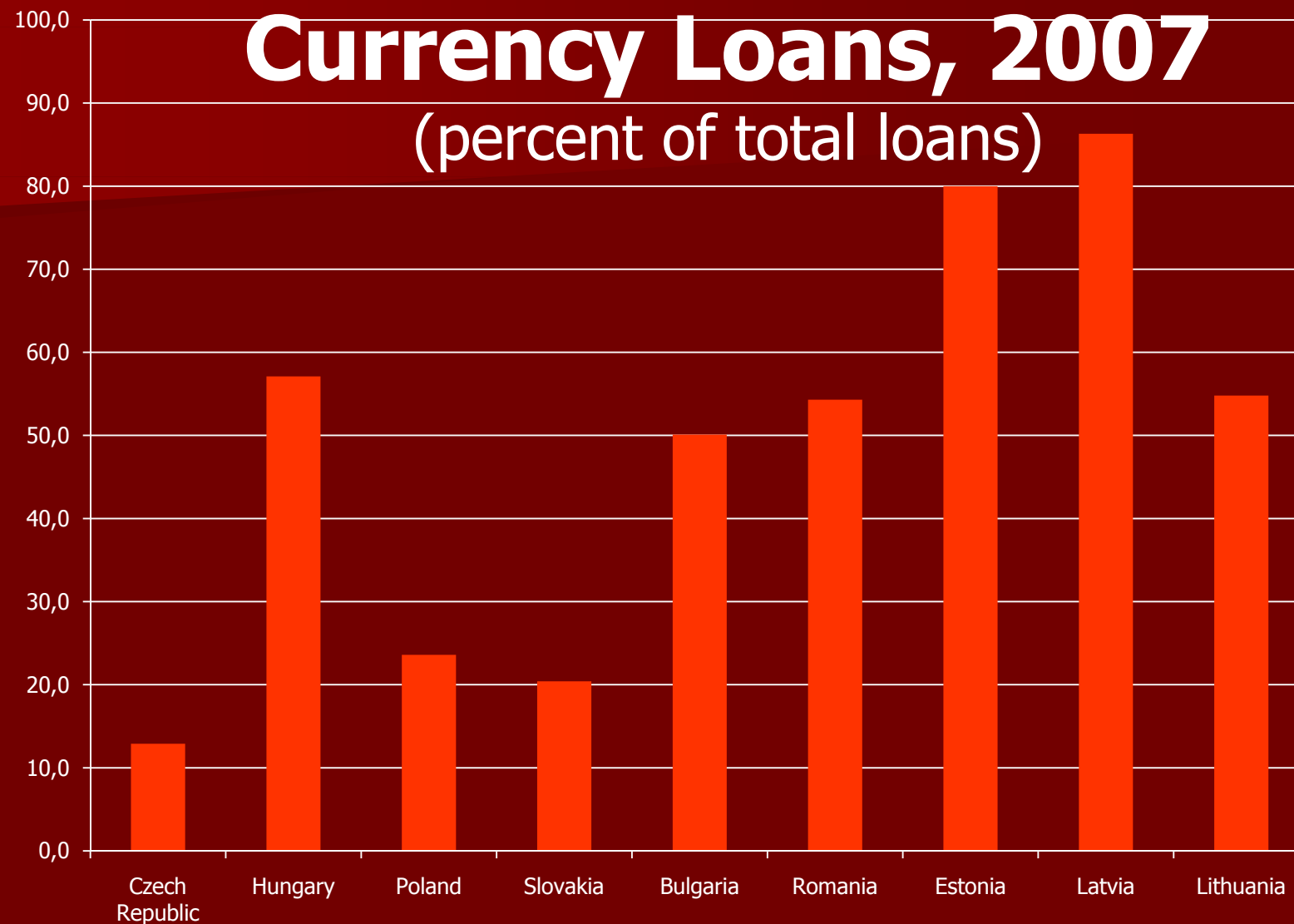
(percent of GDP)



Source: EBRD, Accessed October 28, 2009

Poland: Small Share of Foreign Currency Loans, 2007

(percent of total loans)



Source: Darvas, Zolt, and Jean Pisani-Ferry (2008) "Avoiding a New European Divide," Bruegel Policy Brief No. 10: 2, Brussels: Bruegel, December, www.bruegel.org.

Conclusions

- Capitalism has been successfully built
- It is likely to last because it is not questioned
- The current East European crisis looks like a temporary blip like the East Asian crisis of 1997-98

Conclusions for Poland

- The crisis has proven the quality of Poland's economic success in the last 20 years
- Stay the course!
- Maintain inflation targeting until euro adopted!

How Capitalism Was Built

The Transformation of
Central and Eastern Europe,
Russia, and Central Asia

Anders Åslund

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