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Grzegorz W. Kołodko

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CRISIS, ADJUSTMENT AND GROWTH  
IN SOCIALIST ECONOMY –  
POLITICAL CHALLENGES AND THE DILEMMAS  
OF ECONOMIC SCIENCES

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**Crisis, Adjustment and Growth in Socialist Economy -  
Political Challenges and the Dilemmas of Economic Sciences**

The crisis syndrome which now reaches beyond the economic sphere, to embrace also social and political institutions, presents a serious challenge to both policy and science, specifically - to economic sciences. Science is often held liable for adverse social and economic developments (consequently also for political events). One thus comes to ask, to what extent the level of theoretical knowledge and scientific postulates with regard to social and economic policy share the joint liability for crisis phenomena and processes. Is science keeping abreast of the challenges of development processes and proving its usefulness? Is policy willing and able to use the wisdom that science proposes? Answering these questions is worth a try, especially in view of accelerated changes taking place in the socialist countries at the turn of the eighties. Speaking of socialist countries, I refer to the economies other authors call, increasingly often - real socialism, communism or Soviet-type economy. The problem however is not with definitions, but with the meanings they stand for. One could say that on the one hand, science fails to follow the pace of political challenges and, on the other, both policy and practice draw too little on scientific achievements.

**1. General Crisis of the Socialist Economy**

Socialist economy is undergoing a general crisis. This is no business cycle recession, due to an adverse combination of events and consisting in the appearance of unfavourable trends in the process of macroeconomic reproduction, but a wholesale crisis of economic, social and political relations, along with their concurrent institutions. The difference between the

general crisis and that related to cyclical growth processes<sup>1</sup>, observed already at the earlier stages of socialist economic development<sup>2</sup>, is that it cannot be cured under the set of conditions which had created it. Hence, the general crisis can be cured by a major reform of the socialist economy or its outright negation. In the second case, never practically implemented as yet, we would have a very peculiar case of development through a double negation, as if it were. Socialist economy came into being as a negation of the capitalist economy and now, it would be coming back to where it came from, though on a different level and in a considerably modified form, because no one, I believe, would like to bring back the *status quo ante*. After all, the only escape route lies ahead, though for ideological and political reasons, various factions and social and professional groups give different interpretations to such basic concepts as development, national interests and macroeconomic performance.

The general crisis of the socialist economy appears in three planes: systemic, structural and political. Attempts at overcoming it must therefore also consist in fundamental transformations in all these planes. Comprehensive and radical economic reform is the answer to the systemic crisis. Attempts are made to counter the structural crisis with far-reaching structural transformations, while a re-evaluation with regard to former objectives and means and methods used thus far, are the

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<sup>1</sup> I expanded on cyclical economic growth in socialism, including the so-called long cycle elsewhere (Kołodko 1986).

<sup>2</sup> Janos Kornai divides the history of socialist economy to date into three phases: heroic, classic and reformed socialism (Kornai 1987). The following periods should correspond to these phases in Poland: 1946-1956, 1956-1980 and 1980-1989. According to my interpretation of the general crisis of socialist economy (Kołodko 1989a and Kołodko 1989d) it started only in the eighties.

reaction to the crisis of economic policy. Speaking of policy, one cannot forget its broader dimension, as we are also concerned here with the ways power is exercised, which have to change in times when we are coping with the general crisis of the socialist economy.

It is clear that the extent of crisis phenomena differs from one socialist country to another. Without getting involved in the subtleties of definitions and methodology, we can say that the crisis syndrome is most obvious in Poland. Poland however is an exception not with this respect. What is exceptional, is the spectacular scale of crisis phenomena in so many areas (e.g. inflation, shortages, foreign debt, environmental pollution, depreciation of the ethos of work, ideological chaos and others), much broader than in other countries. This allows some to deny the existence of such problems, but they are still there, official declarations notwithstanding.<sup>1</sup> While still questioned by many politicians and - less frequently - by economists (even if they do not use this term), the general crisis of socialism is a fact.

This crisis presents both theory and practice, science and policy with special tasks. What they should consist in is another question, on which there are many views. The most convenient point of view would be to assume that science should merely explain reality, leaving the difficult task of its transformation (for the better, of course) to politicians.

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<sup>1</sup> The position of Ramiz Allia, the Albanian leader is an extreme, though not unique illustration. He said on the 45th anniversary of Albania's liberation: *"Everybody knows what is going on in the Soviet Union, Yugoslavia and other Eastern countries. Revisionists have betrayed Marxism-Leninism, abandoned socialist ideology and entered the road of counter-revolutionary reformism. These countries found themselves beset by a deep economic crisis, their debts are choking them. Social and national conflicts are erupting everywhere. Gates have been opened to foreign capital. The growth of the private sector has become the prime goal. Coercion and class exploitation are setting in again. Vid. Tygodniowy Biuletyn Specjalny PAP, No 3129 (1989.09.29) p.V.*

While I do not share this view, I propose to draw a clear distinction between science on the one hand, and policy and ideology on the other, and to distinguish between theory and practice (Kolodko 1990). It is worthwhile to quote here an interesting view of Ralf Dahrendorf, the rector of Anthony's College at Oxford: *"Today, it is much more important to be like a crystal reflecting external light, than to elaborate tomorrow's programs. Our role should above all consist in understanding what is going on. One should not repeat the mistakes of the past, when many intellectuals, became ideologists, only to play a truly negative role. Wishing to take sides, they confused theory with practice"*<sup>1</sup>.

Given that these approaches are interwoven with regard to social and economic phenomena and processes, confusing theory with practice, or science with policy is both frequent and understandable. There should be no doubt however, that economic sciences cannot confine themselves to the role of the crystal, which can all too easily become a crooked mirror. The role of economics is to explain reality and facilitate its understanding, which is no small feat in a period of turbulent changes, but it also should point to the methods and instruments to be used to achieve desirable transformations of this reality. The former is the descriptive approach, while the second - normative.

Much progress has been achieved in the recent years, both in socialist and Western literature, with regard to the theoretical explanation of crisis phenomena in socialist economies. It can be attributed to the - unfortunately - increasing amount of empirical material and a more scientific approach to the subject matter. On the one hand, I specifically refer to the fact, that apologetics often practised in the days of classic

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<sup>1</sup> Vid. interview granted by Ralf Dahrendorf to *La Repubblica* on 13-14 August 1989. (quoting after *Forum* 1989 No 40 p.6).

socialism with regard to economic thought is being very quickly shelved. On the other, primitive sovietology in Western literature is losing ground to an ever richer - as interest grows - professional literature. Advances in these areas hardly mean that unanimity has been reached on the sources, essence and the consequences of the general crisis of socialism. Conversely, there are even more differences, if one also considers the ways of overcoming this crisis.

## 2. Science and Policy

Joan Robinson once said that an economist's answer is a politician's question. Much as it tempting, this is a passive approach. One must ask the question about the origin of such important divergencies between the postulates of economic science (in their normative function) and the decisions of economic policy. These divergencies in turn, make reality very much different from scientific models. Needless to say, reality is usually much worse. Blaming policy for everything would be an obvious oversimplification, because this issue is much more complex.

First, science is imperfect and one must admit that there are even fundamental questions to which it may have no answers at a given time. Second, its answers may not be readily applicable and thus - useless for practical purposes. Third, economic sciences are not, and will probably never be - ideologically and politically neutral. This is why there may often be many answers to a single question and it cannot be always unequivocally determined where the objective truth lies. Fourth, politicians are often unwilling or incapable of using scientific achievements. Fifth, economic postulates (especially in times of deep crisis) may be demagogy in disguise, usurping the name of science, may which turn policy away from science as such, or build policy on demagogy and make science responsible.

Sixth, policy often strives to treat science one more instrument, incapacitating science and leading to scientific servility (if a servile science still deserves being called science). Seventh, science may put forward rational solutions, that policy will readily apply, but the economy, and a population unwilling to bear the necessary therapy, may well make them unenforceable. Eighth, science is not infallible, especially on society and economy.<sup>1</sup> It deserves being stressed here, that spreading economic and political destabilisation - one of the symptoms of the general crisis of socialism - is hardly helpful in enhancing the influence of science on policy and thus - on social and economic reality, insofar as the latter is a function of policy rather than of spontaneous processes. While one may observe an increased interest of policy in science, reflected, among other things, in impatient questions asked of science, there are other, disturbing phenomena. I refer especially to spreading demagogy, mentioned before, mostly in the form of various "miraculous" anti-crisis recipes, uncertainty as to the desired directions of development

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<sup>1</sup> J. Pajestka gives an interesting presentation of this problem in his last work. Asking questions ... why was a mechanism which did not prove itself in practice adopted as socialist and why has it operated for so long without necessary adaptation, the author then states: *The first element of the answer is that science is conceited, and believes its own infallibility. This fallacy needs no comprehension nor should it be directed exclusively at Marxism. (...) man became fascinated with science, showing less than normal human caution, which tends to critically evaluate everything and to be very careful in the formulation of conclusions (...) The blindness of mankind, believing without reserve that science shows the right way and that it should be fully trusted, is proper to that stage of human civilisation in which man became fascinated with himself, with his "divine" qualities. I do not mean to say here that science should not be trusted, but that it should not be trusted indiscriminately. Moreover, the more difficult are the processes under consideration, the harder it is to relate them to real experiences and the more caution is advisable.* (Pajestka 1989, p.171).



processes in the face of ever stronger political struggle and ideological chaos, and the unusually strong pressure of time. In connection with the last remark, one must stress the danger of scientific analyses and syntheses becoming more superficial, of theory becoming journalistic deliberations or - the earlier mentioned confusion of theory with ideology. The period of destabilisation makes it difficult to draw on scientific achievements also because of the complexity of the matter, which is to be transformed. It resembles the case of a seriously ill patient who refuses the proposed therapy despite his poor condition and the dangers he is facing, while we are unwilling or unable to force him. In that case we run into an immunological barrier, as if it were, or a barrier to the society's capacity to absorb undergoing change.<sup>1</sup>

This barrier which can hardly be determined *ex ante*, while ascertaining it *ex post* may mean that we are already dealing with an open social conflict which may take various forms, was present throughout the whole decade of the eighties. The realisation of coming so close to this barrier of acceptance or social protest tends to paralyse policy. This must be understood, though not necessarily exculpated. Science however, not being directly responsible for the decisions of economic policy, is always more radical. This partly explains the inconsistencies in the reforms of some socialist economies implemented in the eighties, especially in China, Yugoslavia, Poland, Hungary and the Soviet Union.

Dogmatism represents a special threat to the proper development of economic sciences and their application.

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<sup>1</sup> Destabilisation can reflect the lack of reformatory efforts, when ignorance, indolence or other factors produce a situation where the authorities fail to meet the demand for adaptation, but also - going beyond the barrier of adaptive capacities. This is a phenomenon which can happen in any reformatory process. It must be understood and countered, because it can jeopardize the whole process of deliberate changes. (Pajestka 1989, p.186).

Unfortunately, it is not only difficult to shed its yoke but, what is more, one can observe a propensity for extreme attitudes with this respect. Negative experiences with one economic system or policy tend to lead to extreme attitudes and to the overrating of radically opposed systems. Such extreme attitudes are to be observed in both science and policy, and their relationship is obvious. Quite naturally the general crisis of socialism diverted the interest of economic sciences towards liberal theories. However, what can be called an explosion of these theories, often expressed in the lack of discrimination in adopting various "ultra-market" programs or primitive monetarism, lacking even serious studies of Western literature - so abundant in this field, makes one wonder. One must also note that fashion is a factor also in economics. And, as we all know, fashions come and go, or at least change, except that falling for fashions may be dangerous when dealing with economies and societies.

While sympathizing with market and monetarist trends in the structural and institutional transformations of the socialist economy, one should avoid taking extreme positions, especially on economic policy. This point is also emphasized with regard to the government's economic program presented in Poland last fall (Program 1989), which is precisely an example of such one-sided espousal of scientific proposals and as such - can be rather disquieting. *The authors' conviction that the market is the only admissible regulating mechanism and that the fullest possible elimination of the state from the economy sounds (...) like a dogma. For it is hard to give another name to a situation where the implementation of a principle seems more important than the balance of losses and benefits derived therefrom.*<sup>1</sup> The fundamental danger involved in such dogmas lies

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<sup>1</sup> Vid. T. Jeziorański (1989)

in a specific revival of wishful thinking. For attempts to transplant solutions proved (though still incompletely) in other institutional and structural environments, to a fundamentally different environment of a destabilised economy of shortage, are nothing less than wishful thinking. Unfortunately, the lessons of practical experience will be available only at a later date. Will science, divided over many aspects, be also responsible in this case? After all, political aspects to which economic arguments have usually lost, are decisive.

### 3. "Non-market, Non-plan" System

The plan versus market dilemma has been solved. This statement applies to at least some of the socialist economies, more advanced in their reforms (Yugoslavia, Poland and Hungary and, to a lesser extent, China and Vietnam). In the Soviet Union, we can observe increasingly heated discussions typical of the period of naive faith (the early eighties in the case of Poland and Hungary) in the chances of combining the advantages of central planning with the merits of market economy.

As of now, it is difficult to speak of economic reforms in other socialist countries, in the sense I give to this term in the present essay.<sup>1</sup> For them, it is still a matter of time. What is more, these countries or - more precisely - their politicians deny the need for market-oriented reforms and this cannot fail to bear on the condition of economic sciences and research patterns.

One can come across views which we may perceive as coming from a different era. The Romanian interpretation of the processes in Hungary is following: *It is a historical nonsense to turn back to reformatory concepts and practices, to revert to*

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<sup>1</sup> For more on non-European socialist countries refer to, among others: V. Andreff (1989), D.S.G. Goodman (1989) and S.G. Roca (1989).

capitalist forms which would be implied in the privatisation of the means of production, to belittle the role of socialist property, to legalize the so-called market socialism, which opens wide the gates to competition, private profit, egoism, individualism, unemployment, inequality and lack of justice, inherent in former societies.<sup>1</sup> Such an approach sounds more like ideological interpretation than scientific argument. However, also this approach is used to question the advantages of market mechanisms over centralized planning.<sup>2</sup>

Assuming however, that the market orientation of systemic reforms in socialist economy and policy, which leans more and more on monetary instruments, will make headway in more socialist countries, the plan versus market dilemma shall be settled in favour of the latter. This should not however imply dumping macroeconomic planning altogether, though a person following discussions on this subject might sometimes get the impression that the market alone provides an adequate mechanism of allocation. Even if we made this assumption just for a moment (though it is not true), then we would be still left with the fundamental problem of building a market economy. The dismantling of a central planning system is one thing, and tangible achievements can be shown, but creating and putting an efficient market mechanism in place is quite a different issue, and most of the economies currently undergoing reforms have precious few positive results to boast with this regard.

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<sup>1</sup> Vid. *Lupta Intregului Popor*, September 1989, (Romanian Military and Historical Magazine), quotation after *Odrodzenie* 1989 No 40 p.2.

<sup>2</sup> For example, H. Nick of the Academy of Social Sciences of the Central Committee of the East German Communist Party points that the advocates of the so-called market socialism ...are fascinated by naive, or even romantic beliefs about the regulating capacities of the market economy, about the allegedly healing influence which can be expected of free competition and of the decartelization of socialist monopolies. Vid. *Tygodniowy Biuletyn Specjalny PAP* 1989 No 3089 (1989.04.08) p.VI.

The economic system now in place is a curious hybrid. It combines the negative features of both planned and market systems. Taking another approach, one might say that it is a "non-plan, non-market" system, a peculiar state of systemic vagueness, very threatening to economic performance. In such a situation, the crisis syndrome develops and becomes more acute. Crisis phenomena have been originally caused by a set of other reasons, but at a point where the old system no longer dominates, while the new has not yet set in, these causes are strong enough to sustain and fuel these destructive social and economic processes.

This is particularly visible in the phenomenon called shortageflation (Kołodko-McMahon 1987, Kołodko 1988). It consists in the parallel growth of both price and repressed [accumulation of excess money balances] inflation. The manifestations of this process have been increasingly strong in reformed socialist economies, especially since the second half of the eighties. For we are now facing an accelerating price inflation and more acute shortages in all the countries undergoing reforms. To a lesser extent, this is also true, especially with regard to price inflation, for the classic centrally planned economies, including the best developed - the GDR and Czechoslovakia. One must add here, that the more these countries delay the inevitable market and monetary type reforms, the more dramatic will their future shortageflation be. This thesis is corroborated by Chinese and Soviet experiences, where price inflation levels were, respectively 25% and 8% in the years 1988-1989 and inflation was accompanied by increasingly acute shortages.

Shortageflation has a special importance in this context. It is not merely a sum of the two types of inflationary processes, but a third, entirely new quality, which has a highly adverse impact on the process of social reproduction and hinders further progress in the implementation of institutional and

structural changes. There is solid evidence to corroborate the statement that the shortageinflation syndrome is the most painful consequence and also, the main threat to the process of economic and political reforms. Among other reasons, this view is based on the fact that market mechanisms are exceedingly hard to introduce under such conditions.<sup>1</sup> Thus, although the outcome of the plan versus market dilemma in favour of the latter is obvious, one should not yield to naive neo-liberal theories, typical of the laissez-faire era. Introducing a market-type regulation into the economy is a task for a whole generation. There is no doubt that many mistakes entailing grave consequences will be committed in the process, owing to, among other things, reasons mentioned earlier.

Interestingly, these mistakes are repeated in a similar sequence and ways by one country after another. This is demonstrated, among other things, in the approach to the establishment of the capital market in Hungary, then in Poland, by the experiences with the operation of employee self-government confronted with the attempted expansion of market mechanisms (Yugoslavia, then Poland) or in debates on the sources, essence and ways to overcome the inflationary overhang. In the latter case, Soviet debates of late 1989 are very much like earlier Polish deliberations. We find that economies and societies behave like people, especially the young and prefer to learn by their own trial and error!

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<sup>1</sup> Without getting involved in the appraisal of particular systems regulating national economies, Janos Kornai is right to emphasize that the relationship between market-type regulation and state ownership is weak (Kornai 1989). Hence, it is difficult to expect market-type behaviour on the part of economic organisations without first introducing appropriate changes in ownership.

#### 4. Second Japan or Second Argentina?

Economic crisis brings necessary adaptive action to the daily agenda. First comes economic stabilisation, which in conjunction with the necessary measures in the systemic, structural and political planes, should assure relatively stable growth in the longer term. Comes the question about the nature of stabilising and adaptive action, about the instruments of economic policy to be used in its course and lastly - about the possible economic (and financial), social and political consequences.

Japan in the title is obviously an epitome. A second Argentina is much less of an epitome and I shall revert to that later. After all, looking maybe not for a standard to be copied, but for some point of reference for the visions of Poland's economic growth is quite natural. It is equally natural to look for intellectual inspiration for economic reasoning and for the formulation of scientific postulates with regard to macroeconomic policy, especially those concerning stabilisation and the ways of speeding up adjustment processes.

Hence, asking: "Second Japan or second Argentina" has a definite methodological sense. What to follow, imitate and what to avoid in systemic (institutional) solutions, what solutions and how to try to adapt to our conditions, what measures from the known arsenal of stabilisation and adjustment policy could be helpful in a socialist economy in a general crisis and suffering from shortageflation? Then - turning our eyes to the development of an already stabilised economy - similar questions should be asked about the growth policy. Many of these questions however, have to be asked still today. And it is in this context that we should decide, whether more is to be drawn from the experiences of the most advanced economies, like Japan, for which even the mighty United States have fear and an

inferiority complex <sup>1</sup>, or from countries whose economies and structures are more like our own.

The second reason to ask the question about a second Japan or Argentina is connected with the declarations of some politicians, who claim to hold the advanced Western economies as their models <sup>2</sup>, suggesting thereby their naive faith that such models (and their development levels) can be within reach in a not too distant future, provided their systemic and political solutions are implemented. One may unfortunately have some very grave doubts with this respect, though there are other views on the subject which sound like fairy tales. <sup>3</sup> These however, can be hardly seen as scientific.

The fundamental problem of a reformed economy, which is no longer centrally planned but not yet market-regulated, is that

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<sup>1</sup> Asked about what they consider a greater threat for the USA - Soviet military power or Japan's economic might - 32% of Americans chose the first answer and 52% - the second. Vid. Newsweek 1989.10.09.

<sup>2</sup> As an example, we might refer here to a statement by one of the ministers of the Polish government, who treats Sweden as a point of reference and consequently believes we should follow its experiences. One should nonetheless remember, that Sweden is more than a definite system and policy but also, most of all, a very high GNP level (15.5 thousand US \$ per capita in 1988) and a modern economic structure. Even if we made the absurd assumption that Sweden should now go into secular stagnation and Poland - into an era of another economic miracle with a constant annual GNP growth rate of 10% per capita, we would still need 25 (!) years to have equal economic development levels. However, not only scientists should not make absurd assumptions but also, or maybe especially - politicians.

<sup>3</sup> During a debate entitled We are sentenced to optimism M. Krassowski asked: "Let's assume that the market is already there. In ten years from now, will we be closer to West Germany or Peru?" J. Korwin-Mikke replied: "West Germany will be very easy to leave behind". Vid. Odrodzenie 1989, No 40, p.6.



it is exceedingly difficult to initiate positive adaptive processes precisely because of the lack of market-type regulation. One actually faces a series of negative adjustments, which fuels shortageflation mentioned earlier, bearing adversely on the process of the market-oriented economic reform. For example, it is by no mere hazard that we failed to attain a positive, real interest rate, although interest rates have been raised many times in the recent years. This simply cannot be done under the conditions of rising inflation and acute shortages (Kołodko 1989c). We can take another example, that of the common fallacy claiming that it is the insufficient liberalization of prices that is the main cause of persisting shortages. Actually, this problem is much more complex, because with shortageflation and the lack of an adequately developed financial and banking sector, compounded by the closed character of the national economy, liberalizing prices without taking other necessary measures, which sometimes require many years to implement, will only produce more acute shortages at ever higher cost, price and income levels. We must emphasize here, contradicting naive liberal theories, that it is the companies that are not interested or willing to raise prices to the ceilings set by the demand, because it is easier to operate in a market with excess demand. A. Topiński is right to stress that "...there is no evidence to confirm the relationship between the acuteness of shortages and the intensity of administrative price controls" (Topiński, 1989, p.31)<sup>1</sup>.

These comments were intended only to additionally corroborate the thesis that if a socialist economy in a deep crisis is set entirely free, to operate only by the market

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<sup>1</sup> For more on experiences with price controls see, among others: J.K.Galbraith (1952) and H.Rockoff (1984).

rules, many negative adjustment processes may be initiated and this may lead to the intensification of crisis phenomena, rather than to their elimination. Parallel to that, we will have previously unknown negative phenomena and processes, such as unemployment. Hence, more analogies fitting especially the Polish economy of the late eighties are to be found in the not so distant - in this aspect - Latin American and some other relatively less advanced countries.

These analogies have been observed by a Swedish journalist, who wrote: "Many freshly baptised "advocates of the free market economy" in the ranks of the opposition put too much faith in the trouble-free relationship between the market and democracy, usually derived from superficial observations of advanced Western societies, rather than from comparisons of Polish reality with Chile or Turkey, which would have been more appropriate."<sup>1</sup> Unfortunately, one must basically agree with this view. Indeed, Poland's economic situation as well as some social and political aspects can be better likened to those of the earlier mentioned and other less advanced countries, rather than to the advanced ones. This has very definite consequences for economic thought and policy. It is therefore worthwhile to have a look at what has been going on in countries resembling Poland, for we should know how to draw the right conclusions from these historical experiences.

The Chilean economy embarked on its stabilization effort under martial law, imposed after the overthrow of Allende's democratically elected government in the autumn of 1973. Thus, adjustment processes took place when democratic institutions were suspended or even ran contrary to such institutions. After nearly a decade of such efforts, inflation was brought down to the psychological barrier of 10%. However, this was paid for

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<sup>1</sup> Vid. A.Ringer, Dagens Nyheter of 6th July 1989 (quotation after Tygodniowy Biuletyn Specjalny PAP 1989, No 3107 (1989.07.12) p.7.

with a very strong differentiation is the population's living standards, which actually drove an important part of the society into poverty. Among other things, it was also connected with huge unemployment, which attained 21% in 1982. A very deep recession was another cost paid for a neo-liberal adjustment policy, based on monetarist ideas. Industrial output in 1982 fell by as much as 25% in comparison with the 1973 level, there was a dramatic decline in domestic savings (and consequently - investment) and a rapid rise in foreign debt service (Ching-yuan Lin 1987). Only after these dramatic stabilisation and adjustment processes did the Chilean economy enter the growth stage, which wasn't trouble-free either. Hence, Chile's "economic miracle" is another mystification, because it was paid for with nine years of huge costs and deprivations (which would have probably been unacceptable to the society if it weren't for the dictatorship).

Chilean stabilization had three stages. The first (September 1973 - summer 1976) consisted mostly in fiscal and monetary restrictions imposed in order to stabilise the economy.<sup>1</sup> The second, lasting from June 1976 to June 1979 featured attempts to use the exchange rate as a means of stabilising inflation (Edwards 1984)(see also footnote 18). Lastly, the third stage between June 1979 and June 1982 was a period of successive attempts at stabilisation, during which efforts were made to follow a passive monetary policy combined with a constant exchange rate of the peso to the US \$. It is worth noting here, that it is then that the notion of hyperstagflation was formed (Ramos 1980) as the most accurate description for Chile's situation in that period.

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<sup>1</sup> Studying the economic program of the Polish government (Program 1989) one may easily observe that also in this case, these instruments of stabilisation policy are to play a major role.

Argentina's experiences with stabilisation and adjustment measures should inspire even more caution. Efforts made by President Carlos Menem immediately after he took power in summer 1989<sup>1</sup> would have succeeded, provided there was the foreign support necessary to stabilise currency. This time, the early effects of stabilisation measures were more promising than ever before. However, the stabilisation effort failed again in late 1989, when - after a deep devaluation - the monthly rate of inflation has soared back to over 50%.

The history of Argentina's stabilisation measures could be divided into many chapters and sub-chapters. One can point to two of them in the seventies. The first, covering the period between March 1976 and December 1978, involved successive attempts at various liberalization programs<sup>2</sup>, designed as panacea to the crisis and hyperinflation. In the second phase (January 1978 - March 1981) attempts were made to check inflation with the exchange rate policy. However, these efforts failed. Inflation was stabilised only temporarily and it was hyperinflation, at that (Calvo 1983, Kolodko 1987). In 1982, that is six years after these liberalization attempts, the GDP in real terms was 1.2% lower than in 1985, while industrial output crashed over that period by as much as 39%. What is more, foreign debt kept on rising. As of now, it stands at over

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1 I see a certain analogy in this case too. In Poland like in Argentina, the government must turn away from election-time populist slogans to difficult, pragmatic stabilising measures.

2 Interestingly, politicians often assume that this time it will be the decisive attempt. It is usually otherwise. The spectacular case of Bolivian stabilisation of the second half of the seventies is now frequently invoked in Poland (without remembering its enormous cost, among other things, the doubling of the unemployment rate from 10% to 20%). It is worth adding, that the Bolivian case involved six successive stabilisation and adjustment programs over three years, implemented by seven successive ministers of finance and seven central bank governors.

60 billion US \$ and the per capita figure is much higher than in Poland. Argentina's export industries however, are better developed than Poland's.

Further attempts at stabilisation failed. The so-called "Austral Plan", consisting in monetary reform launched early in the second half of the last decade failed too (Machinea - Fanelli 1989). Argentina's economy was plunged in hyperinflation and economic stagnation.

If however, we look at measures taken in the framework of stabilization initiated in the second half of 1989, it must be emphasized that Argentina has a developed financial sector (including banking) and a capital market, both operating in a market environment. That is not the case of reformed socialist economies, which is why these important differences must be kept in mind while drawing conclusions from Latin American experiences. These remarks notwithstanding, one should remember that Poland's situation resembles Argentina's<sup>1</sup> more closely than that of any of the advanced capitalist economies. One must realise that Argentina has a per capita GNP of 2,390 US \$, while Poland, according to the same estimates (World Development Report 1989, World Bank, p.165) - only US \$ 1,930. The main problem however, is that a "second Argentina", would hardly be an extremely bad solution of Poland's case. For one cannot preclude a further deterioration of the economic situation and not only in Poland, but also in other socialist countries.

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<sup>1</sup> Some authors go very far in these analogies. T.H.Naylor, professor of economics at the Duke University, wrote: "Poland's fundamental problem is neither political nor economic, but psychological. So-called Polish nationalism is, in fact, a euphemism for Polish narcissism. As a formula for political instability, the combination of Polish fascism, Roman Catholicism and Soviet Communism knows no equal. There is no way socialism could ever work in such an egocentric society as Poland and it never will. Poland is the European equivalent of Argentina, the political and economic basket case of Latin America. Vid. *New York Times* 1989.07.06.

## 5. Imagination and Responsibility

Nowadays, economic sciences and policy need imagination more than ever before. Hence, the further we need to look into the future, the harder it is to have a clear vision. There are many more alternative scenarios for economic, social and political developments, both domestic and with regard to the broader framework of foreign economic relations and to the evolution of socialist economy as a whole. It is against this background that we must formulate the view that there is an urgent need for science to elaborate more extensive warning forecasts and for policy to use them. These are forecasts which are sure not to come true, but which point to the need to combat trends which are bound to appear unless countered (Karpinski 1989, p.25). I believe such forecasts are indispensable given the vast expanse of the area of uncertainty, which becomes even broader given the present destabilisation of socialist economy and contemplated adjustment measures. For long-term adjustment processes can be interspersed with serious perturbations resulting from attempts to introduce market mechanisms under the prevailing conditions. Given this background, one cannot fail to make several remarks on imagination and responsibility with regard to both science and policy.

It has to be admitted that as mentioned earlier, science often fails to provide satisfactory answers to challenges it is faced with. In such cases, it is only natural that people draw on solutions tested elsewhere. This is a partial explanation of the yearning to draw on the achievements of the most advanced countries. This yearning is justified to some extent, like it is justified to observe the experiences of countries which have different economic systems, but similar development levels.

This is why comparative studies, in at least three planes, are particularly important at the present stage. First, in comparison to the experiences of other reformed socialist

economies (especially China, Hungary, Vietnam and the Soviet Union). Second, less advanced countries, especially those with a high share of the public sector on the one hand and suffering from serious social and economic destabilisation on the other, are particularly interesting. Third and last, it is necessary to follow the experiences of advanced market economies, especially those with a high share of the public sector. One should however avoid inconsiderate adaptations of conclusions from these experiences to the conditions of a destabilised socialist economy, struggling with the burden of its crisis. This remark applies also the experiences of other socialist countries, because we always have to take account of certain specificities, and it is precisely here that a measure of imagination is always helpful.

The tales of second Japans, West Germanys or Swedens do little harm, although we should not ignore them altogether. It can be much more harmful to transplant economic policy methods and implement systemic changes which proved themselves in different environments and conditions, without in-depth studies and appropriate adaptation to different conditions.

Science like policy calls for much imagination, which should facilitate the screening of various proclaimed theses and contemplated measures. If we follow the debates on the successive stabilisation programs, starting with the *Government Program for Curbing Inflation in the Years 1983-1985* (Program 1983) to the *Economic Program* (Program 1989) of late 1989, it becomes obvious that imagination is in short supply. This is hardly a specific feature of Polish economy and policy, because these remarks may be just as well applied to the experiences of Latin American countries, mentioned earlier. I think there must be some relationship to economic destabilisation and the pressure of time, associated with it. This leads to only superficially radical, hastily taken measures, made without due consideration precisely because of this lack of time.

This lack of imagination is frequently related to strong pressures exerted on economic policy. We can take the example of the indexation of salaries in Poland in 1989 or the so-called "marketization" of the agriculture. It wasn't all that difficult to anticipate the hyperinflationary threat stemming therefrom (Kołodko 1989b) and yet it was ignored because of the servile attitude of a part of the scientific society and the short-sighted docility of economic policy.<sup>1</sup> The case of indexation was only a minor incident connected to the issue of economic imagination, but also related to the problem of economic, political and moral responsibility.

The lack of imagination can entail much graver consequences than in the case of indexation. We can take the example of the lunatic policies of foreign indebtedness followed by many countries, including Poland, in the seventies. Today, it is hard to conceive how to escape the debt trap. But that already belongs to the past. What should imagination tell us about the future? What phenomena and processes cannot be precluded and, basing on scientific knowledge of their mechanisms, what indispensable measures should be taken in advance with regard to three earlier-mentioned planes: the economic system, structure and policy?

Now, while all reformed socialist economies have entered the

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<sup>1</sup> Strictly speaking, indexation was also used as an instrument in the political game and it is therefore not always possible to say when imagination failed and when action was taken with full awareness of the possible effects. Eventually, even the most ardent advocates of indexation admitted that the *novelization of the Law* (Law on Indexation amended in mid-October 1989 - GWK) was the *rectification of an obvious mistake*. (Vid. *Wyobraznia zawodzi* (Imagination Fails), an interview with Andrzej Topiński, *Zycie Gospodarcze* 1989, No 42, p.5). They also stated that ...there are reasons for us not to have a clear conscience on this issue. (Vid. statement by R. Bugaj, quotation after: *OKP o bledach indeksacji*, *Trybuna Ludu* 1989. 10. 13).



long stage of shortageflation, Poland (and in the future also other countries, if learning from others' mistakes doesn't give better effects than thus far) is faced with an extraordinary state of crisis, which can be called hypershortageflation, as an analogy to the earlier-mentioned Chilean hyperstagflation.

Given economic trends observed in Poland in the end of 1989 and contemplated measures intended to have a stabilising effect in the coming years, there is no doubt that we are threatened with a combination of exceedingly adverse processes: a rise in overall price levels reaching a scale typical of hyperinflation, increasing shortages, an even deeper economic recession accompanied by unemployment and growing foreign debt. This would be an unprecedented situation, because not even the most spectacular South American crises had shortages on top of all other symptoms.

Different criteria can be used to appraise the situation in the end of the eighties, but it would be difficult to view it as more favourable than in the beginning of the decade. Social output is still lower than before the 1979-1982 recession. The net distributed national income in 1989 reached only 95% of the 1978 figure and foreign debt had more than doubled since then. Consumption per capita has not yet recovered to the level of the explosive year 1980, while investment in real terms is lower by about one third than a decade ago. Inflation is many times higher (12.5% was the average annual rate in the years 1979-1981), while the shortages of consumer goods are by no means less acute. Lastly, the condition of the government sector (state budget) is clearly worse than in the beginning of the last decade. Given the situation, it is obvious that the populations' and companies' inflationary expectations are also much higher.

Remarks made by D.M.Nuti during the previous recession of the Polish economy are particularly meaningful in view of the above comparisons: *"If Poland were a capitalist country in a*

similar crisis, painful but fairly automatic processes and policy response would be set in motion. There would be hyperinflation, currency devaluation, drastic public expenditure cuts and deflationary taxation measures, tight money, high interest rates, disinvestment, bankruptcies and plant closures, and a couple of million unemployed. Some external creditors would get very little, or nothing at all, following the financial collapse of their debtors; some of the remaining debt would be offset by the sale to foreigners of financial assets (shares, bonds), land, building and plant. Fresh external finance would be available to the more credible borrowers. Unemployment would keep the unions in check, restraining real wages and ensuring labour discipline. The drop in real wage trends and industrial streamlining would eventually promote exports and encourage new investment, attracting foreign capital; in ten years or so the economy would be getting out of the crisis." (Nut1 1982, p.47; bold print by GWK). This scenario hasn't yet come true for obvious reasons. One should however not forget about the ways and impact of some stabilising and adaptive mechanisms in a different systemic environment. Imagination should not fail economists and politicians precisely in such cases.

This is why extraordinary caution should be advised with regard to realignment on market and monetary solutions, which may be right as to the directions, but may bring, as has often been the case in economic and social processes, quite different effects than promised. Given these remarks, one cannot fail to ask whether the promise of 1 percent of monthly inflation by mid-1990 stems from the lack of imagination or of responsibility? Asking this question I assume that no price and wage freeze shall be imposed to achieve these figures, since that would stand in clear contradiction to the much publicised policy of far-reaching liberalization and deregulation.

Reviewing scientific and political responsibility against

this background, it is difficult to give an unequivocal answer. Economic policies promoted and implemented in various periods and countries are after all based on scientific views. And the latter differ widely, sometimes to the point of being contradictory. Thus, policy is not in an easy position either. All is well when a sound policy is based on wise scientific views. If it is the other way around, it is a disaster. There can also be a situation where there are no wise scientific views for a sound policy to draw on and lastly, when there are enough sound scientific views and policy is nonetheless fallacious.

Looking at a somewhat different angle, it is worthwhile to note the lag between scientific postulates and political decisions. Michał Kalecki, drawing on his experience as adviser, and not only to Polish governments, used to say that it is not true that politicians don't take economists' advice; they do but that applies to the economists of the past generation. One could now add that taking the advice of the next coming generation may be equally inappropriate insofar as their advice may apply their visions of the future, rather than to present-day reality.

J. Pajestka points to another aspect of policy lagging behind science. Writing about the so-called "paradigm of progress", which has a strong influence on economic sciences, he observed that: "...policy tends to lag behind scientific cognition, but this is probably also due to human behaviour, which does not change easily. Scientific argumentation is not sufficient in this light to change human behaviour. In any case, time passing between comprehension and action seems to be rather long (Pajestka 1989, p. 37-38). I will only add that this lag tends to grow in periods of economic and political destabilisation, against both our wishes and expectations.

Given the determinants and relationships discussed above, one may well fear that overcoming the syndrome of the general crisis of socialist economy will be a lengthy and complex

process. Scientific cognition of the subject is rather poor, though there is no doubt that much progress has been achieved in the recent years. Interestingly enough, it is the countries in deepest crisis and with most destabilised economies that seem to have most achievements in this area. It is quite comprehensible, the need being the mother of invention.

The road to stabilisation will probably lead through further destabilisation. In any case, such a scenario cannot be precluded. As professor Czeslaw Bobrowski once said: "questions and problems facing us multiply in geometrical progression, while our knowledge about the ways to overcome them - in arithmetical progression". Hence, the most threatening disequilibrium is becoming ever more serious: that between the questions and the answers. Only a constant scientific progress can contribute to balance this disequilibrium. The lack of time cannot be an explanation for the lack of professionalism which can be sometimes observed, for spreading demagogy and the servility of science to the authorities, whatever they may be. These are threats which cannot be ignored.

One could say that from a strictly intellectual, scientific point of view, our times are very attractive: it's been a long time since we've had it so interesting! However, in the aspect of social and economic reality, and policy, which must aspire to change things for the better, our times are harder than ever!

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