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### **2025: Two Histories of Economic Growth**

**Grzegorz W. Kolodko**

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Professor at the Warsaw School of Economics, Director of **TIGER** – Transformation, Integration and Globalization Economic Research at the Leon Koźmiński Academy of Entrepreneurship and Management (WSPiZ), ul. Jagiellońska 59, 03-301 Warsaw, and John C. Evans Scholar in Polish and European Studies, Department of Political Science, University of Rochester. E-mail: [kolodko@tiger.edu.pl](mailto:kolodko@tiger.edu.pl); homepage: <http://www.tiger.edu.pl>

## **2025: Two Histories of Economic Growth**

### **Summary**

It is the year 2025. Integration with the world economy in an increasingly competitive environment has advanced by another 25 years. For about two decades Poland has been a member of the European Union, which now generates greater output than the U.S. Does Poland's contribution to global GDP exceed 1 percent? Does our share in world trade approach 2 percent? Has per capita GDP on PPP basis risen above 30,000 U.S. dollars – the level that the European Union and the U.S. attained, on the average, a quarter of a century ago? All this is possible, as long as we keep doubling our national income every 12 years over the first quarter of the 21st century.

Or could it be that Poland's share in world output A.D. 2025 stands at a paltry 0.7–0.8 percent and is not much greater than a generation ago? That the volume of our foreign trade remains similarly disappointing? That economic growth oscillating at about 3 percent a year has allowed PPP-adjusted GDP merely to double and reach some 15,000 dollars – a level which Slovenia exceeded already in 2001?

Either scenario is possible. Which one will become a reality depends on the development strategy, which must take into account the opportunities and threats faced by Poland in the current phase of globalization, and on the effectiveness of the correlated policy of structural and institutional change, i.e. the core of postsocialist transformation. The implementation of a socio-economic development strategy founded on four pillars:

- rapid growth,
- equitable distribution,
- profitable integration,
- efficient state

may open up the prospect that a scenario will materialize in which Poland shortens the distance to the most advanced economies.

## 1. Introduction

It is the year 2025. Integration with the world economy in an increasingly competitive environment has advanced by another 25 years. For two decades Poland has been a member of the European Union, which now generates greater output than the U.S. How far have we got, then? Does Poland's contribution to global GDP exceed 1 percent? Does our share in world trade approach 2 percent? Has per capita GDP, calculated on purchasing power parity (PPP) basis, risen above 30,000 U.S. dollars – the level that the European Union and the U.S. attained, on the average, a quarter of a century ago? All this is indeed possible, as long as we keep doubling our national income every 12.5 years over the first quarter of the 21st century. This requires an average annual growth of 5.7 percent.

Or could it be that Poland's share in world output A.D. 2025 stands at a paltry 0.7–0.8 percent and is not much greater than a generation ago? That the volume of our foreign trade remains similarly disappointing? That economic growth crawling along at about 3 percent a year for the time span of a whole generation has allowed PPP-adjusted GDP merely to double and reach some 15,000 dollars – a level which Slovenia exceeded already in 2001?<sup>1</sup>

Both scenarios are possible. Of course, there are countless other possible variants in between. One cannot even rule out *a priori* a situation when long-term growth rate is still lower than in the negative variant outlined above. Which growth path becomes a reality will depend on the development strategy, which must take into account the opportunities and threats faced by Poland in the current phase of globalization, and on the effectiveness of the correlated policy of structural and institutional change.

**Further progress and catching up requires a long-term strategy of socio-economic development, which should be founded on four main pillars:**

- **rapid growth**
- **equitable distribution**
- **profitable integration**
- **efficient state.**

Such an approach increases the likelihood that a scenario will materialize in which Poland gradually shortens the distance to the leaders of the world economy. It follows that the formulation of ambitious yet feasible growth scenarios goes beyond a mere intellectual exercise. A scenario needs to be appropriately staged. To this end, it is necessary to identify the growth factors and prospects and, most important of all, indicate the available socio-economic policy options and instruments which, hopefully, will allow the most favorable scenario to be enacted.

## 2. The Strategy for Poland: 21st Century

Poland enters the 21st century in rather different circumstances than it was imagined until quite recently by some economists, who carelessly predicted much faster growth occurring much earlier. In spite of many serious warnings and proposals for an alternative

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<sup>1</sup> We adopt here the simplifying assumption that real economic growth coincides with growth measured on the basis of purchasing power parity. In the actual growth process, this is not the case. In countries involved in a lengthy process of market transformation, including Poland, it should be expected that growth rates measured at fixed prices and in PPP-adjusted U.S. dollars will follow different paths. As Poland approaches membership in the European Union and, subsequently, participation in the euro zone (Nutti 2001), we will be faced first with the depreciation of the clearly overvalued zloty, whose exchange rate is artificially propped up by the central bank's irrational interest-rate policy, and then with its moderate appreciation. The latter will gradually narrow down the present gap between per capita GDP calculated at market rates (ca. 4,100 dollars in 2000) and on PPP basis (ca. 7,600 dollars; see PlanEcon 2000). The introduction of the euro will eliminate this dichotomy vis-à-vis the remaining EU members, but the problem will continue to exist in relation to other countries.

course of action (Łaski 1990, Nuti 1990, Kolodko 1992), mistaken conceptions and unrealistic forecasts gained the upper hand (Gomułka 1990, IMF 1991). Disappointment resulting from frustrated over-optimistic hopes has sadly engulfed all postsocialist transition economies (Mundell 1995, Lavigne 1999, Kornai 2000), but the situation of Poland in this context is special.

Even the greatest skeptics did not expect that the economic growth dynamics at the beginning of the current decade could be so wretched. The very word “dynamics” used in this context acquires ironic overtones, as symptoms of stagnation are becoming all too evident. Thus GDP growth rate has dropped from 7.5 percent in spring 1997 to just above 2 percent in spring 2001. It is a threshold below which the social impact of this phenomenon starts to be felt. Bearing in mind the large-scale redistribution processes that accompany privatization and an anti-inflation policy, many social and occupational groups experience a drop in the absolute level of real income and consumption.

One aspect of the situation at the starting point (or, rather, on its eve, taking into account the current phase of the political cycle) is that **our growth rate is very low – indeed anemic**. Faced with a drastic deceleration of growth tendencies and, worse still, a breakdown of the mechanisms of economic growth, many independent research centers adjust downwards their earlier forecasts. There is almost no one left who would put medium-term growth rate at significantly more than 4 percent (Bank Handlowy 2001, EBRD 2001, PlanEcon 2001).<sup>2</sup> Even more cautious forecasts are soon likely to emerge.

Merely four years ago, independent analysts predicted that GDP in Poland would grow in 2001–5 at a rate of 5–6 percent annually; now they give us just 3–4 percent and that is rather with a negative outlook. The reason is they assume the policy of the past few years will be continued. Yet they are quite wrong with this regard. The general line of market reform and integration with global economy will certainly be sustained, but surely these goals can be pursued far more wisely. All that needs to be done is to make the necessary adjustments to the available intervention instruments. If we succeed, then in the successive quarters of 2002 we will be climbing the consecutive rungs of the GDP-growth ladder: 3, 4, 5, 6 percent,<sup>3</sup> and, hopefully, maintain the achieved level for years.

On the other hand, Poland still opens the ranking list of postsocialist countries with the highest growth rates during the transformation stage. Taking 1989 as a reference point, GDP in 2000 stood at as much as 127 percent, whereas in 22 other countries of Central and Eastern Europe and post-Soviet republics of Asia, it was still below the level of 12 years ago: from a disastrous minimum of ca. 30 percent in Moldova and 35 percent in Georgia to 95 percent in Uzbekistan and 96 percent in the Czech Republic (EBRD 2001). **Besides Poland, only four countries (in the order of rank: Slovenia, Hungary, Albania and Slovakia) have increased their output quantitatively above the closing level from the previous epoch.**

It should be always borne in mind, however, that the recent years in Poland fall into three distinct periods (and so they will go down in economic history). We thus moved from “shock without therapy” in 1990–3, through the *Strategy for Poland* in 1994–7, to “senseless

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<sup>2</sup> Both Washington-based PlanEcon and Bank Handlowy predicted in their periodic reports from the end of May a 3.5-percent GDP growth in 2001. According to Bank Handlowy, growth rate in the first half of the year will reach 2.7 percent at best and the attainment of an annual growth rate of 3.5 percent is contingent on appropriate coordination between budget and monetary policy, which, incidentally, is hardly likely to be the case. Therefore, the economy may be facing recession (Bank Handlowy 2001, p. 1). PlanEcon, in turn, observes that the situation of the Polish economy is not bad, compared to some developed economies of the euro zone, but its growth remains well below the potentially sustainable level, estimated at between ca. 5 and 5.5 percent (see PlanEcon 2001, p. 16). Furthermore (p. 19), it is noted that the economy is clearly stagnant, although the threat of recession is very distant.

<sup>3</sup> Reversing the trend which set in during the last quarter of 1999 and caused the GDP dynamics to drop successively from 6.2 percent to 6.0, 5.2, 3.3 and 2.4 percent in 2000 and an estimated 2.7 percent and only about 1 percent in the first and second quarters of 2001, respectively.

cooling down” in 1998–2001. During the first two years of the transformation, GDP dropped, in the aggregate, by 18 percent, then rose by 28 percent in 1994–7, while its further growth in the last three years slid to just 13.5 percent. The current year is not going to improve the picture of growth dynamics, either.

The present level of the GDP indicator, i.e. 127 percent of the pre-transformation level of 12 years ago, is the net effect of the dynamic leap forward attained by the collective effort of the Poles in 1994–7 and the aggregate drop in national income by 1 percentage point in the remaining seven years (1990–3 and 1998–2000). This means that the net result of those seven very lean years was negative. In other words, had it not been for the “Strategy for Poland” period, output would still be lower than in 1989.

But there are **grounds for optimism**, too. The defeatist forecasts and increasing pessimism – in particular, among many entrepreneurs and investors, which may have an adverse impact on capital accumulation and economic growth – are based on wrong assumptions. It is surmised that few things will change for the better in the coming years, because the current general line of economic policy will be continued. This assumption must be rejected, because it is downright false. There are no rational grounds to believe that the economic policy will persist in old errors in the near and more distant future. Although, in comparison with the situation after 1993, the present moment seems less favorable as a starting point to resume growth acceleration, such opportunities do present themselves. If it was possible to overcome the transitional recession and double the rate of GDP growth from the average of 3.2 percent in 1992–3 to 6.4 percent in 1994–7, then it may also be possible to return to this path after 2001 and increase growth rate from the current medium-term 3–3.5 percent to 6–7 percent in the coming years.

There are other reasons for cautious optimism, too. **An adequate economic policy can only be based on an adequate economic theory** and an outline of the latter *is* available. Unfortunately, the economic policy of the early and late the 1990s looked up to a wrong kind of model. Alternative courses of action are always available, for even within one and the same framework, there exist various, more or less felicitous, ways to combine the available instruments of financial and income policy, industrial and trade policy, or structural and institutional policy (Kolodko and Nuti 1997).

Moreover, various options are available with respect to the methods of stimulating economic growth and the formation of capital to finance it (Tanzi and Zee 1996, Kolodko 2000b), as well as various approaches to integration with the worldwide economic system, emerging at the current phase of the permanent globalization process (IMF 2000, Frankel 2001). Finally, there exist various possibilities of coordinating particular segments of economic policy proper, in all its complexity, with social policy, which entails the possibility of organizing distribution relations differently (Sadowski 2000).

Poland has been ill served by the **naïve neo-liberal policy**, which is becoming increasingly compromised in public view. Under the circumstances, it becomes feasible to apply some more creative economic conceptions, which at the same time should be more palatable to society. **The new economic policy must be based on modern institutional economics, which provides the foundations of a development strategy that leads to the emergence of a true social market economy** (North 1997). There is no question that we have attained significant progress in this field over the twelve years of transformation, but there is still a lot that remains to be done. Market-economy institutions, that is, new rules applying to the state, economic entities, citizens and foreign partners, as well as institutions that foster compliance with these rules, can only bring about the desired effects in conjunction with a sound policy. In other words, **there are no good institutions without a good policy, and vice versa**.

The third reason for optimism, apart from the fact that we have got useful political experience and deepened our economic knowledge, consists in the favorable combination of economic circumstances marking the early years of the 21<sup>st</sup> century. Our long-term development strategy should turn to advantage several of these circumstances.

The transformation itself and the introduction of market mechanism of capital accumulation and allocation are essential factors in the long-term growth of microeconomic efficiency, on condition, however, that the quality of enterprise management also improves. Yet we still have a long way to go in this area (Koźmiński 1993). In the advanced stages of system transformation, increasing GDP dynamics will depend on higher microeconomic efficiency, which calls for a major breakthrough in management quality.

These effects combine with the **benefits of the current phase of globalization**. The progress of liberalization, with the subsequent integration of hitherto separate markets into a single worldwide market of capital and goods, creates additional opportunities for the Polish economy which outweigh the increased risk (Kolodko 2001a). Wise involvement in the international (or, rather, global) labor division may bring benefits in excess of the costs (which, incidentally, are inevitable). The actual surplus of benefits over costs will crucially depend on Poland's national development policy (PAN 2000, RCSS 2000).

Furthermore, by a lucky historical coincidence, Poland enjoys now probably the most favorable geopolitical situation in the contemporary world. At the current stage of the global economic evolution, to occupy a position between the European Union, of which Poland is almost a part already, and the Commonwealth of Independent States, where the Russian economy is gaining momentum and Ukraine enters the growth path (for us, too, these are "emerging markets" with 200m consumers), is an important factor to be taken into account in the national development strategy. More precisely, it is relevant to the external aspects of this strategy, oriented towards export-led, as opposed to import-fed output growth, the latter being largely fuelled by increasing foreign debt, as was particularly evident in 1998–2001. This strategy should also foster external investment, made possible by the increasing wealth of society and growing internal savings.

Finally, the quality of human capital, although somewhat affected by the ill-advised cooling down of the economy and the attendant reduction spending on education, science, culture and health, remains relatively high. Polish engineers and teachers, managers and financiers, professors and artists, students and pupils have considerable knowledge and skills. These resources should be widely utilized now that the fourth industrial revolution is in progress, accompanied by the Internet revolution and the expansion of information technologies (Kolodko 2001b).

All these factors provide not only grounds for rational optimism, but, first and foremost, the foundations for a concrete vision and a long-term development program – "The Strategy for Poland: 21<sup>st</sup> Century". It is based on four main pillars.

First, **rapid growth**. Through the accumulation of capital, especially domestic (with foreign investment playing only an auxiliary role), and the development of genuine enterprise, the economy may resume the 5–7 percent annual growth path. And not just for a couple of years but at least for the time span of an entire generation. Then, per capita GDP (on a PPP basis) may be even four times higher in 2025 than it is now, reaching levels enjoyed today by rich countries. By that time, however, per capita GDP in highly developed OECD countries will have reached 35,000–50,000 dollars. This means we are pursuing a moving target, and thus have to keep running fast.

Second, **equitable distribution**. It is necessary to increase outlays on education, because in the long run, it is both the fundamental development factor and the best remedy against poverty. On the rapid-growth path, we can bring down unemployment in a matter of 4

of 5 years to 7–9 percent, rather than have it climb to 20 percent. The vision of a 20-percent unemployment rate is based on passive extrapolation of the trends which became established after 1997, but their continuation is by no means inevitable. The redistribution of national income through the fiscal system and budget should also change, so as to attain a reasonable balance between the requirements of efficiency and the imperative of social justice.

Third, **beneficial integration**. The objective is not only to negotiate the best possible terms of accession to the European Union, but also conduct an industrial and trade policy that will create appropriate conditions for Polish enterprises to expand and compete on the global market. Without firm involvement of the state it will not be possible to build sufficiently robust structures to compete in modern world economy. This will not be possible, either, without grass-root initiative and enterprise, based on the domination of private property. And, most important of all, the struggle for beneficial integration will be doomed to failure without enlightened collaboration of the government and the private sector within the framework of modern institutional solutions.

Fourth, **efficient state**. This may sound strange to some, but we have once again enter a phase in which the functioning of the economy and the quality of living largely depend on the state: its regulations, institutions, intervention and support (Hausner 1999). The state should be citizen-friendly, but at the same time it should build on the strength of its democratic institutions. There is no doubt that the lost impetus towards the end of the 1990s was not only a consequence of the harmful idea of “cooling down”. Mounting corruption and bureaucratic barriers in the way to economic expansion also result from the weakening of the state, the erosion of some of its mechanisms, and premature or poorly prepared withdrawal from some forms of activity which cannot be taken over, at the current phase of transformation and development, by either the private sector, or non-governmental, non-profit organizations, which do not evolve in a sufficiently rapid and diversified manner.

### 3. Rapid growth

The notion of rapid economic growth is far from unambiguous in theory and, especially, in practice. What may be considered as “rapid” growth by some, will by treated with greater skepticism by others. Output dynamics which is called “high” in some circumstances may not be seen as such in a different situation.

In theory, it can be assumed that **“rapid growth” means that output dynamics noticeably exceeds over a long time span the dynamics attained by other economies**, although even this evaluative assessment is not sharp enough. Thus growth in a given country will be “rapid”, if its rate exceeds over many years the average attained by the global economy as a whole. During such periods, the country gets ahead of others, or, if has been lagging behind for whatever reason, it catches up with better-developed countries (Lucas 1999).

Likewise, rapid growth – being a relative notion – also occurs in a situation when growth rate considerably exceeds for many years its past levels and the levels attained by other economies at a similar stage of development. In this sense, the 1990s were certainly a decade of rapid growth in the United States, although in comparison with the world at large, including its far less developed parts, its growth rate was not all that impressive.

In the practical aspect, “high” growth rate largely depends on the context in which the growth process unfolds. In economically more advanced countries, say, those in which per capita national income exceeds 20,000 dollars, constant output growth of 3 percent annually maintained over many years undoubtedly *is* “rapid”: very much so, bearing in mind that in just 25 years it would increase the income to 40,000 dollars. But in countries which are only now building up their wealth, struggling to overcome underdevelopment, or just trying to reduce

the distance to the leading economies, this would not be viewed as a high growth rate. In such economies, only an average growth rate of at least 5 percent annually may possibly justify the use of this term.

Of course, output growth – even rapid – is not everything. For while it makes possible the implementation of a selected **socio-economic growth strategy**, it should be perceived only as a specific instrument, and not as an objective in itself. Growth must be of appropriate quality, which manifests itself mainly in the concern for social and ecological equilibrium (PAN 2000, RCSS 2000). It is not enough if it is rapid: it should also be accompanied by equitable distribution relations and take into account ecological considerations, including the depletion of non-renewable resources on which production activities are based.

One should also bear in mind that the economic policy may in actual fact be guided by different objectives than those officially declared and that the strategy being followed may not be oriented towards common good, but rather towards particularistic interests of influential lobbies. Sometimes the recourse to redistribution mechanisms which ensure that, despite the lowered income (caused by slower growth), an appropriate level of benefits will accrue to specific addressees from among the political clientele of the decision makers is only possible at the price of slowing down growth. Unfortunately, this is largely the case in postsocialist transition economies, including Poland, especially in recent years. Thus despite the “cooling down” policy (or, to be precise, *owing* to this conscious and deliberate effort to slow down output growth), such redistribution mechanisms were applied to the (less steeply increasing) income which resulted in much faster growth of the income of certain domestic and foreign interest groups. This, of course, is not the type of “rapid growth” we should pursue.

If output growth is to foster healthy socio-economic growth, it is not enough if it is just based on the existing **human capital**: it must also facilitate the creation of this capital. Therefore, rapid growth requires in the long run not only the high accumulation and dynamic formation of domestic capital in the strict sense of the term, but also constant attention to the qualitative development of human capital. In the Polish situation, of particular importance is a significant increase of public spending on science and culture, including the wages, which should double in these sectors in 2001–5 and then grow at least as fast as GDP.

The economic growth rate may indeed sometimes be too high. Such a situation occurs when excessive growth dynamics upsets the balance of the economic and financial systems, which may lead, among other problems, to the emergence of bottlenecks in manufacturing and trade and increase the inflationary pressure, resulting in an uncontrollable redistribution of income. This is also the case when growth is achieved at the price of devastated environment, leading to a degradation, rather than improvement, of the living conditions. All such effects have an adverse impact on growth. In the long run, growth is not “rapid” in such circumstances, because after a temporary high, its dynamics drops or even plummets and the average growth rate over the entire period is lower than it would have been in a more sustained variant.

Such adverse circumstances did not occur in the final years of implementing the “Strategy for Poland”, when growth rate soared to nearly 7 percent in 1996–7. Financial equilibrium was steadily improving at that time, while the utilization of the existing industrial capacity, following its dramatic plunge in the early 1990s, was still far from complete. The subsequent **slowing down of growth rate and its current drop to a mere 2 percent were not caused by an “overheated economy”, but by the inability to maintain the previous level of economic activity.**

Most importantly, without rapid growth it is impossible to build prosperous future, and then all strategies aiming to improve the material standing of society are futile, because any attempts to improve the living standards lack economic foundation. In such circumstances,

society directs a large part of its thoughts and efforts to issues of redistribution and to haggling over the ways to divide the inadequate income, rather than to generating new value added. This pushes down the already inadequate growth rate even further. It is in such atmosphere that the **populist threat** is greatest, leading to various forms of action undertaken by poorer and passive social groups in order to increase their share in the too-slowly-growing national income. Such reactions are hardly surprising, although in most cases they do not merit support, either.

On the other hand, one must not overlook another major threat, consisting in the **greed of the richer strata**, which – rather than concentrate on business and on maximizing their contribution to further growth of output, thus securing their own well-being in harmony with the improved living standards of the other strata – exert political pressure to make arrangements that will further improve their situation at the expense of others. Calls for tax cuts provide a classic illustration of this kind of attitudes. It is only seemingly paradoxical that such pressures become stronger as the dynamics of the economy weakens. Of course such expectations would be more realistic in a stronger economy.

**It is not true that growth accelerates when taxes are lowered: rather, taxes are lowered when growth accelerates.** Such was precisely the sequence envisaged by the “Strategy for Poland”, which first concentrated on accelerating growth and broadening the tax base and only then provided for a substantial<sup>4</sup> reduction of the tax burden, so as to keep up the high growth rate using the fiscal policy to facilitate capital formation. The fact that this path was not consistently followed in the subsequent years, while tax cuts remained an empty slogan, should be first of all attributed to inept policy, and not to external shocks.<sup>5</sup>

Taking into account the broader context of still-incomplete postsocialist systemic transformation, as well as European integration and globalization, an accelerated growth strategy for the Polish economy should be built on four solid cornerstones.

First, what is needed is giving clear **priority to the formation of domestic capital**. It should be fostered, on the one hand, by an increased marginal propensity to save, which in turns requires faster growth of the real income of households than in recent years and the development of domestic financial institutions, and on the other, by strengthening the capital market. It is from this perspective that the continuation of the social-security reform (with some necessary adjustments) should be viewed, particularly in the context of the pension system.

Second, the **progressing financial stabilization needs to be fully consolidated into stability**, taking into account the necessity to strengthen the export orientation of the Polish economy. This task cannot be achieved in conjunction with accelerated growth, if the current monetary policy is continued. It is the weakest segment of the entire financial policy and needs to be thoroughly overhauled. The direction these reforms should take is defined by the necessity (and possibility, for this objective *is* possible to achieve) of reversing the currently dominant tendency. It is not interest rates (the price of capital) that should be adjusted, largely *ex post*, to the changing prices of goods and services (inflation), with exchange rates being merely a function of interest-rate manipulation (and the movements of speculation capital); the problem must be approached from an exchange-rate perspective, which – in view of the

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<sup>4</sup> Pursuant to the “Package 2000”, adopted by the government in 1996, the 6-percent import surcharge was totally eliminated, personal income tax rates were reduced and corporate income tax was cut, in several stages, by as much as a quarter.

<sup>5</sup> It should be remembered in this context that the depth of recession in Russia, Ukraine and other post-Soviet economies in 1994–7 was much greater than in the aftermath of the Russian financial crash in summer 1998. Besides, soon after the latter crisis, Russian – as well as Ukrainian – economy saw a radical increase of output growth rate, which, however, the Polish economic policy did not – and would not, mainly, it seems, for extra-economic reasons – capitalize on. In contrast, many other countries did, both among the richest and the less developed, the large (e.g., China and Germany) and the small (e.g. Finland and Sri Lanka).

ongoing relative price stabilization – will encourage (and enforce) a radical and lasting reduction of real interest rates (and hence also financial costs and the costs of public debt servicing).

Steps in this field must also lead to a substantial change in the cost/price relationships and bring about an abrupt increase in the profitability of export output, while decreasing the relative magnitude of those imports which limit the utilization of domestic productive potential. This will ensure that it is in Poland that consumption spending, production, employment and budget revenues (hence in particular, the possibility of increasing, in real terms, public spending, including investment in human capital) will be growing. The current financial policy, in contrast, tends to create jobs abroad, rather than at home. It is a consequence of this policy that unemployment is increasing in Poland and decreasing in those countries (especially of the European Union) with which Poland has run up a high trade deficit.

Third, Poland will be able to accelerate growth and keep it on a high level for a long time only when **labor is successively shifted from low-technology branches to more advanced industries and services where value added is relatively higher**. The immature, still nascent market mechanism will not guarantee this of itself. It is a task which requires active involvement of the state through wise scientific, industrial and trade policies, and appropriate forms of intervention, including ones financed with public money. In time, this money will bring returns. In this context, one should also recognize the fundamental role of human capital in ensuring long-lived return to the path of rapid development.

Fourth, even a perfect macroeconomic structural and financial policy (which is unattainable anyway for political reasons) and further institutional strengthening of the market, necessary in order to counteract corruption and curb bureaucracy, will not be enough to ensure dynamic output growth. What is also needed to this end is **steady improvement of the quality of enterprise management** and a systematic growth of microeconomic competitiveness. A deficiency of these skills cannot be compensated for by fiscal and monetary means. Such measures can be of assistance, but in reality, the success of a growth acceleration strategy will depend mainly on the enterprises. This phase of the transformation will be more difficult than eight years ago, because the so-called shallow reserves of production dynamics have dwindled.

#### **4. Equitable distribution**

There is no such thing as an just social system. This age-old dream of philosophers did not come true during the socialist episode, even though it was supposed to be the cornerstone of socialism. It was an even more distant vision in the preceding socio-economic formations and also later on, during the postsocialist transition and re-emergence of capitalism economy (which, incidentally, occurred in totally altered circumstances). The quest for “social justice” is one of the noblest pursuits of mankind, but alas, it is an unattainable ideal. However, this utopia does have practical implications, also for Poland at the beginning of the new decade and in the current phase of systemic transformation. It should be noted, that no single “justice” exists, because it is historical and social processes, not science, that decide what is just. Science may help, but it will not bring an ultimate answer to this question.

One thing, however, should always be borne in mind: **what is disapproved of by society as a matter of principle, is certainly unjust**. From this point of view, the notion of justice – also in connection with distribution relations – evolves in history. What was once considered just may be seen today as an injustice. Conversely, what we perceive today as

consistent with the accepted standards of justice would have been rejected by the society of yesteryear.

In this context, the belief that transition to market economy should automatically guarantee more social justice than real socialism did is amazing. It is only in rare cases that seemingly rational societies show such stunning naiveté. Recollecting the ideals of “Solidarity” from 21 years ago or the spirit (or even letter) of many provisions of the agreements negotiated at the “Round Table” 12 years ago, one cannot fail to notice the heavy load of proposed arrangements which, when implemented, would supposedly lead to a more equitable society (Baka 1999). Therefore, those agreements appear from today’s perspective mostly as a grave misunderstanding.

One cannot help wonder, either, at the fact that changes that would inevitably lead to a tremendous increase of the inequality level were instituted with extremely strong political support from those who believed they were championing just the opposite cause: greater equity, understood as leveling down the existing, quite moderate in fact, inequalities. However, as some types of inequality disappeared or were eliminated, many other immediately sprang up, which went much further than in previous decades (Milanovic 1998). Society thus has reasons to feel disillusioned, and this is indeed the way people feel, for the new reality, contrary to the promises, has brought about something totally different from the new and better world they expected (Kowalik 2000).

Such promises followed not only from the naïve convictions harbored by some intellectuals, politicians, economists or trade union activists. They were also (or, in certain political circles, predominantly) inspired by a calculated political intention. To put it bluntly, the people were being deceived (and this is still done, quite deliberately, today) so as to ensure their support, or at least a neutral and passive permission for the changes under way, which were only profitable to some narrower interest groups.

The case of Poland, of course, is by no means exceptional. Or, if anything, it is an exception in the positive sense of the term – although not so much any more in recent years, because **social inequalities and the injustice of income distribution have been once again on the increase since 1997**. But the fact remains that, in comparison with many other postsocialist transition economies (especially the ex-Soviet republics), the scale of inequality has increased in Poland (and also in the Czech Republic, Slovenia, Slovakia and Hungary) less steeply. The most common measure of inequality, known as Gini’s coefficient, remains markedly lower in Poland than in, say, Russia or Ukraine.

If Gini’s coefficient stood at zero, it would signify a fully egalitarian income division, where everyone gets exactly the same. On the other hand, a value of 100 corresponds to a division that is unequal in the extreme. In Poland, this coefficient increased from ca. 26 points in 1988 to ca. 28 in 1993 and around 32 in 1994 and then – in the years when the “Strategy for Poland” was being implemented – it stabilized at this latter value. Afterwards it began to grow again. It can be estimated that in recent years – when, as a result of “cooling down” the economy, relative income growth became accelerated among certain richer groups, while its dynamics disproportionately slowed down in relatively poorer sectors of society – Gini’s coefficient has been oscillating around 35–36 points. This is much more than in Italy (27), Germany (30) or France (33). By comparison, in Russia, it reached 48 already in 1996 (the level of Burkina Faso or Guatemala), and in all probability will have exceeded 50 points by now. In contrast, in Belarus it stands at a mere 22 points (World Bank 2001).

The increasingly pronounced, ever more unacceptable socially differentiation of the material situation of the population in the course of the postsocialist transformation results not only from unequal income streams but also from the movements of resources (property). This follows from the denationalization of state assets. **Privatization turns out to be yet another**

**instance of “historical justice” denied.** Gini’s coefficient does not reflect directly changes in the control of capital (ownership rights); hence the actual inequality is far greater than the changing current income proportions might suggest.

This conclusion also applies to international comparisons. Thus, for instance, even though Ireland has maintained fast growth for many years and thus closed the distance to Great Britain on the scale of income level, the difference in living standards between the two countries remains far greater. This is due to the fact that the value of capital accumulated over the ages is considerably greater in Great Britain than in Ireland (not to mention the fact that the build-up of British capital in some historical periods was financed in part by the Irish). It is for this reason, and not because of differences in current income flows, that Ireland remains considerably poorer than Great Britain.

The same is true about postsocialist countries, even if they succeed in sustaining rapid growth for the next quarter of the century. And so Poland, for example, may become comparable in 2025, in terms of income, with Spain, Lithuania with Portugal, and Estonia possibly even with Finland, yet all postsocialist countries will be lagging behind as far as living standards go. For the latter are a function of both the current income flow *and* the use of the capital accumulated in the historical development process.

It is evident that during the transition from centrally planned socialist economy to capitalist market economy, the distribution relations, and hence income proportions will change significantly. It should be even more obvious that the **amount of wealth available to various individuals and social groups will be drastically altered**, with all the implications this fact carries for the structural differentiation of their respective material positions. Capitalism, now under construction in Poland, must inevitably lead to social diversification and the formation of a new social structure in which some will become richer and some most certainly will not. The point is that the enrichment of the ones should not entail the absolute or relative impoverishment of the others, or, if it does, then the scale of this phenomenon should be kept down so that it should not affect economic growth.

A long-run strategy of socio-economic development, embraced for the time span of an entire generation, should contain an efficient mechanism of reconciling the contradictory interests that arise along the way. If such conflicts are not resolved in due time and using appropriate methods, conflict-prone situations may evolve into open conflicts, which is not only undesirable in itself, but also adversely affects the processes of economic growth.

Justice certainly precludes any forms of property and income division in which affluence and wealth do not correlate with an individual’s diligence and skills, as well as the contribution of his or her capital (obtained by honest means) and work to the national income. If some entity – an individual, group, region or sector – draws from the common resources, that is, the GDP, more than it contributes to their creation in the long run, it is also unjust. Of course, speaking about the principles of proportionality and equivalence in this field, one should take into account such factors as intergenerational distribution or social solidarity, denoting society’s readiness to subsidize those who are threatened for various reasons with marginalization.

It is thus easier to ascertain what is *not* than what *is* equitable distribution. However, it might be possible to assert by way of a counterpoint (far from being a platitude, this claim would constitute a pragmatic guideline for the economic policy-makers, particularly in the field of fiscal and income policy) that a **distribution system (including the inequalities it entails) may be called equitable if it meets with understanding and acceptance in society.** It is not true that vindictory or populist attitudes dominate in Poland. It is simply the case that society disapproves of obvious and unjustified disproportions in people’s material standing,

particularly if these are related to the rampant government corruption and the sale of public assets below par.

One should formulate some conclusions that will be applicable to the economic policy for many years to come. All the more so since a reasonably equitable distribution is justified not only by normative arguments; quite simply, **people have the right to enjoy the fruits of growing capital and labor productivity**. In this context, pensioners should also participate in the growth of real income, although they make no contribution to the current increase in output. This is one of the things social market economy is about. Yet the Polish economy, which began at one point to approach this model, has recently drifted away from it.

Equitable distribution is also needed for purely pragmatic reasons, also by those who are doing well or extremely well. Even the International Monetary Fund has recently shed its naïve dogmatism and now claims that relatively more balanced (that is, more equitable) distribution of income contributes to faster output growth (Tanzi, Chu and Gupta 1999).

In Poland, yet another cause of the sharp decline of GDP dynamics after 1997 was the widening inequality in income distribution. **Too much inequality affects economic growth in a negative way**, and hence also the interests of not only the poorer groups, but also the rich owners, investors and industrialists. Many of them seem to notice this with increasing clarity, although they tend to emphasize in this context the disadvantages involved in a faulty financial policy, rather than distribution relations *per se*. As it happens, unacceptable inequalities weaken the motivation to improve qualifications and work harder. In such circumstances, too much energy and effort is spent on attempts to improve one's material position at the expense of other participants in the production process, instead of increasing one's income by way of greater involvement in output growth.

What then to do? It turns out that a **policy of more equitable national income distribution is not only a political necessity, but also an economic imperative. Without the desired changes in this field, sustained acceleration of growth rate will be impossible.**

From a purely quantitative point of view, it is obvious that leveling down excessive inequalities requires that the income of less affluent groups should grow faster. Leaving aside the poorest social groups, whose material standing – especially in the next couple of years – can only improve through politically instituted changes in the composition of revenues and expenditures of the public finance system (that is, through redistributive measures), only those steps which foster a rapid increase of productivity in these social groups may not interfere with the pro-growth orientation of the economic policy. This is a major problem, because it is precisely these groups who are typically unable, without radical retraining, to increase productivity above the average level. A shift to higher-productivity branches and sectors thus requires far-reaching and costly structural adjustments in the economy, extended over many years.

Reducing the scale of inequality should also be assisted by active measures to curb unemployment, resorting, if and as necessary, to state intervention, industrial and trade policy, as well as fiscal instruments. The state, local governments and the business community itself should take active part in the tedious process of labor retraining and its successive shift to sectors which generate relatively greater value added. This is the best way both to stimulate growth and to level down social inequalities.

This, in turn, must be facilitated by an appropriately oriented educational policy and enterprise-stimulating measures. In this context, the educational system will continue to play a crucial role in the coming decades, alongside the economic subsystem based on science and the implementation of new technologies, also in the service sector. In other words, attention to the general level of education and culture, and the development of a knowledge-based economy are not only indispensable in any policy intended to stimulate long-term, sustained

growth, but also contribute to the emergence of a socially acceptable income structure, while successively increasing income levels. **The better educated a society is, the faster its economic growth becomes and the lesser is the scale of social inequality.** And although the perennial “efficiency vs. equity” dilemma will persist, it will be possible to produce ever more efficiently and distribute ever more equitably.

## 5. Beneficial integration

For the Polish economy, the coming years – both before the accession to the European Union in a couple of years’ time and for at least two decades afterwards – will be dominated by processes of economic integration with the external environment. This process should be viewed from a broader perspective than this is commonly done, not only in the current political debate (where it seems more understandable), but also in academic discourse. As a result of the present narrowed-down approach, the **integration of the Polish economy into the worldwide economic system is perceived not so much in terms of globalization, which is the key sign of the times and a main development factor in the early years of the 21<sup>st</sup> century, as of Europeization.**

Such a distortion is harmful, because it causes one to overlook many important opportunities brought about by globalization. Europe is not the whole world and the European Union is not the same as the world economy. It is true, however, that integration with the EU *is* of key importance for Poland’s long-term strategy of socio-economic development. The same applies to some other postsocialist economies, in view of their situation. Therefore, we should pursue in this context a policy of beneficial integration with the external economic system that surrounds us, of which we are increasingly becoming a part.

This process will inevitably gain momentum, so it is important to know how to turn it to advantage. It creates more opportunities than threats, although this is not always so with other postsocialist economies, whose situation varies greatly in many respects. A great deal depends on the inheritance of the past, the advancement (or delay) of structural reform and the building of the institutions of market economy, as well as the geopolitical position (Kolodko 2000a). But the highest stakes are attached – as is the most common situation – to the quality of the economic policy.

The opportunities and threats – or, put differently, benefits and costs – of the ongoing integration should mainly be seen in the context of the new factors that emerge in the sphere of broadly construed economic relations. The present phase of globalization boils down to the formation of an integrated worldwide marketplace for capital and goods (and, to a lesser degree and subject to more significant limitations, also labor). What it means is simply a next, higher phase in the development of world capitalism, because a worldwide market can only be capitalist in character. This, in turn, is a source of additional opportunities and threats for development.

**As the transformation proceeds, Poland is becoming part of the worldwide capitalist economy,** taking the rough with the smooth in the process. However, the balance of these additional benefits and costs will mainly depend on the position Poland will be able to take in the redefined international labor division. The key components of this “new deal” include the integration of the increasingly liberalized, “emerging” markets of the “Third World” and postsocialist countries with the entire world economy, and the fourth scientific/technological revolution, connected with the Information Age and the spread of the Internet (Kolodko 2001c).

It follows that no new processes exist which either create solely opportunities, or solely threats – that is, which either bring nothing but benefits, or nothing but costs. It is the

very essence of integration that the one implies the other; neither can occur by itself. **The opening and integration create additional opportunities for economic expansion through the development of export production and placement of one's products on foreign markets.**<sup>6</sup> Under such circumstances, new jobs and sources of income – and hence also budget revenues – are created domestically, although their existence depends on outside demand. This form of expansion will always depend on the market situation in other sections of the global market, but also on the international competitiveness of a given economy. Thus only high-quality goods and services, utilizing the comparative advantages of domestic producers, will find their way onto the global market. And this is the additional chance we are given by integration.

But at the same time this is an additional threat. Poor-quality products, the lack of marketing skills, or, worst of all, a relative drop in the profitability of investment and manufacturing caused by miscalculated fundamental financial parameters (especially interest rates and exchange rates) – any of these factors may well result in a situation when new jobs, particularly in branches where productivity growth is above average, are created abroad instead of at home. If this is the case, then the chronic surplus of imports over exports may weaken the potential of the economy, causing a relative increase of the unemployment level and eroding state-budget revenues. As a result, a kind of “dependent capitalism” emerges, in which the costs of liberalization and integration clearly outweigh the benefits (Poznanski 1997). The actual long-term performance in this area will crucially depend on the appropriateness of the adopted development strategy.

The same holds true for savings and investments. Increased participation in global economic exchange creates additional possibilities of both investing savings in other sectors of the world economy and absorbing the stream of external savings. Both these possibilities simultaneously involve an opportunity and a threat: the very fact that one invests does not guarantee the profitability of that venture. However, in the case of postsocialist countries at the current stage of transition to an institutionally mature market economy, still troubled by an acute shortage of capital, the transnational movements of savings should be seen in the first place as a chance to attract foreign savings. On the other hand, the countries concerned have not as yet accumulated a sufficient surplus of savings to be deposited abroad causing a net outflow of cash. But such a time will come, or, more precisely, capital flows will become a more pronouncedly two-way process with monies both coming into and flowing out of the country, and the net outcome of these transfers will determine the current account balance. This also applies to Poland, which not only remains and will remain one of the principal recipients of investments from other corners of the world, but also, as domestic capital accumulates, will increase the scope of its outgoing investments.

The influx of investment likewise brings an additional opportunity and additional threat. The structure of the investments is of crucial importance here. If these are mainly direct investments, which facilitate the absorption of new technologies and improve management quality, they not only enhance the quality of goods on the domestic market, but also generally boost the competitiveness of the entire economy. They also stimulate employment in those branches which generate greater value added and bring about the increase of wages and budget revenues. This, in turn, may encourage non-inflationary internal demand, leading to further economic expansion, which helps maintain growth rate at a relatively high level. Thus in the long run, **the influx of foreign savings in the form of direct investments undoubtedly promotes rapid growth, if only the profits are reinvested domestically.** For

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<sup>6</sup> By and large, one should speak in this context not so much of foreign markets as of other sectors of the world economy, of which we are part.

such an effect to occur, an appropriate climate is necessary, which is fostered by overall political, and especially financial stabilization, clear market regulations and strong institutions.

But if too much of the foreign savings that reach the country takes the form of portfolio investments, usually of short-term type, oriented predominantly towards interest- or exchange-rate arbitrage, such transfers usually mean costs, and not benefits to the recipient country. Misaligned interest rates and a faulty exchange-rate policy impose an additional burden on manufacturers, who sustain higher financial costs and thus their capacity to accumulate capital diminishes. Very high real interest rates, ostensibly maintained by the central bank in order to retain foreign capital, also entice domestic investors into portfolio investments, thereby absorbing funds which might have found an alternative use in the manufacturing sector. And consumers bear an extra cost, because the manufacturers and vendors attempt, quite understandably, to pass on to them their own high financial costs. Finally, an additional cost is imposed on all taxpayers, who have to pay higher interest on public debt. Needless to say, debt grows rapidly in such circumstances, especially if budget deficit persists, while the real interest rate on public debt exceeds the growth of real GDP.<sup>7</sup>

Thus also in the case of foreign investments, which are an inseparable component of integration with the global economy, the impact is, *a priori*, neither absolutely beneficial, nor absolutely harmful, from the point of view of economic growth and, more specifically, the sources of its financing. By taking an additional risk inherent in the integration and accepting the possibility (or even, temporarily, certainty) of extra costs, one gains additional opportunities and chances for extra benefits. Whether their long-term net balance will be favorable depends, as usual, on the development strategy.

There is no doubt, however, that in the Polish circumstances – taking into account the size of the internal market, the vicinity of the CIS emerging markets, the quality of human capital and the qualifications of labor – the inflow of foreign savings may give a significant boost to the long-term dynamics of economic expansion. The same applies to exports, which should increasingly assume the role of a lever that pushes up growth. The fact that this has not been the case in recent years only exposes the errors of an economic policy which has been unable to maximize the additional chances offered by integration with the world economy, while forcing upon society costs which could largely be avoided. Accordingly, a positive scenario for the next 25 years must assume such an optimistic variant, for there are no objective reasons why the errors of development policy should be continued in the long run.

## 6. Efficient state

The role of the state in the modern world undergoes significant changes and the necessity of its active involvement in the control of socio-economic development is not called into question by recognized professional bodies (World Bank 1997). The ongoing transformation reflects first and foremost the changing interrelations and interactions between the state, its agencies and the private sector on the one hand, and non-governmental organizations on the other. Thus **the question is not how to limit the role of the state in the economy, but how to redefine this role and restructure the forms and means of its involvement in the social reproduction process** (Hausner 1999).

The evolution of the state's role over the last ten or twenty years has also been driven (and this tendency is going to intensify in the future) by the ongoing globalization of commodity and capital markets (Szymański 2001). The constantly increasing scale of capital-

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<sup>7</sup> Unfortunately, this mechanism has become very prevalent in Poland over the past few years as a result of the “cooling down” policy. Consequently, debt, both internal and external, has been sharply increasing.

movement liberalization, the growing importance of transnational corporations, the internationalization of the goods and services market, and the development of the so-called “new economy” (OECD 2000) – these are the factors which cause an ever greater proportion of economic activity to remain outside government control, or even regulation.

Globalization, by definition, results in the emergence of a global economy, yet nothing like a global state, which might attempt to control the processes taking place therein, has arisen. Which is a good thing, because no such structure is needed. However, **it is necessary to coordinate economic policy at a global level and far-reaching changes can be expected in this field in the 21<sup>st</sup> century, which will require extensive reconstruction of the current international institutional order** (Kolodko 2001c). Regrettably, this process is noticeably delayed, which is bound to create mounting social tension on the global scene. Frequent protests and expanding anti-globalization movements clearly prove this point.

It is in this context that one should perceive the role of the state in postsocialist transition economies in general and in Poland in particular. False economic doctrine (which, incidentally, has a strong ideological motivation, while also being subservient to the interests of narrow groups which attempt to take advantage of the market transition at the expense of others) has already done much harm, mostly irreparable. Its most dire consequence was the **Great Transitional Depression, as a result of which the national income in Eastern European countries and the former Soviet republics, after a decade of transformation, still falls behind the pre-transition level by more than a quarter** (EBRD 2001). The weakness of the state also manifests itself through the inability to tap the genuine potential offered by market economy. For the relation of the state to the latter is complementary, not competitive.

As the state progressively withdraws from direct involvement in and control of production processes through denationalization of assets, privatization and deregulation, it ought to increase its activity in the field of institution building. **Fostering strong and well-developed institutions – as well as clear rules of the economic game, the law, and organizations that enforce the compliance with these rules by all participants in the reproduction process – constitutes the principal domain of the state, particularly in transition from socialism to capitalism.** Building a market economy (which, after all, is what the postsocialist transformation boils down to in the economic sphere) consists not only, or, at some stages, not even mainly, in liberalization and privatization, but rather in institution building (North 1997, Stiglitz 1998, Kolodko 1999, Blejer and Skreb 2001).

Besides, **the state bears a particular responsibility for the formation of human capital.** In the young market economies, this question must not be left to itself, because this would lead to a rapid erosion of this capital, which was inherited from centrally planned socialist economy in relatively good shape. This is one of the few elements in the legacy of socialism on which one can and should build creative development strategies under the new circumstances of market economy. The quality of human capital is one of the factors deciding about a country’s international competitiveness and position in the global economic system – particularly at a time when long-term growth must be increasingly stimulated by the expansion of knowledge-based economy (Koźmiński 2001). Therefore, any reasonable development strategy must involve, as an indispensable element, genuine support for the formation of high-quality human capital. This means both direct financial involvement and appropriate systemic regulations. It is up to the state to ensure high standards in education and to finance numerous research projects and, occasionally, implementations, because this obligation cannot be assumed, particularly in moderately or poorly developed postsocialist countries, by either the private sector, or non-governmental organizations.

Finally, **the state has and will continue to have an important role to play in the development of hard infrastructure**, on which the functioning of the entire economy, including the rapidly developing private sector, depends. The heedless and hasty withdrawal of the state from the redistribution of national income (which formerly provided, in particular, means to finance the infrastructure) – invoking the argument about the necessity of reducing its role in the economy – has left many sectors of the infrastructure, particularly in the area of transportation, in a state of neglect, while the private sector (including potential foreign investors) shows no intention to tackle this problem. As a result, numerous bottlenecks arise, which hinder enterprise and growth in the entire economy – including, of course, the private sector.

The state has various other functions to fulfill as well. These may not be directly connected with the functioning of the economy – as is the case with, say, public safety or diplomacy – but their performance does have an indirect bearing on socio-economic development, too. Therefore, a comprehensive development strategy should also envisage appropriate conditions for the state to fulfill adequately its extra-economic obligations. As an example, one can mention our diplomatic relations with Russia and certain other CIS states, where gross neglect and numerous failures to act have noticeably weakened our economic cooperation with this geopolitical region. As a result, the growth of the entire economy was further hindered.

**An efficient state thus means a mode of its functioning which fosters the improvement of microeconomic efficiency and rapid, as well as financially, socially and ecologically sustained, long-term growth.** Of course, this must be a democratic state. For democracy is not only a value in itself, but also promotes the improvement of allocative efficiency in the longer time span. Accordingly, a state is efficient if, acting within the framework of democratic institutions and procedures, it curbs the excesses of the market, while facilitating its efficient functioning in the long-term perspective.

An efficient state should also conduct a wise industrial policy and, especially under the present circumstances, coordinate it with the policy of pro-innovation change in the material structure in the economy on the one hand, and the trade policy, which is so important in time of globalization, on the other.

Last but not least, an efficient state entails a form of organization of civil society in which the government, conducting an appropriate redistribution policy, prevents the scale of inequality in the distribution of national income from reaching a point beyond which it might have an adverse impact on economic growth.

At the moment, **the Polish state could hardly be called efficient.** Taking into account all the circumstances and challenges posed by development, one cannot fail to notice that the state is weakening and its efficiency in sustaining favorable economic conditions has clearly diminished over the past few years. This, however, is neither an objective necessity, nor an inevitable outcome of the ongoing, irreversible transformation, but a consequence of specific political choices and ideological preferences. These harmful phenomena and trends should be reversed. It is a task which requires strenuous effort, but increasing the role of the state in those areas where its efficiency is necessary to sustain economic growth is possible, if only there is enough political determination to pursue this goal.

At the same time it is obvious (but maybe not always, not everywhere and not for everybody) that another threat exists, which has to be avoided at all times. Namely, measures intended to strengthen the role of the state might not lead to its increased efficiency, if **populist and bureaucratic tendencies** were to gain the upper hand. Such a threat is always present – even in a market economy with a dominant private sector – but this does not in any way imply that the state should be weak or “small” (in the sense of reduced redistributive

functions). It follows that an efficient state is not a static system of permanent solutions, but a dynamic process of oscillation between the Scylla of anti-efficiency populism and Charybdis of naïve neo-liberalism.

An efficient state must not be either “large”, or “small”; this is simply not the right criterion in this case (Tanzi and Schuknecht 1995). It should be in the first place friendly to the citizens and private enterprise alike, and, most importantly, it must create appropriate conditions for reasonably creative cooperation of all the participants in the market economic game. It is up to the state to provide such conditions and run a policy which ensures, in the interest of rapid economic growth, that the rules of the game are always obeyed.

## 7. The year 2025

What, then, is the situation of the Polish economy and society going to look like in 2025? What kind of economic history are we going to write at the end of the quarter of a century that is still before us? It all crucially depends on the development strategy that we are going to choose by way of conscious selection and on the economic policy pursued in the implementation of this strategy.

There is **no historical determinism** applying in this case. This is not to say that all is possible and all objectives are within reach of the economic policy, no matter how good the underlying economic theory is. And, it should be remembered, in real world, policy results more often from compromise – not always healthy – between contradictory interests than from scientific logic. This is not going to change in the future. Therefore, although the options are many, the room for maneuver is limited. In many fields it will be even narrower after Poland's accession to the European Union and the shift to the euro. The progressive integration with the world economy and the ensuing liberal deregulation, pursuant to our obligations as members of the OECD and WTO, also limit the range of available choices. However, let us repeat, the net outcome of the integration processes signifies more opportunities for economic expansion than barriers to it.

So, how are we going to assess our position from a year-2025 perspective? It all depends on the path along which we are going to get there. Are we going to shun high output dynamics and needlessly slow down the economy, as we did in 1998–2001, or are we going to accelerate growth to some 6 or 7 percent a year, as was the case, despite less favorable external circumstances, in 1994–7? If we follow the latter path, our **GDP will nearly have quadrupled by 2025, approaching, on per capita PPP basis, 30,000 dollars**. But if this vision is to materialize, the long-term growth strategy must be based on four pillars: rapid growth, equitable distribution, profitable integration and efficient state. The logic of development processes is such that these pillars are interconnected and positively correlated with one another: they constitute a single, intricate construction. If care is taken of one of these elements, the remaining ones are strengthened – and vice versa.

But it is also possible that, looking back in 2025 at the distance we have covered over the past 25 years, we will have few reasons to rejoice and quite a lot to worry about. The shortcomings and weaknesses of our economic policy resulting from dogmatism and particularistic interests, and especially the inability to stimulate and sustain economic prosperity in the context of increasing international competition following from globalization, may cost us dearly. If growth rate remains for years at a low level, in the order of 2–3 percent, a generation from now we will still lag a generation behind Portugal and Greece, and even behind some postsocialist economies now at a similar development level as Poland. Moreover, given the relatively low GDP level – say, 12,000-15,000 dollars on a PPP basis, which would amount in 25 years' time to just a quarter or a third of the level attained by

highly developed countries – the existing inequalities in distribution might be aggravated. The same applies to Poland's international position, because such sluggish growth would suggest that no practical way has been found of maximizing the benefits of integration with the global economy. If that be the case, than **even as a member of the European Union, we will remain paupers on the fringe of the global village.**

Under such circumstances, a state with weak institutions and a poorly integrated society, rent by internal conflicts spurred by slow growth and large-scale inequalities, would additionally exacerbate the already inauspicious state of affairs, further jeopardizing the prospects for more distant future. And, let us not forget, history will not come to an end in 2025. Challenges to and opportunities for further growth will most certainly not disappear, either. But first of all, we need to get thus far. It will be far better, if we do it along a path of rapid growth, reaching a per capita income of ca. 30,000 dollars, with Gini's coefficient down to about 30 points and an efficient state, than if we lag behind global growth rate and allow Gini's coefficient to climb to 40 points or so.

Most interestingly, both these scenarios are possible from today's point of view. But in 2025, there will be only one economic history.

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