

Letter to the Editor

Dear Editor,

In his paper 'The Economic Transformation of Eastern Europe: The Case of Poland', published in your journal, volume 25 (1992), Jeffrey Sachs maintains that the first two years of economic reform (i.e. 1990–1991) in Poland had a "...profound and a beneficial effect on the Polish economy". Further on in the text he sees the positive effects primarily in ending inflation and shortages, and in promoting the private sector. He acknowledges that some groups lost ground in the first two years. "The evidence suggests that on average, Poles are now consuming somewhat more meats, fruits and consumer durables than they were before the reforms, so that greater availability of goods has, on average, more than compensated for higher prices" (p. 13). A glance at statistical figures on consumption shows that there was a tiny decline in meat consumption in 1990 compared to the second half of 1989 (*Wiadomosci Statystyczne*, 1991, no. 6). I do not have figures for 1991 and I doubt that Sachs could have had figures for 1991 when he wrote his paper. Let us say that he is correct with regard to fruit and consumer durables. Are these figures by themselves relevant indicators of the state of the standard of living, in the absence of other essential figures on consumption, and in the light of a 32% decline in real wages (see S. Gomulka, *Zycie Gospodarcze*, 1991, No. 18) and a huge drop in the purchasing power of savings (estimated to be 30%) in the first year of the reform, facts which he ignores in his article? At any rate, the allusion to consumption is an argument which makes more economic sense than the one he used in the past. As proof that the situation in Poland had improved, Sachs used to argue that, after the reform, Poles could get more dollars for their wages than before the reform. He has, however, forgotten to mention that, after the reform, the amount of goods and services one could get for a dollar declined much more than the value of wages in terms of dollars increased.

In his paper he also mentions that the standard of living in Czechoslovakia, Hungary and Poland was much lower in 1989 than was assumed. As proof he quotes World Bank figures on GNP per capita. According to those, Czechoslovakia had a GNP per capita of \$3450 in 1989. This figure was probably achieved by computing the output of the Czechoslovak economy on the basis of the present exchange rate, which deeply undervalues the crown. Such a computation may be good for some purposes, but has no great value for comparing the standard of living. An example will show why this is so. In 1991, in Czechoslovakia, the average monthly wage of an industrial worker was Kcs 4500, which is approximately US \$170, if computed according to the official exchange rate. In

the USA, a family with a monthly income of \$170 can afford to sleep on the street and must often eat in soup kitchens, whereas in Czechoslovakia it can afford to pay rent and get by, very modestly. To compare standards of living in different countries, the exchange rate must be based on purchasing-power parity. And such a comparison will surely show – as such computations have shown – that Czechoslovak GNP per capita is more than double what the World Bank indicates.

Despite Sach's optimism, the Polish economy finds itself in a deep recession even after two and half years of reform have elapsed. Industrial production – which declined in 1990 by 24% and in 1991 by 12% – has not yet started to recover. It increased in March 1992, but continued to decline in April and May. Inflation was 68% in 1991; in 1992 it will be much lower, but still high. The budget deficit is very high. Unemployment creeps slowly upwards: it was 12.3% in May 1992 (See Misiak, *Zycie Gospodarcze* 1992, Nos. 13 and 14 and *Zycie Gospodarcze* 1992, No. 27, p. 13). It is difficult to predict how long it will take the Polish economy to extricate itself from the recession caused by the shock treatment. One might ask whether Poland would not have been better off and endured less hardship if the transition to a market economy had been carried out gradually?

JAN ADAM

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Reply to Jan Adam

Dear Editor,

Mr. Adam's comment misses the main point concerning living standards made in Sachs (1992). The measures that Mr. Adam cites, such as a '38% decline in real wages' or a 30% decline in the 'purchasing power of savings', mean little or nothing about real living standards when the baseline for comparison is a situation of *extreme shortages* of consumer goods at the official prices.¹ The 'real wage' or the 'real money balances' obviously don't measure purchasing power if the income or savings cannot be used to purchase goods at the official prices used to measure the 'real' wage or savings.

As we can see in Table 1, Poles on average consumed more meats and fruits in 1991 than in 1989.² Contrary to popular conceptions, this was true of pensioners' as well as employees' households. Interestingly, there was a small decline in meat consumption for farmers' households and employee's farmers' households (constituting around one fourth of the households), but from much higher levels than city workers. Fruit consumption went up for all groups except farmer households. In any event, there is absolutely no evidence of any sharp drop in real consumption after price liberalization.

The data on changes in Polish ownership of consumer durables render even more silly the vision of Poland in depression. As seen in Table 2, the proportion of households owing consumer durables showed a significant

Table 1. Meat and fruit consumption, 1989 and 1991 (average monthly kg per capita)

Type of household	1989	1991	Percent change
		<i>Meat</i>	
Employees	5.01	5.11	2.0
Employee farmers	5.45	5.32	-2.3
Farmers	6.66	6.47	-2.9
Retired persons and pensioners	5.70	6.34	11.2
Average (weighted)	5.42	5.56	2.6
		<i>Fruits</i>	
Employees	3.00	3.35	11.7
Employee farmers	2.72	2.86	5.1
Farmers	3.16	3.01	-4.7
Retired persons and pensioners	3.81	4.20	10.2
Average (weighted)	3.14	3.41	8.6

Source: *Buletyn Statystyczny*, various issues, Table 46, 'Average monthly per capita consumption of selected foodstuffs of households'.

Table 2. End-of-year stocks of consumer durables per 100 households (workers' households)

	1988	1991
Radio	88.9	91.1
of which stereo	22.6	38.9
Portable radio	68.7	58.6
Color TV	41.7	82.9
Video player	1.9	41.0
Tape recorder	68.8	81.5
of which stereo	20.6	46.0
Bike	93.2	93.3
Car	30.2	38.3
Automatic washing machine	55.5	67.2
Refrigerator	100.0	99.9
Freezer	16.4	27.4
Vacuum cleaner	96.2	97.6
Sewing Machine	60.7	59.6
of which electric	43.7	47.0

Source: GUS, *Survey of Workers' Households*, 1992

increase between 1988 and 1991 for virtually every category of durable. The Poles were starved for consumer goods for forty years. Now, with free trade, currency convertibility, and the rapid expansion of the retail sector, there is a ready availability of these goods.³

Barg and I (1992) looked at a more comprehensive group of consumer items, including food, clothing, and consumer durables, to assess the changes between 1989 and 1990. Using consumer expenditure data, we found that the weighted volume of consumption fell in 1990 compared with 1989 by around 4 percent, *not taking into account the rise in product variety, product quality and the end of queuing time*. Starting from our estimates on real consumption flows, Roberts (1992) computed the additional gains from the time saved in queuing, and found that "the welfare gains from price liberalization were very significant" (p. 21).

If we take into account the additional gains in real consumption between 1990 and 1991, which even official statistics put at around 2 percent, we can safely conclude that, counter to the superficial judgments based on the statistical real wages, average consumption levels in Poland were higher in 1991 than in 1989.⁴ Even if there is an error in these estimates, and real living standards are lower on average in 1991 than 1989, there are absolutely no grounds for believing that there has been a sharp fall of living standards as the result of rapid reforms.

Nor do the Poles themselves believe it. A survey last year (November 1991), asked Poles to assess their living conditions almost two years after the start of the reforms (see Ammeter-Inquirer, 1992). Their responses demonstrate a positive response, on balance, to the economic changes. Fully 82 percent of the respondents held that their family's economic situation was the same or better than five years before.⁵ This was at a

time in which the popular press depicted the Poles as seething with unhappiness over the hardships of the reforms. Similarly, 43 percent of respondents preferred "an economy like we now have", to "a socialist economy like before the revolution", while 24 percent preferred the socialist economy, and 33 percent saw no difference.

Adam's focus on the drop in industrial production is also misplaced. Adam neglects the important point that economies emerging from the Stalinist model have too much industry compared with other sectors of the economy. Therefore, when market-based economic transformation begins, industrial production declines while non-industrial production, particularly in services, expands. This is transformation, not 'deep recession'. It is no deep recession when number of registered small businesses rises by 700 000 from the end of 1989 to mid-1992.⁶ The increase of 709 900 small business owners represents almost 5 percent of the working population. Total employment in these enterprises rose from 1 475 500 to 2 800 400, an increase of almost 9 percent of the total labor force. As for larger enterprises, the number of private commercial law partnerships (partnerships, limited liability companies, and joint-stock companies), rose from 11 693 at the end of 1989 to 51 174 by mid-1992.⁷

Even if we restrict our attention to industry, it is not true as Adam claims, that industry "has not yet started to recover". The industrial production in mid-1992 has risen significantly above the levels of a year before, as shown in Table 3, signalling a (seasonally adjusted) turnaround in industrial output. And the particular kind of output is clearly tied to market forces, rather than to the previous emphasis on heavy industry at all costs. This year's recovery seems to be taking place most strongly in new consumer-related areas, such as wood and paper, and food processing, while traditional, Soviet-related production in electro-engineering continues to be weak. It should also be stressed that the decline in industrial production in 1991, and to some extent in 1990, was the result of the collapse of trade with the former Soviet Union (FSU), not the result of economic reforms in Poland. That is why Finland, which was

Table 3. Industrial production, monthly, 1992

1992:	Industrial Production	
	Index (1990 = 100)	Percent change year-over-year
January	82.4	-15.1
February	84.1	-8.7
March	86.4	-3.6
April	90.3	3.3
May	85.9	6.3
June	86.0	4.0
July	93.7	9.1

Source: *Biuletyn Statystyczny*, No. 7, August 1992, Warsaw, Table 1, p. 18 (column 3).

closely linked to the FSU via trade, also suffered a sharp drop in industrial production last year.

The conclusions are clear. Poland is in the midst of a profound and successful transformation, which is creating private ownership (now producing more than 50 percent of GDP); a market system; an export boom (with convertible currency exports up from \$8 billion in 1988 to around \$14 billion in 1992); an end of the misery of endless shortages and queuing; and a chance for a normal economic life integrated in Western Europe, with realistic prospects of converging living standards in the future.⁸

Notes

1. As has been widely described, in Lipton and Sachs (1990) for example, the extreme shortages were the result of artificial controls on consumer prices combined with an enormous expansion in aggregate demand (as a result of large budget deficits, rapid credit expansion, and an explosion in take-home pay).
2. This is based on a weighted average of the four types of households shown in the table. The weights, using 1991 data, are: employees' households, 52 percent; worker farmers' households, 15.2 percent; farmers' households, 12 percent; pensioners' and retired persons' households, 20.8 percent. Incidentally, data for much of 1991 was available at the time of writing (contrary to the suggestion of Mr. Adam), since the data are reported on a monthly basis in the *Biuletyn Statystyczny*.
3. These data also show how inappropriate it is for Mr. Adam to dismiss the increased purchasing power of Polish wages in terms of dollars, the counterpart of the huge increase in consumer durable imports.
4. Since the problem of shortages no longer exists after 1989, the official consumption data for 1990 and 1991 are more accurate than the official data for 1989. Nonetheless, there is still probably undercounting of consumption due to underrepresentation of purchases in the unregistered retail sector; undermeasurement of quality improvements; and a failure of the official data to capture the vast increase in the variety of consumer goods available in Poland.
5. Much better, 19 percent of respondents; a little better, 38 percent; much the same, 25 percent; a little worse, 15 percent; a lot worse, 3 percent.
6. The number of registered small businesses rose from 813,500 on December 31, 1989 to 1,523,400 on June 30, 1992.
7. Source is *Biuletyn Statystyczny*, Central Statistical Office, Government of Poland, Warsaw, May 1991 (pp. 57-58) and August 1992 (pp. 89-90).
8. Mr. Adam also suggests that living standards in Eastern Europe are not, in fact, lower than was assumed prior to 1989. His discussion about purchasing parity parity, while correct, is beside the point. Pre-1989 analyses routinely held that East Germany living conditions were more than half of the West German level, and that living standards in Czechoslovakia and Hungary were not far from that. Only after the fall of communism have many analysts recognized just how much catching-up will be required.

References

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