Chron

Office Memorandum

To: The Managing Director
The Deputy Managing Director

April 10, 1985

From: Peter Hole

Subject: Poland - Staff Visit

A staff team 1/ was in Poland from March 25 to April 4. The main objectives were to clarify and deepen our understanding of the workings of the economic mechanism and to collect and evaluate additional data, particularly on the fiscal and monetary accounts. In addition to meeting with government officials, the team held useful discussions with the managers of a number of enterprises which helped us to explore the motivation of and constraints on enterprise behavior, as well as how enterprises respond to various policy variables. We also called on a number of academic economists in the research institutes to discuss various conceptual issues, including some related to the interpretation of data. At the end of the visit, the mission met with the Minister of Finance, Mr. Nieckarz; inter alia, he emphasized that the Government, particularly the Prime Minister, was fully determined to carry through the economic reform process launched in 1981-82, and he appeared anxious to have the process of membership in the Fund completed expeditiously. As in February, the cooperation of all on the Polish side was very good.

As a result of its two technical visits this year, the staff now has a reasonable understanding of the basic features of the economic system. The reform legislation lays down the framework for a decentralized system subject to control through indirect policy instruments. However, while there may have been a considerable increase in the degree of autonomy enjoyed by enterprises, it remains abundantly clear that in practice the operation of the price, wage, investment and trade and payments mechanisms, as well as the implementation of fiscal and credit policy, are riddled with exemptions, preferences and distortions--often for no very predictable reason. Three examples may illustrate the point. In the wages field, there is a highly progressive tax, paid out of profits, on wage increases in excess of productivity increases; the precise specification of the tax liability is, however, essentially a matter for negotiation on an enterprise-by-enterprise basis. In the external area, the exchange rate is set--for fear of inflation--to assure the profitability of only 75-80 percent of exports to the convertible currency area; export subsidies, tax breaks for exporters, and foreign exchange retention rights--all subject to some element of negotiation--are thus often crucial incentives. In the field of price determination, the reform initially freed a significant share of consumer and producer prices for determination by enterprises; more recently, the scope for increasing these "free" prices has been sharply limited by official decree. At present, there are thus few market-determined prices, and direct allocative mechanisms remain important.

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The staff has also been able to collect and familiarize itself with a substantial body of data. For the most part, these seem to be adequately comprehensive and reliable. A number of thorny issues relating to the valuation of production and external transactions for the purpose of calculating a quota remain, of course, to be addressed.

While the staff has limited its remarks and questions to the technical issues delineated above, it has sensed--in some of the more general pronouncements of senior Polish officials--not only exaggerated expectations of the financial assistance that membership of the Fund could bring and large gaps in officials' knowledge of the Fund's practices on the use of its resources, but also a blanket belief that adjustment cannot be other than extremely gradual. The latter is brought out by the repeated references by officials to the impracticability of adjusting prices at all quickly or of reducing real incomes further. It is also reflected in their targeting to reach a current account surplus in convertible currencies only around the turn of the decade.

With regard to recent economic developments, Poland--like other countries in Eastern Europe--has been adversely affected by the severe winter. This, however, is thought to have made previously comfortable targets for 1985 (GDP growth of 3-3 1/2 percent, and an increase in the trade surplus in convertible currencies of US$100 million, to US$1.5 billion) more challenging, but still attainable. The lower than expected trade surplus in January and February has nonetheless clearly complicated the immediate task of managing the external finances. Officials indicated that they did not foresee an easy or quick resolution of the impasse with government creditors. They said that signature of the draft Paris Club accord for restructuring debt in arrears from 1982-84 could not be contemplated without adequate assurances from western governments of new credits. Certain new credits are beginning to be offered--notably DM 100 million from Germany--and bilateral talks with western governments are being stepped up this month. But the amount of new money presently in prospect clearly falls very far short of what Polish officials are seeking.

cc: Mr. Habermeier
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Mr. Finch
Mr. Mohammad
Mr. Nicoletopoulos
Mr. Ouattara
Mr. Shaalan
Mr. Tanzi
Mr. Tun Thin
Mr. Van Houtven
Mr. Wiesner
Paris Office
Geneva Office
Mr. Collins

bcc: Mr. Ungerer

cc: PCF
PCH
JP

Lyne: Pl arrange a mtg RdeF, PDH c Mr Rust

cc: PCH DMD ③

Office Memorandum

→ MD

My reactions
RDE 4/10/85

R 10 PM 5:38
OFFICE OF THE MANAGING DIRECTOR

APR 12 1985

TO: The Managing Director
The Deputy Managing Director

April 10, 1985

FROM: L.A. Whittome

SUBJECT: Poland

(Mr. Sal / Mr. Whittome
The more I think of this question the more I believe we should not hasten. I have doubts on the advisability of "aiming" at the Annual meeting in Seoul. You must ask them very precise questions on how economic policies work (or could work) before thinking. I am not convinced by the argument relating to banks.)

April 12 85

Following the completion of a second technical visit to Warsaw, we need to consider what the next steps should be.

The staff team now has an adequate appreciation of the economic mechanism in Poland (always recognizing that discretionary administrative decisions continue to play a crucial role) and has concluded that we can be generally satisfied with the quality and coverage of the available data. This is also the impression of the economic institutes in western Europe and of the banks. In these circumstances, I doubt whether a further technical visit could serve any constructive purpose and I think that we now need to consider sending a full membership mission.

I know you remain uneasy on the timetable for Poland and I certainly do not feel confident that I know the correct approach. If we were to delay sending a membership mission until, say, mid June then our procedures are such that a vote on membership at the time of the Annual Meeting would not be possible. Membership would therefore require a postal vote and might take place in, say, December. If we were to delay further in sending a membership mission we could easily postpone the vote on membership to 1986. Delayed membership would postpone a series of difficult decisions but would not avert them.

Indeed delay would aggravate the problems facing Poland simply by prolonging uncertainties. As we see the figures, a rescheduling of earlier rescheduled debt to the banks is likely to be unavoidable in 1986. Similarly, without new credits the Poles are most unlikely to be able to meet the commitments they are being asked to assume by the official creditors. These difficulties will be more awkward to deal with if Fund membership is postponed simply because some banks and governments have tied possible future credits to actual Fund membership. Secondly, there is the simple argument that good administration should incline us to process relatively rapidly an application that was submitted in November 1981--at the same time as that of Hungary.

→ presumably because they expect a Fund financial arrangement

On balance I would incline to sending a membership misssion to Warsaw to begin work on May 21. This should on a normal timetable allow us to ask for a vote on October 8 in Seoul. However, if we, or any member country, wished later to delay the vote this could be easily done by, for instance, asking for further information before the quota recommendation was endorsed. I should also emphasize that this timetable assumes no delays in the provision of further information or

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I agree

On the Seoul scenario--we might have Article IV discussions around the turn of the year, with Board consideration of the staff's report in the early spring of 1986. This would presumably be followed in the late spring by discussions concerning a use of Fund resources--which could, of course, well drag on.

We need also to reflect on the distinct possibility, noted in the attached back-to-office report, that ministers and senior officials in Poland are--or choose to pretend to be--less than fully informed of the practices of the Fund, in particular the terms on which the Fund is prepared to consider extending financial assistance to member countries.

I do not think we should allow any fundamental ignorance or misunderstanding of Fund lending practices to persist until after membership. I think therefore that I should visit Warsaw for a few days in early June (on the Seoul timetable, or late June on the delayed timetable). I would join the mission and seek to set out candidly a broad description of the sort of economic policy changes and pace of adjustment that we would be looking for in order to be able to extend financial assistance.

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More immediately, there are the Paris Club discussions with Poland which are scheduled for April 25 and to which we have--for the first time in the current round--been invited. I would recommend that we accept the invitation and ask Mr. Hole or Mr. Prust, together with the representative from ETR, to attend.

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Mr. Collins

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To: The Managing Director
The Deputy Managing Director

April 10, 1985

From: Peter Hole

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Office Memorandum

1 Dr. Erb
2 Mr. Whittome
April 10, 85

TO:	The Managing Director ✓ The Deputy Managing Director	April 10, 1985
FROM:	L.A. Whittome	cc. PCH
SUBJECT:	Poland	

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On balance I would incline to sending a membership misssion to Warsaw to begin work on May 21. This should on a normal timetable allow us to ask for a vote on October 8 in Seoul. However, if we, or any member country, wished later to delay the vote this could be easily done by, for instance, asking for further information before the quota recommendation was endorsed. I should also emphasize that this timetable assumes no delays in the provision of further information or

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yes

On the Seoul scenario--we might have Article IV discussions around the turn of the year, with Board consideration of the staff's report in the early spring of 1986. This would presumably be followed in the late spring by discussions concerning a use of Fund resources--which could, of course, well drag on.

We need also to reflect on the distinct possibility, noted in the attached back-to-office report, that ministers and senior officials in Poland are--or choose to pretend to be--less than fully informed of the practices of the Fund, in particular the terms on which the Fund is prepared to consider extending financial assistance to member countries.

I do not think we should allow any fundamental ignorance or misunderstanding of Fund lending practices to persist until after membership. I think therefore that I should visit Warsaw for a few days in early June (on the Seoul timetable, or late June on the delayed timetable). I would join the mission and seek to set out candidly a broad description of the sort of economic policy changes and pace of adjustment that we would be looking for in order to be able to extend financial assistance.

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FROM: L.A. Whittome /LAW/

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INTERNATIONAL MONETARY FUND

9/iv

TO : Mr. Whittome

FROM: Peter Hole

Poland

I attach:

- a draft 48-hour report
- certain draft points for incorporation in an accompanying note from you to Mgt. (I remain slightly uneasy about "your" visit taking place so late in the process. I wonder how they will react -- at such a late stage -- if your message genuinely comes as a shock, the more so if perchance it followed some untoward event in East-West relations).
- a timetable, for information, which would culminate in Korea.

PH

Nov 81 appl'n
at time of Hungary

Process Culminating in

Poland: A Timetable for Membership in Korea

October 9	Sign Articles
October 8	Governors vote
September 25 (approx.)	EBM on Membership Committee's Report; draft Resolution to Governors
September 11	Report by Membership Committee to Executive Board recommending Resolution to Governors
September 5	Meeting of Membership Committee
August 7	Calculation of Quota Paper to Membership Committee
July 24	Draft Calculation of Quota Paper to Management
Early July	Committee on Membership established
May 21-June 7	Membership mission

Art IV Jan Dec/Jan

to Bd March

Stand-by April May/June

Bk debt - dec 85
285
c800 in 86
Govt debt 7.7
maturities

9120

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cc: EED

RCV: @1IM/1.09557 LINE: 1

440385 FUND UI 651997

812516B IHC PL

ORIG: EUR

EUROPEAN DEPARTMENT
INTERNATIONAL MONETARY FUND
WASHINGTON D.C.
USA

POLAND TEAM ARRIVED
WILL NOT BE IN WARSAW FRIDAY SATURDAY AND MOST OF SUNDAY

P.C. HOLE

440385 FUND UI

812516B IHC PL

.....
REPLY VIA ITT

?
TIME: 04:05 03/26/85 ???
CONNECT TIME : 76 SECONDS

Being Called;

Jacqueline Prust--

Mary Manison--

Peter Hole--

Depts--EUR

INCOMING CABLE/TELEX

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ØPOLAND TEAM RETURNING AS SCHEDULED
P.C. ØHOLE

248331 IMF UR

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Time: 08:10 04/03/85 ???
Connect Time : 56 seconds

CALLED: M. MANISON
BEING CALLED: J. PRUST
K. HOLE

dept; EUR

INCOMING CABLE/TELEX

Front office

INTERNATIONAL MONETARY FUND

WASHINGTON, D.C. 20431

Room 9-406

CABLE ADDRESS
INTERFUND

March 12, 1985

Mr. Z. Karcz
Director,
Foreign Department
Ministry of Finance
Warsaw
Poland

Dear Mr. Karcz:

With a view to facilitating our forthcoming discussions in late March/early April, I am enclosing a preliminary list of questions and topics which we should like to explore, together with a number of related tables which I hope can be completed for the discussions.

The main purpose of our visit, as I see it, is to deepen the understanding we were able to gain in February of the role of the various policy instruments and the workings of the economic mechanism in Poland at the present time. Toward this end, and as I mentioned to you in February, it would be most useful if, following discussions with officials, we could meet with a cross-section of enterprise managers and with economists in the research institutes. A second purpose will be to collect certain data not readily available to us in Washington.

Against this background, may I suggest that after an organizational meeting on the afternoon of our arrival (March 25), the first four days of the visit (Tuesday 26-Friday 29) be devoted to discussions with officials. Over this period, Mr. Prust, Ms. Swiderski and I could perhaps spend a half day each on the following eight topics (in whatever order best suited yourselves): I Prices; II Wages; III Money and Credit; IV Government Finance; V Aggregate Supply and Demand and Liquidity Overhang; VI Investment and Enterprise Accounts; VII Agriculture; and VIII Balance of Payments and External Debt. Mr. Manison and Mr. Boonekamp could join us for the two sessions on Tuesday and the two on Friday, but on the Wednesday and Thursday (if suitable) I should be grateful if they could meet with your experts on the exchange and trade system to take up a long list of detailed questions (section IX of the Questionnaire). As you know, it is required that we cover this latter area in considerable depth as part of the membership process.

During the second week of the visit (Monday April 1-Thursday April 4), it would be much appreciated if arrangements could be made for us to visit with the managers of three or four enterprises (section X of the Questionnaire) and with economists in the professional institutes attached to the Ministry of Finance, the Ministry of Foreign Trade, and the Planning Commission (section XI). If at all possible, I should also very much welcome the opportunity to meet again with Professor Sadowski on the economic reforms.

I regret that these requests are being made at short notice--much shorter than we had earlier intended--but hope that they will prove manageable. I am looking forward to resuming our dialogue later this month.

Sincerely yours,

Peter C. Hole
Assistant Director
European Department

IMF OFFICIAL MESSAGE

WASHINGTON, D. C. 20431

DO NOT SOFT ROLL EXCEPT WHEN ALIGNING INTO LINE 23

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MR. Z. KARCZ
DIRECTOR, FOREIGN DEPARTMENT
MINISTRY OF FINANCE
WARSAW, POLAND

DISPATCHED IMF 1985 MAR 12 PM 8 16

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DISTRIBUTION

MR. ROSE, EUR

cc LAW

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FOLLOWING OUR TELEPHONE CONVERSATION OF TODAY, I SHOULD LIKE TO CONFIRM THAT A STAFF TEAM WILL VISIT WARSAW FROM MARCH 25 TO APRIL 4 FOR FURTHER TECHNICAL DISCUSSIONS RELATING TO POLAND'S APPLICATION FOR MEMBERSHIP IN THE FUND. IN ADDITION TO MYSELF, THE TEAM ON THIS NEXT OCCASION WILL AGAIN INCLUDE MR. MANISON, MR. PRUST AND MS. SWIDERSKI, TOGETHER WITH MR. CLEMENS BOONEKAMP, ECONOMIST IN THE EXCHANGE AND TRADE RELATIONS DEPARTMENT.

I SHOULD BE GRATEFUL IF RESERVATIONS COULD BE MADE AT THE VICTORIA INTERCONTINENTAL FOR ONE SUITE PLUS FOUR SINGLE ROOMS FOR THE PERIOD MARCH 25-APRIL 4 INCLUSIVE. WE PLAN TO ARRIVE ON LUFTHANSA 346 AT 11:55 ON MARCH 25 AND DEPART ON APRIL 5.

I AM SENDING TO YOU TOMORROW VIA OUR OFFICE AND YOUR EMBASSY IN PARIS A SERIES OF TOPICS FOR THE DISCUSSIONS AND A NUMBER OF TABLES.

LOOKING FORWARD TO MEETING WITH YOU AND YOUR

IF REQUIRED INITIAL BELOW

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(267) [illegible] [illegible] MINFIN PL

TELEX NO.: CABLE ADDRESS:

DRAFTED BY NAME (TYPE): Peter C. Hole EXT.: 8811 DEPT.: EUR DATE: 3/12/85

AUTHORIZED BY NAME (TYPE): Peter C. Hole

AUTHORIZED BY NAME (TYPE):

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SIGNATURE

IMF OFFICIAL MESSAGE
WASHINGTON, D. C. 20431

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WARSAW, POLAND

- 2 -

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ASSOCIATES AGAIN.

BEST REGARDS.

PETER HOLE

INTERFUND

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INTERNATIONAL MONETARY FUND

2

Mr. Lari telephoned me later today to say that he had specificially confirmed that the view of his quoted above is fully shared by Mr. Wapenhans.

Brian Rose

Office Memorandum

March 12, 1985

MEMORANDUM FOR FILES

Subject: Poland

I spoke to Mr. Lari today to invite the Bank to send someone on the forthcoming Fund visit to Warsaw (March 25-April 5). Mr. Lari said he did not believe that the Bank had any interest at this stage in sending anyone on the visit: Poland had made no sort of contact of any kind with the Bank, and he asked the Fund mission to be very circumspect on this matter in Warsaw. He said he would check with colleagues in the Bank and get back to me if any different feelings prevailed.

Brian Rose BR

cc: Mr. Hole

DMD ~~Approve~~ March 20

CC: EED

Office Memorandum

→ MD

ok
RDE
3/17/85

1985 MAR 15 PM 5: 11

OFFICE OF THE
DEPUTY MANAGING DIRECTOR

March 15, 1985

MAR 18 1985

To: The Managing Director
The Deputy Managing Director

From: Brian Rose BR

Subject: Poland - Briefing Paper

I attach for your consideration a briefing paper for the forthcoming staff visit to Poland, which has been cleared by Mr. Hood (RES), Mr. Boorman (ETR), Mr. Leddy (TRE), and Mr. Holder (LEG). After approval the paper should be returned to the European Department.

Mr. Hole, who will head the mission, is at present on official travel in Austria and Germany from where he will proceed to Poland.

cc: EED

Attachment

cc: Mr. Collins

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

POLAND

Briefing Paper - Staff Visit

Prepared by the European Department

(In consultation with other Departments)

Approved by Brian Rose BR and J.T. Boorman

March 15, 1985

A staff team consisting of Messrs. Hole (head), Manison, Prust, and Ms. Swiderski (all EUR) and Mr. Boonekamp (ETR) will visit Warsaw from March 25 to April 5, 1985 to continue technical discussions relating to Poland's application for readmission to the Fund which were started during a previous staff visit in the first half of February. The focus of this second visit will be on improving the staff's understanding of the working of the Polish economic system and for this purpose the team will hold discussions with a range of enterprises and economic research institutes as well as with the ministries and other agencies of the central government. The team will also gather further statistical information and continue discussions with the authorities on various aspects of the presentation and interpretation of Polish economic data, including those pertaining to the structure and historical evolution of the exchange and trade system.

As previously, the staff will emphasize the exploratory purpose of the visit and will not discuss matters relating to the possible size of Poland's quota or the timetable for the formal processing of Poland's application for readmission to the Fund, or possible use of Fund resources.

If asked about ~~the latter,~~ timetable the staff will respond that the situation will need to be reviewed at Fund headquarters following the second staff visit before any decisions are made.

→ MD 3/18

Office Memorandum

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1985 MAR 15 PM 5:04

OFFICE OF
THE MANAGING DIRECTOR

March 15, 1985

To: The Managing Director
The Deputy Managing Director

From: Brian Rose BR

Subject: Poland - Briefing Paper

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Attachment

cc: Mr. Collins

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

POLAND

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If asked about the ~~latter,~~ timetable the staff will respond that the situation will need to be reviewed at Fund headquarters following the second staff visit before any decisions are made.

Front Office

Poland: Questions for Discussion During IMF Staff Visit, March-April 1985

I. Prices

1. Please describe the objectives, instruments, and achievements of pricing policy in 1981-84 and plans for 1985. Please list the main commodity groups subject to administrative, regulated, and contract prices, respectively, and identify the contribution of each group to changes in the overall price level in each of the years 1982, 1983, and 1984. According to what criteria, on whose authority, and how frequently are administrative and regulated prices established and adjusted? What restrictions apply to changes in contract prices and what is their rationale? What would be the likely impact on the price level if all controls on contract prices were removed?

2. Please assess the relationship between the present structure of domestic prices and prices on international markets. For traded goods, please identify the major commodities or groups of commodities whose price in Poland differs substantially from that obtaining internationally. Please describe the extent and speed with which changes in international prices or the exchange rate for the zloty are passed through to (a) producer prices; (b) consumer prices; and (c) state procurement prices. Please identify constraints on this pass through. Please describe the method of operation and coverage of the price equalization fund.

3. Please assess the size and commodity composition of sales in the black market in relation to sales through legal channels and describe the relationship for selected major items of black market to official prices.

4. Please complete the attached tables 1 through 4.

II. Wages

1. Please describe the main objectives, instruments, and achievements of wage policy in 1981-84 and plans for 1985. Please provide data on the planned and actual percentage change in wage rates (including bonuses) for each year since 1981, and comment on the reasons for any differences. Please discuss the evolution of incomes in the socialized sector in relation to the nonsocialized sector since 1981.

2. Please identify major changes in the system of wage determination since 1981. How have the roles of the various levels of government, management, enterprise councils, and trade unions in this process changed? What proportion of enterprises have adopted new wage systems pursuant to the legislation introduced in January 1984 and what proportion of the work force do they cover? How do the adopted new wage systems differ from those previously in force? To what regulations are enterprises subject regarding wage scales and differentials?

3. Please describe in detail the operations of the Government Fund for Occupational Activity (FAZ), with particular reference to the rates applied, the basis on which they are levied, and the range of exemptions allowed. Which government agencies are responsible for setting and adjusting these terms? What share of enterprises are exempt from FAZ and in which sectors are they concentrated? Does FAZ apply to the private sector and, if so, at what rates? Please identify any major changes in the operation of FAZ since its introduction. What have been total annual payments of FAZ by enterprises and what share of these payments have been transferred to the state budget?

III. Money and Credit

1. Please provide data in the form of a consolidated balance sheet of the banking system and a monetary survey (see Tables 5 and 6). Please present foreign assets and liabilities in gross terms.

2. Please provide data showing the evolution of foreign assets and foreign liabilities of Bank Handlowy, the National Bank of Poland, and Bank Polska Kasa Opieki from 1980 to the latest available date. Are these banks obliged to keep any minimum foreign exchange reserves against their foreign exchange liabilities?

3. Please provide details of the new regulations governing deposits in and withdrawals from foreign exchange accounts.

4. Please complete the attached tables 7 and 8; the breakdown given is only a suggested one and should be modified as appropriate. What sectors and/or types of activity are extended credit at preferential rates? What is the share of credit received by enterprises at preferential rates? Do enterprises have to pay any noninterest charges on loans extended to them? When the schedule of interest rates is adjusted are the rates charged on existing loans similarly altered? What are the penalties levied on the late repayment of loans by enterprises?

5. Please complete the attached Table 9 on developments in the sectoral composition of bank credit.

6. Please comment on the relationship between changes in net credit to Government in the monetary accounts and the surplus or deficit recorded in the State's budgetary accounts.

7. Please provide a copy of the Bankruptcy Law which came into effect on October 1, 1983.

IV. Government Finance

1. Please describe any changes in the procedures for drawing up and implementing the central and local government budgets from the situation described in April 1982 in answers to questions from the IMF.

2. Please describe the expenditure responsibilities and revenue-raising authority of the central and local government, respectively. What revenues accrue directly to local governments? Please explain the rationale and modalities of the equalization payments between the central and local governments.

3. Please describe the main ways in which arrangements for paying profit tax (and, if applicable, other taxes, too) are adapted so as to encourage the development of particular sectors, e.g., the export sector.

4. Please list the major items subject to turnover tax and state the amount of revenue received from each in 1983 and 1984.

5. Please describe the considerations that have affected the level of tax and other payments from enterprises to the budget. What have been the objectives with regard to the impact of taxation on (a) the proportion of enterprise investment and working capital requirements met from own funds and bank credit, respectively, and (b) the need for subsidization of enterprises?

6. What part of government expenditures on capital formation is for government installations and infrastructure and what part finances enterprise investment? Under what circumstances does budgetary financing of enterprise investment occur and on what terms?

7. Please describe the rates and entitlement requirements for the main social benefits provided by the state. Please provide information on recent changes in social benefits.

8. Please list the main extrabudgetary funds maintained by the government. What are the rules governing transfers between these funds and the budget and where are the transfers reflected in the budgetary accounts?

9. Other questions on government finance may arise, for example in the light of information provided in the two tables--on revenues and expenditures--left during the February staff visit. Also we should like to discuss certain aspects of Table 10.

V. Aggregate Supply and Demand and Liquidity Overhang

1. Please describe in detail the methodology used in deriving the official estimates of the inflationary gap and overhang, with particular reference to the assumptions about the voluntary propensity to save and the manner in which it has evolved in recent years. Please explain how the analysis distinguishes between macroeconomic imbalances between aggregate demand and supply and the effects of shortages in particular markets at particular times. Please also describe any alternatives to the official methodology that are used in Poland to estimate the inflationary gap.

2. With reference to the table provided to the recent mission entitled "Income, Expenditure, and Financial Position of Households," please list and quantify the main components of the item "other incomes." At what exchange rate are foreign currency denominated components of this item converted into zlotys? To what extent do the data in this table reflect activity in the so-called "second economy?" Where is the dividing line drawn between legitimate private sector activity and the illegal second economy?

3. Further questions on the aggregate supply and demand situation may arise in the light of information provided in the two tables on the national accounts (SNA basis) left during the February staff visit.

VI. Investment and Enterprise Accounts

1. Please discuss the major targets, instruments, and achievements of investment policy in the period 1980-85 and plans for the period 1985-90 including an account of changes in sectoral priorities. Please identify any significant differences in the sectoral composition of investment projects carried over from before, say, 1980 and those started subsequently. In which sectors has the abandonment or postponement of carried-over projects been concentrated and at what level of government have the relevant decisions been taken? Please assess the reasons for the tendency for investment to exceed plan targets.

2. Please describe the considerations which determine the planned levels of expenditure in the Annual and Five Year Plans. How is the total allocated as between the government and enterprises? To what extent and how does the government control or influence the level of enterprise investment during a year and what agencies exercise these powers? Do investments subject to central control include items other than those covered by government contracts and operational programs? Do financing arrangements for centrally controlled investments of enterprises differ from those for other enterprise investments? To what extent does the central allocation of basic materials and the granting of import permits limit the scope of enterprises' effective autonomy in investment decision

making? Are there any limits on the size of investment projects which enterprises can initiate on their own authority? Are enterprises required to use any particular criteria in the appraisal of investment projects?

3. Please discuss the sources of investment financing in the socialized sector (see Table 11). What determines whether enterprise investment qualifies for budgetary financing and what are the terms of such financing? How much of their capital depreciation allowance are enterprises able to retain and may they use it at their own discretion? Please describe arrangements within an enterprise for deciding on allocation to the Development Fund and any restrictions on their use.

4. Please discuss recent developments in the amount and pattern of stockbuilding.

5. Other questions on enterprise finances may arise on the basis of information supplied in the table left during the February staff visit.

VII. Agriculture

1. Please describe the differences between state agricultural holdings, cooperative agricultural units, and agricultural associations both from the point of view of their institutional structure and legal status and from the point of view of the agricultural operations in which they each specialize. Please describe the legal status of private agricultural land holdings under the constitution. What limits are there (if any) on the size of private farms? Is it the government's policy to encourage an increase in the average size of private farms and, if so, how? Please describe the operations and policies of the State Agricultural Land Fund.

2. Please describe the main trends in cropping patterns and yields and in animal husbandry in recent years distinguishing, where appropriate, experience in the socialized and nonsocialized sectors. Please describe plans in these areas for the 1986-90 period and the policy instruments to be used to achieve them? What are likely to be the key constraints on agricultural growth? What steps are contemplated to improve storage and distribution facilities?

3. Please describe the distribution and marketing arrangements for agricultural products. What regulations, if any, apply to the quantity, destination, and timing of the sale of agricultural produce by producers? Please distinguish arrangements for the socialized and nonsocialized sectors where appropriate

4. Please evaluate the present structure of state procurement prices for agricultural products and identify any recent major changes. In particular, for each of the main crops please comment on the relationship between procurement prices and (i) production costs; (ii) prices for

comparable items in domestic markets; and (iii) prices for comparable products in world markets. For the latter, a comparison with the prices (in U.S. dollar or transferable ruble terms) actually recorded in Poland's recent international transactions would be useful. What restrictions, if any, apply to prices charged in private markets for agricultural produce?

5. Please describe the arrangements for the allocation of agricultural inputs. To what extent are these allocations subject to central control and which organs of the government exercise this control? What criteria do they apply? To what extent are agricultural inputs subsidized from the state budget? How have these subsidies evolved in recent years?

6. Please assess the effects of recent balance of payments difficulties on the agricultural sector. To what extent have imports of agricultural inputs been reduced? Have domestic substitutes been available? Please describe the recent performance of exports of Polish agricultural produce in foreign markets, both in socialist and nonsocialist countries. What have been the main constraints on such exports? What are the prospects for future growth?

VIII. Balance of Payments and External Debt

Please complete the attached Table 12. We should also like to clarify certain statistical information supplied in February and discuss the most recent developments in the external situation.

IX. The Exchange and Trade System

A. Exchange arrangements

1. Please supply one set of exchange rate bulletins issued by the National Bank since January 1, 1982. Please provide buying and selling rates for different types of transactions, spot and forward (e.g., telegraphic transfers, clean-documentary, delivery rates, bills of collection, travelers checks, currency notes, etc.).

2. Which entities are authorized to engage in foreign exchange transactions with the public (e.g., the Polish National Bank, the Bank for Foreign Trade, the Bank Polska Kasa Opieki, S.A., ORBIS, etc.)? What is the role played by other entities such as Pewex, Cepelia, or Desa chains which are permitted to sell their merchandise against convertible currency. How are the spreads between buying and selling exchange rates presently determined? Are there any other spreads, agios or commissions, prescribed for institutions other than the buying/selling spreads of the National Bank? Please provide a table of commissions and charges currently being applied by banks to foreign and domestic customers.

3. We understand that consideration is given to adjustment of the foreign exchange value of the zloty whenever domestic prices relative to export prices change by more than 5 percent; what are the relevant price indices used in this computation?

4. What exchange rates are currently quoted for the currencies of the CMEA and other socialist countries? On what basis are these rates determined? How frequently are such rates changed? What rates are used for trade transactions (including any foreign trade multipliers) and noncommercial transactions? Are any other exchange rates applied such as, for example, rates for capital transactions relating to the functioning of joint enterprises, including the "mixed companies with foreign capital shares"?

6. Are forward exchange rates quoted for the zloty? If so, by which institution(s) and how are such rates determined, and for what transactions is forward cover available?

7. Are any taxes or subsidies applied to the purchase or sale of foreign exchange by private individuals, enterprises, or others? If so, please describe all such arrangements now in force.

B. Exchange Controls

1. Please supply the texts of the basic and supplementary laws currently governing exchange controls, together with any implementing regulations, including general instructions (e.g., circulars) to banks and enterprises.

2. Please describe the foreign exchange plan or budget (if any) and the principles and priorities governing foreign exchange allocation.

3. Please supply a list of all bilateral payments agreements and details of all such agreements with Fund members, including original dates of entry into force, balances outstanding as of the latest available date, the size of swing credit limits, and settlement provisions. What are the policies of the Polish authorities with respect to such agreements? Please describe the present system of settlements with CMEA member countries.

4. Please describe the present arrangements whereby resident individuals and enterprises are permitted to hold foreign currency and resident accounts in foreign convertible currencies. Please provide the regulations governing this subject, including repatriation and surrender requirements, retention quotas, and the use that may be made of any foreign exchange accounts. What criteria are taken into account in determining the enterprises eligible to retain a proportion of their export receipts and what factors determine the magnitude of the export retention quotas for individual enterprises? Do separate regulations govern the holding of convertible and nonconvertible currencies? Please describe the foreign exchange operations authorized for the Bank Polska Kasa Opieki, S.A. and for ORBIS.

5. What categories of accounts in domestic or foreign currency may be maintained by nonresidents? What transactions are permitted on these accounts and which payments can nonresidents make and receive in zlotys?

6. Does an import license still provide an automatic authorization to effect settlements to a foreign supplier, or must an exchange license now be obtained additionally? If so, what are the regulations governing the issuing of exchange licenses?

7. Are imports of consumer and other nonessential goods (and related services) from the convertible currency area subject to a quota in value terms? If so, what has been the annual values of the quota in the years from 1982 to 1985?

8. Please provide any regulations governing payments and receipts, for invisible items (in addition to those mentioned in answer to staff questionnaire in April 1982). How are the following treated for both convertible and nonconvertible payments (indicate any quantitative limits where applicable): (a) payments related to merchandise trade (e.g., insurance, warehousing, customs charges); (b) freight charges; (c) insurance premia (general, life, accident, reinsurance); (d) other services (e.g., repairs abroad, technical assistance, professional services, royalties, rental, advertising expenses, subscriptions); (e) private expenditure (business and tourist travel expenses, study abroad, medical treatment, group travel, transportation tickets, family support payments, remittances

of emigrants); (f) government and diplomatic missions' expenditure and payments to international organizations; (g) income from investments, amortization of loans and depreciation payments (primarily on joint venture assets); (h) transfer payments arising from salaries and earnings of foreigners working in Poland and transfer receipts from earnings of Poles employed abroad; and (i) other payments?

9. Please describe the system whereby amounts of convertible currency can be purchased through so-called "effectiveness bids."

10. Please supply an update since April 1982 of any new regulations governing the import and export of Polish and foreign banknotes?

11. What are the present regulations governing the import, export, and holding of gold? Have there been any changes since April 1982 affecting the setting of official prices for gold?

C. Trade Controls

1. Please comment on any changes in legislation after the law of February 10, 1982 determining which Polish entities are permitted to import and export?

2. Please update the basic laws governing foreign trade, trade licensing, and customs duties beyong those mentioned to the staff in the answers to questionnaire (April 1982).

3. Please describe the present import licensing system. Which imports are prohibited (by commodity or by country) and what is the reason for such prohibition? Please provide the details of special regulations regarding imports for export after processing or for re-export.

4. Please provide the current tariff schedule and outline any taxes currently applied to foreign trade besides those included in that schedule.

5. Please describe the present system of subsidizing imports and exports.

6. Please outline the equalization system that is maintained in order that imported goods should be resold at domestic prices?

7. Are there any export restrictions and, if so, for what reason?

8. Please outline incentive schemes for exports currently in force?

9. What rules presently govern imports and exports by individuals?

E. Foreign direct investments

Please provide the text of any new laws or regulations governing foreign direct investment or joint ventures in Poland since March 1982, and recent data on volume and types of such transactions.

X. Meetings with Enterprise Managements

Our overall objective is to better understand the motivation of, and constraints on, enterprise behavior and the policy variables to which enterprises are responsive. More specifically, we would like to focus on the following areas although, of course, not all questions will be relevant to all enterprises:

- Choice of output (type, quantity, quality, etc.) and flexibility of output decisions.

- Exporting: incentives to export versus domestic sales; the pricing of exports; experience with the foreign exchange retention scheme; relations with foreign customers, Polish foreign trade organizations, and the Bank Handlowy.

- Domestic sales--relations with customers; marketing channels.

- Access to inputs, both domestic and imported.

- Pricing decisions; procedures for changing prices; access to price subsidies.

- Investment: criteria for project selection; access to and terms of different sources of financing; relations with the banking system.

- Use of profits; allocations between different funds; the role of management, enterprise councils, and trade unions.

- Wage determination (including bonuses and earnings of management); the effects of recent legislation regarding wage structures.

- Taxation; determination of tax rates and exemptions; responsiveness to taxation arrangements.

- Relations with founding bodies, specialized ministries, and enterprise associations; experience with operational programs and government contracts.

XI. Meetings with Economic Research Institutes

In these meetings we would like to explore various conceptual issues, including some related to the interpretation of data. While other issues may arise in the course of our discussions that could be explored with the Institutes, the following are some of the main topics that we would initially like to cover:

- Measurement and significance of the inflationary overhang.

- The amount, role, sources and uses of foreign exchange held by the population.

- The "second" economy: measurement of the volume of activity and prices; influences on the scale and character of "second economy" transactions; its significance for the formulation of economic policy.

- Incentives and disincentives to/constraints on greater economic efficiency.

- Methodology for converting transactions with socialist countries in transferable roubles into meaningful U.S. dollar equivalents.

- A comparison of the relative attractiveness to Polish producers of exporting to the convertible and nonconvertible currency areas, respectively, taking account of price and nonprice factors; the influence of the exchange rate on foreign exchange flows.

- The derivation of unit value and volume series for exports and imports with the convertible and nonconvertible areas, respectively; an appraisal of the data currently available.

- A general appraisal of the coverage of data pertaining to the domestic economy, especially financial and price data.

Table 1. Poland: Distribution of Prices by Category, 1982-85

(In percent of the total value of sales for the relevant items covered by each category of prices, respectively)

			Administrative Prices	Regulated Prices	Contract Prices
Prices for consumer goods and services - total		1982			
		1983			
		1984			
	Plan	1985			
Of which:					
Foodstuffs		1982			
		1983			
		1984			
	Plan	1985			
Producer prices - total 1/		1982			
		1983			
		1984			
	Plan	1985			
Of which:					
Agricultural items		1982			
		1983			
		1984			
	Plan	1985			
Manufactured goods		1982			
		1983			
		1984			
	Plan	1985			

Source: Data provided by the Polish authorities.

1/ Producer prices are prices received by production units for their output.

Table 2. Poland: Selected Indicators of Price Changes

(In annual percentage changes)

	1978	1979	1980	1981	1982	1983	1984	Plan 1985
Implicit price deflator of gross material product				21.9	118.9	16.6		
Retail price index								
Of which: foodstuffs	(7.4)	(7.4)	(12.8)	(22.5)	(136.3)	(11.9)		
Cost of living index of households of employees in the socialist sector								
Of which: foodstuffs								
Producer prices 1/								
Industry								
Food processing								
Electro-engineering								
Energy								
Metallurgy								
Chemicals								
Minerals								
Textiles and leather products								
Wood and paper								
Construction								
Agriculture								
Forestry								
Transport and communications								
Trade								
Other								
Prices of industrial inputs 2/								
Of which:								
Energy								

Source: Data provided by the Polish authorities.

1/ Producer prices are prices received by production units for their output. Please use an alternative sectoral breakdown if this is more convenient for providing data corresponding to the above definition.

2/ This item is intended to capture movements in the prices of major inputs used by the industrial sector. If data cannot be supplied in index form please supply prices of specific major items.

Table 3. Poland: Subsidies of Selected Retail Products, 1980-84

(In percent of total final expenditure on the relevant products, unless otherwise indicated)

	1980	1981	1982	1983: In percent of total expenditure on the relevant products	1983: In billions of zlotys	1984: In percent of total expenditure on the relevant products	1984: In billions of zlotys
Foodstuffs							
Meat and meat products							
Dairy products							
Eggs							
Grain products							
Sugar							
Fish and fish products							
Potatoes							
Vegetables							
Clothing and footwear							
Furniture							
Energy and transportation							
Rail transport							
Bus transport							
Coal							
Coke							
Household heating							
Fuel for transport							

Source: Data provided by the Polish authorities.

Note: The data requested in this table are intended to capture the direct subsidization of items of final expenditure by the population, i.e., the difference between the price paid by the consumer and that received by the producer, (as opposed to the subsidization of industrial inputs or of the general losses of enterprises). The breakdown given is only a suggested one and should be modified as appropriate.

Table 4. Poland: Subsidies of Selected Production Inputs

(In percent of total expenditure on the relevant inputs)

	1980	1981	1982	1983	1984
Primary material inputs used by the manufacturing sector					
Of which:					
Energy					
Material inputs used by the agricultural sector					
Of which:					
Fertilizer					
Animal feed					
Energy					
Water supplies					
Agricultural equipment					
Other					

Source: Data provided by the Polish authorities.

Note: The data requested in this table are intended to capture the subsidization of material inputs used in the manufacturing and agricultural sectors, i.e., the difference between the cost of production or import cost and the price paid by the user (as opposed to subsidies targeted at specific final goods to cover the general losses of enterprises). The breakdown given is only a suggested one and should be modified as appropriate.

Table 5. Poland: Consolidated Balance Sheet of the Banking System 1/

(In billions of zlotys)

	1970	1975	1980	1981	1982	1983	1984	Official Forecast 1985
Assets								
Credits to the socialized sector	535.3	1,509.4	3,079.7	3,305.0	3,788.0	4,145.7	4,538.6	4,902.7
Operational credits								
Investment credits								
Credits to nonsocialized entities	41.8		109.7	116.3	147.6	175.7	209.8	257.8
Agriculture	40.8		107.3	113.3	140.3	162.5		
Operational credits	(29.2)		(35.4)	(37.7)	(43.4)	(43.2)		
Investment credits	(11.6)		(71.9)	(75.6)	(96.9)	(119.3)		
Nonagricultural small enterprises	1.0		2.4	3.0	7.3	13.1		
Credits to households	20.9		46.5	48.4	76.0	119.2	162.5	211.0
Installment purchases of goods and services	(11.8)		(18.6)	(18.7)	(40.5)	(66.6)		
Housing (construction and repair)	(9.1)		(27.3)	(28.5)	(34.1)	(50.6)		
Other	(--)		(0.6)	(1.2)	(1.4)	(2.0)		
Credits to general government				195.0	216.0	319.3		
Other domestic assets								
Foreign assets								
Liabilities								
Resources of the socialized sector								
Cash holdings	5.1	13.5	30.7	38.3	51.2	67.5	74.3	84.5
Demand deposits	59.5	158.3	245.5	322.2	486.6	531.8	660.8	771.8
Special accounts	45.2	150.3	253.2	262.0	364.6	421.6	564.6	671.6
Investment accounts	110.9	159.5	186.2	197.9	188.5	182.2	188.8	242.2
Resources of the private sector								
Cash holdings 2/	53.5	127.7	266.0	370.7	564.2	663.1	764.3	845.6
Demand deposits 3/	2.6		6.9	13.8	13.9	17.3	23.7	...
Savings deposits	114.8		492.9	664.7	866.9	1,058.2	1,237.2	1,453.0
Resources of financial institutions								
Deposits of the State Insurance Institute	--	--	39.5	45.8	55.1	70.7	92.3	100.7
Bank's own funds	27.4	63.6	98.3	97.6	110.3	174.2		
Interbank and interdepartment settlements	22.2		79.1	147.4	225.3	268.4		
Centralized settlement accounts	--	--	--	--	4.8	--		
Earmarked state budget deposits	148.6	210.5	498.8	370.5	198.6	226.9		
Ordinary state budget deposits								
The State Fund for Occupational Activization					24.2	40.5		
Foreign liabilities or foreign operation accounts	10.5		1,142.6	1,460.3	2,086.0 4/	2,280.1 4/	4/	
Other liabilities	0.5	4.5	18.2	5.3	29.5	290.7		
Total liabilities = total assets								

Sources: Central Statistical Office, Concise Statistical Yearbook of Poland, 1984; and data provided by the Polish authorities.

1/ Derived from the balance sheets of the National Bank of Poland, Bank Handlowy Warsaw, the Bank of the Food Economy, and the Bank PKO.

2/ Excluding holdings at cash offices of socialist units.

3/ Since 1982 includes resources of foreign enterprises and other accounts in Bank Handlowy Warsaw.

4/ Includes long-term settlements due to changes in conversion rates of Zl 787.1 billion in 1982, of Zl 1,006.5 billion in 1983, and of Zl .... billion in 1984.

Table 6. Poland: Monetary Survey 1/

(Outstanding in billions of zlotys)

	1980	1981	1982	1983	1984	Official Plan 1985
1. Foreign assets						
2. Domestic credit	2,737.1	3,314.2	4,029.0	4,332.9	5,150.8	5,661.5
Claims on General Government (net)	-498.8	-175.5	17.4	92.3	239.9	290.0
Claims on rest of domestic economy	3,235.9	3,489.7	4,011.6	4,440.6	4,910.9	5,371.5
3. Broad money (= 1+2+4+5)						
Money	549.1	745.0	1,115.9	1,279.7	1,523.1	1,711.9
Quasi-money holdings 2/						
4. Foreign liabilities	--	--	--	--	--	--
5. Other items (net)						

Sources: Data supplied by the Polish authorities.

1/ Derived from a consolidation of the balance sheets of the monetary institutions--the National Bank of Poland, the Bank of the Food Economy, Bank Handlowy Warsaw, and the Bank PKO.

2/ Should include savings and fixed-term deposits of households, socialized entities, and other entities.

Table 7. Poland: Interest Rates on Bank Credits 1/

(In percent per annum)

	End of period					
	1980	1981	1982	1983	1984	Latest 2/
Credits for socialized economy						
Investment credits for enterprises						
Of which:						
Central						
Enterprises						
Investment credits for housing cooperatives						
Operating credits						
Of which to:						
State enterprises						
Cooperatives						
Credits for nonsocialized economy						
Agricultural credits						
Of which:						
Investment						
Operating						
Nonagricultural credits						
Credits for households						
Installment purchases of goods and services						
Housing						
Credits for financing state budget deficit						

Source: Data provided by the Polish authorities.

1/ Please indicate main exceptions to interest rates indicated for particular categories.
2/ Latest date for which interest rate information is available.

Table 8. Poland: Interest Rates on Bank Deposits

(In percent per annum)

	End of period					
	1980	1981	1982	1983	1984	Latest 1/
Deposits with the Polish National Bank of Poland						
Demand deposits						
- Households						
- Enterprises						
Time deposits of households fixed for at least:						
- Six months						
- One year						
- Two years						
- Three years						
Time deposits of enterprises fixed for at least:						
- Six months						
- One year						
- Two years						
- Three years						
Five-year premium interest-bearing accounts						
Housing deposits						
Advanced payments for car purchases						
Premium bonds						
Deposits with the Bank of Food Economy						
Demand deposits						
Saving deposits						
Fixed deposits representing advanced payments for cars						
Other fixed deposits						

Source: Data provided by the Polish authorities.

1/ Latest date for which information is available.

Table 9. Poland: Medium- and Long-Term Investment Credits from Banks

(Outstanding in billions of zlotys)

End of Period	1980	1981	1982	1983	1984
Investment credits					
To enterprises					
To cooperatives					
To nonsocialist entities					
Investment credits					
To industry					
Mining					
Engineering					
Light industry					
Metallurgy					
Chemicals					
Food processing					
Other					
To nonindustrial activities					
Of which: Agriculture					

Source: Data provided by the Polish authorities.

Table 10. Poland: Grants and Payments from State Budget

(In billions of zlotys)

	1978	1980	1981	1982	1983	1984	Plan 1985
Total	599	799	953	1,249	1,136		
Of which: From state budget	(565)	(753)	(891)	(1,080)	(955)		
A. Paid to enterprises	515	657	784	894	800		
1. Noncommodity specific ("subjective")	36	90	157	72	22		
2. Commodity specific ("objective")	231	272	323	525	466		
(i) For consumer items	137	172	223	253	276		
a. Foodstuffs	133	164	213	211	236		
Of which:							
Meat and meat products	(62)	(66)	(72)	(57)	(39)		
Dairy products	(32)	(44)	(73)	(79)	(98)		
Cereals	(14)	(18)	(14)	(45)	(74)		
Sugar	(12)	(13)	(16)	(7)	(8)		
Fish and fish products	(9)	(13)	(15)	(9)	(5)		
Edible oil and related products	(--)	(2)	(5)	(8)	(5)		
b. Nonfood items	3	8	9	43	41		
Of which:							
Coal and coke	(--)	(5)	(6)	(38)	(36)		
Childrens' clothing and footwear	(1)	(1)	(1)	(3)	(3)		
(ii) Agricultural inputs	16	32	18	30	30		
Of which:							
Grain (for animal feed)	(13)	(23)	(9)	(6)	(5)		
Mineral fertilizer	(3)	(4)	(6)	(16)	(23)		
Machinery and implements	(--)	(1)	(--)	(3)	(--)		
Seeds	(--)	(4)	(3)	(3)	(--)		
Plant protection	(--)	(--)	(--)	(1)	(1)		
(iii) Transport and community services	25	47	65	174	58		
Of which:							
Bus services	(2)	(6)	(10)	(32)	(13)		
Railways	(5)	(16)	(23)	(52)	(44)		
(iv) Construction materials	29	7	6	1	—		
Of which: Cement and concrete	(4)	(4)	(4)	(1)	(--)		
(v) Other	...	14	10	67	102		
Of which:							
Raw materials for light and chemical industries	(...)	(12)	(8)	(12)	(11)		
Hard and brown coal	(...)	(--)	(--)	(28)	(38)		
Land transport	(...)	(1)	(1)	(2)	(2)		
Transport by PKP and PKS	(...)	(--)	(--)	(14)	(44)		
Of which: PKS	...	--	--	1	--		
Other transport (express cars)	(...)	(--)	(--)	(6)	(--)		
3. For investment and other purposes	248	294	304	297	312		
Of which:							
Agriculture	(46)	(38)	(29)	(22)	(37)		
Import and export settlements	(150)	(249)	(267)	(220)	(139)		
B. To Other Units	84	143	169	356	336		
Of which: To budgetary units	(57)	(73)	(96)	(236)	(257)		

Source: Rozcnik Statystyczny, 1984, Table (129), page 92.

Table 11. Poland: The Distribution, Financing, and Composition of Investment, 1978-85 1/

(In billions of zloty at current prices)

	1980	1981	1982	1983	1984	Plan 1985
Total investment						
Socialized sector			( )	( )	( )	
State entities 2/			( )	( )	( )	
Local authorities 2/			( )	( )	( )	
Cooperative residential construction 2/			( )	( )	( )	
Financed by:						
State budget						
Bank credits						
Own resources						
Other						
Socialized enterprises 2/			( )	( )	( )	
Financed by:						
State budget						
Bank credits						
Own resources						
Other						
Other 2/						
Nonsocialized sector						
Investment classified by type						
Construction and assembly						
Of which: Socialized sector						
Machinery and equipment						
Of which: Socialized sector						
Memorandum items:						
Expenditure on projects started before 1980						
Of which: By socialized enterprises						
Total cost of investment projects started in each year						
Expenditure in each year on investment projects started in that year						

Source: Data supplied by the Polish authorities.

1/ For the years for which parentheses are included please provide the originally planned figures in the parentheses as well as actual realizations.
2/ Please define the institutions included in each category.

Table 12. Poland: International Reserves and Other Foreign Assets of the Banking System and Other Official Institutions

(In millions of U.S. dollars)

At End of Period	1979	1980	1981	1982	1983	1984 1/
International reserves in convertible currencies 2/						
Gold 3/						
Foreign exchange						
Held by National Bank of Poland						
Held by other banks						
Other 4/						
Other foreign assets 2/						
Convertible currencies						
Held by National Bank of Poland						
Held by other banks						
Other 4/						
Nonconvertible currencies						
Held by National Bank of Poland						
Held by other banks						
Other 4/						
Total international reserves and other foreign assets						

Source:

1/ Please specify the exchange rates used for the conversion of the various items into U.S. dollars at end-1984.
2/ Please describe the criteria which determine whether or not a particular foreign asset is included in international reserves.
3/ For each date specify the U.S. dollar valuation of gold in terms of troy ounces.
4/ Please specify the institutions which hold the assets in question.

Front Office

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 1
Held at the Foreign Trade Research Institute
on March 26, 1985, at 9:00 a.m.

Polish representatives

Foreign Trade Research Institute

Mr. Aleksander Czepurko, Deputy Director
Dr. Jan Bossak, Secretary
Dr. Ryszord Michalski
Dr. Juliusz Kontynski

Ministry of Finance

Mr. Ilczek

Fund representatives

Mr. Hole
Mr. Manison
Mr. Prust
Mr. Boonekamp
Ms. Swiderski

1. Methodology for computing external accounts transactions

Mr. Kontynski said that customs data for exports and import transactions with the convertible currency area reflected current exchange rate quotations. For example, an export invoiced in deutsche marks was converted into zlotys at the actual exchange rate for the transaction and for purposes of aggregated customs data was converted into U.S. dollars at average exchange rates over brief periods of time such as one week. Balance of payments data and customs data for yearly series were, however, constructed on the basis of longer-period averages for U.S. dollar/zloty exchange rates (usually quarterly averages). Discrepancies between customs and balance of payments data largely arose from leads and lags in payments. For example, in 1982 substantial payments advances had to be made to overseas suppliers for imports. Such advances had subsequently decreased and divergences between payments and customs data were narrowing.

In transactions with the so-called "first payments area" (namely CMEA countries) trade mostly took the form of balanced bilateral deals. Prices for raw materials were determined largely on the basis of five-year moving averages of world prices for particular commodities. Of course, these prices were sometimes affected by bilateral negotiations. For manufactured goods the prices determined in trade arrangements with CMEA partners reflected to a large extent the outcome of bilateral bargaining. Polish trade with CMEA partners settled in convertible currencies was relatively small and decreasing. Unlike Hungary, which sold meat and other agricultural commodities directly to the CMEA area for convertible currencies, Poland was not well endowed with such exportables.

In aggregating data on trade for transactions with the convertible and nonconvertible currency areas, there were a number of problems and no ideal solution. Firstly, prices of the same commodities traded in the two areas were in a number of cases significantly different. Secondly, trade transactions in transferable roubles with the CMEA countries were converted into U.S. dollars at the cross rate between the U.S. dollar and the rouble rather than at the U.S. dollar/transferable rouble rate published by the IBEC.

Another statistical problem--this time for time series analysis--related to the break in the series for balance of payments transactions after 1981. In 1981 and earlier years foreign transactions invoiced in various currencies had been converted into foreign exchange zlotys at exchange rates which bore no relation with actual transaction exchange rates, whereas after 1981 the conversion had been done at the uniform exchange rate. The Polish representatives in undertaking time series' analysis tended to use volume rather than current price data. This was relatively easy in the case of homogenous commodities like fuel where precise physical measurements could be made, but difficulties arose where commodities were more heterogenous and where the geographical composition of trade had changed. Attempting time series analysis for the more aggregated variables, was thus considered a very questionable exercise. Apart from these special difficulties the representatives of the Foreign Trade Research Institute viewed Polish foreign trade data, including volume and unit value indices as being of a sound quality.

2. Exchange rate and equalization accounts

Under the present system an exchange equalization account was used to bring the effective prices of a considerable proportion of external transactions into line with domestic prices, especially officially administered prices. In 1982 substantial imports of wheat took place at prices below domestic prices. Taxes were levied on such imports to reduce the profits of importers. Accordingly, for 1982 it was difficult to say whether importers and exporters overall faced a more overvalued zloty after the levying of taxes and payment of subsidies through the equalization account. However, since then subsidies from this account have tended to dominate and consequently in this sense the effective exchange rate for the zloty could be considered to be overvalued, perhaps by 10 percent to 15 percent. There was widespread use of the domestic price structure to stimulate exports in that export receipts in zlotys were enhanced by subsidies paid out by the Ministry of Foreign Trade. However, because of high profit taxes the net amount of payments was substantially less. Under the economic reforms enterprises were to be largely left alone to decide where to direct their production and to negotiate prices of external transactions. There were of course commodities such as coal where the domestic selling price and effective price from selling exports were deliberately set below the cost of production.

Mr. Hole raised the question of where the Polish representatives drew the line in deciding on whether an export transaction should be taxed or subsidized. Dr. Michalski said that it was done on a transaction-by-transaction basis. In certain cases, where exporters enjoyed a monopoly position taxes were levied. However, the present exchange rate policy was considered as being "too timid," in that it was not serving as the main stimulus to exports. The Polish representatives agreed with the assessment of Mr. Hole that the effect of exchange rate changes were difficult to determine, but were probably not very significant in view of the vast array of subsidies and taxes that influenced the effective return obtained by enterprises from export transactions.

3. Export retention scheme

Mr. Michalski said that the scheme whereby producers could retain on average 20 percent of their foreign exchange receipts from exporting to the c.c. area served a feeding function in that such enterprises were virtually assured a source of foreign exchange. It also helped to limit the system whereby foreign exchange was centrally allocated. However, the scheme often stimulated exports in an adverse way in so far as inefficient producers often directed as much production as possible to exports in order just to obtain foreign exchange. This meant that foreign exchange was often used up in maintaining current operations of inefficient export producers and/or in fostering import-intensive export industries, rather than being used to help shift and provide resources for enterprises with a potentially greater comparative advantage.

Under the foreign exchange retention scheme producing enterprises did not have an automatic right to the foreign exchange they had earned from exporting. Enterprises only had a preferential claim on the retention deposits held at Bank Handlowy. These deposits constituted a pool and were not earmarked for each individual enterprise participating in the scheme. If an enterprise wished to import using foreign exchange held under the scheme it had to apply for an import license from the Ministry of Trade. If successful it thereafter would have preferential access to use of the pool of foreign exchange under the retention scheme.

Mr. Hole asked about the possibilities for liberalizing the export retention scheme. The Polish representatives thought that it would be preferable if enterprises could hold foreign exchange on their own account under the scheme and be in a position to freely sell it at commercial exchange rates. There could be a market in rights to foreign exchange, for example, in so-called dollar bonds. However, such a liberalization was likely to be resisted by the authorities, particularly the branch associations, as they might wish to maintain or even regain their previous power to distribute foreign exchange.

During 1984 there had been small-scale auctions for foreign exchange allowing enterprises or cooperatives not eligible for foreign exchange under the export retention scheme to bid for foreign exchange at the uniform commercial rate. These auctions had not been successful and only very small amounts of foreign exchange had been made available.

It was noted that the determination of foreign exchange retention quotas for particular enterprises was on an enterprise-by-enterprise basis and determined on the basis of transaction prices. The percentage of imports financed under the retention scheme had increased from 7 percent in 1982 to 19 percent in 1984.

4. Other export incentives

The Polish representatives said tax rebates, and the provision of various types of management and employee bonuses were given for exporting. These incentives were mainly applied for exporting to the convertible currency area. Generally, few problems were encountered in increasing exports to the CMEA area; at times, demand from the internal market pre-empted exports to the nonconvertible area, while at other times the U.S.S.R. refused to take excess supplies from Poland.

5. Recent foreign trade developments and prospects

Export volume to both the convertible currency and nonconvertible currency area had increased at rapid rates in 1984. Coal exports had reached a record level of 43 million tons, of which 29 million tons went to Western countries. This constituted a ceiling level for coal exports which was unlikely to be exceeded, especially with the recovery of internal demand and the depletion of stocks as a result of the recent severe winter. There was, however, some prospect that world market prices for coal might recover from their present low level. Agricultural products, mainly in the form of processed foodstuffs, vegetables and sugar beet together with alcoholic drinks and copper, offered some scope for moderate export expansion. Exports to certain developing countries such as India and in Latin America offered good prospects. However, performance with respect to exports of manufactured goods to the convertible currency area were likely to continue to be disappointing. Overall, the volume of exports to that payments area was expected to rise by 3-4 percent in 1985, while prices were estimated to rise by 4-5 percent in U.S. dollar terms. The deterioration in the terms of trade with the convertible currency area was expected to moderate and the terms of trade with the CMEA area were forecast to show little change. Prospects for increasing receipts from Polish construction projects abroad were also regarded as favorable. In sum, Mr. Kontynski predicted a US$1.5 billion trade surplus with the convertible currency area in 1985. In physical terms, there was further scope for substituting imports from the convertible currency area with imports from CMEA countries. However, such continued substitution had become very difficult financially as Polish debt to the U.S.S.R. had shown a considerable rise in recent years.

The meeting adjourned at 11:00 a.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 2
Held at the Office of the Deputy Minister for Economic Reform
on March 26, 1985 at 11:00 a.m.

Polish Representatives	Fund Representatives
Professor Sadowski, Deputy Minister for Economic Reform	Mr. Hole
Mr. Stypulkowski, Advisor to the Deputy Minister	Mr. Manison
Mr. Ilczek, Ministry of Finance	Mr. Prust
	Ms. Swiderski
	Mr. Boonekamp

Mr. Hole noted that the outside observer was forcibly struck by the many constraints on the process of economic reform. He wondered whether the official intention was to move gradually on all fronts or to move only on a smaller number of fronts but somewhat more rapidly. In particular, he wondered how this strategic decision affected pricing policy.

Prof. Sadowski replied that the original intention had been to attack the question of pricing policy on a broad front. Partly this reflected the experience of previous attempts at economic reform which had failed largely because there had been an excessive concentration on changing the operation of enterprises with inadequate attention to changing the environment in which they operated. Regarding the latter, it was particularly important to break the bureaucratic hierarchy within which enterprises had traditionally operated. Against this background preparatory work on price reforms, particularly for basic materials and intermediate goods, had been started in 1980 and completed in 1981. The date for introduction of the new price measures--January 1, 1982--coincided with the launching of numerous other measures and had been unfortunate in that it came at a time of falling output and productivity. The unified commercial exchange rate that had initially been selected--Zl 50 = US$1--had soon become obsolete. This presented the authorities with a choice between persevering with an unrealistic exchange rate or moving to a more depreciated rate and making the necessary corresponding adjustments in domestic prices. In the event a compromise solution was adopted which involved moving to an exchange rate of Zl 90 = US$1 but, for fear of the inflationary consequences of doing otherwise, leaving domestic prices unchanged. As a result the actual commercial exchange rate differed substantially from the typical ratio of domestic to foreign prices. Subsequently, there had been a gradual adjustment of both prices and the exchange rate which, with various ups and downs, had by the beginning of 1985 resulted in a somewhat improved alignment of the two.

The adjustment of consumer prices had started in 1981 but was only limited because of opposition from the trade unions. The first major changes were made in February 1982 when food prices rose on average by 135 percent. At the same time the whole price system was reformed with a viewing to giving it greater flexibility and all prices were classified in one of three groups--administered, regulated, and contract. In the event when contract prices (which, in principle, were to be determined by market forces) started to rise (especially for motorcars and consumer durables) there was a public outcry. The scope of administered and regulated prices was increased and limits were placed on increases in contract prices. The monopolistic structure of industry had been harmful in moving to freely determined contract prices. The increase in the relative importance of regulated prices, which at one point covered 15 percent of sales, was particularly inimical to the reform because regulated prices were determined on a "cost plus" principle. The importance of regulated prices had since declined: they currently cover only about 3 percent of total sales with other sales split roughly evenly between administered and contract prices.

Turning to the present situation, Prof. Sadowski said that there was general public resistance to price change. People preferred the combination of queues and low prices to no queues and higher prices. There was little popular faith in the benefits of free markets, and so far events had not produced any spectacular demonstration of these benefits. There had, however, been a modest success in bringing down egg prices following the breaking of a monopoly in the egg market. In addition, the market for fruit and vegetables worked satisfactorily on a more or less freely competitive basis. But even this brought the complaint that some people were allowed to make too much money. The main controlled prices at present were those for foodstuffs and consumer durables. However, within these and other broad categories of price-controlled items, the authorities were allowing increases in the prices of higher quality goods.

Mr. Hole observed that the situation which Prof. Sadowski had described pointed to the importance of reducing the element of monopoly in the Polish economic structure and maintaining tight and well-coordinated monetary and fiscal policies while allowing the latter to have their full potential impact. Prof. Sadowski replied that the importance of policies in these areas was well realized by the authorities and, in this connection, he described the implementation of the Bankruptcy Law. Three firms had been bankrupt and over 1,000 had recovery programs of which 500 were accounted for by state enterprises and the rest by cooperative ventures. Management had been changed in 11 state enterprises of medium size or larger which had not been successful in implementing recovery programs under their original managements. A major problem remained the ability of unprofitable large firms to stave off both having to improve their performance and bankruptcy; the availability of financing from the budget was important in this context.

Prof. Sadowski went on to describe the authorities' attempts to achieve greater uniformity in the tax system. He wanted to see tax reductions and exemptions to be based on a solid legal basis--as was now the case for the encouragement to investment and exporting given through the profit tax regime--rather than being simply arbitrary. Prof. Sadowski described some of the problems that arose in the administration of the FAZ. There was a question as to the justification for the differentiation in coefficients (relating output (value added) increases to permissible FAZ-exempt earnings increases) as between different enterprises and sectors. Generally, these coefficients ranged from 0.5 to 0.8 but in some exceptional cases in the service sector were equal to one. The coefficients were set in the annual plan but, within limits, there was scope for ministries to adjust them and to grant exemptions in the course of the year. Particularly favorable treatment had been given to enterprises whose output had risen, but this could produce anomalous results because enterprises whose output had fallen most sharply in the crisis years were sometimes those who could recover most easily thereafter. In view of this, the rules had been changed in 1983 and 1984 so as to give more favorable treatment to those who had been most successful in maintaining their output during the crisis. Another difficulty that arose in the administration of the FAZ was the need to give some special treatment to agricultural and fishing sectors because of the inevitable fluctuations in their output. A further difficulty lay in the definition of valued added: in principle the FAZ-exempt increase in earnings was the product of a specified coefficient and the change in value added at constant prices. In some cases the latter could not be satisfactorily measured and it had been necessary to use sales value or a measure of physical output. Neither was very satisfactory in that their use reduced the incentive to cut costs of production. Moreover, physical output volume was often extremely hard to measure on a consistent basis, even for supposedly homogeneous commodities. Prof. Sadowski said that the authorities wanted to make improvements in the operation of the FAZ in the coming quinquennium. One of the desired changes was a greater provision for exemption from FAZ for cost of living-related increases in earnings.

Prof. Sadowski described various meaasures to reduce the degree of monopoly in the Polish economy. The authorities wished to encourage the growth of small and medium scale enterprises. At present the relevant incentives were not adequate and, in Prof. Sadowski's private view, three-year tax holidays should be introduced to improve them. At the same time, greater integration was needed in some sectors and a new law was being prepared that would facilitate the creation of joint ventures between domestic enterprises--whether state-owned, cooperative, or private--or between domestic enterprises and foreign partners. A law was also being prepared to prevent the abuse of monopoly power. Prof. Sadowski said that, while such a law was needed, it was perhaps not immediately applicable and the emphasis of attempts to reduce monopoly power would for the present be on the creation of new small and medium scale enterprises.

Mr. Hole noted that some commentators had drawn attention to the adverse effects of the very high marginal rates of taxation of enterprise profits. Prof. Sadowski replied that he thought there was something in these concerns. There were two, sharply divided, views, however. On the one hand there were those who argued for greater financial autonomy for enterprises. On the other hand there were those who argued that any move in this direction would inevitably be inflationary and would be likely to cause an undesirable boom in investment. Prof. Sadowski did not think it would be appropriate to try to limit investment in Poland by imposing a tax on it, as was being done in Hungary. A similar end was served by the requirement for a deposit to be put up by enterprises investing in construction. Prof. Sadowski said that it remained to be seen how this would work but, personally, he feared that too many exemptions would be granted. In general, Prof. Sadowski regretted that enterprises were all too often in a very strong negotiating position in exacting exemptions from the central authorities such that the latter often had to give in to blackmail.

Mr. Hole said that the acid test of the success of the reform was the medium-term outlook for the balance of payments. Prof. Sadowski agreed. He said that exports needed to grow faster and their composition to change, although export growth had not been too bad. The foreign exchange retention scheme was working well. A major task was to create an environment in which enterprises could plan ahead with confidence. The authorities were therefore planning some further major reform measures for introduction at the beginning of the 1986-90 plan period but thereafter were intending to preserve as stable an environment for enterprise decision making as possible.

The meeting ended at 12:45 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 3
Held at the Institute for National Economy
on Tuesday, March 26, 1985 at 3:00 p.m.

Polish Representatives	Fund Representatives
Mr. M. Ostrowski, Director, Institute of National Economy	Mr. Hole
Mr. A. Ilczek, Division Head, Foreign Department, Ministry of Finance	Mr. Manison
	Mr. Prust
	Ms. Swiderski
	Mr. Boonekamp

The meeting covered four main topics: (1) the quality of the Polish data; (2) the liquidity overhang; (3) investments; and (4) the labor market.

1. The quality of the Polish data

Mr. Ostrowski explained that the information system was in the process of being reshaped and one had to be cautious in interpreting the data. Prior to the reforms, the statistical base had been formulated in an environment of virtually no inflation. Most of the planning had been based on statistics that were expressed in terms of physical units. Those variables that were expressed in value terms represented only a few very broad aggregates. Furthermore, an in-depth analysis of the current reform requires data on the economic situation of individual enterprises, which is for the most part unavailable from the previous information system. The Institute obtains this information for its own use from the results of a detailed survey that it developed, covering over 50 enterprises which they considered to be representative of the general situation of enterprises. By contrast to the previous information system, more attention is being paid to the financial aspects of enterprises' operations. As regards the reliability of data provided by enterprises, Mr. Ostrowski believed that it was reasonably reliable since it was used and cross-checked by various economic groups which had different vested interests. He believed that the quality of this data had improved since 1982.

2. Liquidity overhang

Mr. Ostrowski expressed no preference among the different methodologies used for measuring the liquidity overhang and believed that the range of estimates resulting from these different methods was more relevant than a single point estimate, particularly in view of the aforementioned data limitations. He thought that for purposes of measuring the inflationary overhang foreign exchange holdings should be valued at a rate somewhere between the official and black market rates since if the foreign exchange in the black market were dumped onto the official market its price would fall markedly. As regards the liquidity overhang in foreign currency, he did not feel this was an area of concern as most of these savings were voluntarily held for long periods of time as a store of value and for reasons of psychological well being. The portion that was spent on foreign goods was seen as a favorable development as it improved the supply situation in the domestic market. While there are no official statistics on the stock of foreign exchange in the black market, he guessed that its value would be up to two times the amount held legally with the PKO. He agreed with Mr. Hole that some reconstitution of wealth was taking place following the more than doubling of prices in 1982. This was particularly evident in the last year. Surveys indicated that, in response to better supply conditions, people were increasingly more willing to hold zlotys and postpone purchases into the future. This contrasts with the situation evidenced in 1982, when the supply of goods was drastically reduced and people bought whatever was available. Further evidence pointing to an increase in voluntary savings is the fact that there has not been a large demand to cash in the "revalorization bonds" that came due early this year. In general, he considered the liquidity overhang more of a micro problem concentrated in a few sectors. While having negative distributional effects, recourse to the black market tended to alleviate the shortage evidenced in certain markets. In general the black market concentrates in the trade of higher quality goods. While some observers are of the opinion that it is easier to equilibrate the consumer market on the demand side by means of a strict incomes policy rather than a policy of price increases, in Mr. Ostrowski's view both of these approaches were severely constrained by their social implications.

3. Investment

Mr. Ostrowski viewed investment developments as a major obstacle to the reforms. The level of productive investment has fallen by about 50 percent relative to the pre-crisis level. While attaining the overall level of investment outlays reached in 1978 may not be feasible in the short run, the Government is attempting to change its structure. He views the Government policy of (1) limiting the expansion of central investments which have a long gestation period and (2) increasing investments that are decentralized to enterprises for purposes of modernization and restructuring as a reasonable one. However, in view of the economic crisis, in the foreseeable future, investment outlays will be constrained to lower than required levels because of the high priority given to consumption. The biggest constraint to investment is the lack of foreign exchange, and consequently, the lack of imports. He felt that the interest rate was an ineffective policy instrument as long as shortages of foreign exchange existed. He agreed with Mr. Hole that, given the monopolistic situation in many sectors of the economy, even in the absence of foreign exchange shortages, investment decisions may not be too responsive to interest rate movements as these costs could be passed through to prices. One of the reasons for the bias toward investing in building relative to machinery and equipment is the shortage of spare parts. The two main criteria used for deciding in favor of continuing an investment project are: (1) whether the investment outlays are related to the agricultural or food processing sectors and (2) whether the outlays contribute to providing import substitutes. Secondary criteria include their potential to increase (1) exports and (2) the level of efficiency of the system. While there is an ongoing debate as to which of the old projects should be abandoned in order to make room for new investments, Mr. Ostrowski felt that such discussions had begun at too late a stage since the average degree of completion of projects started prior to 1980 was already on the order of 70 percent. He noted that the excess liquidity of enterprises was very unevenly distributed. The Institute was currently preparing a study for the Government on the distribution of liquidity among enterprises. A part of this excess liquidity was redistributed through inter-enterprise lending which, in his opinion, often generated investments that conflicted with the basic Government objectives.

4. The labor market

Mr. Ostrowski was of the opinion that the reforms had markedly increased labor mobility as a result of increasing wage differentials among firms. In response to this trend, enterprises were often more concerned with their relative wage structure than with profits given the shortage of labor following the shortening of the work week and the surge of early retirements in 1981-82. (The ratio of vacancies to job seekers is on the order of 50 to 1.) As a result of the decline in the labor force, productivity levels have been restored to pre-crisis levels. Labor mobility among cities, however, has been constrained by the housing shortage.

As regards the new wage system introduced in 1984, which allows enterprises to determine their own payroll funds, the Government is moving very cautiously in this direction because of the fear that this system may result in stronger pressures for wage increases which, along with monopolistic practices, are considered to be the main stimuli to inflation.

It was noted that activity in the black market decreases the working efficiency of labor in the socialist sector.

The meeting adjourned at 4:45 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 4
Held at the Institute of Planning and Statistics
on March 28, 1985 at 10:00 a.m.

Polish Representatives	Fund Representatives
Prof. Kamecki, Institute of Planning and Statistics	Mr. Hole
Mr. Ilczek, Ministry of Finance	Mr. Manison
	Mr. Prust
	Ms. Swiderski
	Mr. Boonekamp

Mr. Hole enquired about the feasibility of, and conditions necessary for, achievement of the authorities' medium-term goal of an approximately 5 percent annual increase in export volume. Prof. Kamecki replied that indeed this was a major objective of government policy to which, it was realized, there was no alternative. It exerted a major influence on the design of policy. For this reason great stress was placed on the restoration of macroeconomic equilibrium. There had already been considerable progress in reducing inflation and it was hoped that the negative impact of market disequilibrium on exports would weaken. In fact, the primary importance of the need to restore domestic macroeconomic equilibrium lay in its expected beneficial effect on the external sector. In practice, though, it was the achievement of equilibrium in particular sectors which would be decisive. In some sectors there had already been a big improvement, for example, for shoes. One of the results of a better balance between domestic supply and demand was that shoe producers were becoming more interested than previously in exports. Prof. Kamecki went on to say that he hoped that the process of economic reform would gradually yield some positive results for export performance. However, this would take time as new habits and attitudes had to be formed at various levels. He noted that there were many unexploited possibilities for increasing exports and that organizational improvements alone could have a considerable impact even in the short run. However, the Government's economic policy had to be geared to achieving many objectives, of which export performance was only one. The structure of incentives was correspondingly complex which tended to weaken the individual impact of each. Prof. Kamecki hoped that when the domestic macroeconomic balance improved there would be less of a need for special incentives. The Government was currently reviewing the whole range of such incentives with a view to decreasing their number.

Prof. Kamecki felt that the level of imports would exert a vital influence on export performance. According to some estimates prepared by the Institute for Foreign Trade about two years ago, an extra US$1 in imports could lead to an increase in total domestic production worth US$6 and in production for export alone of US$4. Prof. Kamecki hoped that Poland had now reached a point from which imports would continue to increase steadily. Of course, an agreement with the Paris Club and a general improvement in credit relations with the West would be of great assistance in this connection. The actual impact of rising imports on export potential would naturally depend to some extent on the rate of increase of domestic incomes.

Another major concern of Polish policymakers was the quality of production. This had been deteriorating for a number of reasons. These included the running down of the capital stock; the lack of imports and the enforced substitution of domestic alternatives; and the fact that the pressure of domestic demand had led to a decline in the quality of workmanship. Prof. Kamecki hoped that there would be improvements on all these fronts.

Summing up his views on export prospects, Prof. Kamecki said that he thought that the official forecast of 5 percent growth of export volume over the medium term was reasonable. He was not among those that thought that efforts to raise exports should be confined to industrial products alone and looked for raw materials and energy items to continue to play a major role in export performance.

Mr. Hole said that he did not take issue with the notion of an import multiplier but he suspected that there was considerable scope for lowering the import intensity of Polish production patterns. He wondered how this could be best achieved and what assurances there could be that any increase in imports would be used efficiently for the generation of additional exports. Prof. Kamecki replied that it was generally accepted that import intensity was too high although there had been considerable adjustment in this respect in recent years. The potential for further such adjustment was less in the short term but could be considerably higher if there were scope for fundamental changes in technology and the pattern of investment. However, the large carryover of unfinished investment projects from the past made such a radical change in investment policy unlikely. It would be desirable to cancel a large number of these unfinished projects but generally there were very strong pressures from many quarters to keep them going. Prof. Kamecki did not think that in the coming three to five years, Poland would be very successful in reducing the import intensity of production and technology. Nevertheless, he expected more success in this area than, for example, in reducing the energy intensity of production. This was because the shortage of imports was an unalterable fact of life to which enterprises had no choice but to respond. Such was not the case for energy supplies which remained relatively plentiful.

Mr. Hole sought Prof. Kamecki's view on incentives for raising enterprise efficiency and, in particular, on the question of whether the high rate of profit taxation had an inhibiting role in this context. Prof. Kamecki replied that he was very critical of the high level of taxation, a side effect of which was the need for a similarly high level of subsidization. However, he realized that in designing policies in this area the government had to be strongly guided by their anti-inflationary objectives. In addition, the Polish economy had to be seen as being at a transitional stage in which the linkages between the domestic and foreign price levels were imperfect. The need for the widespread and simultaneous taxation and subsidization of enterprise activities arose essentially from this fact. Social and political pressures meant that progress in reforming the exchange rate and the price structure could only be gradual. Prof. Kamecki noted that according to the law the exchange rate had to be set at such a level as to make 75-80 percent of export activities profitable. In fact, though, his guess was that only about 55-60 percent of such activities were profitable at the moment. He thought that the authorities were becoming more bold in their use of exchange rate policy and less afraid of its inflationary impact. He noted that a study carried out by the Institute for Foreign Trade had calculated that a 1 percent change in the exchange rate had a 0.2 percent impact on the level of domestic prices. However, he was not fully persuaded by these results which in any case were very largely dependent on the response of taxation and subsidization to any change in the exchange rate.

Prof. Kamecki thought that an exchange rate devaluation could have some positive impact on export performance but he did not believe that the exchange rate was now the main factor in limiting exports. The shortage of imports and the supply situation generally was a more important constraint, although the significance of these factors could decline as further progress was made toward domestic macroeconomic equilibrium. Prof. Kamecki believed that a package of measures should be introduced to give stronger encouragement to exports. An important component of such a package would be an increase in the scope of the foreign exchange retention scheme. The uses to which retained foreign exchange could be put should be increased. The current operation of the scheme was already much freer than when it was first introduced when retained foreign exchange could only be used to finance imports of raw materials and when exporters' subcontractors were ineligible to participate. Prof. Kamecki believed that exporting enterprises should be free to auction their retained foreign exchange to other possible users rather than being obliged to use it all themselves. In fact he believed that enterprises should have full freedom to use their retained foreign exchange for any purpose. He believed that the Government's thinking was increasingly sympathetic to this point of view although there was an understandable desire to prevent abuse of the scheme and to ensure that it was used to finance imports of high priority items.

Prof. Kamecki described the system for auctioning foreign exchange. Its results so far had been very poor partly because of the many restrictions which applied to the use of foreign exchange acquired in this way. The auctions were designed for the benefit of enterprises that did not have access to foreign exchange through the retention scheme. Up to the present there had only been three or four auctions for very small amounts which had been administered by the Bank Handlowy. All sales of foreign exchange under this scheme took place at the commercial rate but the scheme had proved unattractive to enterprises because of the strict conditions which Bank Handlowy applied. These included the need for bidders to demonstrate that the foreign exchange acquired would be used to increase exports or the production of consumer goods. In addition, those allocated foreign exchange were required to make an advance deposit, in zlotys. Prof. Kamecki expected these conditions to be liberalized in the future.

Prof. Kamecki described the procedures for determining foreign exchange retention quotas. These were agreed between the Government and specific enterprises. They differed from one enterprise to another depending on several factors. These factors included the import content of an enterprise's production and also the proportion of exports in its total sales. Other things being equal, an enterprise with a high ratio of exports to total sales could expect a relatively low retention quota. Mr. Hole suggested that this scheme could carry the danger of promoting import-intensive exports. Prof. Kamecki thought that this was not a major problem, in the short run at least, because the technical coefficients relating imported inputs to output were more or less fixed in the short run. However, he acknowledged that the way in which the scheme operated created an incentive for enterprises to exaggerate their need for imports.

Prof. Kamecki felt that time was needed for the full effects of recent legislative changes governing the relationships between producing enterprises and foreign trade organizations to have their full effect. A lack of experience and the continuation of old habits meant that many enterprises still turned, more or less automatically, to a foreign trade organization to take care of its exporting. But this was not uniformly the case and the freedom which industrial enterprises now had either to trade directly with overseas customers or to collaborate at their own discretion with foreign trade organizations was likely to have a considerable impact over time. Some new foreign trade organizations had recently been established which were very active in seeking out new business.

Prof. Kamecki noted that in bargaining on various matters with the central authorities, there was often a strong community of interest between foreign trade organizations and the producing enterprises which they serviced. For instance, a foreign trade organization typically had a strong interest in ensuring that its client enterprises obtained as many imports as possible. Foreign trade organizations could either act on their own account (which would involve buying exportable output outright from the producing enterprise) or it could act as an agent on a commission basis. These factors could significantly affect the short run consequences of a change in the exchange rate. A further influence would be whether the price agreed between the producing enterprise and the foreign trade organization was a transactions price or a controlled price. Because of the relatively low coverage of the former, the short run response to a devaluation of the exchange rate could be rather small.

Prof. Kamecki said that the Ministry of Foreign Trade took the main operational decisions regarding the subsidization of, and the imposition of levies on, imports and exports in cases where settlements were not made at transactions prices. The costs of these operations was limited by a budgetary allocation from the Ministry of Finance but, in deciding on its use, the Ministry of Foreign Trade was subject to pressures from many quarters. These included branch ministries, foreign trade organizations, production enterprises, the Ministry of Finance, the Ministry for Wages, Labor, and Social Affairs, and the Office for Economic Reform.

Prof. Kamecki said that it was hoped that the monopoly law would be introduced in the course of the current year. A draft of the law would very soon be sent to the Parliament. He noted the many difficulties that had arisen in drawing up this law and said that personally, while he was in favor of it, he did not think that it would in itself be a decisive influence. It would be useful in bringing the facts concerning the extent of monopoly in the Polish economy to light and its provisions could from time to time be invoked. However, it would be unrealistic to expect that the latter would happen more than rarely. The real solution to the problem of monopoly in the Polish economy lay in the extension of competition and the restoration of market equilibrium.

Prof. Kamecki said that he thought that the aggregation of trade flows with the convertible and nonconvertible areas, respectively, and their expression in some common currency unit posed more or less insuperable problems. Not only was the structure of prices in trade with the two areas completely different but the relationship between the two structures was continuously changing over time. Prof. Kamecki believed that the zloty was overvalued both with respect to the dollar and with respect to the transferable ruble but the extent of the overvaluation was greater in the case of the dollar.

Prof. Kamecki suggested to the mission that it should seek to formulate its views of the Polish economy in a way that took account of the dynamics of the situation. What was important was not only the current state of affairs but also the longer run tendencies.

The meeting ended at 11:45 a.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 5
Held at the Institute of Finance
on Thursday, March 28, 1985 at 3:00 p.m.

Polish representatives	Fund representatives
Professor (Dr.) Stanislaw Gora, Director of the Institute	Mr. Hole
Dr. Rorman Skarzynski	Mr. Manison
Dr. Marek Oles	Mr. Prust
	Ms. Swiderski
	Mr. Boonekamp

The meeting covered four main topics (1) the liquidity overhang, (2) the black market, (3) constraints on economic efficiency and (4) the quality of the Polish data.

1. Liquidity overhang

Mr. Oles defined the liquidity overhang as the share of the money stock that is held involuntarily and which, in the absence of a supply constraint, would have been spent on goods and services. While expressing scepticism on the conventional methodologies used for measuring the overhang, he described the one most commonly used. The money stock held by the public is divided into three basic categories: transactions balances, and voluntary and involuntary savings balances. Cash balances are assumed to be held entirely voluntarily for transations purposes. As regards savings, the distinction between those voluntarily held and those involuntarily held is normally made using the following proportions: 50 percent for fixed-term deposits (which includes deposits earmarked for housing and other purposes); 60 percent for time deposits and 30 percent for demand deposits. Using this method the current liquidity overhang is estimated on the order of Zl 600 billion (compared to Zl 500 billion in 1982). This methodology excludes the public holdings of foreign exchange which Mr. Oles felt was justified since the inflationary overhang was only relevant for domestic currency. He guessed that to restore market equilibrium a price increase on the order of 50 percent was required. He felt that the crux of the problem was on the supply side and did not consider that the situation warranted a monetary reform.

Given that the range of assets available to the public was limited to cash and deposits, most of which were quite liquid, Mr. Oles felt that interest rates played a very insignificant role while expectations of inflation were very important. In fact, it was his opinion that the disequilibrium in the money market was dynamically unstable. While price increases tend to diminish the inflationary overhang by reducing the stock of real money balances, actual price changes occur only slowly and at discreet intervals of time. Expectations of inflation, on the other hand, tend to increase the disequilibrium in the money market by reducing further the desired holdings of money. Given the lag structure of price increases, the latter effect tends to dominate the former producing a dynamically unstable system. Mr. Oles believed that the correct method of calculating the liquidity overhang would be to estimate aggregate functions for the demand and the supply of money. This, however, was an empircally difficult task in a situation of market disequilibrium.

In response to a comment by the staff on the interest sensitivity of the revalorization bonds which was recently evidenced, Mr. Skarzynski felt that this case should be treated as an exception since these bonds were one of the few available instruments considered to be a good store of value. Furthermore, even if real interest rates were to become positive, the total amount of savings would not change due to the persistence of an excess supply of money. Only the composition between voluntary and involuntary savings would be affected. The staff noted that, even at an unchanged level of total savings, a reduction in involuntary savings would have important policy implications. Mr. Skarzynski, was not optimistic that real rates of interest would become positive in the near future. The Government was socially constrained to raise interest rates further and the rate of inflation was being reduced only gradually.

2. The black market

The black market was defined to include all economic activity that was outside the tax system.

The general view was that the black market did not help to reduce the liquidity overhang in the domestic market; its role was only to redistribute income (in 1984 the redistribution amounted to about Zl 300 billion, or 13 percent of personal income). While no official statistics are available on the size of the black market, it was considered reasonable that the public held about twice as much foreign exchange outside of the banking system (i.e., about US$2 billion) as it did in the banking system. Other estimates of black market foreign exchange holdings, however, are as high as US$6 billion. The main sources of obtaining foreign exchange are from (1) tourists (between one half and two thirds of their expenditure in zloty are converted in the black market), (2) relatives, and (3) Polish residents going abroad to work. Foreign exchange is held as a store of value as well as for purchases of goods in both the black market and in state-owned PEWEX shops. The main incentives for holding foreign currency in the PKO bank is the high rate of interest (up to 11 percent) as well as the fact that foreign currency taken abroad must be withdrawn from the banking system. The main reason why more foreign exchange is not being absorbed by the banking system is the fear that these accounts will be frozen or confiscated. This is particularly true in the rural areas and among the elderly who have witnessed too many monetary reforms.

3. Constraints on economic efficiency

One of the major objectives of the reform was to increase the economic efficiency of enterprises using the three principles of self-financing, self-management and independence. In this new system the level of profits was to be a signal of effectiveness. To date the effects of the reforms on efficiency have not been as significant as had been originally anticipated. The main obstacles have been the existance of disequilibrium in the market as well as psychological factors that take time to overcome.

The staff noted that the budgetary system consisted of a very steep system of taxes combined with a very generous level of subsidies. Mr. Skarzynski explained that this was a temporary phenomenon and that as the reforms advanced subsidies would be cut considerably, although a certain minimum level of subsidies would have to be maintained for social reasons. As regards the high level of taxes, they were necessary in the transitional period of the reforms in order to control the increase in profits, mostly due to the price policies of monopolies which currently dominated the market. The requirement to control profits was accentuated by the fact that there was virtually no capital market operating among enterprises with the budget acting as the main intermediary for capital redistributions. Professor Gora did not feel that the income tax was at a too high level. The idea to tax expenditures more, for example though an investment tax, and profits less did not appeal to him since, in the absence of positive rates of return on deposits, enterprises which did not direct their profits to investment projects would distribute them in the form of wage increases which was considered even worse. In any case, a tax on excessive wage increases already existed. Profesor Gora noted that most increases in profits in the recent period had been a result of increases in prices rather than reductions in costs, which was one of the current failures of the reforms.

4. The quality of the Polish data

There was a consensus that the quality of data had improved markedly in 1984 in terms of reliability, timeliness, coverage and greater access to previously confidential sources. No data were available on the distribution of income (although there was a distribution based on wages) since there is no income tax system which could serve as a data base. Also private sector activity, with the possible exception of agriculture, was most likely understated. Consumption in the national accounts was fairly reliable being based on a sample of households (about 10,000). As regards budget data, while there are a substantial number of extrabudgetary funds, data on these funds were published and presented to Parliament in annexes to the budget.

The meeting adjourned at 4:45 p.m.

INTERNATIONAL MONETARY FUND

Minutes of Meeting No. 6A
Held at the Ministry of Finance
on Wednesday, April 1, 1985 at 10:00 a.m.

Polish Representatives

Ministry of Labor, Wages, and Social Affairs

Mr. Wieslaw Jasinski, Director, Policy Department
Ms. Urszula Jelinska, Main specialist, Department of Wages in the Productive Sphere

Planning Commission

Mr. Kazimierz Dzienio, Director, Department of Employment and Incomes of the Population
Mr. Stanislaw Raczkowski, Advisor
Mr. Slaw Milewski, Director, Department of Economic Analysis
Mr. Romuald Szlimiewicz

Ministry of Finance

Mr. Zbigniew Karcz, Director, Foreign Department
Mr. Krzysztof Krowacki, Advisor, Foreign Department
Mr. Zbigniew Lichocki, Senior specialist, Foreign Department

Central Office of Statistics

Mr. Leszek Zienkowski, Advisor
Mr. Boguslaw Szybisz, Director, Analysis Department

Office of Prices

Mr. Jerzy Chabros, Director, Prices Policy

Fund Representatives

Mr. Hole
Ms. Swiderski
Mr. Prust

The meeting covered two topics (1) wages and (2) prices.

1. Wages

a. Objectives of wage policy

The objectives of wage policy changed markedly over the 1981-85 period due to the changing economic and political situation. As a result of increasing social unrest, the main aim of wage policy during 1981 was to satisfy wage demands to the extent allowed by the economic circumstances. Consequently, average wages increased by 27.4 percent (compared to a retail price increase of 21.2 percent). This, however, was insufficient to put a halt to the strikes, reduction in work hours and output. The consequence was a sharp increase in the disequilibrium in the consumer market. During 1982 prices of procurement materials and retail goods more than doubled in an attempt to restore market equilibrium. Consequently, the main objective of wage policy in 1982 was redirected to the protection of the purchasing power of the lower income groups which were particularly affected by the steep increases in the prices of foodstuffs. An across the board increase in the cost of living was granted which ranged between Zl 1,050 to Zl 2,100 depending on income level and type of work. Wages in the socialized sector increased by 51 percent; in real terms they declined by 24.9 percent. Wage earners in the lowest 20 percent of the income distribution received average wage increases of 52 percent; those in the highest 20 percent received 43 percent. As a further step in protecting the incomes of the lower income groups, the Government increased social benefits by 137.8 percnt. Consequently, the share of payments from the wage fund in total income dropped from 54.6 percent in 1981 to

48.1 percent in 1982. The corresponding increase in the share of social benefits was from 12.2 percent in 1981 to 17.5 percent in 1982. In line with the aims of the economic reform, enterprises were given more autonomy in setting their wage structure. In order to prevent excessive wage increases the Government simultaneously introduced a tax on excessive wage increases (Fund for Occupational Activation--FAZ). The Funds were to be used for financing and retraining workers temporarily unemployed. The cost of living that was granted nationwide was exempted from the tax. A consequence of the wage policy of 1982 was to reduce wage differentials. Furthermore, the increase in market disequilibrium reduced the motivation to work.

The main wage policy objective of 1983 was to improve the relationship between wage increases and productivity gains. This was to be mainly achieved through the use of the FAZ instrument, whose method of operation was significantly altered so as to have a more direct link between productivity gains and wage increases (see section c). The Plan for 1983 targeted an increase of real output of 4 percent, an increase in prices of 15 percent and an increase in wages in the socialized sector of 16 percent. In the event, wages increased by 24.5 percent, prices by 22.1 percent, and output by 6.4 percent. A part of the larger than expected increase in wages was attributable to the unexpectedly large liquidity of enterprises.

The main objective of wage policy for 1984-85 is to keep real wages constant while improving the relationship between wages and productivity by stronger recourse to FAZ. The Plan for 1984 targeted an increase in output of 4.5 percent, an increase in prices of 15 percent, and an increase in wages of 17 percent. In the event, provisional estimates indicate that wages increased by more than 19 percent, prices by 15 percent, and output by over 5 percent. For 1985 the Plan targets an increase in real output of 4-4.5 percent, an increase in prices of 12-13 percent, and an increase in wages of 13 percent. As in 1984, the main instrument of controlling excessive wage increases will be FAZ.

b. Income developments in the private sector

The following table presents the changes in nominal incomes in the socialized sector relative to the private sector for the 1981-84 period.

	1981	1982	1983	Prov. 1984
	(In percentage change)			
Socialized sector	27.2	44.2	26.9	17.4
Nonsocialized sector	57.6	64.9	12.0	13.2
Of which:				
Agriculture	61.8	61.7	5.7	9.6

During 1981-82, incomes in the private sector grew at a much more rapid rate than in the public sector largely due to the large increases in the price and in private market sales of foodstuffs, to shifts in employment from the socialized sector to the private sector as well as to sharp increases in wages. This trend was reversed markedly in 1983-84 reflecting sharp increases in taxes paid by the private sector (with the exception of agriculture) as well as relatively sharper increases of procurement vis-à-vis retail prices in the private agricultural sector.

c. The Fund for Occupational Activation--FAZ

In 1982 enterprises were given more autonomy in determining their wage sytem. The FAZ was introduced in the same year as an instrument for controlling excessive wage increases. It is a tax on profits rather than on costs. FAZ does not apply to either the private sector or to budgetary entities. Its mode of operation is also modified for the agricultural sector. During its first year of operation, wage increases of 3 percent were exempted from FAZ. This threshold could be increased by 1 percentage point (to a maximum exemption of 8 percent) with every percentage point reduction in employment. Beyond this threshold, the FAZ was applied to average increases in wages. The tax rate progressively steepened between the ranges of 25 percent and 300 percent for each additional percentage point increase in average wages.

During 1983 the operating mechanism of FAZ was significantly altered. The across the board increase in wages that was previously exempted from FAZ was abolished. In its place a coefficient relating a selected indicator of productivity gain to wage increases was introduced. The average coefficient was set at 0.6, implying that 60 percent of the increase in the indicator of productivity could be passed on to wage increases without the enterprise having to pay FAZ. The indicator of productivity was to be net sales in constant prices, the aim being to motivate firms to economize on costs. Wage increases were defined for the total wage bill rather than for the average as was the case previously. Furthermore, FAZ rates were increased markedly. The table below relates the tax rates applicable to each additional percentage point increase in wages that is subject to FAZ.

Percentage Point Increase in Wages over Tax Exempt Increase	Tax Rate Charged
(In percent)	
Less than 1	40
1-2	100
2-3	200
3-4	300
4-5	400
Over 5	500

The rates were lower for special cases, such as the cooperatives for the disabled where the highest tax rate was 200 percent. The power to change these rates rests with the Council of Ministers within the limits specified in the law on FAZ. Finally, increases in net production that were not paid out in wage increases could be put into a reserve fund for future wage payments that would be exempted from taxes. Wage increases that are taxed in a given year, however, are to be excluded from the calculation of increases in wages, making it more difficult for an enterprise subject to FAZ in a given year to grant wage increases in the following year that are exempt from the tax.

In practice, there are many exceptions to the general system. The coefficient relating output gains to wage increases can range between 0.5-0.8 and in exceptional circumstances it can even be 1. Furthermore, certain enterprises are granted across the board wage increases that are totally exempted from FAZ and are unrelated to output developments. These exceptions normally occur in enterprises which have little potential for increasing their output (e.g., cooperatives for disabled, oil refining), where it is socially undesirable to increase output or where it is difficult to construct a reliable measure of production (e.g., transit system). Certain enterprises receive both a flat perentage tax exemption as well as a preferential coefficient relating output gains to wage increases. Furthermore, the indicator of "net production" is often replaced by gross production, in some instances being measured in terms of physical units, and in others by gross sales. As of 1985, however, enterprises using the net production concept cannot redefine production in gross terms. (It was noted that in 1984 enterprises who used net production as their base experienced much larger output gains than those that used gross production.) Depending on the enterprise, the indicator of wages is expressed in either average or total terms. The scope of exceptions and special regulations for individual enteprises results in substantial resources being devoted to enterprises to lobbying for special FAZ treatment.

As regards bonuses, under the system introduced in 1983 they are subject to FAZ only when their value causes the wage bill to increase by more than 7 percent. The table below relates the tax rate applicable to each additional percentage point increase in bonuses that are subject to FAZ.

(In percent)

Percentage Point Increase in Wages over Tax Exempt Increase	Tax Rate Charged
Less than 1	100
1-2	150
2-3	200
Over 3	300

As in the case of basic wage increases there are exceptions to the rule. For 1985, exporters which receive a reduction in profit taxes, can use 25-35 percent of the resulting increase in profits to pay out bonuses that are exempt from FAZ. Similar rules apply to certain enterprises who have shown substantial savings in raw materials. Tax exempt preferential bonuses also exist for the performance of duties that are in the national interest (e.g, the timely completion of centrally planned investment projects or investments under government contracts). These two areas of exemptions were determined by the Council of Ministers, and are set out in the Plan. Normally, the Minister of Labor can add further exemptions, taking into account the broad guidelines set out by the Council of Ministers. By contrast to 1984, however, the 1985 Plan does not give the Minister of Labor the flexbility to determine additional cases which would be exempted from FAZ. Other exemptions from FAZ include wages of students, severance payments for retiring workers, remuneration of workers in training programs, remuneration of workers on new production facilities, etc.

FAZ payments are paid to a special account with the Ministry of Labor, Wages and Social Affairs. There are two exceptions to this rule: (1) cooperatives for the disabled which place FAZ payments into a special account (Fund for Work Protection) which provides subsidies to enterprises employing disabled workers, provides equipment and vocational training for the disabled etc., and (2) the agricultural sector which places the funds with the Ministry of Agriculture. These funds are used to assist state farms that are operating under difficult conditions.

The table below presents the sources and uses of FAZ funds. The balance is transferred to the central budget. The use of FAZ for revenue raising purposes is considered of secondary importance relative to its primary role of preventing excessive wage increases.

	Payments into FAZ	Uses of FAZ
	(In billions of zlotys)	
1982	52.5	1.2
1983	49.2	3.9
1984	99.2	10.2
1985 Plan	...	15

The planned 13 percent increase in wages in 1985 will stem from the following sources:

		(In percent)
(1)	wage increases that are exempted from FAZ as a result of the coefficient relating production increases to wage increases	4.1
(2)	average exemptions from FAZ that are independent of productivity changes	5.5
(3)	payments out of profits (bonuses)	2.0
(4)	payments on account of elements of remuneration excluded from the base	0.2
(5)	wage increases on which FAZ is paid	1.1
	Total	13.0

As a concluding remark, it was noted by Mr. Zienkowski that one of the largest problems confronting FAZ was policing the misreporting by enterprises of productivity increases. The increase in valued added implied by the report of enterprises for FAZ purposes differed significantly from that shown in the national accounts.

d. The system of wages

Prior to 1982 the wage structure was determined by collective branch agreements which were strictly defined in terms of the universal conditions set out in the labor code. Wage flexibility was limited by detailed wage tables. The wage tables for blue collar workers included nine grades, the top rate being Zl 30 per hour. For white collar workers the wage tables consisted of 22 grades the highest being Zl 9,000 per month. The tables varied among different branches of the economy. Bonus payments were also strictly defined by table grids.

In 1982 the labor code and collective branch contracts were replaced by Law 283. Enterprises were given more flexibility in designing their own wage tables within the bounds specified by the minimum and maximum wage rates. The top rate in the pay tables for blue collar workers was increased to Zl 40 per hour and for white collars to Zl 12,000 per month. The law also made it possible to reclassify workers by one to two grades as well as to provide additional compensation to those experiencing difficult working conditions (e.g., coal miners working underground could earn a maximum of Zl 45 per hour while the top rate for while collar workers in difficult working conditions was adjusted to Zl 17,000 per month). However, the most significant change introduced in the 1982 wage system was to grant enterprises complete autonomy in determining bonus payments out of profits. Consequently, with the freezing of the maximum wage rates since 1982 bonus payments have increasingly become the dominant source of remuneration.

Since 1984 enterprises that fulfill certain conditions (e.g., good financial performance) have been given the option to adopt a more flexible system of pay which they design themselves taking into account certain stipulated requirements (e.g., rights to earn the minimum wage and certain social benefits including retirement and seniority bonuses, the requirement that the remuneration for overtime be at least equal to the regular pay, etc.). In contrast to the 1982 system of pay, the new system introduced the possibility of having a wage structure that was not bound to national wage tables. No limits are set on the hourly pay of blue collar workers. Indirectly, the maximum income of a white collar worker is limited by the director's salary. Director's salaries are classified into four separate categories currently ranging between Zl 21,000 and Zl 30,000 per month. One of the aims of the new system of pay is to decrease the relative role of bonus payments in overall remunerations in favor of wage payments. Within the firm there must be a signed agreement between the trade union and director approving the proposed system. Furthermore, the workers' council must be notified of the new system and give a positive judgement as regards its introduction. Once approved within the firm it is sent to the Minister of Labor for final acceptance. Presently about 1,700 enterprises are operating under the new system and 400 applications are pending. Excluding the sectors of the economy that do not have the option of considering this new system of pay (e.g., central administration, PKP, PKS), the new system of pay currently covers about 30 percent of the remaining labor force.

2. Prices

The price policy of 1982-84 was an instrumental part of the overall policy of restoring market equilibrium and promoting economic growth. It pertained to all levels of prices. As regards procurement prices of basic inputs, the goal has been to increase them to world market levels. Following a marked increase in these prices in 1982, the policy has been to spread the adjustment period over several years so as to be able to control, and in fact gradually reduce, the rate of inflation. The duration of this period is difficult to estimate since it depends on world price developments. In certain basic materials, such as steel products and materials in the light industry (using the Polish definition), domestic prices are only a few percentage points below world prices. The spread is much larger for energy products (the spreads in 1984 for crude oil and coal were 25 percent and 30-45 percent, respectively). With respect to coal, the aim is more to raise prices sufficiently to cover production costs (which are lower than world prices) rather than to use world market prices as the benchmark.

The policy with respect to retail prices is to restore market equilibrium and reduce the scale of consumer subsidies. As with procurement prices the sharpest increases in these prices were observed in 1982 (prices increased by 100.8 percent) followed by increasingly smaller changes (22.1 percent in 1983, 15 percent in 1984, and an estimated 12-13 percent in 1985). A major consideration in this area has been the maintenance of real incomes of the population following the sharp decline in purchasing power experienced in 1982. In the period

1982-84, nominal incomes increased by 51.3 percent, 24.5 percent, and 19.9 percent, respectively. In real terms, following a decline of 25 percent in 1982, in 1983 and 1984 they increased by 1.1 and 3.7 percent, respectively. The Plan for 1985 targets no growth in real incomes. The main effect of the price reform at the retail level has been to reduce market disequilibrium, making it possible to abandon the rationing of certain items. Further evidence of more favorable market conditions can be seen by the narrowing of the gap between black market prices and official prices of certain consumer durable goods that were previously in short supply. For example, the black market and the official prices for imported refrigerators are Zl 70,000 and Zl 55,000, respectively. Washing machines from Czechoslovakia sell for Zl 65,000 in the black market; their official price is Zl 53,000. A complete reversal of the situation has occurred in the market for color televisions where the black market price (Zl 115,000) is currently lower than the official price (Zl 145,000). Prices of radios and cassettes are about the same in both markets.

The reforms introduced three categories of prices: administrative, regulated, and contract prices. Administrative, or fixed prices, are set by the Government for (1) consumer goods and services that are of basic importance in daily consumption; (2) for basic intermediate goods, as well as for (3) alcoholic beverages and tobacco products and postal and telecommunications services. While the majority of basic goods and services are subsidized, products such as alcohol and tobacco are major revenue earners. 1/ Administrative prices are normally adjusted once a year and, thus, there is a lag in transmitting any movements of international prices into domestic prices. As mentioned previously, the full transmission of international prices to domestic prices is spread over several years.

In 1982, the subsidies on food were reduced markedly; thereafter their level has been kept broadly unchanged (implying a reduction in the rate of subsidy on total foodstuff expenditure). However, temporary increases in subsidies are required, for example, in cases where world prices increase and domestic prices remain unchanged for a period of one year. The average time period that elapses before such a temporary subsidy is eliminated was not specified directly. The Plan for 1985 does not foresee an increase in subsidy payments. It was noted that the subsidy payments for most imported goods that are priced administratively are made to the foreign trading organization; the producing enterprise pays only the administrative price. As regards exports, when the domestic price of a product is higher than the foreign price, as with most agricultural products that are priced administratively and a small portion of manufactured products, the export producer generally prefers to sell his product to a foreign trading organization (FTO) which guarantees that he receives the domestic price for his product. The FTO, in turn, requests a subsidy for this transaction from the Ministry of Finance for its own account. In cases where the domestic price of a product is less than the

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1/ It was noted that while the value of expenditure on foodstuffs, which is subsidized is Zl 700 billion, the value of expenditure on alcohol, which is taxed, is Zl 600 billion.

foreign price the export producer may be more willing to either sell his product directly onto the foreign market or to use the FTO as an agent in the transaction. In this case, the exporter would bear the taxes directly.

Contract prices are to be set freely in the market place. In 1984 they represented 50 percent of consumer goods and 63 percent of procurement goods. In practice, since the middle of 1983 the Government has imposed a freeze on all producer prices unless the increase is considered to be beyond the control of the manufacturer (e.g., increases in the price of raw materials). Reasons such as increases in wages or employment do not entitle enterprises to raise prices. Also, in 1985 a new regulation was introduced limiting the passing on of increases in the administrative prices of raw materials into producer prices to 95 percent (90 percent of fuels and energy). In 1984 the price freeze was extended to retail prices of manufactured consumer goods. At the same time a ceiling on the permissible rise in prices of these goods--resulting from increases in external costs beyond the enterprises' control--was set at 10 percent. The remaining one-third to one-half of contract prices at the retail level, however, can be freely determined (e.g., foodstuffs, not covered by administrative prices). By 1986 the Government intends to reverse the rules concerning contract prices, allowing them to be freely determined with the exception of a few groups. The Price Office requires notification of all increases in contract (and regulated) prices two weeks after their implementation. No prior notification is required. If the price increases are deemed unjustified the enterprise may be required to pay a penalty for earning undue profits as result of the price increase.

Regulated prices are set by producers on the basis of costs borne in production or in selling plus a certain rate of return. From the beginning, they were considered only as a transitional stage between the move from administrative to contract prices. Consequently, their share of retail and procurement prices has fallen from 13 percent in 1983 to 3 percent in 1984 and they are expected to be reduced further to 2 percent in1985.

Price increases in 1982 were dominated by changes in administrative prices. In 1983-84 it was believed that the contribution to inflation from contract and administrative prices was about equal. The recent 1985) increases in administrative prices (netting out the effects of compensations) are expected to absorb Zl 111 billion of purchasing power (compared to an inflationary gap of Zl 100 in 1984). The planned range had been between Zl 96 billion and Zl 143 billion. The compensations granted were not much above what had been estimated in the Plan and were mostly directed to the lower income groups, pensioners, etc. In total, the excess over planned level of compensations amounted to only Zl 15 billion.

The 13 percent increase in prices estimated for the current year is made up of the following elements:

	(In Percent)
Inflation carried over from 1984	3-4
Increases in administrative prices of foodstuffs - (in two stages)	2.5-2.75
Increases in prices of fuel and energy (in April)	0.3
Increases in prices of nonfoodstuffs mostly due to increases in raw material prices and increases in depreciation write-offs	4.1
Other increases - e.g., services and foodstuffs	1.6-1.8

It was generally believed that the average level of consumer prices was higher than the average level of producer prices but there were many exceptions to this rule due to the heavy subsidization of certain consumer goods. As a result of the subsidies at the retail level, the dispersion of consumer prices was much larger than for producer prices. In 1982 the spread between consumer and producer prices narrowed (retail prices increased by 100.8 percent compared to producer price increases of 122.3 percent in industry), while some widening of the spread was evidenced during 1983-84.

Price indices are based on samples of actual prices. As regards their interpretation it was noted that they were constructed for a representative household and that there were variations in the rate of inflation experienced by different income groups; however, no detailed breakdown was available. These variations, however, were not considered to be large. In addition, as a result of the market disequilibrium many purchasers were forced to buy goods of higher quality and price, which was not taken into account in calculating the index. Some adjustment for quality of goods is being made.

The meeting adjourned at 1:30 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 6B
Held at the National Bank of Poland
on April 1, 1985, at 10:00 a.m.

Polish representatives	Fund representatives
Mr. G. Wojtowicz, Director, Foreign Department, National Bank of Poland	Mr. Manison
Ms. M. Rubel, Advisor, Foreign Department, National Bank of Poland	Mr. Boonekamp
Mr. I. Ilczek, Division Chief, Foreign Department, Ministry of Finance	

The meeting dealt with exchange arrangements, exchange rate policy, entitites authorized to undertake foreign exchange transactions, and black market exchange rates.

1. Exchange arrangements

The exchange rate of the zloty against currencies other than those of the member countries of the Council for Mutual Economic Assistance (CMEA), 1/ Albania, and the Democratic People's Republic of North Korea, is determined on the basis of a weighted basket of currencies, each with a share of at least 1 percent in the external current account settlements with the convertible currency area. The basket and the currency weights are set monthly, based on the previous (calendar) month's convertible currency current account, for which data are usually available with a lag of 15 days. On April 1, 1985, the basket consisted of the following nine currencies (weights in parentheses): U.S. dollar (.648), deutsche mark (.179), Austrian schilling (.037), French franc (.036), pound sterling (.032), Swiss franc (.025), Netherlands guilder (.015), Italian lire (.014), and Swedish kroner (.014). Although the basket's structure is relatively stable on a month-to-month basis, it has undergone substantial change since the inception of the "basket method" on April 1, 1978. At that time, both the Danish and Norwegian crowns were included in the basket, together with the above currencies, and the weights of the U.S. dollar, deutsche mark, and pound sterling were, respectively, 0.49, 0.17, and 0.07. 2/ The authorities had not considered basing the basket on Poland's direction of trade; however, they expressed an interest in

1/ The participants in the CMEA are Bulgaria, Cuba, Czechoslovakia, German Democratic Republic, Hungary, Mongolia, Poland, Romania, USSR, and Viet Nam.

2/ Before unification of the exchange rate at Zl 80 = US$1.00 on January 1, 1982, the basket had been used to determine the financial rate against the U.S. dollar and other (non-socialist) currencies. This rate was multiplied by a factor of 16 to arrive at the commercial rate, at which some 97 percent of all transactions were settled. The remaining transactions were cleared at the financial zloty rate times a factor of 10.

being briefed at a later date on the Fund's use of trade-direction data in calculating effective exchange rates, particularly for the exchange rate information notice system. The authorities had chosen their present method of basket selection in order to ensure that the international exchange value of the zloty "remained in touch" with the convertible currency settlement pattern of Poland's current account transactions.

The National Bank of Poland (NBP) quotes exchange rates for 29 "market-economy" currencies, and for the ECU, 1/ because the July 1980 rescheduling agreement with commercial banks provided for the extension of some ECU credits to the Bank Handlowy. While the NBP does not deal in the notes and coins of a limited number of the currencies, 2/ it stands ready to effect transactions in all 29 currencies. It is the only bank authorized to transmit notes and coins to foreign correspondent banks. Buying and selling rates are set with a spread of 0.5 percent about the middle rate, except for notes and coins, for which the the spread is 2 percent about the middle rate. Rates are set at least once a week, on Thursday, and become effective the following Monday, when they are published. Rates for currencies included in the basket are usually based on the exchange rates between these currencies in international markets on the day the rates are set; however, at times of relative stability in international currency markets, the rates may be based on the average exchange rates in those markets during, at most, the previous four working days. 3/ Rates for the currencies are based on the quoted rate for the U.S. dollar and the dollar rates for the currencies concerned in international markets. 4/ Provision exists for the intra-week resetting

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1/ Australian dollar, Austrian schilling, Belgian franc, Canadian dollar, Danish kroner, Deutsche mark, Finnish markka, French franc, Greek drachma, Indian rupee, Italian lire, Iranian rial, Irish pound, Japanese yen, Kuwaiti dinar, Lebanese pound, Libyan dinar, Luxembourg franc, Netherlands guilder, Norwegian kroner, pound sterling, Portuguese escudo, Saudi Arabian riyal, Spanish peseta, Swedish kroner, Swiss franc, U.S. dollar, Turkish lira, and Yugoslav dinar.

2/ Indian rupee, Iranian rial, Irish pound, Kuwaiti dinar, Libyan dinar, and Saudi Arabian riyal.

3/ The quoted U.S. dollar rate is used to effect settlements under bilateral agreements with Afghanistan, Angola, Argentina, Bangladesh, Brazil, Columbia, Ecuador, Iceland, Iran, Lebanon, Mexico, some with Pakistan, and outstanding balances under a terminated agreement with Greece. The pound sterling rate is used for bilateral agreement settlements with Nepal and some with Pakistan, while the Swiss franc rate is applied for settlements under the bilateral agreement with the People's Republic of China.

4/ The NBP sets, but does not publish, bi-monthly exchange rates for the currencies of some other non-socialist economies (e.g., the Bahamas, Gabon); if activity in a currency becomes sufficient, its rate is added to the list of the at least once-weekly quoted and published exchange rates. For its internal use (not for public dissemination), the NBP also sets weekly exchange rates against the pound sterling and the U.S. dollar, both of which differ from the officially published rates, for the settlement of outstanding balances under otherwise dormant accounts with Egypt; it also sets a separate U.S. dollar rate for a similar account with Turkey.

of the quoted rates if exchange rates on international markets move by more than 1 percent. However, due to delays in the communication of new rates to all authorized dealers and to the newspapers in which the rates are published, an intra-week resetting of the quoted rates is normally not undertaken. 1/2/ The authorities are aware that a once-weekly setting of quoted rates (with the implicit delay of ten days before the rates are realigned with international market rates) can lead to broken cross rates, and they are therefore examining the possibilities of setting the quoted rates at least twice a week. The NBP does not quote forward exchange rates. There are no taxes or subsidies on purchases or sales of the currencies of non-socialist economies for normal business transactions; however, a surcharge of 100 percent is applied on the sale of such currencies to Polish tourists traveling abroad. Maximum allowable commissions and charges on foreign exchange transactions are set in line with international practice by the Council of Banks, of which the president of the NBP is the chairman. These levies are paid in zlotys (foreign currency) by domestic (foreign) customers.

The largest portion of Poland's trade and financial settlements with the member countries of CMEA is settled in transferable rubles through the International Bank for Economic Cooperation (IBEC). Each of the ten member countries of CMEA authorizes one of its banks, the Bank Handlowy in the case of Poland, to carry out all transferable ruble transactions. The clearing ruble is used for the settlement of most transactions with Albania and the Democratic Peoples Republic of Korea, and for some settlements with Viet Nam, Lao People's Democratic Republic, and Kampuchea. Official exchange rates for the transferable ruble and the clearing ruble are set by the NBP each Thursday for publication on the following Monday, when they become effective. The exchange rates for the transferable and clearing rubles are set at the same level. In practice, these rates remain constant for extended periods of time. On January 1, 1982, the zloty/transferable ruble rate was devalued from Zl 44.44 to Zl 68 per transferable ruble; it was further devalued to Zl 72 per transferable ruble on March 1, 1984, and to 77 on January 1, 1985 (see exchange rate policy below). Buying and selling rates for both the transferable and clearing ruble are set at 0.5 percent about the middle rate.

The NBP also quotes rates of exchange on a weekly basis for the zloty against the currencies of member countries of the CMEA, Albania, and the Democratic People's Republic of Korea. These rates are used for noncommercial settlements, for example, international travel, scholarships, expenses of diplomatic representation, etc. The rates are set by the Minister of Finance after consultation with the president of the NBP and subsequent to multilateral and bilateral agreements with the

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1/ Prior to the end of 1981, rates were set every two to three weeks.

2/ In point of fact, given that we received all the exchange rate bulletins issued by the NBP in the period January 1, 1982-April 1, 1985, the rates have not been set more than once a week in the 3 1/4 years ending March 1985.

socialist partners. At the multilateral stage, an appraisal is made of each currency's purchasing power in terms of the retail prices for an agreed basket of goods and services used by tourists. These multilateral talks set base national currency rates in terms of the Soviet ruble, from which base zloty/"socialist partner currency" exchange rates are derived. Due to differential rates of inflation, these latter rates may undergo adjustments by up to 20 percent as a result of bilateral negotiations. Current rates in force were set on the basis of Zl 66 per Soviet ruble for Albania, Bulgaria, Cuba, Hungary, the Democratic People's Republic of Korea, Mongolia, Romania, and Viet Nam; and (b) Zl 69 per Soviet ruble for Czechoslovakia, the German Democratic Republic, and the U.S.S.R. 1/ In recent years, these rates have been changed on an average of once to twice per year. The zloty was devalued by 10.7 percent against the GDR mark (in foreign currency terms), with effect from April 1, 1985. Buying and selling rates (including for notes and coins) are set with a spread of 0.5 percent about the middle rate. A surcharge equal to 30 percent is applied on the sale of these currencies for private trips abroad.

2. Exchange rate policy

Since January 1, 1982, the authorities have sought to follow an exchange rate policy which sets the basic exchange rate of the zloty vis-à-vis the U.S. dollar at a level which should secure the profitability of 75-85 percent of exports. (Once the basic rate is set, the nominal effective exchange rate of the zloty is held constant against the basket of currencies.) On a monthly basis, the value of at least 75 percent of exports in terms of domestic (wholesale) prices is compared with their value in foreign (actual transactions) prices expressed in U.S. dollars. If the resultant ratio changes by 5 percent or more, consideration is given to changing the basic exchange rate. Information pertaining to the calculation of the rates is usually available with a lag of about 20 days. Adjustments of the basic exchange rate are not automatic, nor need they be equal to the calculated differential. After a detailed economic analysis, the decision on a change in the basic rate is taken by the president of the NBP, in agreement with the Ministers of Finance and Foreign Trade, and in consultation with other relevant institutions (such as the Planning Commission and the Price Adjustment Board), and outside experts.

The exchange rate of the zloty against the transferable and clearing rubles is set according to the same methodology and procedures as in setting the basic rate for the U.S. dollar, i.e., the rate in a submarginal one which should ensure the profitability of 75-85 percent of exports to the socialist countries. 1/ The authorities emphasized that they had complete autonomy in setting the transferable (and clearing) ruble rate.

1/ A separate rate is quoted for Soviet-ruble-denominated travelers' checks. This rate is derived from the zloty/U.S. dollar rate and the official Soviet ruble/U.S. dollar rate.

2/ It is not clear which foreign prices are used in calculating the required ratio.

With respect to the 15-25 percent of exports whose profitability is not secured by the intentions of exchange rate policy, the authorities noted that these--and other--exports were subject to the Equalization Settlement System, whereby foreign trade transaction prices may be equalized with domestic prices by means of a scheme of subsidies and taxes operated by the Ministry of Foreign Trade. In 1984, some 40 percent of exports to market economies and about 70 percent of exports to socialist economies were settled at transaction prices.

3. Authorized entities

Narodowy Bank Polski (the National Bank of Poland), Bank Handlowy w Warszawie SA, and Bank PKO SA are the three entities which, under the Exchange Regulations Law of April 1, 1984, have "general permission" to undertake all required foreign exchange transactions. Other entities receive "individual permission" to engage in such exchange transactions as are necessary to meet the activities allowed by their charters; these entities include trade enterprises such as PEWEX, Cepelia, Desa, and Baltona (which deals mainly with diplomatic missions and operates duty-free stores at airports, etc.) and service units such as ORBIS and its affiliated hotels. The rights of these institutions are granted on a permanent basis. Other bodies, such as the Poznan International Trade Fair, may receive permission to deal in foreign exchange on an ad hoc basis; such rights are "profile restricted" and are not permanent. 1/

4. The black market

The NBP attempts to collect data on black market foreign exchange activity via the militia and its own officials. While it considers its data on exchange rates to be reasonably accurate, its knowledge of supply and demand is limited. Through the end of 1980, the U.S. dollar rate showed an average multiple of about four to the official rate. For example, in 1980, the average black market rate was Zl 125 per U.S. dollar, and the average official rate was Zl 31 per U.S. dollar. Between August and end-November 1980, the multiple increased rapidly, to a record of some 15 1/2 in November 1981, when the black market rate was about Zl 539 per U.S. dollar as compared with an official rate of Zl 35 per U.S. dollar. Since then the black/official market spread has narrowed, and indications are that it is now returning to its pre-1980 average. Average black and official market rates for the period 1981-1st quarter 1985 were as follows, in zlotys per U.S. dollar:

	Official	Black market
1981	35	286
1982	85	400
1983	92	585
1984	114	638
1985 (1st quarter)	140	670

1/ We were promised, but have not yet received, the exchange control regulations.

The latest available rates were for March 29, 1985, when the rate across Poland (the authorities appear to have quotations from all areas of the country) was Zl 670-Zl 690 per U.S. dollar.

The currency predominantly demanded on the black market is the U.S. dollar, which was ascribed as being due in large measure to the Poles' "love for the dollar." Activity in the market derives from (a) the use of foreign exchange for transaction purposes (in PEWEX stores, etc.), which was linked to shortages in the internal markets, (b) rumors about currency reform, and (c) the desire for a stable store of value.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 7A
Held at the Ministry of Finance
on April 1, 1985 at 3:00 p.m.

Polish Representatives

Ministry of Finance

Mr. S. Tyminski, Director, State Budget Department
Mr. S. Czerniak, Director, State Revenue Department
Mr. A. Wernik, Director, Financial Policy Department
Mrs. Z. Gawlik, Director, Social Sphere Financing Department
Mr. K. Krowacki
Mr. Z. Lichocki

State Planning Commission

Prof. S. Raczkowski
Mr. S. Milewski

Central Statistical Office

Prof. L. Zienkowski
Mr. B. Szybisz

National Bank of Poland

Mr. S. Przywecki
Mr. G. Kolodko, Advisor to the Governor

Fund Representatives

Mr. Hole
Mr. Prust
Ms. Swiderski

The discussion covered two topics: the fiscal system and measurement of the liquidity overhang.

1. The fiscal system

Mr. Tyminski said that the procedural framework for drawing up and implementing the state budget had been provided in two recently enacted laws. The first was the Law on People's Council and Local Authorities which had been passed in July, 1983 and the second was the Law on Budgets passed in December 1984. One general aim of this legislation was to strengthen parliamentary control over the drafting and implementation of the state budget. Accordingly, the law now stipulated that only the Parliament had authority to increase overall budgetary outlays in a particular year; previously, the Council of Ministers or even the Ministry of Finance had had this right. Similarly, any change in the use of budget "credits" (sic) had to be approved by the budget committee of the Parliament. In addition the Ministry of Finance was required to inform this committee regularly on budgetary developments. The draft of the Five-Year Plan submitted to the Parliament was to include projections of budgetary revenue and expenditure. These projections were never incorporated into any legislation but the fact that they were submitted to the Parliament was in line with the intention of increasing the latter's control over budgetary matters.

A second main objective of the recent legislation on budgetary procedures was to strengthen the financial position of People's Councils, and to increase their financial independence. Accordingly, People's Councils had been accorded full financial autonomy which was only limited by other laws and by the size of the general subsidy to local administrations from the central government budget. The latter subsidies had become minor and in 1985 were expected to account for only 10 percent of total spending by local governments. Mr. Tyminski went on to describe various other general features of the recently enacted law on budgets and in this connection he listed the various revenues which accrued to local governments. These were: (i) taxes paid by enterprises whose founding body is a local authority; (ii) taxes on cooperatives established within a given voivodship; there were, however, exceptions to this rule and taxes by certain cooperatives, such as those for the disabled, accrued to the central budget; (iii) 85 percent of proceeds of the tax on wages; (iv) 100 percent of real estate taxes paid by all socialized entities; (v) the proceeds of turnover tax and profit tax from all nonsocialized entities operating within given voivodships; (vi) proceeds from the equalization tax, the tax on agricultural land, taxes on inheritance and gifts, and certain other minor local taxes; (vii) a given share in the revenue accruing the central government; this share was set for five years at a time as a percentage of the value of retail sales of goods and services by socialized enterprises and was determined by the Parliament; (viii) proceeds from the profit tax on cooperative banks; (ix) the proceeds of taxes paid by "agricultural circles" and cooperatives and other agricultural associations; (x) the proceeds of taxes on civic organizations; (xi) the proceeds of turnover tax and profit tax payments by physical persons and entities domiciled abroad and by foreign entities engaged in economic activity in Poland; (xii) charges on administrative units and administrative incomes of such units; (xiii) certain payments made by budgetary units; (xiv) payments of certain funds that Mr. Tyminski described as "surplus funds".

As to financial transfers between the central and local governments, Mr. Tyminski said that the payment of the general subsidy from the central government was effected quarterly. In addition, payments in respect of "objective" subsidies which were the responsibility of local administrations were made in full to the People's Councils when the relevant regulations were enacted. Furthermore, the central budget could make certain exceptional payments to local authorities to cover expenditures incurred because of natural disasters.

Mr. Tyminski said that the central budgetary authorities had no right to order the transfer of surpluses generated by local authorities provided that equalization payments (i.e., general support payments from the central budget) to these authorities had been made on schedule. Thus, any surpluses generated in local budgets remained under the control of the relevant People's Councils and could be used by them at their own discretion. However, the size of local budget surpluses would be taken into account when setting the general level of equalization payments--something which was done every five years.

Mrs. Gawlik spoke about various social benefits. Family benefits were payable to all with children under the age of 14 or with members above retirement age (55 for women and 60 for men). The rate of benefit depended on per capita income in the family. If the latter exceeded Zl 5,000 per month the rate of benefit was Zl 1,300 per month; if per capita income was in the range Zl 3,000-5,000, the rate of benefit was Zl 1,500, and if per capita income was below Zl 3,000 the rate of benefit was Zl 1,800. Lower rates of benefit applied for private farmers and those who were not employed. These basic rates of benefit could be augmented for families who had sick children or who had family members who required permanent nursing care. Benefits in respect of the former were in the range Zl 900-2,700 and for the latter were at a constant rate of Zl 1,500 per month. These benefits were expected to rise as a result of the recent price adjustments--the allowance for sick children by between Zl 250 and Zl 750 and the nursing allowance by Zl 250.

Child birth benefits were payable at a rate of Zl 2,500 per month, apparently during the period of maternity leave. Normal wages or salaries were paid to anyone taking maternity leave which lasted from 16 to 18 months except where twins were born when the leave period lasted for 24 months. Additional benefits were payable to single parent families in respect of children between 24 months and four years of age. The maximum rate of allowance was Zl 3,200 per month for families with a per capita income of less Zl 16,000 per month. There was a declining rate of benefit for those earning higher incomes and no benefit at all was paid if per capital family income exceeded Zl 3,600 per month.

Sick leave was payable at the rate of 75 percent of normal earnings for those who had been working for less than three years; at a rate of 85 percent of normal earnings for those who had been working between three and eight years; and at a rate of 100 percent of normal earnings for those who had been working for more than eight years (it was not clear whether the working periods referred to were for somebody's total working life or in respect of working at a particular job). The normal period for which sick leave was payable was six months but could be extended to up to nine months in cases of serious illness.

Social security payments were made to all women over 60 years old and to all men over 65 years old; to all people classified as first or second category invalids; and to certain other categories of people experiencing temporary hardship. The latter were payable for six months at a time and at a rate equivalent to 80 percent of the lowest old age pension.

Scholarships were paid to students according to a sliding scale of family income. The maximum scholarship was Zl 8,600 per month and the lowest, payable to students with families of income above Zl 8,500 per month, was Zl 100 per month.

Certain social benefits were paid in kind. The main one was the right to free or subsidized medicine. Medicine was completely free to invalids, those with occupational diseases, and certain other groups. The rest of the population was required to pay 30 percent of the cost of medicine.

Mr. Tyminski said that under the terms of the recently enacted law on budgets extra budgetary funds ("purpose" funds) could only be established by Parliament or, in the case of local funds, by resolutions of People's Councils. Previously extra budgetary funds could have been established by the Council of Ministers. The rules for transfers between the state budget and such funds had to be specified in the legislation establishing each fund. There were 24 extra budgetary funds linked to the central government and 13 which were linked to local authorities. Transfers from the budget to the funds would be counted as budgetary expenditure and allocated to the ministry or other government authority most closely concerned with the fund in question: for instance, transfers to a fund which was under the control of the Ministry of Health would be shown as part of central government health expenditures. Total spending by extra budgetary funds in 1985 was forecast to be Zl 1,041 billion of which Zl 237 billion would be covered by transfers from the budget. The largest fund was the Retirement Fund and other important funds included the Cultural Development Fund, the Research Fund, and the Fund for Professional

Activation. In the case of the latter, there was a provision whereby any surplus was automatically transfered to the state budget. Other funds normally had the right to retain any accumulated surpluses. The pension fund had accumulated considerable net assets but these were earmarked for the payment of pensions. Mr. Tyminski was not sure whether any other funds had accumulated significant surpluses.

Mr. Czerniak described the system of tax rebates for encouraging certain forms of economic activity. In 1984 the total cost to the budget of such rebates had been Zl 144 billion of which Zl 51 billion had been in respect of exports. These amounts were not explicitly reflected in the budget as an expenditure and only appeared implicitly in that revenues were lower than would otherwise have been the case. In 1985 rebates would be raised even further.

Mr. Czerniak said that tax rebates to encourage exports took three forms. A tax rebate was given in respect of 5 percent of the zloty value of exports, i.e., the amount of tax to be paid was reduced by this amount. A second concession was that a certain proportion of the growth in exports in hard currency (calculated at constant exchange rates) could be deducted from an exporter's tax liability. This proportion had been 30 percent in 1984 but in 1985 would be raised to 35 percent. Finally, starting in January 1985, a new system of rebates to encourage export-oriented investments had been introduced. The rebates granted could be for up to 30 percent of the cost of the project but it was a requirement that the project be completed within three years. No standard definition of an export-oriented investment had been adopted and no applications for rebates under this scheme had yet been received. The Ministry of Finance was hoping to receive such applications in due course which it would review on a case-by-case basis.

Tax incentives were also used to to encourage investment in particular sectors of the economy for e.g., mining, the recycling of raw materials, environmental protection, and import substitution. The tax system was also used to encourage an improvement in the quality of goods. All those whose output fell into the quality categories 1 and 2 received tax concessions. On the other hand, 70 percent of costs incurred in respect of defective output were added to the profit base for the purpose of calculating income tax; in other words, such costs were considered as unjustified. Mr. Czerniak also mentioned that all interest payable on accrued tax liabilities was deemed an unjustified expenditure and that any gifts by enterprises or any other tax paying unit had to be taken out of profits and could not be treated as a cost. There were variations in the rate of taxation profits with a view to encouraging the growth of the service sector, for example, laundries, tailoring, and repair. Moreover, there were many provisions in the tax system to encourage the hiring of handicapped persons.

Mr. Czerniak said that not all profit tax concessions worked in the form of giving a rebate on tax liabilities. Some, for instance those designed to encourage the growth of service industries, were in the form of a reduction in the tax base.

Mr. Hole enquired whether the Polish tax code incorporated the notion of unreasonable profits. Mr. Czerniak replied that for tax purposes this notion had been abandoned in 1981. Currently, it only had relevance in connection with the law on prices. If prices were set at levels above those permitted by the law, the seller had to refund the resulting excess earnings and to pay an additional penalty equal to 100 percent of the excess. (It was not clear to whom the refund or the penalty was paid.) The tax code did, however, stipulate penal sanctions for enterprises which sought to include investment expenditures as a cost of production. The law required that investment expenditures be financed from enterprise development funds which were fed from after-tax profits. If detected, any enterprise including investment expenditures as a cost of production would have its income tax liability increased by the amount of the misappropriation. The tax authorities sought to ensure that profits were properly calculated which, in the case of socialized enterprises, had to be done on the basis of audited annual balance sheets.

Turning to turnover taxation, Mr. Czerniak said that the most prevalent rate was 10 percent for goods and 5 percent for services. Nearly all food produce was exempt from turnover taxation but some luxury items, such as alcohol, tobacco, and liquid fuels, were taxed at far above the standard rate. However, the number of such items was small. The revenue from turnover taxation accruing to the central budget had been Zl 933 billion and Zl 1,147 billion in 1983 and 1984, respectively. The Minister of Finance had the authority to adjust rates of turnover taxation without parliamentary approval. Prof. Zienkowski referred the mission to a table in the statistical yearbook which showed the commodity composition of turnover tax receipts.

Mr. Czerniak gave the following general information on the purpose and extent of tax relief. In 1984 the effective rate of income taxation on enterprise profits had been 47 percent compared with the notional standard rate of 60 percent. In order to curtail investment demand on the part of enterprises, the standard rate of income tax had been raised to 65 percent in 1985. It was intended to retain this rate for several years. Also with a view to curtailing investment demand, there had been various changes in the taxation of depreciation allowances in recent years. In 1984 the value of fixed assets had been recalculated so as to take account of inflation. This had resulted in a quadrupling in the value of fixed assets but annual depreciation allowances would only gradually be adjusted over the four year period to levels corresponding to the new valuation of the capital stock. A tax, at a rate of 50 percent, had been imposed on enterprise depreciation allowances so as to prevent their giving an excessive boost enterprise liquidity. However, there were numerous exemptions, either partial or total, from this requirement such that in 1984 only 23 percent of depreciation allowances had accrued to the budget. Adjustments in the rate of taxation on depreciation would continue to be a main instrument in influencing investment demand.

The tax on wages was set at a flat rate of 20 percent. The original intention had been that receipts from this tax would more or less finance the costs of training the labor force, including education.

The vast majority of subsidies were intended to support administered prices that were set at a level below that consistent with a normal profit for the production and distribution units concerned. In such cases, the subsidy was determined as a given money amount per unit of output. However, in other cases such precise calculations could not be made and the subsidy was made to the units in question on the basis of their overall financial position. Inter alia, this procedure was used in subsidizing the steel industry and certain municipal services.

Mr. Hole raised two broad questions. First, he invited reactions to the view of some commentators that the budget was an overactive participant in the Polish economy: according to this view, the gross levels of both taxation and subsidization were too high. Secondly, he wondered whether the lack of uniformity in the tax regime faced by various units in the economy was appropriate. Mr. Wernik agreed that there was excessive differentiation in the treatment accorded to various taxpayers. It was the authorities' policy gradually to reduce this differentiation but it was a difficult process.

Mr. Hole also invited comments on the view that incentives to enterprises to raise their efficiency were considerably dampened by the combination of a high rate of taxation and the very high rates of contribution to the FAZ that would result if additional profits were distributed to the workforce. Mr. Wernik said that on this point he did not agree. He felt that the present high rates of taxation were justified by the needs of the government's anti-inflationary policy.

Mr. Wernik said that investment expenditure accounted for 11-12 percent of total budgetary outlays. A certain part of this amount was for investment in areas that were properly the function of the government such as education and health care. More difficult questions arose in connection with budgetary support for enterprise investment. This was only provided if certain conditions were met. The first condition was that the project in question had to be very important to the national economy. A second condition was that enterprises did not have sufficient funds of their own (perhaps as a result of their being subject to price control) and could not qualify for bank credit of the required amount. Further conditions were that the share of enterprise profits allocated to investment financing should not be less than 75 percent and that the share of budgetary financing should not exceed 20 percent of the cost of the project in question. The only exceptions to the latter rule were for investments in railways, communications, and certain maritime enterprises which could be fully financed from the budget. All investment financing from the budget was in the form of grants.

2. Measurement of the liquidity overhang

Dr. Kolodko spoke about the calculation of the size of the liquidity overhang. The general approach he had followed in his work was to monitor the growth of monetary balances held for transactions purposes and for voluntary savings purposes and to compare their actual behavior with some estimate of what would have been their behavior under conditions of full market equilibrium. Experience in the period 1972-74, when the economy was much closer to equilibrium, was an important part of the basis for estimating the equilibrium value of the revelant behavioral variables. Other considerations to be taken into account were the level of liquidity balances in Poland in comparison with other similar countries and changes in the structure of bank deposits. He noted that money balances that were involuntarily held in one period could, under changed conditions, come to be voluntarily held in another period, and vice versa. He also noted, but did not fully explain, that the year 1985 was exceptional because of the maturing of long-term savings instruments issued by the banks three years earliers. The central problem was to determine what part of the population's money balances was voluntarily held and what part not. There were no unambiguously correct methods for doing this. Account had to be taken of many different things, including the composition of the note issue and the savings habits of the population. Taking account of all these factors, Dr. Kolodko had assumed that the stock of voluntary financial savings consisted of all long-term deposits with banks, all special deposits, and 35 percent of demand deposits. For households the demand for transactions balances was assumed to be equal to half a months' earnings. For private businesses, the demand for transactions balances was assumed to be equal to 1 1/2 months of some variable, but whether it was net income or gross sales or something else was not clear. Further assumptions, appeared to be that 5 percent of call deposits at PKO and 25 percent of deposits in cooperative banks represented voluntary transactions balances. It was also assumed that no voluntary savings were held in the form of cash.

On the basis of these assumptions, Dr. Kolodko reached the following general results. In nominal terms the size of the liquidity overhang had increased by 25 percent between 1982 and 1984 but had fallen in real terms by 20 percent over this period. In 1984 the value of stocks exceeded the size of the estimated liquidity overhang. He went on to say that he assumed that the rate of voluntary saving had fallen since 1972-1973 which he regarded as a base year. However, it was not clear whether this was simply an assumption or whether it was a conclusion which emerged from his estimates. Mr. Hole noted that the erosion of the real value of financial wealth in recent years could have had a substantial effect on the voluntary savings rate.

Mr. Prust enquired as to the reasons for assuming that only 35 percent of demand deposits were voluntarily held. He wondered whether there was anything in the available data on the turnover of such deposits to justify this assumption. Mr. Kolodko replied that in the period 1982-84 demand deposits had on average "turned over" about every 11 months to one year. The corresponding figures for the 1972-74 period were similar but there were great variations in the rate of turnover between different accounts. Mr. Przywecki noted that there appeared to be a growing overhang in the form of cash. In the mid-1970s currency issued by the National Bank was on average returned to it in five days; the corresponding period was now fifty days.

The meeting ended at about 6:00 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 7B
Held at the National Bank of Poland (NBP)
on Monday, April 1, 1985, at 3:30 pm

Polish Representatives

Ministry of Finance

Mr. Z. Minarczuk, Advisor to the Minister
Mr. I. Ilczek, Division Chief
Mr. J. Czabanski

National Bank of Poland

Mr. G. Wojtowicz, Director, Foreign Dept.
Ms. M. Rubel, Advisor, Foreign Dept.

Bank Handlowy w Warszawie SA

Mr. A. Sala, Deputy Director
Mr. S. Ludwikowski

Fund Representatives

Mr. Manison
Mr. Boonekamp

The principal topics of discussion were settlements with the member countries of the Council of Mutual Economic Assistance (CMEA), bilateral clearing agreements with IMF member countries, resident and nonresident accounts, and the system of "effectiveness bids" for foreign exchange. Other matters touched upon were import licenses, the import/export of Polish currency, and gold holding and trading by Polish residents.

1. CMEA settlements

Settlements with CMEA member countries are effected in accordance with the intergovernmental agreement which went into force in 1964, and as amended in 1970 and 1977. The International Bank for Economic Cooperation (IBEC) was created under the agreement, as was the transferable ruble, the accounting unit for the bulk of trade and financial settlements between CMEA member countries. IBEC serves as a clearing house, with which the Bank Handlowy, as Poland's authorized bank to IBEC, holds accounts for the settlement of transactions denominated in transferable rubles. Trade, which need not be balanced between CMEA members, takes place on the basis of five-year agreements implemented by annual bilateral and multilateral negotiations. World prices, adjusted according to the Bucharest Summit formula of 1969, are used. Mutual deliveries of goods are agreed upon at the bilateral stage, as is the value of services and transfers between the partners. At the ensuing multilateral talks, the members examine the possibilities of affecting additional commodity supplies and of balancing receipts and expenditures in relation to all partners taken together. If, in settling its accounts, a member's trade expenditures exceed its receipts, then IBEC is prepared to extend a short-term (up to one year) revolving settlement credit of up to 2 percent of that nation's total turnover with the CMEA area in the previous year, at an interest rate of between 2-3 percent per annum, depending on the amount of credit utilized. Given bilateral agreement, these credits may be extended into term credits with a maturity of 2-3 years and at an interest rate of 3 1/4-5 percent per annum. Settlements relating to trade transactions account for about 98 percent of all Polish settlements effected through IBEC; the remaining 2 percent relates to noncommercial dealings, and embraces travel expenses, the cost of diplomatic missions, etc. These latter settlements, for which IBEC keeps separate accounts, are made at the bilaterally agreed national currency rates vis-à-vis the Soviet ruble, multiplied by a multilaterally agreed Soviet ruble/transferable ruble coefficient. The coefficient, which reflects the outcome of domestic to foreign trade "tourist" prices, currently stands at 1.7.

2. Bilateral clearing arrangements

The Bank Handlowy representatives stated that they were not in a position to discuss Poland's bilateral arrangements policy, which is in the hands of the Ministry of Foreign Trade. The latter Ministry would give the staff a complete list of Poland's current bilateral arrangements with IMF member countries, including, for each arrangement, the terms of validity, the currency of settlements, the swing limits, and the relevant interest rates. At present, Poland has bilateral clearing arrangements with 16 Fund members, including, as of late 1984, a minor account with Argentina for the settlement of some trade transactions, entered into due to Argentina's ongoing economic and foreign exchange difficulties. Of the bilateral partners, only Iceland is a "non-third-world country." Of Poland's 1984 convertible currency trade, some 8.6 percent of exports and 9.8 percent of imports were settled through clearing arrangements, the most important of which are with Brazil, Iran, India, and Colombia, in that order. Since 1981, more than 50 percent of the imports under clearing arrangements have come from Brazil. This agreement contains a provision for a quarterly examination of the outstanding balance, and the subsequent possibility of prompt payment.

In the late 1970s, there was a tendency to terminate bilateral agreements, but, due to the economic difficulties being experienced by Poland and its partners, there has been a "forced" reopening of accounts since 1981. However, policymakers are of the opinion, that, in general, trade should be on a convertible currency basis rather than on bilateral clearing terms. Other than its existing clearing arrangements, Poland also maintains some barter accounts for specific goods and/or between certain companies; such an arrangement is in place for a small percentage of Poland's trade with New Zealand, for example.

3. Resident and nonresident accounts

a. Resident accounts

Under Article 10 of a law promulgated on November 22, 1983, Polish residents can hold foreign exchange in the form of currency, stocks, bonds, gold, etc. Four types of foreign currency accounts are available: convertible currency accounts "A" and "N" for residents; socialist currency accounts "S" for residents; and "ROD" accounts for the foreign exchange retention quotas of enterprises against their exports of goods and services to the convertible currency area. The latter accounts are held with the Bank Handlowy; the former accounts are held with the Bank PKO (75 percent), the NBP (23 percent), and Bank Handlowy (2 percent). None of the accounts have reserve requirements against the deposits.

(1) Accounts "A" can be freely credited with convertible currency transferred from abroad and/or received from royalties, copyrights, gifts, etc. Subsequent to a Ministry of Finance ordinance published on November 30, 1984, to take effect on April 1, 1985, the sources of the funds must be declared when they are deposited. Account holders can use the funds, up to the limit of the amount on deposit, to finance tourist travel abroad by them and their next of kin, to purchase foreign exchange coupons for use in PEWEX stores, and to effect gifts to family members. 1/ Withdrawals in zlotys, converted at the prevailing exchange rate, are freely permitted. 2/ Interest, paid in foreign exchange, is earned at the following annual rates: 5 percent on call deposits; and 9 percent, 10 percent, and 11 percent on one-year, two-year, and three-year term deposits, respectively. The funds on deposit cannot be used for effecting settlements between individuals. A minimum deposit of US$10, or its equivalent, is required to open an account "A."

(2) Accounts "N," which came into effect on April 1, 1985, can be freely credited with convertible currency without the requirement that the source of the funds be declared. Funds on deposit in these accounts do not earn interest, and may not be used to finance travel abroad. However, after one year the funds on deposit are transferable to an individual's account "A." In all other respects, the modalities of an account "N" are as for an account "A."

(3) Accounts "S" can be credited with socialist country currencies derived from wages, property sales, inheritances, royalties, gifts, etc., and with transfers from other accounts "S." Funds in these accounts are freely transferable abroad (to other socialist countries) and may be freely withdrawn in any socialist country currency, with conversion effected at the national currency rates quoted by the NBP. Deposits earn interest at 3 percent per annum on call money, and at 4.5 percent per annum for one-year term deposits.

1/ We do not know if "market economy" currencies other than that of deposit are obtainable.

2/ Prior to January 1, 1985, a premium of 100 percent was applied on the conversion of currencies from these deposits into zlotys.

(4) Deposits in "ROD" accounts stem from an enterprise's retention quota of the foreign exchange earned from its sales of goods and services to the second payments area, viz., the nonsocialist countries. An enterprise's retention quota is determined annually by the Ministry of Foreign Trade, in consultation with the Ministry of Finance, and is normally based on the (convertible currency) import intensity of its production. The maximum retention quota is 50 percent, except for certain service companies such as LOT airlines, for whom the quota can range up to 100 percent. An enterprise may use the funds on its account for the purchase of production-related imports from the second payments area, either for its own purposes or for those of its cooperating enterprise. The funds may not be used for business trips, publicity, and/or marketing expenses. In 1984, some 15 percent of Poland's second payments area imports were financed with "ROD" account funds. Although an enterprise's "ROD" account is in its name, the amounts in the account are not in its ownership, and are not carried in the enterprise's balance sheet as claims. Rather, it has "priority rights" to the funds, which at times has meant a delay of about five days to a week before it had actual access to the funds for the payment of imports. The accounts, which came into force in 1982, do not yield interest on call deposits, but, for deposits equivalent to US$5,000 or more, they bear interest at per annum rates of 4, 6, 8, and 10 percent for term deposits of six months, one year, three years, and five years, respectively.

b. Nonresident accounts

(1) Nonresidents may maintain convertible currency accounts (so-called "C" accounts) at the NBP and at designated offices of the Bank Handlowy and of the Bank PKO. These accounts can be credited with funds brought into Poland, with transfers from other "C" accounts, and with amounts legally acquired in Poland. The deposits are freely transferable abroad, may be used to effect purchases from PEWEX and Baltona stores, and can be utilized to make gifts to accounts "A" and "N." The funds earn interest, payable in foreign currency, at the same rates as account "A" deposits, except that provision exists for term deposits of six months, bearing interest at a rate of 8 percent per annum.

(2) Nonresidents are free to hold zloty accounts, but, under the provisions of an April 1, 1983 law, they may be asked to declare the sources of the zlotys when making deposits into such accounts. The declaration requirement relates mainly to ensuring that nonresidents pay hotel, medical, leasing and legal costs, and customs duties, etc., with zlotys converted from foreign exchange brought in from abroad. Such zloty deposits are "freely disposable." 1/ Deposits made with zlotys legally earned in Poland have some limitations on their disposal, mainly with respect to their use for making foreign exchange transfers abroad, for which the permission of the NBP is required.

1/ "Freely disposable" is in quotes because it is not clear to what extent, if at all, such deposits can be used to effect foreign exchange transfers.

4. "Effectiveness bids" for foreign exchange

Enterprises have four foreign exchange sources for financing imports: the centrally allocated pool; their foreign exchange retention quotas; foreign exchange credits; and so-called "effectiveness bids," organized on an experimental basis since March 1983. These provide enterprises without retention quotas with a means of acquiring convertible currency to import goods and services. An enterprise participating in the bids must declare (bid) the zloty value of its proposed production per unit of its intended foreign exchange expenditure. The declaration is a determining ratio in an enterprise's foreign exchange allocation, which cannot exceed the equivalent of US$200,000 (initially US$100,000). Upon making a successful bid, an enterprise is required to deposit with the NBP a zloty amount equal to twice (initially three times) the purchased amount of foreign exchange, at NBP exchange rates. The deposits are noninterest-bearing and are forfeited if the foreign exchange is used for other than the declared purposes and/or the production bid is not attained. Deposits have generally been returned in a relatively short period of time. Enterprises are required to use their foreign exchange allocations, which they buy at quoted NBP rates, within three months. To date, 19 bids have been held, with 69 enterprises participating, of which 45 were allocated foreign exchange, equivalent to US$1.32 million (or 0.01 percent of total convertible currency imports in that period). The scheme has produced some Zl 4 billion of production, mainly for internal use, at an "effectiveness rate" of about Zl 3,000 per US$1 of imports. In the opinion of the NBP, the "rules of the game" should be significantly changed (in a way that was not specified) if the system of "effectiveness bids" is to be continued and made more successful.

5. Other matters

a. Import licenses

An import license grants the holder general permission to acquire the foreign exchange needed to complete the contract; however, it does not guarantee the availability of the necessary foreign exchange.

b. Import/export of Polish currency

Effective April 1, 1984, Polish residents are freely allowed to bring into or take out of the country domestic currency in an amount not exceeding Zl 3,000 per person per border crossing. The total in coins may not exceed Zl 50; the largest permissible banknote is Zl 1,000. 1/

c. Gold

Residents are permitted to hold gold in any form. Trading in gold is subject to permission from the appropriate authorities. Only one enterprise, viz., Jubiler, has general permission to transact in gold; Desa has specific permission to trade in numismatic gold coins. Gold is exported and imported (against low customs duties) at world prices. A note on the pricing of gold for domestic transactions is to be given to the Fund at a later date, as are the specifics of the regulations regarding gold.

1/ We have been promised the regulations with respect to visitors; these regulations have remained unchanged since 1981. The answers to the 1981 questionnaire suggest that visitors may neither bring in nor take out Polish currency without authorization.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 8A
Held at the Planning Commission
on Tuesday, April 2, 1985 at 10:00 a.m.

Polish Representatives

Planning Commission

Mr. S. Milewski, Director, Department of Economic Analysis
Mr. S. Pajewski, Director, Department of Construction Investment
Mr. T. Piekarski, Vice Director, Department of External Relations

Ministry of Finance

Mr. A. Wernik, Director, Department of Financial Policy
Mr. W. Manugiewicz, Department of Financial Policy Department

National Bank of Poland

Mr. H. Mlodzianko, Vice-Director, Department of the Credit System

Fund Representatives

Mr. Hole
Mr. Prust
Ms. Swiderski

The meeting covered three topics: (1) investments, (2) stock behavior and (3) enterprise accounts.

1. Investments

a. Goals

The basic aim of investment policy in the 1981-85 period has been to achieve the most efficient use of technical and financial resources. Priority sectors for new investments are (1) foodstuffs, (2) housing, and (3) fuels and energy. In the area of social consumption new investments are primarily directed to (1) health care and (2) education. New investments account for only 10 percent of total investment outlays which is a much lower proportion than prior to 1980. These investments have tended to be small in scale and apart from social investments, they have concentrated on the modernization and replacement of equipment in industries specializing in exports, transport, and consumer goods. By contrast, investments undertaken prior to 1980 were normally characterized by long gestation periods and large costs and were concentrated in the production of manufactured industrial goods. Since 1980 the share of industrial projects in new investments has declined markedly (particularly in metallurgy and engineering). In its place there has been a steady increase in the share of local investments (from 14 percent of new investments in 1979 to over 30 percent in 1983), reflecting the social needs that were neglected in the 1970s, as well as fuel and energy investments.

b. <u>Instruments of control</u>

The general level of investments is determined in the annual and five year plans on the basis of material and financial balance sheets, particularly with respect to the generation and distribution of national income between consumption and capital formation. There is no formal allocation of investment outlays between the government and enterprises. Investments that are not centrally controlled are not binding; consequently the overall level of investment outlays in the Plan can only be regarded as a target.

Central investments and investments of budgetary units (e.g., in the area of health and social welfare, education, culture, etc) are directly controlled by the State and are bound to the Plan targets. Since over 90 percent of investment outlays of budgetary units are financed by the budget, direct control is easily achieved. Budget subsidies in excess of those stipulated by the Plan are never granted. Central investments mainly cover investments in raw materials and basic inputs, fuels and energy and in social and technical infrastructure, all of which are considered to be in the national interest of the economy. Not all centrally planned investments are included in government contracts or in operational programs. Together directly controlled investments account for about 16 percent of total investment outlays.

The remaining 84 percent of investments are only indirectly controlled via parametric instruments. These include investments of enterprises, cooperative residential construction, social and special funds, and the nonsocialized sector, mainly in agriculture, handicrafts, and Polonia firms. Investments of local authorities are tightly controlled because over 90 percent of their funds stem from the budget. The main tools of indirect control are the conditions associated with the credit and budget subsidy policies. Other instruments include reductions in income tax payments and in depreciation allowances transferred to the budget. In regard to the latter, while the normal retained allowance for depreciation charges is 50 percent, the exemption can range to up to 100 percent. In an effort to bring investments in line with targeted levels, at the beginning of 1984 the Government introduced a temporary regulation requiring investments undertaken by enterprises and local entities, valued at over Zl 500 million and in need of budgetary subsidies, to be approved by the Chairman of the Planning Commission in agreement with the Ministry of Finance.

It was noted that the share of investments in construction and assembly had increased markedly (from 54 percent in 1980 to nearly 69 percent in 1984). This was largely explained by the shortage of imports, pressures to increase housing facilities as well as the improved financial performance of construction and assembly contractors. However, the data had to be interpreted with caution for two reasons: (1) until 1981 price changes were only taken into account every five years with investment outlays in the 1978-1980 period being valued at 1978 prices and (2) since 1980 the price index of construction and assembly has risen at a faster rate than that of machinery equipment. The staff commented that if interest rates on deposits were raised, enterprises might be more willing to refrain from investing in construction projects that were of low quality and await the availability of machinery and equipment. In order to slow the rate of increase in construction and assembly, in 1985 the authorities introduced a compulsory deposit requirement equivalent to up to 50 percent of the value of investments in construction, refundable at the time of completion of the project provided it was finished on schedule.

The authorities did not feel that the central allocation of basic materials limited the autonomy of enterprises in undertaking investment decisions. This was largely because enterprises, especially the large ones, had access to foreign exchange through the export retention scheme allowing them to import the required materials on their own account.

c. Suspension of investment projects

To date a number of investment projects valued at Zl 1,500 billion have been suspended. Decisions on the postponement of large investments are taken by the Council of Ministers. Decisions concerning smaller projects can be taken by the relevant Ministry or voivodship. Suspended projects may be started up again by enterprises which have enough own resources to finance them; however,these projects cannot be financed with bank credits. Thus, in Mr. Pajewski's view, the lowering of investment activity in this manner has not been as effective as planned. Sixty-nine percent of postponed investments stemmed from the industrial sector (of which 39 percent were in steel and iron), 11 percent in transportation and communications (especially highway projects), 5 1/2 percent in socialized agriculture and 4 1/2 percent in construction.

d. Actual investments exceeding their targets

The overfullfilment of Plan targets has been for the most part attributable to the investment activity of enterprises. The central investments, those of budgetary units and local entities, have been on target. The main reasons for higher than planned investments by enterprises are (1) larger than expected increases in output and prices which resulted in a better than expected financial performance of enterprises; (2) large resources being needed to complete projects already started; (3) machinery and equipment of the 1970s having become obsolete and there being a need to prevent a further "decapitalization" of the capital stock; (4) enterprises being pressured to increase investments for social purposes which had been neglected in the 1970s (30 percent of new investments of enterprises has been in the social sphere); (5) the housing shortage which has been aggravated by the skewed age distribution of the population in favor of young people; and (6) the fear that unspent funds would be taxed away in one form or another. Thus, the higher than planned increases in enterprise liquidity were mostly flushed into investments. Some of this excess investment occurred in the initial period of the reforms when the Government was in the process of formulating the instruments of control and during which time there was a lack of financial regulators. For investment activity being greater than planned in the later period, Mr. Pajewski felt that the Government was somewhat to blame since it was continuously adjusting its instruments of control and, thus, not providing an environment of stability and predictability that would be required to gain the confidence of enterprises. While some of the higher than targeted investment outlays were used for modernization, which is considered a positive development, a large share of these expenditures were effected inefficiently, which has resulted in a reduction in the overall quality of investments. This was to some extent influenced by the lack of imports of machinery and equipment.

As regards 1985, the Plan targets a level of investment outlays that is broadly equal to actual outlays in 1984. By comparison to targets set for previous years, this is viewed as a more realistic one to achieve. Furthermore, limiting excessive investment activity should be facilitated by the development of better and more restrictive instruments of indirect control (e.g., tighter credit conditions, limitations on budget subsidies, deposit requirements for investments in construction, compulsory transfer of a portion of the depreciation allowance to the budget, limitations on enterprises' investments exceeding Zl 500 million, etc.). The severe winter has also helped to dampen overall investment activity. An excess of investment outlays over targeted levels on the order of Zl 50-100 billion would not be considered as significant.

In the second half of 1984 the Planning Commission introduced a computerized system to track investment activity. The system encompasses detailed financial information on 70-80 percent of all investment projects (excluding housing). The lag in receiving these data is only one month.

While the authorities felt that the instruments at their disposal were flexible enough for controlling investment activity if it became apparent that the target would be exceeded, their basic aim was to restore a stable policy environment and the confidence of enterprises. This they hoped could be achieved by establishing long-term normatives for operating their instruments. Moreover, they were of the opinion that the state of instruments at their disposal for 1985 was sufficiently adequate to fulfill Plan targets.

d. <u>Financing of investment outlays</u>

During 1984 investments of the socialized sector were financed in the following manner: 20 percent with budget subsidies, 33.8 percent with bank credits, and 46.2 percent with enterprises' own resources. 1/ By contrast, in 1982 the share of outlays financed by own resources was only 23 percent. About 10 percent of enterprises' own resources stem from a central fund administered by the branch ministries. Centrally planned investments in the productive sphere are financed in the majority by bank credits (in amounts exceeding the creditworthiness of the enterprise) and, to a lesser extent, by budget subsidies. These credits are repaid from the enterprises' development funds as well as with budget subsidies in cases where the enterprise does not have adequate means. A small proportion of centrally planned investments; mainly in the nonproductive sphere (e.g., for social and technical infrastructure--sewage, water supply, etc.), are financed entirely by budgetary means. In 1983-84 budget subsidies financed about 8-9 percent of all centrally planned investments. This includes the financing of budgetary entities where budget subsidies accounts for over 90 percent of outlays. In 1985 this share has been increased to 15 percent. Budget subsidies also account for over 90 percent of investments made by local entities.

As regards financing investment outlays of enterprises, the general rule is that budget subsidies cannot exceed 20 percent of total investment outlays. These subsidies are granted only when

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1/ This includes voluntary contributions of the population (e.g., in the National Fund for Health Care).

the investment projects are considered indispensable to the national economy and are in line with the directives of the central plan. Furthermore, they should be completed within 30 months, they must be judged as productive, and that they can be put into operation efficiently. The enterprise must also prove that it can acquire the necessary basic materials and work force. An enterprise that makes use of budget subsidies is required to distribute 75 percent of its profits to the development fund. Applications are examined by the founding bodies, banks, Minister of Finance, and the Chairman of the Planning Commission. In the event, this share amounted to 6 percent for socialized enterprises in 1984 and it is targeted to increase to 8 percent in 1985. Enterprises' own means originate from the development fund (whose basic sources of funds are the depreciation allowance and the distribution of residual profits after allowance is made for the compulsory distribution to the reserve fund and other voluntary distributions to socially-related funds), the crews and social funds and from about 30 funds administered by the ministries. An example of the nature of the latter funds is the one administered by the Ministry of Engineering for purposes of developing the service sector of the auto industry. The fund is financed by taxes paid on the purchase of a car.

About 85 percent of bank credit is allocated for financing central investment projects and nearly all outlays of cooperative residential construction, the latter being repaid by the population, budget, and to a small degree by enterprises. The remaining 15 percent is allocated for financing enterprise investments. It was noted that in the table regarding the financing of Investment Outlays (Table 11 of the Questionnaire), the amount of bank credit includes those credits that will later be repaid by the budget. The fiscal figures on state subsidies differ from the figures presented in the table mentioned above as the former include all subsidies related to the preparation of the projects (e.g., social infrastructure, notary fees, settlement of debts prior to the initiation of the project, preparatory costs, etc.).

e. Investment policy for 1986-90

The investment policy for the 1986-90 period will focus on the completion of major investment projects in progress in order to make room for new investments of a modernization nature. Priorities for new investments will be shifted to those in the sphere of material production, especially selected branches of the manufacturing industry. New investments will focus on (1) limiting the process of decapitalization of fixed assets; (2) arresting the growth of the technology gap; and (3) increasing the economic efficiency of investments, and, in particular, reducing industry's dependence on energy and basic materials. The principal criteria for selection will be the potential for increasing exports, supplying consumer goods, and modernizing the existing capital stock. In the social sphere the two main goals are to (1) increase residential construction due to the acute shortage of housing, and (2) increase educational facilities in reflection of the skewed distribution of the population in favor of youth. While the level of social investments is expected to increase steadily over the period (but at a lower rate than in the previous three year period), their share of total outlays is targeted to decline. The 1986-90 plan is currently being presented for public consultation.

2. Stocks

Available data on stocks are expressed in current prices, which makes the analysis of stock behavior even more difficult, during a period of substantial variability in price movements. Also, the structure of stocks of goods is not known in detail, however, it appears to be substantially different than the supply of goods. With these caveats in mind, it is estimated that stocks reached their lowest level in 1981 (a level equivalent to less than 30 days of sales compared to 90 days in the second half of the 1970s when the consumer market was broadly in balance). Reductions in stocks were most severe in commerce, for both producer and consumer goods, reflecting an acute shortage of raw and basic materials. The depletion of stocks bottomed out in the second half of 1982 and with the upturn in economic activity reached a level equivalent to about 50 days of sales by the end of 1984. Nevertheless, it is estimated that stocks are still too low in comparison to the needs of a normally functioning economy. While the equilibrium level of stocks may be somewhat lower than in the late 1970s, as a result of the economic reforms, the economy is technically constrained to be more efficient in its use of resources by the lack of storage facilities. In order to avoid delays in orders, enterprises prefer to do the majority of the required stockbuilding themselves. It was noted that stocks are valued at purchase prices.

3. Enterprise accounts

The discussion focused on an explanation of the table on enterprise accounts prepared by the authorities for the staff. Depreciation charges, property taxes, wage taxes, social security contributions (Zl 574 billion in 1983 and Zl 509 billion in 1984), as well as legally required transfers to certain funds (e.g., social and housing funds) are charged to costs. Legally required tranfers to the reserve fund, however, are considered as being generated from the distribution of profits. Price equalization taxes (subsidies) on account of foreign exchange transactions as well as transfers of funds between enterprises in a given industry, due to differences in costs, are accounted for under line 2 (4), "Payment of taxes on production, sales and factors of production" ("Subsidies"). Investment subsidies are also included in line 4, "subsidies." The main tax in the latter category, however, is the turnover tax. The calculation of income taxes is based on line 5, "profits before payment of profit-related taxes and other transfers to state and local budgets", which is net of turnover taxes and subsidies. The figures on income tax payments, differ from those in the budget because they refer to the tax due on the profit of a given year while the budget figures are on a cash basis and extend through January 6 of the following year. The same holds true for turnover taxes, however, the differences are not as large because they are paid more rapidly. As regards the reserve fund, in general enterprises are required to place 10 percent of their profits in this fund as a safeguard against future losses. However, enterprises which have accumulated a stipulated (not specified) amount in the fund are exempted from this obligation. On average, therefore, transfers to the reserve fund are less than 10 percent. Resources in the development and reserves funds can either be deposited with the banking system, where they earn a rate of return, or they can be retained by the enterprises for day-to-day financing of operations. The majority of enterprises choose the latter option. Restrictions as regards use of these funds apply only to cooperatives.

The composition of sources of revenue for the Development Fund in 1984 was the following:

	(In percent)
Distribution from profits	46
Depreciation allowance	31
Other (e.g., tranfers from other enterprises for joint ventures, sale of fixed assets, etc.)	23
	100

As regards expenditure of the Development Fund, priority must be given to the repayment of bank credit. In 1984 the composition of expenditure of the Development Fund was the following:

	(In percent)
Financinq own investments	52
Repayment of bank credit	17
Financinq of current operations	16
Other (e.q., tranfer to the fund for science and techonoloqy, etc.)	15
	100

It was noted that the bottom quarter of the table was left blank due to the lack of adequate data. The definition used by the bankinq system for "borrowinq from banks by enterprises" included entities that were not classified as enterprises in this table; however, their share was not too siqnificant. While interenterprise borrowinq is not illeqal, no official data are collected in this area. It is believed that the latter is an insiqnificant share in the overall level of borrowinq.

The meetinq adjourned at 1:00 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 8B
Held at the Ministry of Finance
on Tuesday, April 2, 1985, at 10:00 a.m.

Polish Representatives	Fund Representatives
Mr. Z. Karcz, Director, Foreign Dept., Ministry of Finance	Mr. Manison
Mr. Czybonski, Ministry of Finance	Mr. Boonekamp
Ms. M. Rubel, Advisor, Foreign Dept., National Bank of Poland	

We met to discuss aspects of Poland's exchange and trade system.

1. Exchange Regulations Law

The process of economic reform begun in 1982 altered the structure of the economy, with the result that the Exchange Regulations Law had to be changed with effect from April 1, 1984. The new law permits everything that is not specifically forbidden, rather than--as under the old regulations--forbidding everything that is not specifically allowed. The new regulations also unified disparate laws, defined the responsibility of individuals acting on behalf of enterprises, and made numerous other minor changes, particularly relating to accounts held by the population. In accord with the economic reforms, enterprises were given greater responsibility to comply with the foreign exchange regulations. In general, however, exchange control is still tight. Within the framework of the law, enterprises and individuals (i) cannot hold foreign exchange accounts abroad without the express permission of the National Bank of Poland (NBP), which will only grant such permission on "proof of necessity," and (ii) must either surrender earned foreign exchange immediately, if it is received under contractual payment terms, or else within one month. (In practice, some difficulties had been encountered in inducing foreign trade enterprises to quickly repatriate their export proceeds.)

2. Foreign exchange plan

The authorities stated that they did not have a specific foreign exchange budget, but prepared external accounts projections of an indicative character. Annually, within the context of the five-year plan approved by Parliament, the Government balances import needs against available financing. The Planning Commission calculates the import requirements of the sectors and enterprises according to national goals and by using input/output tables and information from branch ministries.

In forecasting available financing, the Government must observe the foreign debt ceilings set by the five-year plan and stipulated annually, in this context, by the Ministry of Finance; these ceilings are set separately for convertible and nonconvertible currency external debt, and can be corrected for changes in the exchange rates. With respect to debt and external financing, the authorities noted that: (i) under the initialled (but not yet signed) Paris Club rescheduling of 1982-84 maturities, they had requested that their official creditors extend to Poland credit lines totaling some US$1.7 billion, which would be needed to ensure the financing for about US$1 billion of imports; (ii) over 40 percent of the convertible currency external debt is denominated in currencies other than the U.S. dollar; (iii) interest arrears are capitalized into the total debt, with interest on these arrears provisionally entered at a rate of 10 percent per year; (iv) estimated 1985 debt service to be paid was in the order of US$2.2 billion, on the assumption that considerable new credits would be received from Western Governments; and (v) that external debt servicing to the CMEA area was not too burdensome.

The available foreign exchange for import financing (net of retention quota amounts; see below) is allocated either to a central pool (about 60 percent), mainly for enterprise raw material needs, or to the branch ministries for their control. Imports of key materials such as grains, fertilizers, and steel for housing construction are centrally financed and distributed. Over 50 percent of raw material imports fall within the competence of the Ministries of Agriculture and Material Economy. The branch ministries use their foreign exchange for their own functional needs, and, according to National Plan and ministerial priorities, to finance the import requirements of their affiliated economic units. The authorities noted that, due to the foreign exchange shortage, the allocation of import financing was, in fact, rather carefully planned (Mr. Karcz used the phrase "Stalinist method" to describe the system). In the first stage of the planning process, foreign exchange was limited to financing imports for current production needs and, in the second stage, residual foreign exchange was available for purchases of capital equipment. It is anticipated that, in 1985, a further 15-20 percent of financing for imports (equal to some US$1.1 billion, at most) from the second payments area will derive from the funds accumulated by enterprises under their foreign exchange retention quotas on the sale of goods and services to the second payments area. In order to relax the import restrictive system, the authorities are considering an increase in the foreign exchange retention quotas of enterprises and a more liberalized use of the funds from these quotas. Mr. Karcz stressed that, although imports from South Africa were prohibited, enterprises with available financing for purchases in the second payments area were generally free to select their own sources of supply. Poland only has limited trade with Israel and South Korea, mainly because it has no diplomatic relations with these countries.

3. Import licenses

An import license does not guarantee the holder of the availability of the necessary foreign exchange, but it does grant general permission to acquire the foreign exchange needed to complete the contract. A separate exchange license is not needed to purchase foreign exchange. Mr. Karcz noted that economic units generally sought to acquire financing before the placement of import orders 1/ which, in turn, did not become valid until an import license was granted. On an ex post basis, the Customs authority is empowered to check compliance with the import contract and the numbered import license. However, in order to maintain Poland's creditworthiness, import payments are not denied if an irregularity is found.

In cases of barter trade, it was necessary to obtain the approval of the Ministry of Foreign Trade for specific contracts.

4. Accounts "A"

Subsequent to a Ministry of Finance ordinance of November 30, 1984, which became effective on April 1, 1985, the sources of the funds must be declared when they are deposited into these foreign currency accounts, which all Polish residents are entitled to hold. Mr. Karcz estimated that some US$250-260 million had been deposited into Accounts "A" in the period November 30, 1984-March 30, 1985, and that, as a result, there was not much "hidden money" left in the economy and "certainly not" the US$1 billion that one sometimes heard mentioned. Since the amounts deposited had been in excess of expectations, and because the period April through July was the height of the tourist travel season, the authorities expect that withdrawal activity from these accounts will be greater than normal during the next few months. As of January 1, 1985, account holders can use the funds, up to the limit on deposit, to finance tourist travel abroad by them and their next of kin. The banks in which the accounts are held are not legally obliged to maintain reserves against the deposits, but, as a matter of prudence, they voluntarily keep fairly high reserve ratios, particularly in the form of banknotes. The authorities did not consider foreign currency denominated deposit liabilities in domestic banks as part of external debt.

5. International reserves

Mr. Karcz noted that the traditional Polish practice was to include as international reserves only that strategic amount held on hand by the National Bank of Poland for emergency purposes. Normally, this amount is in the order of US$200 million, held in the form of cash, very liquid deposits, and/or gold, but does not include the short-term

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1/ The sources of financing are required to be stated on an import license application.

foreign assets of other Polish banks and entities. However, such assets are potentially available for international settlements. He noted official difficulty in understanding exactly what the Fund would count, and report, as international reserves, and accordingly requested the Fund to supply the authorities with a detailed definition, as it applied to Poland, of international reserves. In this respect, it was noted that Poland had US$1.5 billion on deposit with banks reporting to the Bank for International Settlements, a large part of which had not been included in the traditional definition of official reserves.

6. The black market

The authorities thought that the demand for foreign exchange on the black market was essentially limited to that needed for the purchase of luxury goods not available (for zlotys) on the domestic market, and/or for the purchase of goods (such as alcohol, cosmetics, automobiles) bearing high domestic currency prices. As such, they noted that it "really does not make sense" to look to the black market rate for guidance in setting an appropriate official exchange rate. In this latter respect, Mr. Karcz indicated that calculations made by the authorities showed that, even if the official rate were devalued by some 15 percent, the exchange rate would be "submarginal," in the sense that a sizable proportion of exports would not be profitable at the new rate.

With respect to the black market for goods, it was noted that, as a result of improved domestic supply conditions, speculators in some products, such as colored television sets and washing machines, were now faced with the prospect of selling their stocks at below the original purchase prices. In the opinion of the authorities, it is largely by means of the attainment of greater domestic supplies of all products that black market activity, for both goods and foreign exchange, will be contained.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 9A
Held at the Ministry of Agriculture
on April 2, 1985 at 3:00 p.m.

Polish Representatives	Fund Representatives
Mr. W. Mlynarczyk, Deputy Minister of Agriculture	Mr. Hole
Mr. C. Gawlowski	Mr. Prust
Mr. S. Jankowski	Ms. Swiderski
Mr. B. Nowak	
Mr. K. Placzkiewicz	

The staff team was provided with summary written answers (attached) to its questions and Mr. Mlynarczyk said that in his oral remarks he would concentrate only on some main themes.

He began by noting the important role of state farms in Poland in fostering biological and technological progress. State farms as a group came under the Ministry of Agriculture but there were also various associations of enterprises for specific purposes. For instance, there was an association of seed producers to develop high quality seeds. Yields on state farms had often been higher than in the rest of the agricultural sector. Because they were larger and more mechanized state farms accounted for most of the national production of rape which was the main oleaginous plant. They had also increased their production of pork in recent years and now accounted for 40 percent of total state procurement. One of the reasons was that state farms sold all their output of pigs rather than retaining some for self-consumption. Some state farms had their own retail outlets.

Mr. Mlynarczyk said that the legal position of the various segments of the agricultural sector had been explained in the written answers provided but he wished to note that under the economic reform all parts of the agricultural sector were to be subject to the same conditions as regards pricing and in other respects.

As to the overall position of agriculture in the Polish economy, Mr. Mlynarczyk said that it accounted for one third of the country's fixed assets and almost one third of employment although its share in national income was only 16 percent because of the effects of various prices and wages policies. The main aim of the government's policy was to achieve self-sufficiency in food. This should be a feasible objective since the average amount of land per capita in Poland was 0.51 hectares; the FAO estimated that 0.25-7 hectares per capita should be sufficient for food self-sufficiency. The main deficiencies in Polish agriculture compared with other countries lay in the provision of inputs. Of course, Poland's climate was such that there were certain crops which it would never be able to produce or not in sufficient quantities (such as soybeans and maize for animal protein). The government's policies sought to promote more intensive cultivation and to encourage greater domestic production of animal feeds. As a result, within the overall objective of making production and investment profitable in the agricultural sector, price changes in recent years had aimed at increasing incentives for plant rather than animal production. The purpose of this was to reduce reliance on imported feedstuffs. (One of the effects of recent price changes had been to reduce spreads between official procurement and free market prices. However, Mr. Mlynarczyk noted that money prices in these two markets were not strictly comparable in that sales to state procurement agencies typically entitled producers to access to certain inputs.)

The relationship between the prices of agricultural products in Poland did not differ greatly from what obtained in western European countries such as Germany and Austria. The biggest difference with Germany was in the price of beef. This was because Poland had no great tradition of beef consumption and did not have the grasslands necessary for its production. As a result, beef prices were relatively low. Dairy product prices, therefore, had a greater influence on the size of cattle herds.

It was too early to see the full effects of the pricing changes made in 1983-84 but there were already some signs of improvement. For instance, cereal production had risen to a total of 24.4 million tons in 1984 with an increase in the share of wheat. An additional 174,000 hectares had been planted to wheat in 1984 and sales of wheat had risen by 200,000 tons. There was also greater interest on the part farmers in growing winter wheat but one of the factors inhibiting performance was the lack of high quality seed. A special fund under the control of the Ministry of Agriculture which was established in January 1984 should be of help in this context and would subsidize the development of high quality grains and animal breeding. The size of the fund was being increased and in 1985 its expenditures would be Zl 1.5 billion higher than in 1983.

Another general development that was encouraging was that the fall in the area of farm land had been slowed, if not halted altogether. In 1984 the area of farm land lost had been equal to that reclaimed for agricultural use. Up to 1980, the loss of agricultural land had been proceeding at the rate of about 50,000 hectares per year but in the period 1981-83 this had slowed to about 20,000 hectares per year. There had been a decline in the area of land held by the State Land Fund. Lands held by this fund were under the control of local administrations which, in line with government policy, tried to dispose of it, either by sale to private farmers or, apparently without charge, to state farms. The rate at which the State Land Fund had been disposing of land had declined in the past two years because the better quality land had already been sold. In addition, there had been a fall in the number of people wanting to sell land to it partly as a result of changes in the pension system for private farmers which had reduced the incentives for them to sell.

After substantial declines in earlier years, the animal population was now exhibiting greater stability. There had been a big drop in the slaughtering of pigs and the pig population had risen somewhat in 1984. This trend may in fact have started as early as March 1983 but, since the census of animal populations was only taken in June of each year, it was hard to tell. The pig population had risen by 1 million in 1984 although there appeared to have been a slight decrease in January and February 1985, perhaps due to the exceptionally harsh winter. However, the breeding stock of pigs appeared to have stabilized at its 1984 level. The profitability of pig breeding was very dependent on the scale of operations and there were signs that large scale operators were continuing to breed young sows. It was not intended that the pig population would return to its 1978 level of 22 million head because this had created an excessive dependence on imported feed. The appropriate size of the pig population was very dependent on the level of cereal production. The sustainable pig population was currently 18 million but this could rise by a further 1-1.5 million by the middle of the year. Sales of pigs and related products from state farms had risen by a quarter in 1984. There had been a speed up in the rotation of the herd: previously it had been profitable to keep pigs until they weighed 200 kilos, but at the new price levels the optimal size for slaughtering was now 120 kilos. All pigs above this weight were considered to be of second quality and attracted only a lower price. A further factor contributing to a large percentage increase in sales of pigs was that private producers would always retain a certain minimum for their own use but any production above this required amount would in its entirety be brought to market.

The year 1984 had generally been a favorable one for agriculture with record crops of grains and rape. Production of sugar beet had also been at near record levels. Rape production had been 150,000 tons, cereal production 24.4 million tons, sugar beet production 16 million tons, and potato production 37 million tons. Milk production had also been better than expected and the "commodity" production of meat had risen by 0.1 percent. As a result, the increase in net agricultural production had been greater than that in overall national income. The former had risen by 7.1 percent. This favorable result was partly attributable to the economic reforms which had laid greater stress on effective management; this had been especially important in the performance of the state farms whose net production had risen by 50 percent. For these units 1984 had marked a breakthrough with much improved labor productivity. Net agricultural output per employee in the state farm sector had risen above that in the private sector. In addition, there had been changes in the pattern of production with declining levels of output for various unprofitable animal products, particularly beef. Instead there had been a greater emphasis on plant production which had been a major cause of the achievement of the second largest rape crop ever recorded in Poland. However, the ratio of production to material inputs in state farms which was 2:1 in 1984 was still worse than in private farms where it was 3:1. Overall production (apparently commercial production for the agricultural sector as a whole) had risen in 1984 by 4 percent in constant prices.

There had been considerable fluctuations in the growth of agricultural incomes in recent years. In 1981 there had been an increase in product (procurement) prices of 30 percent while input prices had been frozen. In 1982, input prices had risen faster than product prices. In 1983-84 the aim had been that the two should rise at the same rate. In 1984 product prices had risen by 10 percent, current input prices by 9.3 percent and the prices of investment goods by 14 percent. As a result, gross earnings in agriculture had risen by 11.7 percent compared with a 17 percent increase in industrial wages. Mr. Mlynarczyk did not think this had had a serious effect on incentives especially as incomes of owners of relatively large farms had risen considerably faster than the average for the agricultural sector as a whole.

Another important development was a change in the size structure of agricultural holdings: there had been an increase in the proportion of farms of over 7 hectares. (This was calculated to be the minimum size of farm sufficient for the generation of earnings that were equivalent to the average wage in industry.) There were 820,000 farms of more than

7 hectares which together accounted for over 63 percent of the total area of agricultural land and for 29 percent of the farming population. Agricultural policies were very much framed with farms in this size group in mind. This did not reflect any prejudice against the smaller farms but only a realistic assessment that their contribution to growth in output could only be small.

Mr. Mlynarczyk said that the weakest point in Polish agriculture was the state of the processing industry and of storage facilities. This meant that output could not always be effectively utilized during seasons of high production. The state of affairs in the dairy industry was cited as an example. The government was aware of this problem and had adopted a program for improving agricultural processing facilities which, it was hoped, would be particularly helpful in raising exports.

Export performance had been very good in 1984 especially in western markets. The latter accounted for 70 percent of total Polish agricultural exports. In 1984 there had been a 50 percent increase in agricultural exports to western markets which meant a near doubling since 1981. Compared with an originally forecasted deficit of US$0.5 billion (it was not clear when this forecast was made), the net position on agricultural trade had been much more favorable than expected and a deficit of only US$0.2 billion was recorded in 1984. The main reason for this favorable performance was a reduction in the level of feedstuff imports. However, there had been an increase in 1984 of almost 80 percent in imports of high protein feeds. Export possibilities had by no means been fully exploited, for instance in potatoes, fruits, and apple concentrates. Polish products had a distinct quality edge over many of the competitors.

The relationship between the prices of different agricultural products in Poland was similar to that which obtained on world markets. The main pricing problem which faced the agricultural sector was thus not the structure of relative prices but the absolute level of prices that the present exchange rate implied. Mr. Mlynarczyk had calculated that to earn US$1 from agricultural exports required an expenditure of Zl 240. At the same time, the local currency value of a dollar's worth of imports by the agricultural sector was estimated at Zl 380. The latter helped to offset the costs of export subsidization. Agricultural exports took place only through foreign trade organizations which were responsible for subsidy payments although ultimate responsibility for the latter lay with the Ministry of Foreign Trade.

Mr. Hole inquired how long it would typically take for an exchange rate change to filter through to the farm gate prices. Mr. Mlynarczyk noted that farmers did not export directly. However, through changes in prices offered by foreign trade organizations and domestic processing enterprises, there could be changes in prices received by individual farmers following an exchange rate change. Typically, a premium was incorporated in the prices offered for items that were exported. This premium could either be explicit or could take the form of deliveries of imported materials, such as concentrated feedstuffs, from the exporting organization to the producer. Fixed procurement prices applied to certain commodities. However, these were typically adjusted following an exchange rate change. Farmers were reluctant to enter long-term contracts at fixed prices but rather wanted to have in any contract a clause to the effect that their deliveries would receive the going price at the time of sale.

Mr. Hole inquired whether an improvement in the supply situation would be of assistance in raising agricultural output. Mr. Mlynarczyk replied that this would definitely be the case, as it would throughout the whole economy. Shortages of pesticides for wheat and of tractors were cited. In reply to a question from Mr. Hole on the effects of reform, Mr. Mlynarczyk noted that the most radical reform measure affecting agriculture had been taken in 1970 when obligatory deliveries from private farms were abolished. The main policy instruments were prices, taxes, and credit. However, there had in the past been some abuse of concessionary credit to the agricultural sector. There had for a while been a belief that it was only possible to raise agricultural production through raising prices. This dictum had to be employed cautiously. For instance, the effect of many price changes in the late 1970s was simply to allow a passing on of the higher cost of imported feedstuffs. No encouragement had been given the development of alternative domestic sources of feed.

Mr. Mlynarczyk said that he was still optimistic about the outlook for 1985. He expected commodity production to exceed its 1984 level, especially for meat. More combine harvestors would be in operation and there would be greater planting of improved strains. Therefore, in cereal production he expected an outturn at least as good as that achieved in 1984. The harvest of root crops had not been particularly favorable in 1984 and a better outcome was expected in 1985. The hard winter had apparently not affected grain crops or winter rape and the arrival of the first spring thunder storms indicated that there would be no more hard weather. Overall, Mr. Mlynarczyk expected an increase in agricultural output in 1985 of about Zl 50 billion in constant prices. Similarly, as regards the output of animal products, he expected a reasonably good performance in 1985. Animal populations had been stabilized and, for pigs and beef calves had begun to increase again.

The meeting at ended at about 5:45 p.m.

Ad 1.

In Polish agriculture private farms occupy 76.4 % of all farm land. State farms occupy 18.8%, cooperatives 3.7% and agricultural circles o.5%

State farms work on and manage the property which belongs to the whole nation. Their economic activities are conducted in accordance with the regulations which apply to all state enterprises i.e the law on state enterprises.

The principles and procedure governing the foundation of agricultural cooperatives and farmers' machinery and servicing cooperatives were laid down by the Parliament of the Polish People's Republic in an Act adopted on September 16,1982 - Cooperative Law. According to the provisi of this Act a cooperative is a voluntary and self-managing association with unlimited number of members.

The basic economic activity of agricultural cooperatives includes runnin the collective farm through the work of its members. Agricultural cooperatives can also engage in manufacturing and services in the scope provided for in their charter.

Farmers' circles are the principal organizations of the Union of Farmers Farmers' circles and agricultural organizations.
The main economic activities of farmers' machinery and servicing cooperatives is to provide agricultural services and other types of services which result from the needs of rural community as well as to produce agricultural products and materials and undertake food processing.

The continuity of private farm ownership is now guranteed by appropriate provisions in the Constitution of the Polish People's Republic /in 1983/ in the act on social and vocational farmers' organizations and also by the Parliament of the Polish People's Republic in 1982 increased among others the maximum size of private farms from 2o ha to the sizes resulting from the Law on Agrarian Reform i.e 5o and 1oo ha depending on the region of the country, and also gave all sectors of agriculture equal opportunity for obtaining land, ensured the possibility of taking advantage of the same range of social benefits as in the common system of national insurance/ with the exception of child care benefits and to some extent sickness benefits/, and furthermore it ensured equal access to agricultural inputs and financial aid from the State by:

-a/adopting a uniform pricing policy for the whole agricultural sector

b/introducing uniform contracting terms

c/ensuring equal possibility of purchasing fertilizers and feed from ad 1/

state supplies

d/ introducing a uniform system of subsidies for production activities
e/ adopting uniform principles for granting credits in agriculture

In order to even out the differences in the distribution of farming machines in the last few years the number of tractor and agricultural machines sold to private farmers has been increased.

ad 1/ – the share of private sector in the amount of purchased tractors rose ~~by~~ from 66 per cent in 198o up to 76 per cent in 1982, trailers reppectively from 25 to 55 per cent, tractor driven sowing machines from 76 to 92 per cent.

The State Soil Fund covers soils which are at the disposal of basic administrative units and are destined for agricultural use. This fund has at present 811.6 thou hectares including 621.8 thou farm land. Some 425 thousand hectares of this land are used by the leasers. The administration of this Fund has at its disposal 53 thou of farm land. The heads of communities have at their disposal the use of this land.

The State Soil Fund lands can be used in the following way:

- free of charge transfer to the state and cooperative farms
- selling to private persons
- leasing to the private persons or state and cooperative farms

The charge for leasing one hectare of arable land amounts to 1oo–8oo zlotys per year.

ad 2. Major trends in agricultural production can be bharacterized by increased cereals growing / 56 per cent in 1983 and 56,4% in 1984, with special reference to wheat the share of which in growing area amounts to 21 per cent.

In socialized sector the share of cereals in total area was 49% and in private sector 59%.

In 1984 record crops were reported. They amounted to 24.6 million tons/ metric/of cereals that is 2.3 million tons more than in 1983. There were also high crops of oil seed plants - 934 thou tons that is 368 thou tons more than in 1983.

Increased procurement prices for slaughter pigs caused positive trends in swine breeding. The swine population by the end of 1984 amounted to 17.2 million ~~cattle~~ heads that is some 8.4 pre cent more t[illegible] last year. There were 91 pigs for 1oo hectares: 1o4 heads in socialized and 87 in private sector.

The cattle population was 1o.9 million heads that is 1.6 per cent less than in 1983. There were 57.8 heads for 1oo hectares farmland at the end of 1984: 57.8 in socialized and 6o.6 in private sector.

In 1984 the total production of slaughter animals in live weight amounted to 3.516 thou tons that is one per cent less than last year. Certain recovery in poultry population was reported. Respective figures in 1983 were 269 thou tons and in 1984 -356 thou tons. /32 per cent increase was reported/.

The milk production was 16.3 billion /thousand million/ litres and was higher by 4.6 per cent than last year.

In the years 1986-9o it is planned that total growing area for cereals will amount to 8.2 million hectares and that of legumes will ~~xxxxxxxxxx~~ reach the level of 3oo thou hectares and that of oilseed crops will total 48o thou hectares. By taking into account efficient use of the means of production, structural changes in crops growing and introduction of new technologies it is assumed that following yields will be achieved in 199o:

cereals 32 quintals, sugar beets 35o q, potatoes 22o q. It is expected that cereal crops will amount to 26.2 million tons, those of sugar beets some 17 million tons, potatoes 44 million tons and oilseed crops 1 million tons.

The vegetable production is supposed to reach the level of 5.2 million tons and that of fruits - 2.9 million tons.

It is expected that cattle population will total in 199o 12.5 million ~~km~~ heads,/11,6 growth/, the swine population will grow by 5.7 per cent and will total 18.5 million heads, sheep population will rise by 2.2 per cent and will total 4.7 million heads. The livestock production will grow by 13.6 per cent in the years 1986-199o and will reach the level of 4o9o thou tons including bovine production up to 1.4 ~~million~~ thou. tons and swine up to 2.15o thou tons.

In order to achieve these targets a mobile price system was introduced into the agricultural and food processing economy. This system consists in this that procurement prices and retail prices of food products are mobile subject to the increase of the prices for the means of production.

At the same time more favourable credit system was introduced./lower rate of interest, easier availability of credits/.

In 1985 the reform of land tax was carried out. This reform includes equal system of tax burdens for all sectors in agriculture, identical way off tax calculation for each hectare comparable in statistical terms, introduction of special priveleges for farm modernization and new projects.

A fund for biological progress was established. From this fund the seed and breeding material are partly subsidized.

In the grain processing industry up to 199o new elevators and grain storage facilities /2 million tons capacity/ including steel containers /1 million tons/ and grain drying facilities are planned.

Ad 3

The sale of agricultural production is conducted within the follo... g system :

1. socialized purchasing centers /purchase through commune cooperatives/,
2. direct purchase from the producer by state industry,
3. on markets and to the private network of retail trade,
4. in the own trade network of socialized producers.

About 82 % of the commodity agricultural production is purchased by the socialized purchasing centers both under contracting system and out of the system. All basic agricultural products are produced and purchased within the contracting system according to the agreements concluded individually with single farms. The contracting agreements guarantee the collection of contracting products at times fixed with the producers and according to purchasing prices. Moreover, the contracting farms benefit from extra preferences as regards tax reductions, supply with basic production mea including the imported ones, and they have priority in benefiting from production services. Some articles such as grains, livestock are purchased by state enterprises in unlimited quantities, i.e. every amount offered by the producer.

In the group of industrial plants, which include rapeseed, fibrous plants, tabacco, hope, sugarbeets, the volume of production is determined by the contracting plan according to the needs of industry. Other products, particularly fruits and vegetables, are covered by contracting in 60 %.

The part of products which is not contracted is being sold on the free market.

Bigger part of products /grains, rape and livestock/ are collected directly from the producers' farmsteads by the contracting units at the cost of those units. The terms of sale and the purchasing prices are the same for the socialized sector and for private farms.

Some products such as fruits, vegetables, eggs and poultry, produc above the volume covered by contract, are sold in markets in the own trade network of agricultural producers.

Ad 4

...chasing prices in the recent years in relation to the antire nonsocialized agriculture guaranteed the labour payment in agriculture on the level of labour payment in industry.

The profitability of single agricultural products is differentiated by the mutual proce relations. It amounted in 1983 /relation of the purchasing price to production costs without labour payment/ to the following :

- live pigs	150 %
- live beef	103 %
- milk	438 %
- wheat	327 %
- rye	250 %
- sugarbeets	198 %

The purchasing prices for agriculture products changed on 1 July 1983 and in 1984. The price level in the years 1982-84 is illustrated below :

in zł

PRODUCT	units	since 1st July 1983	= rye	since 1st July 1984	= r
rye	1 kg	17,50	1,00	17,50	1,00
wheat	"	20,00	1,14	22,00	1,26
barley	"	18,50	1,06	20,00	1,14
oats	"	17,50	1,00	17,50	1,00
sloughter piggs	"				
meat-fat					
class I	"	140	8,00	156	8,91
class II	"	140	8,00	150	8,57
young beef					
/avarage price/	"	101	5,80	117	6,69
potatoes					
edible	"	7,50	0,43	7,50	0,43
for proccessing	"	5,80	0,33	5,80	0,33
3,5% fat milk					
summer basic price x	1 l	14,00	0,80	14,00	0,80
winter basic price x	"	17,50	1,00	19,95	1,14
sugar beets	1kg	3,40	0,19	3,70	0,21
low erucic rape	"	47,00	2,69	47,00	2,69
chicken broilers	"	110	6,30	120	6,86

x/ an extra prime is used to the basic price of 1l of milk

in 1st class - 5,20zł

in 2nd class - 2,00zł

Prices for major agricultural and food products
in 1983-1984

in rubles or dollars per metric tonn

PRODUCT	1983		1984	
	Rbl.	$	Rbl.	$
RYE	-	137	-	131
edible potatoes	130	118	133	42
grass-seeds	-	-	1.187	697
rape-seeds	-	-	-	345
sugar	-	236	-	155
rape oil	-	543	-	799
rape meal	-	-	-	101
tabaco	-	2.061	-	2.265
malt	-	300	-	-
hops	-	4.666	-	4.750
mellasses	-	83	-	52
chilled fruits and vegetables	730	689	608	482
meat	-	2.300	-	2.100
bacon	-	1.620	-	1.780
hams	-	2.960	-	3.060
canned and smoked meat	-	1.820	-	1.660
cattle	-	1.460	-	1.240
calves	-	2,000	-	1.470
sheep	-	2.500	-	2.430
slaughter horses	-	1.930	-	1590
~~horse meat~~	~~-~~	~~1.650~~	~~-~~	~~1.470~~
slaughtered poultry	-	2.550	-	1.980
feathers and down	-	9.600	-	14.380

It should be remembered that there are no restrictions on agricultural products on the free market exept meat which is forbiden by the State due to the food rationing system.

Ad 5

The distribution of agricultural tractors and of some agricultural machines is rationed.

A part of production means is bought by farmers within contracting agreements for delivery of agricultural products. The criteria of distribution of tractors and agricultural machines covered by the rationing system are established by the Minister of Agriculture and Food Ecpnomy. These criteria are the basis for controlling their distribution by the Main Regional Inspection. The prices for production means are also controlled by the Minister for Prices.

The following are subsidized by the State : fertilizers, feedstuffs, pesticides, coal, a part of services for nonsocialized agriculture, biological advance. The subsidizing of retail prices was as follows :

	1983	1984
- fertilizers	43 %	60 %
- pesticides	11 %	22 %

In 1984 a substantial growth in foreign trade turn-over was reportedm
This increase can be reflected in the following way: as compared with 1981 there was 6o,5 billion zlotys increase/1o4,4 per cent/ and decline in import by 55.2 billion zlotys /29.3 per cent/
A negative balance of trade dropped from 133 billion zlotys in 1981 to 18 billion zlotys in 1984.
Due to negative balance of trade in agricultural and food products the funds needed by the agriculture for imports of raw materials had to be supplied by other sectors of national economy.
Difficulties in payment cause diminished import of agricultural raw-materials. The import of high protein feeds and grains are affected at most by the restrictions. ~~Cacao~~ grains not produced in Poland also belong to this group.
Irregular supplies of animal feeds coming from exports cause problems in poultry and egg production.

Diminishedimport of ~~xxx~~cacao seeds also ~~continues~~ contributes to this that the production capacity in the respective industry cannot be used and exports of products based upon cacao dropped to null.
85 per cent of total exports in this sector go to the convertible currency markets.

47 per cent of total exports to the convertible currency markets include animal products mostly hams, canned meat and smoked meat, cattle and slaughter horses.
Other products include - sugar, rape seeds and rape oil, frozen vegetable and fruit products, seeds.
Export to convertible currency markets grows dynamically.
Its value in 1984 rose by 97.4 per cent as compared with 1981.
This growth can be illustrated as follows:

- hams and canned pork loin	-	by 14.8 per cent
-canned and smoked meat	-	53,o "
-slaughter cattle	-	68,8 "
-slaughter horses and sheep	-	145,7 "
-rape seed oil	-	86.2 "
-frozen fruit and vegetable	-	1o1.o
- molasses	-	528,3

Forreighn trade turnover in agricultural and food products

/ in mln zł fob, mln Rbl, mln $ /

YEAR	TOTAL	Socialist countries		Other countries	
	mln zł	mln zł	mln Rbl	mln zł	mln $
Import					
1981	191.173,0	16.948,0	249,2	174.225,0	2.177,8
1984	135.960,0	13.529,0	187,9	122.431,0	1.083,5
Export					
1981	57.916,0	7.289,0	107,2	50.627,0	633,0
1984	118.442,0	18.566,0	258,0	99.876,0	869,5
Balance					
1981	-133.257,0	-9.659,0	-142,0	-123.598,0	-1.544,8
1984	-17.518,0	+5.037,0	+ 70,1	-22.555,0	- 214,0

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 9B
Held at the Ministry of Foreign Trade
on Tuesday, April 2, 1985, at 3:00 p.m.

Polish Representatives

Ministry of Foreign Trade (MFT)

Mr. B. Mikaezewski, Deputy Director, Economic Department
Mr. J. Poiyczka, Deputy Director, Financial Department
Mr. A. Szczypior, Deputy Director, Organization Department
Mr. K. Jozwiak, Expert, International Economic Organization Department
Mr. J. Mank, Expert, Programming and Planning Department
Mr. S. Pieckokisni, Expert, Legal Dept.
Mr. K. Popiokek, Expert, Organization Dept.
Mr. M. Weglarezyk, Expert, Economic Dept.

Ministry of Finance

Mr. I. Ilczek, Division Chief, Foreign Dept.

Fund Representatives

Mr. Manison
Mr. Boonekamp

The topics discussed in the the meeting were bilateral clearing arrangements with IMF member countries, quotas, trade entities, the import licensing system, the equalization settlement system, export subsidies and taxes, and foreign direct investment. Poland's tariff schedule and the extent of protectionism against Polish exports were also briefly touched upon.

1. Bilateral clearing arrangements

Table 1 (attached) lists Poland's 15 operative bilateral clearing arrangements with Fund member countries, and provides information on the terms of validity of each of the bilateral arrangements, as well as on their swing limits (limits of technical credits), currency of settlement, and applicable interest rates. Since late 1984, Poland has also had a non-operative barter arrangement for some of its trade with Argentina, which does not contain a convertible currency clearing provision for imbalances. The arrangements with Afghanistan, Bangladesh, Mexico, and Pakistan are essentially barter agreements which do not account for all of Poland's trade with those countries; in each case, financial clearing arrangements exist for barter imbalances. The other 11 are full clearing arrangements, in terms of which Poland conducts all its trade with those countries. A "gentlemen's agreement" exists with Brazil to settle imbalances quarterly on request. Due to Brazil's insistence that Polish exports lead its imports, the arrangement lately has shown a positive balance in Poland's favor. In 1984, the bilateral arrangements accounted for 6.4 percent of exports to, and between 9 and 10 percent of imports from, the convertible currency area. The volume of trade within the framework of bilateral arrangements has decreased significantly in the last ten years. Ideally, Poland would like to move toward terminating the bilaterals, but some of Poland's partners insist that the arrangements remain in effect. 1/

2. Quotas

There are no import (or export) quotas, per se. However, in the context of the (annual) National and five-year plans, import needs are determined by commodity groupings and value. These are balanced against financing according to priorities, ranging from raw materials as the most important to social and cultural sphere goods, essentially as a remainder. The National Plan allocates the financing to effect the purchase of the imports into various pools, as shown in Table 2 (attached) for 1984. The size of the pools is changeable intra-yearly, depending on the availability of foreign exchange and emerging needs. Normally, some 50 percent of convertible currency imports are financed centrally; these imports, largely raw materials purchased in line with the National Plan's needs, are distributed to the enterprises by the State. Enterprise foreign exchange retention quota funds, from sales of goods and services to the convertible currency area, are usually expected to finance 15-20 percent of imports. 2/ A larger portion of the remaining foreign exchange expected to be available for imports is allocated (to the control of branch ministries) for enterprise needs related to government contracts and operational programs. Separately, the branch ministries are apportioned the control of exchange for their own functional requirements, such as the financing of consumer goods imports by the Ministry of Internal Trade for on-sale to the public by its affiliated enterprises. The residual is allocated to the relevant branch ministries for the import needs of the "nonproduction" sphere. The authorities noted that the National Plan was meant to be indicative, with enterprises planning their production

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1/ In a minor way, some of the information in this section contradicts that given in a meeting held at the National Bank of Poland on Monday, April 1, 1985 at 3:30 pm. These contradictions are (the present minute is referred to first): (i) 6.4 percent of 1984 exports, compared with 8.6 percent; (ii) a "gentlemen's agreement" with Brazil, rather than "the agreement provides for;" and (iii) the agreement with Argentina is not operative and does not have a clearing provision, whereas the contrary, on both counts, was implied at the NBP.

2/ We were told by the Ministry of Foreign Trade that the retention quotas were set for two-year periods; at the aforementioned meeting at the NBP, it was stated that the quotas were set annually.

and related imports according to the Plan's guidelines. However, due to the severity of the present foreign exchange constraint, the above system of virtually direct allocation of foreign exchange for imports has had to be used.

3. Trade entities

Foreign trade is a state monopoly. In practice, this means that exports and imports may be effected only by economic units authorized for this purpose by the MFT. Units that are not authorized to conduct foreign trade channel their imports and exports through authorized organizations. At end-December 1984, 333 units were authorized to engage in foreign trade on a permanent basis, 61 of which were specialized foreign trade organizations (FTOs). Of this latter number, 20 are controlled directly by the MFT, which also holds 51 percent of the shares of 28 other FTOs. Prior to January 1, 1985, the remaining 13 FTOs specialized in representing the interests of foreign companies in Poland (e.g., Timex SA). Since then, their rights have been extended to cover the export of goods of small-scale industries. Generally, an FTO is authorized to trade in all goods, subject to the limitations of its charter and its rights as specified by the MFT (i.e., an FTO has general rights within the context of its specified "profile restrictions"). Except in those instances where an FTO trades in goods (such as grain and steel) which are basic to the economy, no FTO has a monopoly in any one item. The majority of Poland's trade is channeled through FTOs.

In addition to the FTOs, 272 economic units have specific trading rights. These units have been granted their rights in the period since the proclamation of a public law on February 26, 1982, liberalizing the framework for the granting of trading rights. Of the 272 units, 86 are (or are affiliated with) major state-controlled producing and servicing companies, as, for example, the trading arm of the Hortex group, Hortex-Warszawa, which has specific authority to export the group's products, to import various input needs for the group's enterprises, and to trade, on a limited basis, for companies outside the group. Thirty-one of the 272 units are legal entities, such as small-scale producers and cooperatives. The remainder are individuals, of which 13 are foreign residents established in Poland. Subject to an appeal in the administrative courts, the MFT is empowered to withdraw the trading right of any unit that ceases to meet the conditions stipulated in that unit's trading authority.

4. The import licensing system 1/

Specific import licenses are necessary for all imports of goods. Licenses are issued by the MFT or by its "full powers" agent employed

1/ The export-licensing and import-licensing systems are the same in all but minor respects. The information in this section is based in part on "Directive No. 55 of the Ministry of Foreign Trade, December 31, 1984," which was frequently referred to by the authorities and handed to us toward the end of the mission. The Directive includes sample copies of a general authorization, an import license, and an export license.

by the economic unit applying for the license. The customs authority issues licenses not exceeding Zl 100,000 in value for imports of gifts, souvenirs, and "loans of goods." Only economic units with permanent trading rights are eligible to have a MFT licensing agent in residence. These agents issue licenses within the context of a "general authorization," which is granted to an economic unit by the MFT, remains valid until the end of the calendar year in which it is issued, and specifies the type, amount, and price of the goods. General authorizations are not issued for imports of certain goods, including those in the area of construction engineering, building technology, and leasing transactions. The MFT must render its decision on the issuance of a general authorization within ten days after such an application is filed with the MFT. The same time limit applies to decisions on the granting of import licenses. For statistical purposes, the importation of services requires a license issued by the MFT.

General authorizations and licenses are readily granted at no cost, provided the relevant regulations are adhered to and National Plan allocations are not abridged. 1/ Import contracts do not become valid, nor may payment orders be drawn, until an import license has been issued, except in cases of intergovernmental agreements and instantaneous contracts, such as those made on a metals exchange. A license application must be filed with the appropriate authority within seven days after agreement on a contract is reached, and must contain, inter alia: name of importer; type, volume, and unit price of goods to be imported; price in the foreign currency to be used for payment; exchange rate; 2/ country of origin of imports; payment terms; financing source; the National Plan section within which the imports fall; and the contract's expiration date. 3/ A license remains valid until the final delivery date for the goods, or until the date of final payment. For data collection purposes, the economic unit must forward a general authorization and a license to the Foreign Trade Information Center within two days of their respective issuance. The documents are returned to the units within ten days of their registration by the Center. Based on the registered documents and the utilization records that the units are required to keep, the customs administration monitors whether goods are imported according to valid documents. Customs have the authority to inspect all relevant documents and to issue instructions for the elimination of irregularities.

1/ The authorities stated that imports from South Africa were prohibited, by reason of internal trade legislation and United Nations resolutions rather than by the foreign trade regulations. Under the penal code, certain imports are prohibited for social reasons.

2/ The rate entered on the license is the NBP's quoted rate, either on the day the contract was entered into, or else on the day the application was completed. The Directive states that the rate is fixed "for a given contract."

3/ In general, the expiration date of a contract must coincide either with the date of final delivery of the goods or the date of final payment. The term of a contract is not to be longer than 9 months, except in the case of the electrical machinery industry, for which an import contract may not have a term to expiration of longer than 18 months.

In the event of changes in the contracted provisions, the economic unit must notify the relevant authorities (the MFT or its agent, and the Information Center) of the appropriate changes in the license within seven days of its receipt of the documentation stating the need for the changes. In addition, in the case of (i) a 5 percent change in the foreign currency price, and/or (ii) mistakes or errors in data, changes in the license can only be effected by the issuance of a new license, which automatically and simultaneously rescinds the former version. If a license has not been fully utilized, the economic unit must declare this to the appropriate authorities within 14 days after confirmation of this fact. Such a declaration is not necessary if the underutilization of the license amounts to less than Zl 50,000, or does not exceed 5 percent of the price or volume as stated in the license. 1/

5. Equalization settlement system

The system came into effect in 1982, as a result of the February 1982 reform in the setting of internal prices. Beginning on the latter date, and at discrete intervals thereafter, the Government publishes a list of goods to be traded internally at official (Government-set) prices. It has been the intention of the authorities to base official prices on international prices. Despite this, however, official prices have been--and, in many instances, remain--significantly different from world prices, creating a disincentive for efficient foreign trade. The authorities contend that, for social reasons, the existing margins between international and official prices cannot be eliminated in one step. However, the Government intends to phase out the margins gradually, albeit not to a pre-set timetable. Owing to the margins, the settlement system, which is under the authority of the MFT, automatically credits (debits) the relevant economic unit with an equalization amount if the official price is greater (less) than its actual (foreign trade) transaction price (converted to zlotys at the NBP-quoted exchange rate). Settlement is effected through an account the MFT holds with the NBP for this purpose. The system applies to trade with both the first and second payments areas. All goods for which there are official prices are subject to the system, although the MFT has the right to delete products from the list. Table 3 (attached) gives a breakdown of trade settled at official prices in 1984. On a case-by-case basis, the system may also be applied to goods subject

1/ Several other points emerged during the discussion on this topic: (i) there are no special regulations regarding the licensing of goods for border trade; however, an agreement is being negotiated with the German Democratic Republic; (ii) regulations concerning the importation of noncommercial goods by returning residents are in the purview of the Customs authority; the MFT officials stated that they would attempt to supply the mission with a copy of the relevant regulations; (iii) re-exports, which, as is the case for all other exports, also need to be licensed, account for about 2-3 percent of total exports to the second payments area.

to contract (free) prices, with the decision whether to do so negotiated between the MFT and the economic unit concerned. The system is meant to be self-financing, but has in fact incurred deficits in each year. The MFT receives an annual budget allocation, which sets a limit to the deficit the settlement system is entitled to run. The 1984 and 1985 budgeted allocations were Zl 12 billion and Zl 55 billion, respectively.

The authorities indicated that the MFT wanted to limit the role of the settlement system, and that economic reform would diminish its role. Instead, the exchange rate should be the main instrument in implementing foreign trade policy. In this respect, they noted that about 60 percent of exports were profitable at the present exchange rate, and that, in order to ensure the profitability of some 80 percent of exports, the rate would need to be in the order of Zl 200 = US$1.

6. Export taxes and subsidies

There are no direct taxes on exports. Turnover taxes levied on exports are calculated according to a special formula and, after the submission of a legitimate claim, are refunded to exporters. Duties and turnover taxes on imports for export production are also refunded. Further, economic units are entitled to income tax drawbacks based on both the value and the incremental value of their exports. The present rates at which these drawbacks are allowed is as follows:

	Income Tax Drawback (in percent)	
	On value of exports	On incremental value of exports
Exports of machinery and electrical goods to developing countries	6	35
Other exports to the second payments area	5	35
All other exports	3	25

The rates are set annually by the Minister of Finance.

In addition to the above, the following export incentives are in place, or are under consideration.

i. Export producers generally have a higher-than-average FAZ coefficient. The average coefficient for exporters is 0.6, compared with a nationwide average of 0.5

ii. Producers of goods for export to the second payments area are guaranteed the necessary inputs to the extent that these are centrally allocated, and otherwise are assured of priority.

iii. The MFT receives an annual allocation of about Zl 3 billion from the budget for distribution as bonuses to employees of export-producing units. According to both the value and incremental value of exports, allocations are made to the management of the units for onward distribution by the management to employees.

iv. The MFT tries to help enterprises to negotiate a lower-than-usual interest rate on (zloty) credits for export production. The NBP, however, is not always cooperative. Consequently, the Ministry is considering the proposal of legislation to subsidize such credits.

7. Foreign direct investment

A public law of July 6, 1982 sets out the principles governing the economic activity of foreign nationals, either as individuals or as small-scale legal entities for production. An agent of the Ministry of Internal Trade coordinates the scheme, but decisions on whether to allow the establishment of a foreign entity are taken at the Voivodship level. Such establishments may employ no more than 200 persons. They may be wholly owned by foreign nationals or, at the discretion of the ownership, they may have Polish shareholders. Some 600 have been established to date, most of which are without Polish shareholding. The total amount invested by these units has been relatively small. Fifteen of the establishments have been granted permanent foreign trading rights; of these units, two are legal entities. In all, the units produced about Zl 40 million of exports in 1984.

A proposal is now with the Council of Ministers to allow large-scale joint ventures with foreign nationals and companies. It is hoped to present the proposal to Parliament by end-June 1985. It has the full support of the MFT, which has stressed that the proper incentives have to be offered in order to encourage foreign investment in Poland.

8. Other matters

a. Tariff schedule and other charges on imports

Work is ongoing on proposals to change and modify both the tariff classifications and tariff rates. The authorities did not know when the new schedule would be announced. They stated that discussion of the tariff schedule would come under the responsibility of the Ministry of Finance.

Turnover taxes are levied on imported goods at a rate similar to those on domestic goods. Imports are subject also to stamp duties.

b. Protectionism against Polish exports

According to the authorities, about 16.8 percent of Polish exports to the European Economic Community (EEC) in 1982 were subject to quantitative import restrictions. The products most seriously affected were coal, textiles, steel, shoes, and agricultural goods. Owing to methodological and data difficulties, estimates are not available for later years. They further noted that (i) Poland faced particularly serious difficulties in exporting to the United States, caused largely by the fact that the latter had withdrawn Poland's most-favored-nation status in 1982; and (ii) Poland and Finland had recently agreed to eliminate all obstacles to trade between the two countries.

Table 1. Poland: Bilateral Clearing Agreements with IMF Member Countries (at December 31, 1984)

Country	Terms of Validity	Currency	Limits of Technical Credits	Rate of Technical Credit	Rate of Overdraft Over Technical Credit
Afghanistan	1985	US$	US$650,000	--	3% p.a.
Bangladesh	1985 Barter 5 Barter 6	US$ US$	US$1.932 million US$1.500 million	-- --	10% p.a. 10% p.a.
Brazil	Yearly renewals	US$	US$4 million	5% p.a.	6% p.a.
People's Republic of China	1984	Swiss franc	Sfr. 10 million	--	2% p.a.
Colombia	Yearly renewals	US$	US$3.5 million	--	Repayment of balance in free currencies
Ecuador	Yearly renewals	US$	US$2 million	4.5% p.a.	Half-yearly repayments of balance in free currencies
Iceland	1985	US$	US$1 million	5.5% p.a.	Repayment of balance in free currencies
India	1985	Indian rupees	RS 180 million	7.1% p.a.	--
Iran	Yearly renewals	US$	US$3 million	--	Repayment in free currencies at request
Kampuchea	1985	Clearing rubles	300,000 rubles (transferable)	--	2% p.a.
Laos	1985	Clearing rubles	200,000 rubles (transferable)	--	2% p.a.
Lebanon	Yearly renewals	US$	US$275,000	--	Repayment with commodities
Mexico	Yearly renewals	US$	--	--	LIBOR + 3/4%
Nepal	Yearly renewals	Pounds sterling	£300,000	--	Repayment of balance in free currencies
Pakistan	1985 Barter 15	US$	US$1.5 million	--	10% p.a.

Source: Ministry of Foreign Trade.

Table 2. Poland: 1984 Plan for Financing Imports from Area II (Nonsocialist Economies)

US$4,568 million for the purposes of financing imports;

that is (in millions of U.S. dollars),

1.	Products centrally financed	2,056
2.	Government contracts	182
3.	Retention accounts	850
4.	Operation programs	321
5.	Branch necessities	248
6.	Social and cultural sphere	68

Source: Ministry of Foreign Trade.

Note: The components add to US$3,725 million, as compared with stated planned financing of US$4,568 million. The difference may be accounted for, in part, by countertrade. (The table was compiled at our request by the Ministry of Foreign Trade and given to us on the last evening of the mission.)

Table 3. Poland: Trade at Official Prices, 1984

Official Prices (Settlements Between the Foreign Trade Units and the Producers Supplying for Exports)	
Export total	29.4 percent
Payment Area I	14.9 percent
Payment Area II	41.8 percent
Official Prices (Settlements Between the Foreign Trade Units and Importers-Producers)	
Import total	40.4 percent
Payment Area I	47.2 percent
Payment Area II	32.5 percent

Source: Ministry of Foreign Trade

INTERNATIONAL MONETY FUND

Poland--Staff Visit

Minutes of Meeting No. 10
Held at the Ministry of Finance,
on April 3, 1985, at 10:00 a.m.

Polish representatives

Mr. Karcz, Director, Ministry of Finance
Mr. Wojtowicz, Director, National Bank of Poland
Mr. Przywecki, Director, National Bank of Poland
Mrs. Rubel, Advisor, National Bank of Poland
Mr. Ilzek, Ministry of Finance

Fund representatives

Mr. Hole
Mr. Manison
Mr. Prust
Mr. Boonekamp
Ms. Swiderski

Money and Credit

1. Items in consolidated balance sheet of banking system (Table 5 1/)

Mr. Wojtowicz provided comments on certain items in table 5 of the staff questionnaire. He said that bank credits to the local authorities were channeled through the state budget; as a result, the entry "Credits to general government" could read "Credits to the State Budget." "Special accounts" of the socialized sector (more properly "Special funds accounts") included accounts labeled "Resources for Development," "Housing funds," and the "Fund for Technological Innovation." At the same time Mr. Wojtowicz explained that the resources for development funds of enterprises were essentially used as demand deposits. Up to the beginning of 1985 these special funds accounts and also investment accounts had earned interest of 3 percent per annum. However, because these accounts

1/ Table numbers refer to tables incorporated in staff questionnaire submitted to the Polish authorities in March 1985.

were primarily used as demand deposits interest payments were stopped in order to induce enterprises to channel their funds to fixed deposit accounts.

Bank balances of the State fund for Occupational Activisation (PFAZ) understated the total amounts paid into this fund since part of the surplus on the PFAZ account was transferred to the State budget.

Deposits required against construction investments would be included as a new and separate item in the consolidated banking balance sheet.

Mr. Wojtowicz said that there were no deposit liabilities of banks which represented advance deposits against import transactions.

The item foreign operation accounts under bank liabilities was a net item in that it represented foreign liabilities (including foreign currency deposits) minus foreign assets. Foreign liabilities of the banking system were said to be currently at around Zl 3,500 billion while foreign assets were around Zl 600 billion. Banking and foreign exchange regulations did not require banks to keep minimum reserve covers against their foreign curency liabilities.

2. Foreign currency accounts

Inflows into and withdrawals from foreign currency accounts were treated as transfers in the balance of payments. Even amounts of foreign currency that were previously held outside the banking system and which had been deposited in bank accounts between November 30, 1984 and March 31, 1985 (estimated at $250-260 million) represented incoming transfers in the balance of payments. These transfers in the first quarter of 1985 were considerably higher than those recorded in the same period of 1984 and preceding years due to the special regulations that had come into effect on November 30, 1984. Under these regulations residents could deposit foreign currency in A accounts before March 31, 1985 from which amounts could be automatically withdrawn for transfers abroad. Amounts deposited after March 31, 1985 and which did not have a legitimate source, were placed in N accounts and could not be withdrawn for transfers abroad until after 12 months when they were converted into A accounts. Given the recent substantial inflow of foreign currency into A accounts and the considerable increase expected in the number of Poles going abroad as tourists in 1985 (could be as high as 450,000 compared with 350,000 in 1984) sizeable outward transfers were predicted for the last nine months of 1985, especially in the July-August period. Net inflows into foreign currency accounts normally occurred from September onwards and reached a peak just prior to Christmas. For the year as a whole net transfers to foreign currency accounts were estimated at $100 million for 1985.

3. Interest rates

a. Loan rates (Table 7)

The basic loan rate of interest on bank credits applied to all sectors was 12 percent. There was a vast array of lower interest rates charged on loans for various priority purposes. For example, investment credits for financing cooperative housing carried an interest rate of 1 percent. As a consequence the basic loan rate was applied on less than 50 percent of bank credits. Since 1981 there had been a rise in rates of interest with the basic loan rate of interest rising from 8 percent to 12 percent, rates on loans to state and cooperative farms and for food processing increasing from 6 percent to 8 percent, those on loans to individual farmers rising from 3 percent to 6 percent, and those on loans for instalment purchases by households increasing from 3 percent to 9 percent.

Mr. Przywecki said that up to 1984 higher loan rates of interest were only applied to new credits. However, a clause had been inserted in recent loan contracts for long-term credits to farmers permitting increases in interest rates on existing loans. For late repayments of loans borrowers were charged a penalty rate of interest of 18 percent on outstanding balances. Borrowers were not subject to noninterest costs on their loans from banks, and were not required to keep compensatory balances. Provisions existed whereby borrowers could avail themselves of reduced interest rates for early repayments of loans.

b. Deposit rates (Table 8)

Similarly, rates of interest on bank deposits had been increased since the 1981/82 period. Interest rates on saving/passbook accounts had been increased from 3 percent to 6 percent, while those on household time deposits had been raised from 6 1/2-8 percent to 8-13 percent. Rates for deposit saving bonds had been increased from 9-10 percent to 13-15 percent. Interest rates on earmarked individual deposits for eventual housing purchases now obtained interest of 6 percent compared with 3 percent before 1982 and included premiums to cover increases in housing costs. However, a new type of saving passbook for housing earned a rate of interest of 15 percent with no premiums to cover increases in housing costs. Interest rates on fixed-term deposits of enterprises ranged from 5 percent for those of six months' maturity to 9 percent for deposits of three years' maturity or more.

If a depositor prematurely withdraws a time deposit from a bank only the demand deposit rate would be paid. In the case of premature withdrawal of savings bond deposits, no interest is paid.

4. Credit instruments and policy

Mr. Przywecki said bank credit was partly advanced on the basis of something akin to an overdraft system. Socialized enterprises could not automatically obtain credit to meet current expenditures such as wage payments. Emergency credits were extended in cases where enterprises were experiencing serious payments difficulties, but had to be paid once their problems had been overcome. Certain of these enterprises would eventually be required to institute financial recovery programs. If enterprises experiencing liquidity difficulties were not given financial support there was the prospect that they would stop paying their suppliers setting off a chain reaction that could endanger the production of essential commodities.

Mr. Hole raised the question of how quickly the NBP could tighten credit policy if such a need arose. Mr. Karcz said that at the beginning of the year banks entered into contracts with enterprises to meet their annual financial needs. Certain adjustments could be made to new credits extended during the course of the year, and indeed, during the May-June 1983 period credit policy had been tightened. Just recently, the Governor of the NBP had proposed that there be some limiting of bank credits since government expenditures in the first two months of 1985 were exceeding tax revenues by a larger amount than planned. However, the Ministry of Finance had thought that it would be premature at this stage to take corrective action.

The stock of bank credit extended to enterprises as a proportion of total bank credit had fallen since 1981 and now was around 53 percent. This decline reflected the larger claim of cooperative housing on bank credit resources, with the share rising from 16 percent at end-1980 to 24 percent at end-1984. The authorities were aiming at increasing the proportion of housing investment financed by internally generated funds.

5. Reconciliation of banking and budget data

It was pointed out by Mr. Prust that banking data for 1982 and earlier years showed a larger deficit for the state budget accounts than what budgetary data indicated. Mr. Karcz said that banking data for a particular budget year did not reflect tax collections that were actually recorded in banking transactions after the end of the year. Also, actual budgetary cash disbursements tended to be heavy before the end of the year. However, it was agreed that a reconciliation between budgetary and banking data could be pursued in technical meetings.

The meeting adjourned at 12:15 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 11
Held at the National Bank of Poland
on April 3, 1985, at 3:00 p.m.

Polish representatives

Mr. Karcz, Director, Ministry of Finance
Mr. Wojtowicz, Director, National Bank of Poland
Mr. Przywecki, Director, National Bank of Poland
Mr. Krowacki, Advisor, Ministry of Finance
Mr. Ilczek, Division Chief, Ministry of Finance
Mr. Lichotski, Ministry of Finance
Mrs. Rubel, Advisor, National Bank of Poland

Fund representatives

Mr. Hole
Mr. Manison
Mr. Prust
Mr. Boonekamp
Ms. Swiderski

1. International reserves

Mr. Karcz said that the Polish representatives from the Ministry of Finance and National Bank of Poland were encountering difficulties in completing table 12 of the staff questionnaire on international reserves. There was the problem of finding more precise criteria for determining what foreign assets should be included in international reserves. Even the guidance provided for such a determination in the Fund's Balance of Payments manual was couched in general terms. There was also the question of how international reserves were defined for the purpose of calculations of Poland's quota in the Fund.

The Polish representatives had traditionally only included gold and foreign exchange held by the National Bank of Poland in their gross external reserves. However, both Bank Handlowy (which handles foreign commercial transactions) and the PKO Bank (which mostly handles noncommercial foreign transactions) also held foreign assets. These banks were authorized to carry out foreign exchange transactions on behalf of the state and their foreign assets were at the disposal and subject to the effective control of the central authorities, especially in times of emergency. Should all of the foreign assets of these two banks be included in Poland's international reserves? For example, should the deposits in foreign banks which served as cash collateral requirements against letters of credit for imports be included?

There were also foreign assets held by Polish enterprises, some relating to the delayed repatriation of export proceeds by foreign trade organizations. In the case of an emergency the authorities could use such means to finance payments imbalances.

It was the view of Western creditors that transferable roubles could not be used in exchange for convertible currencies. However, more than half of Poland's external trade was with countries where transactions were denominated in transferable roubles. Transferable roubles were particularly valuable for intra-CMEA trade and for Polish participation in joint CMEA investment projects. A second question concerned the exchange rate at which transferable roubles should be converted into U.S. dollars for purposes of the valuation of reserves. Should one use the IBEC rate or the implied cross rate derived from the rates set by the Polish authorities for converting transferable roubles and U.S. dollars into zlotys. In view of the tendency for prices of raw materials in transferable roubles to be lower than for similar products in U.S. dollars in trade with the convertible currency area, Mr. Karcz thought that conversion of transferable roubles into U.S. dollars at implicit cross rates vis-à-vis the zloty might understate the ability of Poland's foreign assets in terms of transferable roubles to finance real trade with CMEA partners.

In addition, should Poland's assets in clearing account arrangements with market economies be included in reserves?

Mr. Hole said that a meaningful definition of international reserves and how international reserves should be defined for quota calculations were in principle separate issues, although it was clearly desirable to limit differences between the two concepts. The Fund did not have a rigid all-encompassing definition that was applicable generally. There were certain criteria which foreign assets needed to meet to be considered reserves, foremost among which were that the asset was readily available to the central authorities and usable to finance payments imbalances. But for some assets, application of the criteria would require judgement and interpretation. In view of this, it would be preferable if detailed information could be provided on the nature, ownership, and amounts of the central authorities' foreign assets, broadly defined. This would permit the staff to reach a better judgement on what should, and what should not, be included in Poland's international reserves.

Mr. Karcz then sketched the principal asset holdings. He noted that a decision of the Council of Ministers required that the authorities keep \$200 million in gold reserves. There were also deposits in the accounts of foreign banks to be kept as cover against import transactions. To date, amounts kept with foreign banks for replenishing the revolving trade credit facility had not been included in reserves. Of course these deposit balances fluctuated in relation to specific payments dates. Apart from the accounts of Polish banks with 300 correspondent banks abroad, Polish entities overseas, especially those involved in construction and transportation activities, held sums in foreign banks. Polish entities also had claims on foreign companies and governments, all of which could be sold at some price. For instance, Saudi Arabia was interested in purchasing Poland's claim on the Sudanese Government. In summing up Mr. Karcz said that foreign assets could be classified as follows:

1. Classical reserves;
2. Operational reserves;
3. Fluctuating deposits;
4. Accounts abroad held by Polish nonbank entities.

He asked the staff to help in providing precise criteria to enable Poland to work out a meaningful measure of its international reserves.

2. Balance of payments developments and propects

Mr. Karcz said that balance of payments developments in the first two months of 1985 revealed that exports on a seasonally adjusted basis were $120-150 million below plan. The shortfall in exports was due in part to the adverse effects of the severe winter on sea and railway transportation. The freezing of Polish ports had been abnormal and it was possible that some lags in shipments of exports would be made up. A more serious problem related to energy shortages during the winter which caused irretrievable losses in the output of fertilizers and cement, plus adversion to the domestic market of more domestic coal than usual.

Overall, Mr. Karcz now thought that Poland would be fortunate to reach its export targets, which initially had seemed quite modest. On invisibles account it was likely that transfers into individual foreign currency accounts would be higher than expected. However, receipts from transportation companies were lagging.

Given the shortfall in current account receipts in the first quarter and the need to meet debt servicing obligations Mr. Karcz said that imports would have to be limited in the second quarter of 1985. For 1985 as a whole there was very little chance that external trade targets would be exceeded.

A more difficult problem related to the servicing of external debt obligations. Gross repayments could not be met unless there were sizable inflows of new credits. In this context the Polish authorities thought that if US$700-800 million in new funds could be obtained from governments, it might be possible to sign the Paris Club accord, although even then some payment dates might have to slip. The process of normalizing external financial relations had slowed down but the Polish authorities hoped that Western governments would show sufficient flexibility to enable repayments obligations to be met. At the time of the initialling of the Paris Club agreement it had been envisaged that the interest payments arrears from 1981 would be cleared up by December 20, 1985. However, there now seemed to be a need for a slight postponing of this deadline until 1986 and for positive progress in the Paris Club talks (including bilateral discussions) to take place before the end-May-June period. Otherwise the whole process of normalizing financial relations with the West could be delayed.

The extension of export credits in net terms were expected to be zero in 1985 with gross flows equal to $300 million.

3. Exchange rate

Mr. Hole said that earlier meetings with Polish representatives and experts had suggested that at the current exchange for the zloty a considerable volume of exports were unprofitable. Mr. Karcz replied that presently around 50 percent of exports were profitable while the remainder required subsidization, against the formally mandated 75-80 percent. Proposals had been considered for adjusting the exchange rate so that 80-90 percent of exports were profitable. However, such an exchange rate would involve a substantial increase in subsidies for keeping the domestic prices of imported goods low. Quarterly time series analysis had shown also a lag of 4-5 months in the adjustment of exports to a more depreciated rate for the zloty and during this period certain exports would once again become unprofitable at the new exchange rate. Mr. Karcz added that he was unhappy that the law requiring that the exchange rate of the zloty be adjusted when domestic prices relative to export prices changed by 5 percent or more was not being fully observed. Mr. Karcz said that subsidies extended mainly related to exports of raw material and agricultural commodities and that costs of 90 percent of other exports did not require the payment of a goverment subsidy. Foodstuff subsidies amounted to Zl 611 million in 1984.

2. National Accounts

The discussion focused on the national accounts table presented on an SNA basis (table attached). Currently, the national accounts on an SNA basis are not available in constant prices; however, the authorities felt that the appropriate deflators would not be significantly different from those used in calculating real material product. Mr. Zienkowski noted that, based on calculations done for previous years, the output deflator on an SNA basis was about 1/2 percentage point less than the relevant one on a material product basis.

As regards an international comparison of the relative shares of gross fixed capital formation in GDP, the the Polish representatives agreed that this ratio may be biased upward in the case of Poland because prices of consumption goods have been kept at an artificially low level relative to the price of investment goods.

The definition of gross fixed capital formation used in the Polish national accounts differs from the concept of "investment outlays" in that the latter includes outlays of a nonmaterial character as well as expenditures that are associated with, but not directly linked to, the investment outlays (e.g., the purchase of beds and other equipment for newly built hospitals, notary fees, etc.). Furthermore, the national accounts data include an estimate of the change in the capital stock of agriculture, which is excluded from the concept of investment outlays.

The definition of stocks in the national accounts differs from the one used in the table on "stocks of socialized enterprises" in the following ways: (1) in the national accounts the annual change in stocks is taken on January 1 which incorporates the new year's price level changes; in the table on enterprises' stocks the relevant date is December 31 which is based on the price level of the terminated year; (2) the definition used in the national accounts includes an estimate of stocks in private agriculture and construction; and (3) work in progress in construction and some material investments, which are included in the table on enterprises' stocks, are reclassified into gross fixed capital formation for national accounts purposes.

In the table on "Household's Disposable Income" the item "other money income" includes: net bank credits for housing, net (nonbank) loans for construction, benefits from the social fund, benefits for newlyweds, interest earned on savings deposits, per diems of Parliamentary members, incomes from official travel, incomes of agents, compensations for mining damages, remunerations for blood donations, incomes from the distribution of the surplus of agricultural and construction cooperatives, benefits related to health care, incomes of the population from the sale of goods and services, gold, and agricultural products to the socialized sector, incomes other than in the form of wages earned from work done for the socialized sector, expenditure of the Minister of Defense, paid expenses at sanitoria, payments from FAZ, rental income, value of foreign currency used to purchase commodities (mainly in Pewex shops), exchange of foreign currency into zloty, etc. The above items are not ranked in terms of order of magnitude. The exchange rate used to convert the value of foreign currency into zloty was based on an average rate that was constructed by comparing the foreign currency prices of a selected basket of goods to the relevant domestic retail prices.

The Composition and Distribution of Gross Domestic Product of Poland /at current prices/

Specification	1980	1981	1982	1983
	in billions of zlotys			
I. Composition of GDP				
Industry	1164,7	1044,5	2536,2	3122,1
Construction	222,6	179,7	529,2	662,6
Agriculture	330,8	656,7	907,5	1064,5
Forestry	26,0	26,8	75,1	87,9
Transport and communications	184,1	182,4	247,0	364,7
Trade	260,4	276,6	662,6	809,5
Other	47,5	51,7	79,8	116,7
1. Gross Material Product /produced in the sphere of material production/	2236,1	2418,4	5037,4	6228,0
2. Value added of non-material services	329,9	403,2	618,5	977,7
3. Consumption of non-material services in the sphere of material production	15,3	26,6	46,2	76,5
4. Other differences[1/].	39,5	42,4	63,3	87,6
5. Gross Domestic Product /1+2-3-4/ ...	2511,2	2752,6	5546,4	7041,6

[1/]Allowances for business trips, expenditures on social and cultural services to employees, imputed gross output of financial institutions destined for enterprises.

The Composition and Distribution of Gross Domestic Product of Poland /at current prices/

Specification	1980	1981	1982	1983
	in billions of zlotys			
II. <u>Distribution of GDP</u>				
1. Consumption	1910,3	2301,3	3931,2	5214,2
2. Gross fixed Capital Formation ...	621,2	513,9	1117,4	1394,5
3. Increase in stocks	40,5	-5,8	433,2	339,4
4. Total domestic expenditure	2572,0	2809,4	5481,8	6948,1
5. Net exsports of goods and material services, losses and unallocated items ..	-60,8	-56,8	64,6	93,5
of which:				
- Exsports	706,8	638,4	1077,8	1192,4
- Imports	780,3	696,5	961,8	1070,2
6. Gross domestic product /4+5/ ...	2511,2	2752,6	5546,4	7041,6

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of Meeting No. 12
Held at the Ministry of Finance
on Thursday, April 4, 1985 at 12:00 noon

Polish Representatives	Fund Representatives
Mr. S. Nieckarcz, Minister of Finance	Mr. P. Hole
Mr. W. Bien, First Deputy Minister of Finance	Mr. L. Manison
Mr. Karcz	Mr. J. Prust
Mr. Krowacki	Ms. K. Swiderski
Mr. Minkiewicz	Mr. C. Boonekamp
Mr. Lichocki	

Mr. Nieckarcz welcomed the staff team and said that he hoped that for him the present meeting would be the first of a series of contacts with the Fund staff over the years.

Mr. Hole thanked Mr. Nieckarcz for his welcoming remarks and said that the main purpose of the staff's visit had been to build up an understanding of Poland's economic mechanisms and to understand and explore various statistical issues. In its two visits, Mr. Hole continued, the staff had made very good progress. He could not profess to a complete understanding of the economic system but thought that a reasonable understanding of the basics had been achieved. He expressed thanks for the cooperation of Mr. Karcz and his associates. This had greatly facilitated the team's work which had taken place in a pleasant atmosphere. The visits to the local office of the National Bank of Poland in Cracow and to enterprises had been interesting nd instructive. The staff had found such visits useful in its work on other nonmarket economies.

Mr. Nieckarcz inquired about the staff's impressions of Poland's economic data: did they correspond with the mission's impressions of economic developments from other sources? Mr. Hole replied that this was a hard question to answer. He had the impression that the managements of all three enterprises that the team had met with welcomed the greater freedom that they enjoyed as a result of the changes introduced since 1981. He wondered whether this was representative of industry generally or whether the process of changing attitudes could only be expected to develop gradually.

Mr. Nieckarcz offered some impressions and information. He recalled the practically ruinous state of the domestic economy in 1982: shortages were widespread and inflation was very rapid. The economy had become involved in a political battle. The financial effects of this situation were still felt and two-thirds of the inflation currently experienced was due to the effects of the earlier period of difficulties. However, broad and unprecedented reforms had been made. Although various opinions were expressed both in Poland and overseas, Mr. Nieckarz wished to stress that the entire government of General Jaruzelski was determined to carry through the economic reforms which had been started. There could be no turning back and everyone concerned realized that economic reform offered the main chance for improving efficiency. Practically two-thirds of the managers of key enterprise had been replaced by persons with a high degree of economic knowledge and management skill. Without these changes it would be much more difficult to carry through the reform. He also noted that most of the members of the present government had been appointed within the last three years and were not burdened by the traditions of the old command system. Another important ingredient in the reform process had been the fundamental changes made in the financial apparatus.

Mr. Niekarcz went on to say that he felt sure that from its contacts with other socialist countries the staff would realize that the Polish economic reform went deeper than in all other cases, not excluding that of Hungary. The reform was not limited to the economic mechanism but encompassed many other aspects including the introduction of enterprise self-management and changes in the role of trade unions, ministries, and the organs of local government. Many new institutions had been created of which Mr. Niekarcz specifically mentioned two: the Social and Economic Council of the Parliament and the Consultative Economic Council to the Government. The latter was an assembly of distinguished scholars.

Mr. Nieckarz reiterated the commitment of the government of General Jaruzelski to economic reform. Foreign press reports were very misleading in questioning this commitment. For the future the main directions of policy would remain unchanged but in the course of the coming five-year plan period there would, of course, be certain policy adjustments in the light of evolving conditions.

Mr. Nieckarz went on to make some remarks about the current economic situation of which his evaluation was positive. The stage of falling output and national income was over and, even on the most pessimistic assumptions, he did not expect it to return. An assumption in formulating the next five-year plan was that Poland would continue to generate a balance of payments surplus. Another assumption was that there would be a full normalization of financial relations with external creditors; Mr. Nieckarcz could not foresee any other outcome. It was realized that there were difficulties. Shortages of material inputs continued and the coming years were expected to see only very small growth in the labor force. There had also been delays in introducing measures for environmental protection. But the authorities would try to limit the effects of these factors as much as possible.

In response to Mr. Nieckarz's remarks, Mr. Hole agreed that there were visable signs of recovery including the strengthening of the trade balance. He wondered, though, whether it would be fair to say that what had been achieved so far, especially in restoring exports of raw materials and primary products, represented the relatively easy part of the adjustment process that Poland faced. The more difficult issues were perhaps those that were addressed by the economic reform, in particular the need to generate more exports of manufacturers. Mr. Hole wondered how quickly a greater export orientation in the industrial sector could be brought about.

Mr. Nieckarcz agreed that primary commodities, especially coal, had represented a considerable part of exports in recent years and that there had been a drop in the share of manufactures. However, he noted that in the past few years there had been practically no imports of production inputs because of the suspension in the flow of foreign credits. Much of Poland's productive capacity was dependent on Western technology and on access to Western inputs. In the space of 1 1/2 years imports from the West had fallen by half. With the normalization of financial relations it would be possible very rapidly to reverse the enforced under-utilization of capacity that the import shortages had caused. Technological change was needed but its extent should not be exaggerated: it was more a question of "plugging gaps" than "starting from scratch." There were a number of incomplete investment projects which were based on cooperation with the West. These needed finishing but this could not be done with domestic resources alone.

Mr. Hole inquird as to the authorities' views on the time path to the point where Poland's external debt would start to fall, on the assumption of a normalization in financial relations. Mr. Nieckarcz replied that the first priority was the finalization of agreement with the Paris Club. This, of course, required the assent of both sides but Mr. Nieckarcz said that the present state of affairs was such that he believed that agreement by the end of the year was certain. He could not say whether this would be in June or September but hoped it would be the former. He noted that the process of bilateral negotiations with 17 creditor countries was very time consuming. The time when Poland's debt would start to fall was some years away.

Returning to the topic of economic reform, Mr. Hole said one thing that was surprising to outsiders was the extent of variations in application of the parametric instruments of economic policy. He wondered whether any move to greater uniformity was envisaged or whether it would be unreasonable to expect this. In reply, Mr. Nieckarcz said that there must be some fixed basic parameters such as tax rates and in the link between wages and output. It was true that in some respects arrangements in these areas were somewhat complex in Poland but to some degree every country had such domestic complications. The Ministry of Finance was fully in favor of stabilizing the tax system and had proposed that a fixed income tax rate of 65 percent be maintained for the next five years. This proposal had to be submitted for wider discussion. However, some

some flexibility in the parameters of economic policy was necessary and desirable in such areas as the exchange rate and turnover taxes and as to the form of tax relief and rebates so as to give encouragement to various sectors in line with the changing priorities of overall policy. This did not imply any endorsement of unstable parameters and it was hoped that by the end of 1985 the basic economic parameters (both fixed and variable) would have been set for all enterprises for the following five years.

Mr. Hole said that he accepted that no country's tax system was totally uniform and went on to make some remarks about the FAZ. On the one hand, it was clear that enterprises did not like it, which proved that it was effective. On the other hand, there were many variations in its precise method of application which meant that FAZ rates were potentially different for every enterprises. Mr. Nieckarcz said that the original intention of FAZ had been to raise funds to meet the costs of unemployment. But, with no threat of significant unemployment, it had come to be seen as a device to prevent excessive wage increases. However, one could not be fully satisfied with the way in which it was working and Mr. Nieckarcz said that he would not exclude the possibility that it would be abandoned altogether before the start of the next five-year plan period. It was true that it was a complicated instrument and in applying it the authorities often faced a difficult choice between the urgent demands of an immediate situation and the need for long-run stability. For instance certain steel plants were trying to make up for the effects of the hard winter but would be quite unable to get people to work the necessary third shift to do this unless they could offer much higher wages than their present FAZ regime allowed.

Mr. Hole observed that the need for instruments such as the FAZ and for price controls highlighted the difficulties created by the highly concentrated structure of Polish industry and the fact that decentralization was in itself likely to strengthen the power of monopolists. Mr. Nieckarcz replied that the classic way to approach these issues was to foster competition between domestic and foreign producers. When circumstances permitted, this would be done but for some sectors Mr. Nieckarcz could see no sense in breaking up the existing monopolies. In the context of a socialist economy this could be a waste of resources. Moreover, energy, steel, coal, and other basic materials would need to remain under price control and subject to central allocation until there was an improved balance of supply and demand. There was the alternative possibility of freeing all prices but this would be highly inflationary and would be incompatible with the Government's social policies. Of course, it was desirable to achieve an equilibrium between aggregate demand and supply but the Government was approaching the problem by raising supply rather than reducing demand and raising prices. For this reason a wide range of basic items continued to be subsidized although Mr. Nieckarcz noted more had been done in changing the prices of basic foodstuffs in the last three years than in the previous 15 years. In sum, the authorities were trying to raise production and decrease production costs and would only raise prices very judiciously.

In conclusion, Mr. Nieckarcz said that he was sure that he would have more opportunities to meet with the officials of the Fund. He wondered how Mr. Hole saw the likely course of events. Mr. Hole replied that on returning to Washington he would report to the Managing Director on the progress made in understanding the Polish economic system and in analyzing the statistical data in substantially the same terms as he had earlier indicated to Mr. Nieckarcz. The Fund's Management would then decide on what steps should be taken next and at that time Mr. Hole would be in touch with the Ministry of Finance through Mr. Karcz.

The meeting ended at 1:00 p.m.

Office Memorandum

April 11, 1985

MEMORANDUM FOR FILES

Subject: Poland: Visit to Hortex

The mission (comprising Messrs. Hole, Manison, and Prust, and Ms. Swiderski) visited a Hortex fruit and vegetable processing plant in Przysusze on Wednesday, March 27, 1985. The mission was received by Mr. M. Kucharczyk (Managing Director of the Hortex group), Mr. W. Spoczynski (Director of the plant), Mr. E. Etwert (Deputy Director of the plant), and Mr. Z. Maroszek (Director of Hortex' foreign trade enterprise).

1. The Hortex enterprise group comprises twelve entitites plus a foreign trade organization, specializing in the processing of food and agricultural products for market, both export and domestic. It consists of eight food processing and freezing entities (with a ninth under construction), a restaurant chain, a transport unit, and two building and machine production entities. Each plant is nominally independent of the other, but receives guideline directives from the Hortex managing unit, under the direction of Mr. Kucharczyk. The group employs some 10,000 workers, with about 1.8 thousand of these engaged by the restaurant arm.

2. In 1984, the Hortex group processed some 230,000 tons of fruit and vegetables, and a volume of about 300,000 tons is anticipated in 1985. Approximately 60,000 tons of its 1984 supply derived from about 20,000 private farms, with the balance coming, under subcontract, from farming cooperatives. In all, the group handled about 60 percent of Polish fruit and vegetables. The group buys its produce outright from the farmers and cooperatives. Prices are negotiated with the sellers and are typically set for the season in June; they are renegotiable subject to changing market conditions. The domestic price offer (with each unit acting independently but utilizing the information pool of the central managing unit) is based on both harvest forecasts and foreign market prices. When needed, the plants provide technical assistance to their suppliers and supply them with seeds.

3. The entity at Przysusze specializes in fruit and vegetable processing. It has two plants, with the latter of the two built in 1978 with the aid of a US$18 million (convertible currency) credit which had been amortized from export earnings by mid-1984. There are four production lines: (i) for frozen vegetables and fruit (mainly strawberries, raspberries, blackcurrants, beans, and mixed vegetables); in 1984 it handled 15,000 tons, 80 percent of which was exported; (ii) for concentrated fruit juices (mainly apples), which produced 3,000 tons in 1984; (iii) for apple storage, with facilities for 5,000 tons in a controlled atmosphere plus a further 5,000 tons under normal atmosphere; and (iv) for sugar syrup production, with a capacity, which was only recently brought onto line, of 20,000 tons.

4. In 1984, the Hortex group exported some 70,000 tons of fruit and vegetables, of which fully 50 percent went to the convertible currency area. Its exports to the latter area included 20,000 tons of strawberries (60 percent of EEC imports), 10,000 tons of vegetables, and 15,000 tons of raspberries and blackcurrants (20-25 percent of EEC imports). The group is doing well in the U.S. market, despite a 34 percent import duty. It faces an 18 percent import duty for its exports to the EEC. Generally, Hortex exports directly to producing enterprises in the West (Kraft, Unilever, etc.) rather than to distributors to the consumer market, since its products are used as ingredients for further production (e.g., strawberries for flavored yoghurt). The group does not produce specifically for export. It seeks to satisfy the home market (or, at least, takes its needs into account), exporting its residual produce thereafter. Exports are effected through the group's foreign trade enterprise (FTO), which has a general authority to export fruits and vegetables and a prescribed right to import various-input needs for the enterprises of the group. The entities sell their produce for export to the FTO at a negotiated price, based on current and forecast world market prices. The FTO trades on its own account, absorbing profits/losses and any subsidies and/or taxes from the export/import price equalization scheme. It negotiates its own access to the export/import price equalization fund with the Ministry of Foreign Trade. The FTO also trades, but only on a limited basis, for companies outside the Hortex group. In doing so, it competes with other FTOs on the basis of service, quality, and price. The Hortex FTO accounted for 60 percent of Poland's 1984 exports of fruit and vegetables. It does not require an export license for each individual contract. The entities have their own export retention rights, which average 20 percent across the exporting units of the group. In general, the entities do not have access to the centrally allocated pool of foreign exchange for imports. Rather, their imports are against the exchange retention scheme and are effected by the FTO. Imports in the main consist of spare parts, some raw materials, and, occasionally, seeds, particularly for the supplying units, whose import needs are satisfied, to the extent possible, from the export exchange retention pool of the entity which it supplies. The 20 percent export retention quota was not regarded as adequate to fully meet import needs in the form of packaging materials, in particular, and new machinery. The FTO requires a specific import license for each import contract.

5. <u>Other matters</u>

a. The export entities of the Hortex group receive a 3 percent (of the value of exports) income tax drawback for exporting, and are also permitted an income tax drawback equal to 20 percent of the value of incremental exports in one year.

b. The entities of the group pay 25 percent of their net profits (after income tax) into a development fund and 20 percent into an investment fund, and the remainder is used for assorted purposes, including the improvement of social facilities for the community. Profits subject to taxation amounted to Zl 71 million in 1984, but tax allowances reduced them to Zl 41 million.

c. The FAZ payments of the members of the group are based on gross sales addition (in constant prices). Around Zl 11 million was earmarked for FAZ on the basis of the 1984 operations. However, Hortex was negotiating to obtain a preferential correction coefficient under FAZ.

d. Hortex had introduced a new wage system some five months ago gearing wage payments more closely to employee productivity and taking account of job hardships (e.g., working in sub-zero temperatures). Although this had helped in eliminating unproductive workers, it was still too early to determine whether the new wage system was having a discernible impact on productivity.

C.F.J. Boonekamp
Trade and Payments Division, ETR

cc: Mr. Hole
Mr. Manison
Mr. Prust
Ms. Swiderski

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of a Meeting
Held at "Krakowska Fabryka Kabli", Krakow
March 29, 1985, at 2:45 p.m.

Polish Representatives

Krakowska Fabryka Kabli

Mr. Morenski, Managing Director and other members of the Board of Directors

Treasury Chambers, Krakow Branch

Mr. S. Smietana

Ministry of Finance

Mr. Z. Lichotski, Foreign Department

National Bank of Poland, Head Office

Mr. S. Przywecki, Director, Planning Department
Mr. G. Wojtowicz, Director, Foreign Department

National Bank of Poland, Krakow Branch

Mr. Z. Patroczka, Managing Director

Fund Representatives

Mr. Hole
Mr. Manison
Mr. Prust
Ms. Swiderski
Mr. Boonekamp

On March 29, 1985 the staff team visited Krakowska Fabryka Kabli (KFK), an enterprise which produced cables and some machinery for its own needs. The enterprise had been established in the early 1930s and much of the plant comprised old heavy industrial machinery. After a tour of the plant the following matters were discussed.

1. Reforms and institutional structure

The Managing Director of the KFK said that since the implementation of reforms in 1981 management had been given more freedom in the running of their enterprise, with only directives or guidelines from outside on a very few matters. The enterprises' workers' council was consulted by management on most decisions including the five-year plan, how production targets should be achieved, and the distribution of profits. The founding bodies of KFK comprised the branch ministries with which it was associated and the local authorities involved in the setting up of KFK. The founding bodies were influential in KFK obtaining government contracts. KFK also belonged to an industrial association consisting of cable producers and other production-related enterprises.

The implementation of reforms had now made the management and workers of KFK more cost conscious and motivated to obtain higher profits since the latter could be used for the development fund and higher wages.

2. <u>Production, inputs and pricing</u>

At present, KFK was endeavoring to direct a considerable part of its output to the export market as this would allow preferential tax treatment and hence more resources for the development fund and for wages. In addition, KFK could obtain foreign exchange under the export retention scheme. Its export transactions were carried out by a foreign trade organization chosen by KFK. Management was quite satisfied with the performance of the foreign trade organization through which it had links with the buyers of its products that enabled negotiation of transaction prices.

Production sold on the domestic market was handled by a central distribution enterprise which sought out potential customers. However, it was said that 90 percent of the output of KFK went to fulfilling government contract orders. Accordingly, most of the essential production inputs of KFK, including imported materials, were directly allocated from central bodies. Output for exports to socialist countries was determined according to bilateral agreements, with production inputs supplied from central sources in a similar way to those secured under government contracts.

The output of cables of KFK were sold at officially-administered prices which were approximately equal to current costs. If costs increased there was little difficulty in obtaining commensurate adjustments in prices. The last change in administered prices for cable products was on January 1, 1985, which was 2 percentage points less than what had been requested. In presenting their case enterprises usually joined together with their founding bodies in their submissions to the Price Adjustment Board. Prices of cable producing machinery were negotiated with purchasers and required no subsidies.

3. Investment

Fixed investments were largely financed from internal funds, with the emphasis being on the modernization and replacement of the existing capital stock rather than on building new structures. Bank credits could be obtained, especially if it could be shown that production was being directed to export markets and/or was based on import-saving techniques and/or helped to protect the natural environment. In general, banks assessed whether enterprises would generate sufficient funds to finance investments within a scheduled time period. The rate of taxation on the profits of KFK were reduced to around 35 percent because of drawbacks obtained as a result of export performance and the good quality of production. Most of the profits of KFK were allocated to the Development Fund which was available for fixed and working capital investments. Smaller sums were distributed to the social and housing funds.

4. <u>Wages</u>

KFK had introduced a new wage system on December 1, 1984 the agreement on which was signed by the factory management and workers and the Ministry of Labor. The latter was responsible for judging whether the new system is in line with overall guidelines specified by the central authorities. With the new wage system there was now more scope for tailoring wage increases to labor productivity gains. Wage payments were adjusted mostly in line with the extent to which planned production schedules were being achieved. In comparison with the previous wage system, the scope for paying workers' bonuses was now more limited. Presently, bonuses represented around 15-20 percent of worker earnings, whereas previously they amounted to 80-100 percent. There were no automatic adjustment of wages to cost of living changes. Wage increases were limited by the FAZ with a coefficient on rises in net production providing the effective constraint. The large rise in production in 1984 helped to keep payments into FAZ at a low level. While labor shortages constituted another production constraint to KFK, offering higher wages was unlikely to be a solution as the present wage structure was said to be very competitive. An enhanced supply of consumer goods on the domestic market would be helpful in raising labor productivity through among other things causing workers to spend less time in queues.

5. Exports

The exports of KFK to the West were limited by the demand from these countries, as there was strong competition in this market. Prices obtained by KFK for such exports were similar to domestic prices with there being no tax payments into or subsidies from the exchange equalization account. On the question of whether a change in the exchange rate would have a significant impact on exports, the Managing Director initially assessed the influence of the exchange rate through its impact on the costs of raw material inports. He noted that the factory management had autonomy in deciding on the size of its exports. In value terms they had risen by 28 percent in 1984 and were planned to increase by 15 percent in 1985. If KFK could retain higher amounts than the present 15 percent under the export retention scheme, this was unlikely to significantly affect the attractiveness of exporting as foreign exchange resources were already sufficient to cover raw material imports. Indeed, the shortage of foreign resources have never hindered production activity and the export retention quota could be negotiated upwards with the Ministry of Foreign Trade if the import intensity of production rose. Profits were said to have been a more important constraint on production since it tended to place a limit on the formation of new productive capacity and hence future output.

The meeting adjourned at 6:30 p.m.

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of a Meeting held at the
National Bank of Poland, Krakow Branch
March 30, 1985, at 9:00 am

Polish representatives

National Bank of Poland, Krakow Branch

Mr. Z. Patoczka, Managing Director
Mrs. L. Sweder, Deputy Managing Director
Mrs. H. Marawska, Director
Mr. R. Arwija, Division Chief (Trade Credit and Local Economy)
Mr. S. Srikorki, Division Chief (Credit to the Population Sector)
Mr. J. Palka

Treasury Chambers, Krakow Branch

Mr. S. Smietana, Managing Director

Ministry of Finance

Mr. K. Krowacki, Advisor, Foreign Dept.
Mr. Z. Lichotcki, Specialist, Foreign Dept.

National Bank of Poland, Head Office

Mr. S. Przywecki, Director, Planning Dept.
Mr. G. Wojtowicz, Director, Foreign Dept.

Fund representatives

Mr. Hole
Mr. Manison
Mr. Prust
Ms. Swiderski
Mr. Boonekamp

After a brief introduction by Mr. Patoczka on the administrative area and organizational structure of the Krakow Branch, the discussion centered on, respectively, credit policy, the Bank's activities in the restructuring of enterprises under the Bankruptcy Law and, finally, the role of the Treasury Chambers.

1. Administrative area and organizational structure

The Branch serves a population of about 1.2 million residents in the municipality of Krakow and its surrounding area, 400,000 of which are employed in the socialized sector. It deals with 587 enterprises, of which the Lenin metallurgical works, employing 30,000 people, is the largest. It also meets the banking needs of numerous research institutes and 11 centers of higher learning. Within the Bank's administrative jurisdiction are nine Voivodship sub-branches, four savings banks, and a data processing center. Some sub-branches specialize in the needs of production-specific groups of enterprises, e.g., two deal chiefly with the Bank's 170 industrial-enterprise clients, while another meets the banking requirements of 70 construction and assembly enterprises. Although this sub-branch specialization allows the branches concerned to become closely familiar with the sector of industry that they serve, it does carry the disadvantage that not all enterprises have a bank branch within ready distance that is able to meet their requirements. In all, the branch employs some 1,700 people, including 180 credit inspectors whose task it is to supervise the Bank's relationship and accounts with the enterprises. Although a group of inspectors handles the Lenin works account, each inspector deals with three enterprises, on average.

2. Credit planning

The 1982 reforms have allowed the National Bank of Poland greater independence from the Ministry of Finance and national and local authorities in its dealings with enterprises. The Bank operates within the Central Planning System, which at times implies that preferential treatment is accorded to certain enterprises in line with the dictates of the Central Plan, but, in general, the degree of interference with the Bank's lending policies and credit decisions has been sharply reduced. This has meant that, at the Krakow branch level in particular, the system of automatic credits to enterprises has been eliminated in the past two years and the branch has become quite strict in extending funds to enterprises. Within the guidelines established by the national credit plan and the President of the National Bank, the branch now seeks to implement a tight credit policy in order to reduce and prevent excess liquidity and to encourage enterprises to rely more on their own resources. Accordingly, with information gathered from both the National Bank's nationwide network and the branch's credit inspectors, enterprises with sufficient own funds may have their credit restricted (or applications denied), as may those enterprises not operating efficiently, and/or producing low-quality goods, and/or not deemed to be creditworthy, and/or distributing profits by means of wage increases in excess of productivity increments, and/or with a production technology which is excessively energy- and/or import-intensive. With respect to the latter category, the Bank is guided, in part, by a centrally prepared list of "inefficient goods."

Indicative of the tighter credit policies is that, although production rose, the share of short-term bank credits in financing the current activity of the branch's clients fell from 42 percent in 1982 to 36 percent in 1983, and to 31 percent in 1984; the share is expected to drop further in 1985. Further, whereas industrial output in the Krakow area rose by 7 percent in 1984, the volume of Bank credit to industrial enterprises declined by 14 percent. In the construction sector, 1984 sales increased by 10 percent, while Bank credits to the sector fell by some 21 percent. Also in 1984, 13 long-term credit applications by enterprises were rejected, as were 18 applications for one-year credits.

Explanations on any of the Krakow branch's credit decisions may be requested by the relevant branch ministry, by the Ministry of Finance, or by the Warsaw head office of the National Bank. An appeal procedure culminating in consideration by the Warsaw head office exists, but in most cases the decisions of the Krakow branch are upheld; only four of its 1984 credit decisions were rejected by a higher authority.

In the Krakow branch's opinion, the tighter credit policies have led to improved efficiency in the use of financial resources by the area's enterprises and have served to put enterprise management and workers' councils on notice that only those units that are prepared to operate efficiently and with the future in mind are likely to have reasonably ready access to the Bank's resources. In this respect, however, it was noted that some enterprises may receive special treatment, but only in accordance with the Central Plan and/or directives from the President of the National Bank of Poland. Such treatment concerns, in particular, the food industry, export-oriented companies, and those enterprises fulfilling government contracts. As an example, credit to trade enterprises was increased by 3 percent in 1984, to enable them to build stocks of goods which were currently in short supply and/or to encourage them to hold larger-than-normal stocks of imported materials presently priced lower than usual.

In 1984, the Krakow branch extended long-term credits to 64 enterprises, some in the form of converted working capital credits. On average, converted credits account for 11 percent of enterprise liabilities to the branch, although in some instances the share may be as high as 60 percent. The maximum maturity of the long-term credits extends to June 1996, but on average they are granted with a date to maturity of seven years. In general, they carry a basic interest rate of 12 percent per annum (with converted credits being charged 9 percent per annum). In the main, and in accord with the branch's own priorities, the credits extended have been for the completion of projects already in process; where progress on such projects has been sluggish, the Bank has withdrawn credits, which in 1984 resulted in the return of Zl 7 billion. In granting long-term credits to new projects, the branch in 1984 sought to apply a rate of return criteria of Zl 1.5 per Zl 1 in a "short time;" such projects had to have a completion timetable of two years (one year in the case of funds for modernization) and a slated amortization period of five years from the date of commencement of the project.

Although the National Credit Plan does not set an annual limit on the amount of credit the Krakow branch is entitled to extend, the investment credit activity of the branch is circumscribed. On its own authority, the branch may make such credits up to a limit of Zl 100 million per annum to a nonindustrial enterprise; the limit per industrial enterprise is Zl 150 million a year. The Warsaw head office considers applications for amounts beyond these limits, with the Krakow branch serving to collect, process, and forward the required information. The head office allocates credits on the basis of the most effective proposed use of the funds, usually in line with the priorities set by the Central

Plan. Nonpriority projects are occasionally granted credits, both by the Krakow branch and the head office, but only if such projects hold outstanding promise. The authorities noted that, due to the severe selection criteria, the emphasis on the completion of ongoing projects, and the concerted drive to reduce the excess liquidity of the area's enterprises, less long-term credits had been extended to enterprises in the Krakow area of jurisdiction than in other regions of Poland.

In 1984, about 26 percent of the enterprises drawing Krakow branch funds did so under maturity terms of one year or less. The majority of branch credits to enterprises were extended against accounts receivable, with an average coverage against such accounts of about 54 percent. To encourage an active collection policy by companies, the branch does not extend credits against the surety of overdue accounts receivable. In general, it does not operate against set area, enterprise, or industry branch limits on the extension of working capital credits. In making such--and other--credits, however, it does seek to observe the national guideline that enterprise bank credits should not exceed 30 percent of an enterprise's total funds; the share per enterprise can go to 80 percent in cases of need. Further, the branch indicates its extensions (and, at times, its intentions regarding the granting) of working capital credits to a central information pool which coordinates nationwide adherence to the National Credit Plan. These working capital credits, which are normally not extended to enterprises availing themselves of inter-enterprise credits, carry an interest rate of 6 percent per annum; for enterprises (such as those which re-utilize materials) on a preferred list, the rate may be reduced to as low as 1 percent per year. The authorities thought that credit demand by all but the most cost-conscious of enterprises would not be significantly affected by a change (even of 5 percentage points) in base borrowing rates. Similarly, they were of the opinion that bank deposits would not be very sensitive to an increase in interest rates, largely because savings, reflecting the excess demand for goods, were already high. They went on to note that there had been a constant increase in savings in the recent past, and that the share of deposits in three-year and longer term accounts, which yield interest at the rate of 15 percent per annum, had been rising.

The branch operates within fixed limits in granting credits to cooperative housing units. As a guarantee that the limits will not be exceeded, credits are extended according to an agreed list. Investment credits to the population are limited to Zl 1.5 million per person, with preference given to those utilizing the funds for building houses with a living area of 170 square meters or less. Housing credits are generally not granted for homes with an intended area of greater than 220 square meters. The maturity of individual and cooperative housing unit credits can extend up to 60 years, at interest rates ranging from 1 to 6 percent, depending on the builder and need. The branch also has strict limits on the extension of consumer credits, particularly for purchases on an installment plan; preference is generally given to young married couples (aged 35 years or less) who can expect to own an apartment within three years. In addition to the above loans, the branch is prepared to extend credit to individuals for the purposes of house repairs, refurbishing, and the cultivation of garden plots.

3. Bankruptcy law activities

At present, 30 enterprises in the branch's area of jurisdiction are operating under recovery programs within the framework of the bankruptcy law. In general, these enterprises had operated under inefficient management, had produced low-quality goods, and had allocated excessive funds to consumption in the form of wages, at the expense of development needs. The branch extends credit to such an enterprise provided it undertakes to follow--and permits the bank to supervise--a negotiated adjustment strategy. In the case of three large construction companies, the strategy has included the divestiture of branches of the firms, a delimitation on their areas of operation, and restrictions on the type of jobs contracted. At present, most of the firms operating under restructuring programs are showing signs of improved financial health. However, the programs are in their initial stages, and it is as yet too early to judge if all the enterprises will recover completely or if some of them will proceed to bankruptcy. The most difficult cases are the larger enterprises in need of modernization, to which the branch has invariably not been able to grant credits, largely owing to uncertainty regarding their repayments. In these circumstances, the government and/or the relevant founding ministry must decide whether to come to the assistance of the enterprise, in which case, with appropriate guarantees, the branch might again stand ready to open lines of credit to the firm. In certain cases, decisions on whether to keep enterprises afloat through bank credits have been taken up to the deputy prime minister level.

4. Treasury Chambers

The Treasury Chambers is a branch of the Ministry of Finance whose task is to monitor the financial situation of enterprises and to ensure that they operate efficiently, do not make unreasonable profits/losses, and pay taxes in accordance with the relevant legislation. The Chambers employ a staff of financial specialists and, due to a shortage of skilled personnel, also make use of outside experts, such as bookkeepers. Should an investigation reveal that an enterprise is not operating efficiently as a result of its observance of the prevailing rules, the regulations pertaining to that firm can be adjusted and/or preferences may be granted to the company, especially if its functions are considered vital in the context of the Central Plan, which tends to give priority to export-oriented and import-substitution activity.

The Krakow arm of the Chambers oversees the operations of about 1,100 entities. There are three phases to the oversight functions of the Chambers. If necessary, an initial preliminary investigation is followed by an in-depth scrutiny of the current activities of an enterprise. At the third stage, completed on an annual basis for some 350 of the area's enterprises, the firm's balance sheets and profits are fully verified. If these accounts are found to be in line with the regulations, they are returned to the enterprise for confirmation by the Workers' Council. In its investigations, the Chambers has found that numerous firms try to bend the rules according to their own needs, usually under pressure from employees to increase the wage fund. FAZ is a controlling mechanism in this respect, with the result that the Chambers keeps a watchful eye on FAZ payments. Part of these payments are allocated to enterprises for the retraining of workers and/or for vocational training. The remainder goes to the central, state, and local budgets; the latter receives some 20 percent of the total funds collected, although the actual percentage may depend on decisions taken by the enterprise's founding body and on the amount of property tax enterprises pay to the local authorities. These property taxes are not uniform; the rate depends in part on an enterprise's contribution to the social services of the community. Both property and turnover taxes paid by an enterprise are accounted as part of its costs, whereas "unreasonable cost/losses" (as determined, but not defined, by the Chambers) are part of an enterprise's tax base. Profits are taxed at a linear rate of 65 percent, with drawbacks allowed for both exports and incremental exports, and also where enterprises have taken measures to protect the environment and save on imports. "Unreasonable" profits--which are not defined to include cost reductions due to improved efficiency--are taxed at a penalty rate of, for example, 10 percentage points in addition to the base rate of 65 percent. The determination of "unreasonable" profits, and taxes thereon, is left to the judgment of the Chambers.

The Chambers has often noted errors in enterprise calculations of FAZ payments. These mistakes occur both because documents relating to FAZ tend to be changed frequently, and because of differences in interpreting and measuring production increases. Technically, each firm can have its own FAZ system, its own FAZ coefficient (negotiated with the Ministry of Finance), and a unique (either to itself or to the sector of activity in which it operates) production measure. This latter is particularly important for determining "allowable" increases in the wage fund, with the result that enterprises seek liberties in its interpretation, such as including unfinished output in total production statistics.

Office Memorandum

MEMORANDUM FOR FILES April 3, 1985

Subject: Poland--Statistical Issues on the Real Sector

Mr. Zienkowski and I met briefly this morning to discuss several of my statistical queries that were based on data in the "Rocznik Statystyczny."

1. National Accounts Data

Statistics on material product are calculated at market prices. Net consumption is larger than gross consumption because it includes (1) an estimate of the depreciation of residential buildings in the nonsocialized sector (which may be considered as some sort of imputed rent) as well as (2) an estimate of the depreciation of fixed assets in enterprises outside the sphere of material production. Although net consumption is only larger than gross consumption by 0.8 percent, Mr. Zienkowski agreed that this procedure was incorrect. At a minimum these adjustments should be reclassified into the gross concept. The closest approximation to a definition of public consumption is given by the line on page 79 "glownie o charakterze ogolnospolecznym". (In the English version this is translated as "consumption of units rendering services to society as a whole"). This includes the material consumption of the state, justice, and other budgetary entities. The concept of gross fixed capital formation used in the national accounts differs from the concept of "investment outlays" in the Investment chapter mainly by the fact that the latter includes expenditure that are only indirectly related to investment projects (e.g., expenditure on social infrastructure, installation of required equipment, notary fees, etc.). Mr. Zienkowski thought that the largest underestimation of stocks in the private sector stemmed from handicrafts. Estimates of stocks in private agriculture and construction were quite accurate in his opinion.

2. Industry

In the chapter on industry, socialized industry is defined to include (1) industrial enterprises, (2) industrial enterprises of establishments that are not normally classified under the industrial branch, and (3) administrative bodies for these industrial enterprises translated into English as "units financed by surcharges." Since the output of these bodies is of a nonmaterial nature they are frequently excluded from the tables. Gross production is calculated at factor cost (e.g., Tables 1 and 2, p. 207) while net production is valued at market prices (e.g., Tables 7-10, p. 210-211). Both concepts encompass industrial establishment of nonindustrial enterprises but exclude units financed by surcharges because of the nature of the output that they produce. Production sold in Table 4 (p. 208) is based on producer (market) prices while in Table 11 (p. 212) it is calculated at actual sales prices (which may include sales at both the retail and producer levels). Table 2 on gross production (p. 207) and Table 4 (p. 208) on gross sales differ in three respects: (1) the former is valued at factor cost while the latter at market (producer) prices, (2) the former includes work in progress, and (3) the latter stems partly from inventories.

The calculation of labor productivity in industry in Table 21 (p. 223) is calculated using the net production figures given in Table 9 (p. 211) and employment figures in Table 14 (p. 218). The appropriate line for employment is titled "w tym grupa przemyslowa i rozwojowa" which is equivalent to about 90 percent of industrial employment and is the relevant group of workers that produce material output. (This line is not included in the English version.)

3. Investments

Table 7 (p. 177) titled "Budownictwo Inwestycyjne w Gospodarce Uspolecznionej"; (Building Investments in the Socialized Sector) includes about 80 percent of investments in the socialized sector since all the machinery and equipment associated with the construction of factories and other establishments is encompassed in this definition. This table is extremely useful since it provides information on the average degree of completion of investments, past and future requirements for investment projects in progress as well as year-to-year expenditure on these projects. In Table 8 (p. 179) "Finansowanie Inwestycji i Kapitalnych Remontow" (Financing of Investments and Capital Renovations), payments for investment outlays differ substantially from the value of outlays presented in Table 4 (p. 175) because they include actual payments made for current and past investment outlays. An increase in the value of uncompleted projects in a given year tends to reduce the financing requirements relative to the value of total investment outlays. Analogously, a reduction in the amount of work in progress in a given year produces an increase in financial payments relative to the value of outlays. As regards the classification of outlays between "Investments" and "Capital Renovations" the latter primarily includes major repairs.

4. Employment and remunerations

"Wynagrodzenia bezosobowe" in Table 23 (p. 224; not included in the English version; literally translated as impersonal payments) includes employee remunerations for work done at home, various honoraria and agents' fees. "Osoby wykonujace prace nakladcza" in Table 14 (p. 218; translated in the English version as "outworkers" with the more literal translation being employees performing outside work) encompasses workers that are considered a part of the permanent work force, however, they are remunerated on the basis of specific contracts completed.

Karen A. Swiderski

Karen A. Swiderski

cc: Mr. Hole
Mr. Manison
Mr. Prust
Mr. Boonekamp

Office Memorandum

MEMORANDUM FOR FILES April 16, 1985

Subject: Technical Meeting on the Balance of Payments and External Debt

Mr. Boonekamp and I met with Messrs. Krowacki and Lichotski of the Ministry of Finance and Mrs. Rubel of the NBP on April 3, 1985 to clarify some matters on the external accounts.

A number of questions related to the attached table on the balance of payments in convertible currencies that was given to the staff at the end of the previous mission. This table was said to be based on the same assumptions as version "h" of the balance of payments presented to the Paris Club earlier in the year. Key assumptions for both tables were that the Paris Club agreement rescheduling original maturities for the 1982-84 period would be signed and implemented and that Poland would receive officially backed new credits in 1984 exceeding US$1 billion.

The US$467 million in interest relief extended to Poland in 1984 represented the rescheduling of accumulated interest payments arrears due to socialist countries from 1981 to 1983. In 1984 interest payments due to socialist countries on convertible currency debt were said to have been fully paid.

It was reconfirmed that compensatory deals with Libya, Colombia, Iraq, and Yugoslavia had amounted to around US$150-200 million to date in 1984. The largest deal by far was with Libya. These arrangements did not reflect any formal agreements between Poland and the countries involved. However, exporters had been compensated with funds due to such countries.

Mrs. Rubel said that if bilateral trade within the swing limits of clearing arrangements with nonsocialist countries were netted out of the trade accounts in the tables entitled "balance of payments in convertible currencies" (e.g., Table 6 given to staff mission in February 1985) to arrive at the trade transactions that were settled in convertible currencies then one had to make a corresponding adjustment to the item "payments agreements assets and liabilities" in the capital account. It was agreed that some of classificatory problems relating to the division of the balance of payments between the convertible and nonconvertible currency areas would be pursued during the next Fund mission to Poland.

Valuation adjustments resulting from the differences between the valuation of external reserves at end-period exchange rates and the valuation of balance of payments transactions at average exchange rates during the period were included in the item "other" in the capital account. Valuation adjustments had amounted to a debit of US$100 million in 1984. The same item "other" included also amounts built up in preparation for payments due to foreign creditors. The latter had amounted to US$317 million in 1984.

The item "principal arrears to other creditors" in the attached table included unpaid amounts to banks that had been rescheduled in a particular year, but which had not been deducted from the arrears total until the operational date of the agreement; in each instance the latter date had been in the year subsequent to that in which the rescheduling agreement had been signed. Estimation of the actual amount of unpaid principal obligations to creditors outside of the Paris Club was complicated by the application of different exchange rates to arrears (end-period rates) and to the amounts of debt rescheduled. Figures provided to the staff on amounts of various reschedulings with western banks were usually valued at the same exchange rate rather than at the exchange rates at which each of the bookkeeping transactions took place. For example, at the exchange rate of January 1, 1984 reschedulings of principal maturities to western banks were as follows:

	In millions of U.S. dollars
1981	1,819 (95 percent of principal
1982	2,146 (95 percent of principal)
1983	1,160 (100 percent of principal)
1984-1987	1,629 (100 percent of principal)

Original maturities falling due in the period 1988-93 amounted to $313 million.

The Polish representatives said that they would attempt to estimate for the staff the amounts of the reschedulings at the bookkeeping exchange rates and hence, as requested, the external payments obligations for recent years with the convertible currency area subdivided into actual payments, rescheduled obligations and unpaid obligations.

The Polish representatives said that there were considerable differences between the value of external trade recorded on a customs basis and those recorded on a balance of payments basis. For export transactions there were significant lags in the receipt of proceeds on a cash basis. These lags were most pronounced for exports of construction equipment. Conversely, there were sizeable leads in payments for imports, particularly as Poland was now frequently required to effect payment before exporters would act on an import order.

L. G. Manison

cc: Mr. Hole
Mr. Prust
Ms. Swiderski
Mr. Boonekamp

Table 1. Poland: Balance of Payments in Convertible Currencies

(In millions of U.S. dollars)

	1981	1982	1983	1984	Assumptions 1985
Merchandise exports, f.o.b.	5,482	4,974	5,402	5,828	6,300
Merchandise imports, f.o.b.	6,233	4,616	4,317	4,372	4,800
Trade balance	-751	+358	+1,085	+1,456	+1,500
Receipts from services	814	577	800	735	
Payments for non-interest services	504	407	607	618	
Interest payments	2,272	1,862	1,591	1,248	2,170
Unrequired transfers, net	+654	+318	+375	+462	+500 1/
Current account balance	-2,059	-1,016	+62	+787	-170
Medium and long-term capital account	+1,333	-950	-2,218	-3,258	+170
Drawings	4,930	1,474	565	218	2,230
Repayments	1,400	268	387	243	1,960
Repayments covered by refinancing	1,778	2,150	2,329	3,059	
Principal		2,150	2,329	2,592	
Interest				467	
Exports credits extended, net	-420	-5	-69	-176	-100
Other capital, net	+1	-1	+2	+2	
Short-term capital account	-703	-14	+122	+169	+200
Revolving credits received		+196	+338	+240	
Inflow		196	878	1,180	
Outflow			540	940	
Other credits received, net	-839	-92	-260	-170	+200
Extended credits, net	-2	-18	-4	-33	
Payments agreements assets and liabilities	+74	-92	-70	+17	
Banking acccounts	+64	-8	+118	+115	
Other financial items	-446	-66	-175	-630	-100
Capital account balance	+184	-1,030	-2,271	-3,719	+270
Overall balance	-1,875	-2,046	-2,209	-2,932	+100
Refinanced maturing loans	+1,778	+2,050	+2,208	+2,938	
Change in reserves	+97	-4	+1	-6	-100
Arrears/at the end of the year/					
Of which:					
Principal	3,042	6,482	7,334	7,460	
To official creditors	670	2,527	5,095	5,862	
Others	2,372	3,955	2,239	1,598	
Interest 2/	500	1,600	2,700	4,100	
Official creditors	100	1,100	2,100	3,600	
Others	400	500	600	500	
Memorandum item:					
Transactions settled in clearing accounts					
Exports	511	430	596	504	
Imports	830	341	427	428	

Source: Provided by Polish authorities at end of staff mission in February 1985.

1/ Services and transfers.
2/ Estimates.

Office Memorandum

MEMORANDUM FOR FILES

April 8, 1985

Subject: Meeting on Banking Statistics at the National Bank of Poland

On April 4 I met with Mr. Przywecki and Mrs. Rubel and their associates at the NBP to discuss the classification of banking statistics and other matters on monetary and credit developments.

1. Monetary survey

For purposes of the monetary survey the banking system comprises the NBP, Bank Handlowy, the PKO bank, and the Bank of the Food Economy. Developments in the banking activities of around 1,500 cooperatives are included in the reported operations of the Bank of the Food Economy.

The main classification problems related to whether particular bank liabilities should be included in quasi money. It was agreed that pension funds, resources deposited in the State Fund for Occupational Activation (PFAZ), and fixed-term foreign currency deposits held by individual residents and nonresidents should be included in quasi money (in the consolidated balance sheet of the banking system and in published Polish statistics foreign currency deposits had been classified as foreign liabilities). It was agreed that foreign currency deposits on call should be included in money. Foreign exchange deposits were valued at the latest official exchange rates of the zloty vis-à-vis foreign currencies; regulations relating to their valuation and operations came under the foreign exhange law rather than under the banking law. It was agreed that deposits of insurance companies that constituted working balances or "technical reserves" should be included in money, while other deposits of insurance companies of a fixed-term nature should form part of quasi money.

It was noted that since the beginning of 1985 interest rates on investment accounts and development fund accounts had been reduced from 3 percent per annum to zero in order to encourage enterprises to deploy their funds on fixed deposit accounts which earned up to 9 percent. This would seem to suggest that investment and development fund accounts (even those classified under special fund accounts) should be classified as components of money.

It was agreed that the Polish authorities should provide as detailed as possible data on the assets and liabilities of the banking system to the staff in order that they, with the help of the Fund's Bureau of Statistics, could ascertain where each of these items could be included in the monetary survey.

Figures for the consolidated balance sheets of the banking system were prepared on a monthly basis and were available with a lag of around 28 days. Data on currency in circulation was received after a 3-day lag, while figures on the operations of the PKO bank were available after a 10-day lag.

2. Credit policy and data

A decision had been made on November 29, 1983 to convert credits used in financing the current operations of the socialized sector into fixed-term credits. Up to late 1983 socialized enterprises were said to be in the hands of the banks in the sense that the financing of 20 percent to 30 percent of their current operations was dependent on the continuous availment of bank credits. It had been initially proposed that such credits be converted into budgetary financing. However, budgetary resources were insufficient and outstanding working capital credits to the more financially viable enterprises were converted into fixed-term credits of up to 12 years. Such credits were to be repaid in annual installments from development resources and on average were extended for seven years. The decision to convert operational credits into long-term credits was put into practice during the first quarter of 1984. Less creditworthy enterprises were extended special one-year credits to help build up their inventories. Partly as a result of these extraordinary credits enterprise stocks were estimated to be equivalent to those necessary for 56 days production at the end of 1984 compared with 30 days at end-1982. Of the total of around Zl 2,200 billion in bank credits for working capital outstanding at end-1984, Zl 320 billion or 14 percent represented converted credits, while a further Zl 592 billion or 27 percent were the aforementioned one-year credits. Around 50 percent of the latter credits were extended to domestic trade enterprises.

On the question of whether the item "new credits to the state budget" in the consolidated balance sheet could be decomposed it was said that the only division was between credits extended to finance the budget during the budget year and those extended for financing of the operations pertaining to the same budget in the initial days of the following fiscal year.

3. Seasonality of credit demand

In the beginning months of the calendar year the demand for credit was usually quite low as stocks of agricultural goods were being run down and construction activity was minimal. With the subsequent pick-up of mining and construction activity there was a rise in credit demand in the second quarter. The seasonal needs for credit usually reached a peak in the July-August period as stocks of agricultural commodities, particularly grains, required considerable financing. With very good harvests such financing could extend through to the winter months.

4. Bank profitability and interest rate subsidies

The failure of a number of Polish banks to be profitable was said to be a concern of the authorities. Banks were required for social reasons to lend to certain sectors (housing, agriculture, mining, etc.) at very low interest rates. The average interest rate on loans to the agricultural sector was around 6 percent, while investment credits to the mining sector carried on annual interest charge of 3 percent. Due to an increasing amount of term deposits the banks' costs of obtaining funds were increasing. In 1984 the average rate of interest on bank deposits was estimated to be 8.7 percent. In contrast, the average interest rates on working and fixed capital credits were 7 percent and 5 percent, respectively, in 1984. This situation resulted in banks being provided with interest rate subsidies from the budget. For example, for loans to the agricultural sector banks received subsidies equivalent to 6 percentage points on such loans; that is, the difference between the 6 percent charged by the banks and the 12 percent basic loan rate.

The lack of profitability of banks was attributable also to factors other than low loan rates of interest. Bank management and employees seemed to give insufficient attention to the return on bank loans and consideration was being given to making compensation of bank employees more sensitive to the financial position of banks.

L G Manison

L. G. Manison

cc: Mr. Hole
Mr. Prust
Ms. Swiderski
Mr. Boonekamp

INTERNATIONAL MONETARY FUND

Poland--Staff Visit

Minutes of a Meeting
Held at ZWAR
on Thursday, April 4, 1985 at 9:30 a.m.

Polish Representatives	Fund Representatives
ZWAR (Zaklady Wytworcze Aparatury Wysokiego Napiecia) Representatives	Mr. Hole Mr. Prust Ms. Swiderski

Mr. Marian Mikolajczyk, Director General
Mr. Roman Skrocki, Director, Production
Mr. Bronislaw Barylski, Vice-Director, Technical Matters

ZWAR is a socialized enterprise, founded in 1918, that specializes in the production of high voltage electrical equipment. It employs 5,300 workers and has six plants in operation (three in the Warsaw area). During the economic downturn of 1981-82, ZWAR was able to maintain its overall level of production, but stopped the production of certain specialized products due to a lack of demand. During the downturn, its workforce was reduced by 1,200 persons. Since then the situation has reversed itself and ZWAR is only able to service one half of its domestic orders.

ZWAR exports 40 percent of its production to the West, mainly to developing counties such as Iraq, Egypt, and Sudan. In the Eastern bloc its principal trading partner is the Soviet Union. Export activity is handled by the foreign trade organization "Electrym" on ZWAR's own account. Its quota for the foreign exchange retention scheme is 30 percent. Because Electrym's role is limited to an agency one, it has no claims on the foreign exchange earned. The claim is based on actual cash receipts rather than the invoiced amount of sales. ZWAR has not had difficulty in acquiring access to its foreign exchange claims, although delays have frequently been experienced. About 15 percent of acquired foreign exchange is used to service the needs of subcontractors. The retention scheme has been insufficient to meet their import requirements because of the high import content of products made for the domestic market. The needs of the domestic market are easily estimated as they are based on forecasts for the energy balance which extend through the year 2000. There is little substitutability, however, between the domestic and export-related products because of the specialized nature of contracts in the latter market. Most of the foreign contracts run over several years. Exports are more profitable than domestic sales, largely due to the limits set on domestic prices. While exports account for 43 percent of sales, their contribution to the profit share is 54 percent. The main incentive for exporting is the tax break received on profit tax payments. The reduction is a function of both (1) the increase in exports (at a constant exchange rate) from the previous year and (2) the value of exports multiplied by a coefficient which has ranged between 3 and 5 percent. Last year ZWAR paid an effective profit tax rate of 33 percent compared to the normal rate of 60 percent. The exchange rate has played a smaller role in motivating export sales as a result of the specialized nature of export contracts. There is no penalty tax for earning higher profits on foreign orders compared with domestic orders. Certain foreign orders are subsidized. Export credits are guaranteed by the Bank Handlowy. The external debt crisis, however, has reduced the amount of export credits extended to a minimum (a recent contract with Sudan valued at US$10 million fell through as a result of the unavailability of export credits). The most recent large export contract has been with Egypt, which was signed in 1983 and is expected to be operational for another two years. The largest obstacle to export growth has been the introduction of technology on a timely basis. In this regard, ZWAR is participating in several joint ventures with other domestic companies in the fields of research and development. These ventures have required little hard currency.

The reforms have provided ZWAR with managerial and financial autonomy in decision making. Prior to 1981 the main goal of the company was to fulfill plan targets. Since then the plan has become of secondary importance, with the enterprise's own plans taking precedence. The company's plans must have the approval of the Workers' Self-Council. Due to ZWAR's relative importance in the economy, its own plans are submitted to the Planning Commission as a basic input for the formulation of the economy-wide plan. ZWAR is not a party to any government contracts; however, input requirements are supplied by the Ministry of Supplies. Although there have been occasional delays in delivery, the company has not been affected by the shortage of inputs.

ZWAR is subject to FAZ payments, but has received preferential treatment in several respects. Its threshold for tax exempt wage increases is 6 percent and its preferential coefficient--relating productivity increases to tax exempt wage increases--is 0.8 (compared to a normal one of 0.5). The measure of output used in calculating FAZ is <u>gross</u> sales at constant prices, instead of the conventional principle of using <u>net</u>

sales. The justification for using gross sales is that it is an easier measure to regulate across six plants. Measuring gross sales at constant prices does not pose any difficulties; current contracts are priced at the previous year's prices. For new products, which over a period of one year are not normally markedly different from the more established lines, the previous year's prices are used as the benchmark with adjustments being made to quality improvements. The company's accounting treatment of FAZ is verified annually by accountants contracted by the Treasury.

A new system of pay--designed internally--has just been approved within the company. It is in the process of seeking final approval for its implementation from the Minister of Labor, Wages, and Social Affairs. The principles governing the new system of pay will not be markedly different from the existing one. The main difference will be that the entire pay scale will be higher in order to increase the relative importance of wage payments in overall remunerations. With the freezing of basic wages since 1982, bonus payments have increasingly become the dominant source of remunerations.

The company does not expect that the introduction of the new wage system will significantly increase its opportunities to attract labor resources. This is because of the lack of available housing in the area. In an attempt to deal with this problem ZWAR has constructed several housing settlements around its plants, with the majority being set up as cooperatives and only a few being fully owned by the company. On leaving the company, the worker is not obliged to sell his share of the cooperative. When purchasing a share in the cooperative, the workers are eligible to receive financial assistance from the Social Fund. ZWAR has also developed two holiday facilities, one in the Tatry mountains and another on the Baltic Coast. Sixty percent of social projects are financed with own resources, the remainder with credit. The legally required distribution to the Housing Fund is Zl 2,700/worker per annum. The company, however, makes additional allocations from its profits.

Investment outlays over the last several years have been mainly directed to the replacement and modernization of the existing capital stock. The feasiblity of investment projects are evaluated by a team of specialists employed by ZWAR. For the project to become operational, it must have the approval of the Workers' Self-Council. Due to credit limitations, the majority of projects are financed with internally-generated resources. This, however, is supplemented by funds obtained from the Central Development Fund which is managed by the Ministry of Power. The latter funds are required to be repaid at the stipulated (often subsidized) interest rate.

The meeting adjourned at 11:00 a.m.

Office Memorandum

April 8, 1985

MEMORANDUM FOR FILES

Subject: Poland

In a private discussion with Mr. Karcz, I was told that the outcome of the visit of the German Government delegation had been less positive than the *Financial Times*' article had suggested. True, it constituted an important step forward and the right sentiments had been voiced. But the Germans had in mind new credits of no more than DM 100 million, against the Poles' request of DM 450 million, and for this reason the Poles had encouraged the Germans not to quantify their intentions in speaking to the press. Bangemann and Genscher were throught to be sympathetic. Kohl's meeting with Jaruzelski at the Chernenko funeral had gone very well on political issues. Stoltenberg was very cool.

Italy and Austria were also making sympathetic noises about new credits, but Britain remained negative. Discussions with the French are scheduled for mid-April.

The early March Paris Club meeting had been surprisingly turbulent with the Germans standing firm on technical issues which Karcz had wanted to discuss bilaterally.

Karcz anticipates two or three more Paris Club sessions before the 1982-84 and 1985 restructurings can be wrapped up.

Peter Hole

cc: Mr. Whittome

Office Memorandum

MEMORANDUM FOR FILES April 18, 1985

Subject: Poland--Translation of the 1985 Budget Document

The translation is not completely literal and minor points have been omitted. The numbering follows the Polish version. This document is not the "Budget Law" document (i.e., the law referring to institutional and procedural matters) referred to on the mission. The latter was not given to us.

Karen A. Swiderski

K. Swiderski

Attachment

cc: Mr. Hole
Mr. Manison
Mr. Prust
Mr. Boonekamp

The Budget for 1985 as of December 28, 1984

Article 1: State budget		(In billions of zloty)
1.	Revenues of the state budget	
	Total revenues	3,692.8
	Of which from:	
1)	Enterprises and other units of the socialized sector	2,947.4
2)	Financial and insurance institutions	39.5
3)	Social security contributions	364.4
4)	Units rendering social and cultural services	22.5
5)	Administrative units	23.6
6)	Nonsocialized sector	83.9
7)	Household sector	58.4
8)	Other revenue	65.1
9)	FAZ	57.0
10)	Other revenues which are not classified	30.9
2.	Expenditure of the state budget	
	Total expenditure	3,980.6
	Of which for:	
1)	Financing of enterprises and other economic units	1,529.9
2)	Science	31.3
3)	Education	375.1
4)	Culture	55.7
5)	Health services, tourism, recreation, and sport	418.5
6)	Social welfare	343.5
7)	National defense	288.8
8)	State administration and justice	200.4
9)	Miscellaneous current expenditure	111.9
10)	Earmarked expenditure not classified by branch or voivodship	56.1
11)	Investment and capital renovations	539.5
12)	Reserves for Council of Ministers	30.0
	Unadjusted deficit	287.8
3.	Reduction in deficit resulting from changes in procurement and retail prices	149.8

4. Adjusted state budget deficit 138.0

5. The adjusted state budget deficit in line 4 will be covered by bank credit.

6. If it is apparent that the state deficit of line 4 will be exceeded, the Council of Ministers has the authority to take measures to increase revenues or to introduce programs entailing cost reductions. In this regard, the Council of Ministers is authorized to change the amount of subsidies directed to the local authorities.

7. Revenues of budgetary and extra budgetary entities (whose operations are based on article 13 of the Budget Law—No. 53—of December 31, 1984), which are under the jurisdiction of the state budget, wil equal Zl 1,495.9 billion of which Zl 305.6 will stem from budget subsidies. Their expenditure will equal Zl 1,342.1 billion, of which Zl 58.7 billion amounts to the surplus tranferred to the budget.

Article 2: Central Budget

1. Central budgetary revenues............Zl 3,349.1 billion

   Central budgetary expenditure.........Zl 3,636.9 billion

   Of which:

   Reserves of the Council of Ministers....Zl 30 billion

2. Revenues of budgetary and extrabudgetary entities (whose operations are based on article 13 of the Budget Law), which are under the jurisdiction of the central budget, will equal Zl 1,206.3 billion of which Zl 211.2 billion will stem from

budget subsidies. Their expenditure will amount to Zl 1,040.7 billion of which Zl 58.3 billion amounts to the surplus transferred to the budget.

Article 3: Budgets of the Voivodships

Budgetary tranfers to voivodships

1) Resulting from the participation of the voivodships in the revenues of the central budget. This is calculated in proportion to the share of retail sales of goods and services by socialized entities which are covered by the central and local plans............ Zl 355.8 billion

2) Subsidies of a general nature............ Zl 120.1 billion

Article 4: Subsidies to State Enterprises and Cooperatives

1. Objective subsidies for state enterprises and cooperatives for the purpose of financing the production of specific goods and for specific services rendered will amount to Zl 689.8 billion

2. The subsidies described in #1 can be increased by the Council of Ministers within the limits established for the level of overall expenditure in this document.

3. The Council of Ministers will list the specific group of goods and services subsidized by the budget.

4. The Minister of Finance will establish the subsidy rates discussed in #3. He is also empowered to change commodity distribution of subsidies in the relevant sections of the budget within the limits established in #1.

Article 7: Subsidies for Repayment of Bank Credits of Investment Projects

The Council of Ministers shall establish the maximum amount of subsidies that can be used for repayment of bank credits that were used to finance central or enterprise investments and which the enterprises could not afford to finance.

Article 8: Subsidies

1. The size of subjective subsidies (those subsidies which relate to an enterprise as a whole) to state enterprises will be reduced by the amount of resources in the reserve funds as of December 31, 1984.
2. In determining the size of objective subsidies and those used for the repayment of bank credits (Art. 7), the Minister of Finance may grant permission to use the resources in the enterprises' reserve funds for financing the above needs. The amount used from the reserve funds, however, cannot exceed 50 percent of the value of resources in the fund on December 31, 1984.

Article 9: Deposit Requirement Scheme on Building Investments

1. Enterprises undertaking investments in building construction will be subject to an obligatory deposit.
2. The following exceptions to #1 hold:
   1) investments in the areas of
      a) health care - as specified by the Minister of Health and Social Welfare
      b) Protection of the environment - as specified by the Director of the Institute for the Protection of the Environment and Water Economy.

c) improvement in the work environment - as specified by the Minister of Labor, Wages, and Social Affairs.

2) housing investments as well as investments in infrastructure for developments.

3) investments associated with the construction of storage space, bakeries, trade and service establishments, foodstuffs industry, ports.

4) investment related to the construction of central telephone establishments as well as investments related to renovating train repair establishments.

5) investments which provide income tax payments reliefs.

6) part of the investments financed by "target" funds (?) whose only source of resources are funds from the population.

7) investments financed in part by budget subsidies.

3. The Council of Ministers is empowered to add on to the list in #2 as well as to rescind any on the exemptions granted if the investments projects are not carried through as planned.

4. The normal deposit requirement is 50 percent of construction outlays. The preferential rate is 20 percent. Investments eligible for the preferential rate are determined by the Chairman of the Planning Commission in agreement with the Council of Ministers.

5. Funds for the deposit scheme are to be obtained from the Development Fund with the exception mentioned in #6 below.

6. Social investments financed by the Social Fund and funds from other than the Development Fund require the deposit to be financed from the Social Fund.

7. No interest is paid on the compulsory deposit against building investments.

8. In general, the bank must return the deposit to the enterprise three months after the completion of the project.

9. The main criteria for determining if the deposit is to be returned are: 1) a) timely completion of the project and b) timely achievement of targeted output and 2) other arrangements stipulated in the contract.

10. In cases where the deposit is not returned to the enterprise it is transferred to either the central budget or the voivodship budget depending on the founding body of the enterprise.

11. The decision on withholding the deposit is made by the relevant Treasury Chamber within two weeks of receiving a statement from the bank that the enterprise has not fulfilled its obligations. The enterprise can appeal to the Ministry of Finance within the two weeks following the decision.

12. The bank will transfer the withheld deposit to the relevant budget three weeks after the final decision is made.

Article 10

State enterprises can use resources from their Development Fund to finance investments of other enterprises when the latter undertake project that will in some way benefit the former. This transfer can take the form or either a loan or a grant. The regulations on such a transfer (interest rate charged, etc.) should be outlined in a contract between the interested parties.

Article 12

1. Transfers of fixed capital between enterprises will take place at agreed prices (which cannot be higher than purchase prices) taking into account additional investment outlays and amortization charges.
2. If the fixed capital stock was acquired free of charge then the transfer must be carried out without cash payment, adjusted for additional investment outlays and amortization charges.

Article 13

The profits of the National Bank of Poland in 1985 will not replenish the statutory or the reserve fund of the NBP (meaning unclear ?).

Article 14

(1) The rate of profit tax is to be increased by 5 percentage points.

(2) Excluded from the increase are:

(a) units of the socialized sector that are exempted from the profit tax

(b) PKP and PKS

(c) cooperatives for the disabled

(d) dairy cooperatives and their establishments

(e) enterprises where over 90 percent of their output is devoted to a list of goods and services that are exempted from this increase (e.g., certain vital services).

(3) Social entities in foreign trade (I believe the foreign trade organizations) are subject to a 75 percent profit tax. This rate may be reduced by up to 8 percentage points provided that the funds from the reduction will be placed in the banking system for use by the Minister of Foreign Trade--in agreement with the Finance Minister--for investments associated with export development.