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EBS/90/205

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December 5, 1990

To: Members of the Executive Board

From: The Secretary

Subject: Poland - Stand-By Arrangement - Request for Waiver and Modification of Performance Criteria

Attached for consideration by the Executive Directors is a paper on Poland's request for a waiver and modification of performance criteria under its stand-by arrangement. A draft decision appears on pages 13 and 14.

It is understood that the Executive Director for Poland will be requesting the Board for a waiver of the circulation period, to enable this subject to be brought to the agenda for discussion on Friday, December 21, 1990.

Mr. Hole (ext. 8979) or Mr. Burton (ext. 6531) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

POLAND

Stand-By Arrangement--Request for Waiver and Modification of Performance Criteria

Prepared by the European Department and the Exchange and Trade Relations Department

(In consultation with other departments)

Approved by Massimo Russo and J.T. Boorman

December 4, 1990

I. Introduction

The second review under Poland's stand-by arrangement with the Fund was completed by the Executive Board on September 10, 1990 (EBS/90/153 and Supplement 1); following the completion of the review, a third purchase of SDR 93.75 million under the arrangement was made on September 14 (Table 1). 1/ At the time of the second review it was already noted that wages were increasing faster during the third quarter of 1990 than targeted under the program. In the event, the limit on the increase in enterprise wage bills during the period July to September 1990 was exceeded (Table 2), triggering a consultation with the Fund on the situation and economic policies and on the circumstances under which purchases may be resumed. The limit on the increase in net domestic assets during the third quarter of 1990 was also exceeded. All other performance criteria for the period July to September 1990 were met.

Discussions with the Polish authorities concerning a waiver for nonobservance of the above mentioned performance criteria and for modification of performance criteria for the period October to December were held in Warsaw during October 9-18 and November 8-17, 1990. 2/ The

1/ The 13-month stand-by arrangement in the amount of SDR 545 million (80.1 percent of quota) was approved by the Executive Board at EBM/90/15 on February 5, 1990 (EBS/90/3 and EBS/90/11). Poland made a first purchase of SDR 170 million, representing the first credit tranche, following approval of the arrangement and a second purchase of SDR 93.75 million, following a first review under the arrangement at EBM/90/74 (5/14/90).

2/ Discussions were also initiated on a possible arrangement under the Extended Fund Facility. The staff team comprised Messrs. Hole (EUR), Allen (Senior Resident Representative), Burton (ETR), Hemming (FAD), Banerjee (EUR), Lane (RES), Ossowski (Resident Representative), and as administrative assistant Ms. Maragh-Burough (TRE) for the first mission and Ms. Earll (EUR) for the second. Mr. Basiuk (Advisor to the Executive Director for Poland) participated in the first set of discussions as an observer.

policies and measures formulated by the authorities, which are described in the attached letter from the Deputy Prime Minister and Minister of Finance and the President of the National Bank to the Managing Director, include measures to bring about a substantial tightening of credit during the remainder of 1990 and increases in interest rates to help contain wage and price pressures. Moreover, the deficit of the core general government during the fourth quarter is to be limited to less than the amount allowed under the existing program.

The next purchase under the arrangement of SDR 93.75 million is subject to approval of the waiver for nonobservance of performance criteria for the third quarter of 1990. The final purchase, also of SDR 93.75 million, is subject to compliance with performance criteria, which it is proposed be modified, for end-December 1990. Fund holdings of zlotys currently amount to 152.6 percent of Poland's quota.

II. Performance Under the Arrangement 1/

The program upon which the Polish Government embarked at the start of this year was designed to bring about a rapid and lasting reduction in inflation and to begin a fundamental transformation of the economic system by moving progressively but comprehensively to market mechanisms. The maintenance of a fixed exchange rate, following an initial devaluation, and a restrictive wage policy were to provide nominal anchors to break the momentum of inflation. These anchors were to be supported by the elimination of the large fiscal deficit and a tight credit policy. At the same time, the economy was to be restructured through a radical program of structural reforms. Steps taken at the start of the arrangement included a major liberalization of the exchange and trade system and the freeing of most prices.

During the first half of 1990, financial policies were generally tighter than envisaged and wage policy was effective in dampening the response of wages to prices. Progress was also made with structural reforms, although the preparatory work in several areas, including privatization of State-owned enterprises, proved to be more time consuming than anticipated. Against this background, the rate of inflation was brought down sharply, shortages were largely eliminated, and the balance of payments strengthened markedly, despite the opening up of the economy. Output, however, fell more sharply than anticipated when the program was formulated (Tables 3 and 4).

In light of these developments, the authorities introduced in midyear some modifications to the balance of economic policies that combined a selective easing of demand restraint and an acceleration of supply-side reform. The objective was to lend some support to economic activity while continuing to reduce inflation. It was recognized that

1/ Developments during the first half of the year are reviewed in more detail in EBS/90/153 (8/21/90) and Supplement 1 (9/6/90).

the relaxation of demand management carried some risks. In the event, there have been some signs of a modest recovery of production in recent months, but at the same time both credit and wages have increased more rapidly than programmed, and the inflation rate, after declining through August, has picked up markedly. The balance of payments position continued to be stronger than expected during the third quarter, but more recently has shown signs of weakening.

1. Financial policies

The fiscal accounts were substantially stronger during the first half of 1990 than anticipated, and the program for the second half year allowed for some easing of fiscal policy, targeting a general government deficit of close to 1 percent of annual GDP during July to December; for the year as a whole, this still implied a general government surplus of some 2 percent of GDP. Despite the intended relaxation of fiscal policy, however, the core general government is estimated to have been in surplus by about Zl 9.3 trillion (1 1/2 percent of annual GDP) during the third quarter, reflecting continued expenditure restraint, strong financial performance by the extrabudgetary funds and local governments, and the persistence of buoyancy in income tax revenues from the enterprise sector. Accordingly, credit to the general government fell by Zl 7.0 trillion during the period July to September, as against an increase of Zl 4.3 trillion allowed under the program.

With regard to monetary policy, the increase in net domestic assets of the banking system remained well within the program limit during the first half of the year. At the same time, because inflation was substantially higher than originally projected, broad money in real terms declined more sharply than envisaged. After picking up in the second quarter, the pace of expansion of credit to the nongovernment sector remained rapid in the third quarter. Preferential credit to agriculture and housing rose particularly sharply, as did credit to the private sector in the wake of a cut in interest rates to the equivalent of about 2 1/2 percent per month on July 1. 1/ Steps were taken in late August and September to restrain credit growth, including the tightening by the National Bank of its refinance policy, an increase in reserve requirements, and the introduction of a freeze on nonpreferential lending to the socialized sector by State-owned banks. However, these actions had only a limited impact on credit growth and the net domestic assets of the banking system increased by Zl 18.8 trillion during July to September compared with Zl 14.2 trillion in the program (Table 6). With a continued injection of liquidity from the balance of payments in the third quarter, broad money rose by 24 percent, an increase of nearly 13 percent in real terms, concentrated in the enterprise sector; the program had envisaged an increase in real broad money of about 4 percent over this period. While the higher increase in real balances may to

1/ The monthly refinance rate of the National Bank had previously been lowered progressively from 36 percent in January to 4 percent in June, in line with the decline in inflation.

some extent have reflected a faster remonetization of the economy and stronger growth in the demand for money than anticipated, it also contributed to an upturn in inflationary pressures in September and October. Credit expansion continued at a relatively fast pace in October, with preliminary data indicating that net domestic assets increased by about Zl 6 trillion.

3. Wages and prices

Under the Government's wage policy, the excess of enterprise wage bills in any month over a norm (which is adjusted each month by a stipulated fraction of the inflation rate for that month), has been subject to high and progressive taxation. During the first half of the year, this approach, combined with tight financial policies, was effective in containing wages: enterprise wage bills (excluding premia from profits) increased by only 29 percent, less than allowed under the norm, and average wages declined by 48 percent in real terms, or more sharply than anticipated. 1/ Under the wage policy, however, enterprises were allowed to carry forward the unutilized accumulated margin under the norm, creating the potential for large wage increases in the second half of 1990.

Given the decline in real wages in the first half year, the unutilized margin under the norm, and certain modifications to the wage policy introduced in midyear, 2/ the authorities expected some increase in real wages in the second half; enterprise wage bills were projected to grow by 12-14 percent during the third quarter and 15-17 percent during the fourth quarter of 1990. In the event, however, the wage bill rose by 26 percent during July to September, well in excess of the program limit of 14 percent. This overrun reflected a larger utilization of the margin under the norm than anticipated as well as a marked increase in wage awards over and beyond the accumulated margin, and was facilitated by the rapid expansion of bank credit during the third quarter. Preliminary data for October indicate that wage increases have subsequently remained rapid, with the wage bill of enterprises rising by a further 11.7 percent. Official estimates now suggest that full utilization of the remaining margin under the norm, together with the

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1/ The effective decline in real incomes was probably smaller given that prior to the reforms goods were often unavailable at official prices and that during 1990 goods have been available at lower--and largely unmonitored--prices in street markets.

2/ The modifications to wage policy included an increase, for some groups, in the base on which tax-free wages are computed, and a reduction in the progressivity of the excess wage tax to allow greater flexibility in the wage structure. In addition, enterprises were allowed to pass through price increases in July fully to wages because of the importance of administered price increases in that month; the tax-free index coefficient reverted to 60 percent for the rest of the year.

payment of sizable traditional seasonal bonuses in December, could result in an increase in the wage bill of over 30 percent during the fourth quarter.

Following a sharp jump in January 1990 caused by the devaluation of the zloty and the liberalization of prices, the monthly rate of inflation remained above the targeted path during the first half of the year but declined progressively from nearly 80 percent in January to 3 1/2 percent in June. There was little change in the monthly inflation rate in July despite sizeable adjustments to administered prices, including the price for coal, and subsequently inflation declined to 1.8 percent in August, partly reflecting a seasonal decline in food prices.

Since August, inflation performance has been adversely affected by the increase in world oil prices and a decline in oil supplies from the Soviet Union at prices well below world levels. The higher cost of oil imports was fully passed through to domestic crude oil prices, which were increased by 83 percent on September 1 and by a further 55 percent on October 5, 1990. To cushion the impact on consumers, however, the ad valorem turnover tax on petroleum was turned into a specific tax leaving the nominal tax unchanged, and retail price increases for petroleum products were in the range of 32 to 54 percent. The authorities estimate that these increases will raise the consumer price index, taking into account indirect as well as direct effects, by some 4-5 percent during September to December 1990. Inflation, however, accelerated to 4.6 percent in September alone and further to 5.7 percent in October reflecting the rapid increase in wages. The authorities are now projecting that, even with the intended tightening of financial policies (see below), consumer prices will increase by about 13 1/2 percent during the fourth quarter of 1990; of this, perhaps some 9-10 percentage points would represent "underlying" inflation.

4. Structural policies

The program of structural reforms is proceeding as described in EBS/90/153. Concerning privatization, a first group of seven large enterprises has been prepared for privatization and public share offerings for five of them are to begin in November; one enterprise is to be privatized by outright sale to a foreign company and another through a leveraged buyout by management and workers. Two further groups of enterprises are under preparation and should be privatized in early 1991. For 1991 as a whole, the authorities currently hope to privatize enterprises accounting for 15 percent of state-owned assets. Progress has also been made in strengthening competition, especially in the retail sector, where it is expected that 70 percent of stores will have been transferred to private management through leasing arrangements by end-year. Other areas where demonopolization is proceeding include road haulage, where 60 percent of the trucks previously operated by state-owned enterprises have been privatized, the grain processing sector, and the insurance industry. Regarding trade system reform, all remaining export quotas except those imposed as a result of agreements with third countries were removed in October.

Modernization and reform of the banking system and of the available instruments of monetary control is also proceeding steadily. In particular, preparatory work is nearing completion for improving the domestic payments system, evaluating the condition of banks' balance sheets, and implementing a system of bank supervision based on clearly specified prudential regulations. In addition, an interbank market is being developed and experience is being gained in the area of liquidity management through weekly auctions of National Bank bills to banks and enterprises. Similarly, administrative preparations are proceeding ahead of major changes in the tax system, notably the introduction of value-added tax from July 1, 1991 and a personal income tax from January 1, 1992.

5. External sector developments

Contrary to expectations, there was a marked improvement in the balance of payments in convertible currencies in the first half of the year following the liberalization of the exchange and trade systems; the current account (including interest commitments) swung from a deficit of \$0.8 billion in the first half of 1989 to a surplus of \$1.1 billion as exports increased markedly and imports declined. Exports continued to grow rapidly during July to September, rising by about 10 percent from the level in the previous quarter. At the same time, with the strengthening of the economy and the relaxation of financial policies, imports increased by 36 percent. Given the relatively low initial level of imports, however, there was only a small decline in the trade surplus, to US\$0.9 billion, and the current account in convertible currencies recorded a surplus of \$0.7 billion in the third quarter. Together with the rescheduling of all pre-cutoff date debt payments to the Paris Club and the limited payments made to other creditors, this resulted in an increase in net international reserves during July to September of \$1.6 billion 1/ (the bulk of which was added to official reserves), taking the increase for the first three quarters of 1990 to \$4.8 billion (Table 7).

Preliminary data indicate that in October imports rose by about 75 percent over their level in the previous month, an increase that was only partly offset by a sizeable increase in exports, with the result that the trade surplus was largely eliminated in that month. While these developments are not yet fully understood, it appears that the jump in imports reflected two main factors: some bunching of oil payments at the much higher international price, and some shift of imports

1/ Valued at the cross exchange rates of January 1, 1990 (as specified in the program), the increase in net international reserves amounted to US\$1,488 million. This compared with a minimum target increase under the program of US\$800 million (Table 2).

from unofficial (unrecorded) to official (recorded) channels following the introduction of visa requirements for Polish citizens by two neighboring countries. Part of the growth in exports, likewise, may have reflected a structural shift from unofficial to official channels.

For the fourth quarter as a whole, expectations are that merchandise trade could be in surplus by about US$150 million and that the current account could shift into a deficit of some US$350 million. On this basis, and after allowing both for new credit inflows and limited servicing of the external debt, there would be a further increase in net international reserves of about US$450 million (or an estimated US$400 million valued at the cross exchange rates of January 1, 1990). This would bring the reserve increase for the year as a whole to more than US$5 billion.

There was a marked strengthening of the balance of payments in nonconvertible currencies in the first half of 1990, largely on account of a sharp fall in imports from the CMEA area in the wake of the drop in domestic demand in Poland and supply difficulties in neighboring countries, particularly the U.S.S.R. Including balances under bilateral clearing agreements, the nonconvertible current account surplus increased to the equivalent of US$1.0 billion from US$0.1 billion in the first half of 1989 (Table 8). Since midyear, a sizable surplus has continued to be recorded on trade denominated in transferable rubles, while trade under bilateral clearing agreements (most importantly with the Soviet Union) has been in approximate balance. As a result, the current account surplus in nonconvertible currencies slackened to the equivalent of US$0.3 billion in the four-month period July-October. This brought the total surplus for the first ten months of the year to the equivalent of about US$1.3 billion, or somewhat less than the current account surplus (US$1.7 billion) with the convertible currency area.

The continuation of inflation at rates higher than programmed since midyear has led to an appreciation in the real effective exchange rate, but this has been limited by the depreciation of the U.S. dollar against major currencies. Measured in terms of relative prices, the real effective rate is estimated by the staff to have been 15 percent higher in September 1990 than in November-December 1989; in terms of relative wages, on the other hand, it remained some 25 percent lower (Table 3). According to the authorities, there have been virtually no complaints from enterprises about a loss of competitiveness, and the continued strong performance of exports would suggest that the competitive position remains adequate.

In the period since the second review under the stand-by arrangement in September, further discussions have taken place between the authorities and the steering committee of commercial banks on Poland's debt and debt servicing obligations to the banks. Little additional progress has, however, been made on the three central issues, viz., the Government's request for market-based debt and debt service reduction;

mounting interest arrears to the banks (following the rescheduling of all debt service due in 1990 to the Paris Club on post cutoff date debt, no interest payments have been made this year on medium- and long-term debt to the banks); and revival of a short-term trade financing facility (which is currently in suspense, but on which interest service has continued to be paid). While both parties have affirmed their desire for a speedy resolution of matters, a further temporary build-up in interest arrears seems likely in the period immediately ahead, with an eventual solution likely to await progress in the parallel discussions with other external creditors. In the latter connection, the President of the United States has recently expressed his willingness to reduce Poland's debt and debt service obligations to the United States, provided that this can be accomplished in an agreed multilateral context, and has stated that the U.S. Administration will be working vigorously to achieve this multilateral consensus within the next few months.

With effect from August 7, 1990, Poland imposed exchange and trade sanctions, including a ban on trade, with Iraq and Kuwait pursuant to United Nations Resolution 661 (1990). 1/ The exchange restrictions involved were notified to the Fund on September 11, 1990, and are approved in accordance with Decision No. 144 (52/51).

6. Output and employment

Whereas agricultural production held up reasonably well and measured (nonagricultural) private sector activity is estimated to have risen by 35 percent during the first half of 1990, production in the socialized sector (measured by the volume of sales) fell by close to 30 percent. The fall was concentrated in the first two months of the year and output was broadly unchanged during April to June. More recently there have been signs of a recovery in activity, with sold production of the socialized sector increasing by about 8 percent in both August and September over the previous month. Moreover, the harvest appears to have been a good one and indications are that the private sector, while remaining small, continues to expand apace. Employment, however, has fallen steadily, lagging the fall in output, with registered unemployment rising from negligible levels at the beginning of the year to over 1 million (7.5 percent of the nonagricultural labor force) at end-October.

1/ Exports earmarked for medical use and food supplied for humanitarian reasons are exempted.

III. Revised Program for the Fourth Quarter of 1990

In light of growing fears that the recent rapid expansion in credit and wages could undermine the progress achieved in lowering inflation and eventually jeopardize the present exchange rate peg, the authorities have taken a number of measures designed to reverse the buildup of inflationary pressures. Because of the difficulty, in the present political circumstances, of changing the announced wage policy for the remainder of the year, reliance has had to be placed primarily on a tightening of credit and interest rate policies.

To curb the demand for credit and also to signal a firm commitment to reduce inflation, the refinance rate of the National Bank was raised from the equivalent of 2.5 percent month to 3.5 percent in October and further to 4.4 percent with effect from November 21, making it positive in real terms in relation to the inflation rate projected for the remainder of the year; 1/ the rediscount rate has been raised by a corresponding amount. In order to strengthen the impact of these adjustments on the deposit and lending rates of banks, from November 21 the restriction limiting the lending rates of State-owned banks to no more than 2 percentage points above the refinance rate has been removed, and State-owned banks have been instructed to set interest rates on six-month deposits at the same level as the prime lending rate.

The rate of credit expansion is also to be reduced more directly (see below). While the surge in credit in the third quarter and the recent increases in domestic oil prices would now make adherence to the original credit program for the second half as a whole unduly restrictive, a tightening of credit policy is regarded as essential to reduce the capacity of enterprises to grant large wage increases and to prevent the present level of inflation from becoming entrenched. The revised financial program has thus been formulated to achieve a decline in the stock of real broad money during the fourth quarter and to limit the growth in real money over the second half as a whole approximately to the rate envisaged on the occasion of the mid-year review (Table 6). While this would imply a significantly larger increase in broad money in nominal terms during the second half than envisaged earlier, the increase during the fourth quarter would be only slightly higher than targeted in the existing program. On this basis, and taking into account the projected increase in net international reserves, the revised credit program allows for an increase in net domestic assets of the banking system of Zl 15 trillion between end-September and end-December.

To help contain credit within the overall limit and to provide room for credit to the nongovernment sector, borrowing by the general government from the banking system is to be limited during the fourth quarter to Zl 3.7 trillion, substantially less than the Zl 14.0 trillion

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1/ Prices are projected to rise by 3.5-4.0 percent a month in November-December.

implicitly allowed under the existing program. This is consistent with a core general government surplus for the second half cf 1990 of Zl 5.2 trillion (a deficit of Zl 6.3 trillion was originally targeted) which is believed to be attainable on the basis of recent revenue trends and with continued firm control over expenditures. For the year as a whole, total general government is now forecast to be in surplus by some 4 percent of GDP. At root have been several factors, but particularly a substantial reduction in real terms in State budget expenditure and an unexpectedly large--and probably nonrecurrent--surplus in the extra-budgetary funds, especially the social insurance funds (which in turn has permitted a reduction in transfers from the State budget to the funds). The projected fiscal outturn amounts to substantial overperformance in relation to the original program target of approximate balance and constitutes a major turnaround from the deficit of 7 1/2 percent of GDP recorded in 1989 (Table 5).

Even with the containment of credit to the government sector in the fourth quarter, the revised limit for net domestic assets leaves only limited room for credit to the nongovernment sector during the last two months of the year, given the credit expansion that took place in October. To ensure that the increase in credit to the nongovernment sector is held within the available amount, the authorities have taken the following measures:

--state and state-owned banks have been instructed to cut their nonpreferential credit to the socialized sector to a level which by end-year would be 5 percent less than at end-September 1990. While this is equivalent to a reduction in credit of Zl 1.8 trillion, the actual decline may be somewhat lower, perhaps about Zl 1 trillion, as additional credit will be allowed for certain contingencies including the arrival of oil deliveries late in the year.

--the outstanding rediscount credit allowed for the Bank for Food Economy, which provides the bulk of preferential credit for agriculture, is to be reduced from about Zl 6 trillion in early November to Zl 4.2 trillion at end-December 1990. Although there is likely to be some switching of agricultural credit to other banks, it is expected that there will be a net reduction in this category of preferential credit;

--obligatory reserve requirements have been raised, in two stages, from 18 to 30 percent for savings deposits, from 7 to 10 percent for time deposits, and from 27 to 30 percent for sight deposits;

--and, in order to reduce further the excess liquidity in the banking system, the National Bank of Poland is to increase the amount of its bills offered at auction so as to raise the outstanding stock from Zl 3 trillion in early November to Zl 5 trillion by end-year.

Concerning wage policy, while there have been no changes in the policy for the remainder of this year, the authorities have made a number of announcements about the incomes policy to be implemented next year with a view to moderating wage increases during November and December 1990. In particular, it has been announced that a tax-based wage policy will be continued and that any unutilized margin under the norm at end-December can be carried forward into 1991. It has also been publicly stated that the starting level, or norm, for wages next year will be linked to the present norm and not to the actual level of wages in December 1990 (which is expected to be substantially higher than the norm). This is consistent with the need to ensure that there is a marked decline in money wages at the beginning of 1991 in line with the normal seasonal pattern.

On the basis of the steps taken to tighten the stance of policies, the authorities request a waiver for the nonobservance of performance criteria for the period July to September relating to the increase in wages and the increase in net domestic assets of the banking system. In addition, the authorities request that the performance criteria for the period September to December 1990 for the net domestic assets of the banking system, borrowing by the general government from the banking system, the deficit of the core general government, and net international reserves be modified as indicated in Table 9.

IV. Staff Appraisal

Poland's adjustment program has achieved notable successes on a number of fronts. Inflation, while remaining above the targeted path, has been brought down substantially from its extremely high level at the beginning of the year, strengthening confidence in the zloty, and international reserves have increased markedly. At the same time, the economy has been substantially liberalized, with the removal of trade and exchange restrictions and the freeing of almost all prices, and as a result shortages have all but been eliminated. There have also been some signs of a moderate recovery in output since midyear following the sharp fall in the early months of the program.

The staff is concerned, however, that in recent months both bank credit and the wage bills of enterprises have been growing significantly faster than programmed. While some recovery in both the real stock of money and the real wage level was undoubtedly appropriate given the sharp and unintended decline in both variables in the first half of the year, it is clear that actual developments in credit and wages have gone beyond what was warranted and have contributed to a significant upturn in inflationary pressure. This has been reflected in the marked increase in the monthly inflation rate in September and October, only part of which can be attributed to increases in energy prices. These developments are particularly troubling as, combined with further increases in administered prices scheduled for January, they could jeopardize the maintenance of the present exchange rate as a nominal anchor, creating the risk of a further escalation of inflation. As it is, the recent increase in international oil prices, the reform of CMEA trading arrangements, and the likelihood of a major fall in exports to the U.S.S.R. and to the former GDR market will add substantially to the pressures on Poland's balance of payments in 1991. While a marked tightening of policies could have an adverse effect on the growth of output, which has only recently begun to show signs of recovery, there exists a greater and more fundamental danger that, without an adjustment of policy, an unacceptably high rate of inflation could become entrenched. In the staff's view, the balance of risks argues for a substantially more restrictive stance of policies.

The authorities share this view and in recent weeks have taken a number of measures to tighten financial policies. These include sizeable increases in interest rates, steps to reduce sharply the growth in credit, and the containment of the budget deficit to substantially less than originally planned. Taken together, these measures should be adequate to hold the growth of net domestic assets within the revised program limit that is being proposed and, importantly, should serve to reassert greater financial policy discipline as the economy enters 1991.

The authorities have also made announcements about the broad features of the incomes policy to be implemented next year that could help to moderate wage increases in November and December. Clearly, direct administrative action to bring wage growth more quickly under control would have strengthened the policy package. Such action, however, was not, deemed feasible by the authorities, particularly in the wake of the fall in real wages earlier in the year and in the prevailing political circumstances. The elements of the wage policy for 1991 that have been revealed do, however, imply that there will be a substantial drop in total wage remuneration at the beginning of 1991 following the payment of seasonal bonuses in December--a decline that is essential if firm control over wages in line with the likely growth in GDP is to be maintained next year.

In sum, the staff believes that, if forcefully followed up in the opening months of next year, the measures that have been taken and announced will be effective in reversing the buildup of inflationary pressures. On this basis, the staff recommends Board approval of the requested waiver for nonobservance of performance criteria for the period July to September 1990 and the modification of performance criteria for the period October to December described above.

V. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board.

Poland--Stand-By Arrangement
Waiver and Modification of Performance Criteria

1. Poland has consulted with the Fund in accordance with paragraph 4 of the stand-by arrangement for Poland (EBS/90/11, Supp. 2) and Section 4 of the letter dated August 20, 1990 from the Deputy Prime Minister and Minister of Finance and the President of the National Bank of Poland in order to review the economic situation and policies and to reach understandings regarding the circumstances in which purchases can be resumed under the stand-by arrangement.

2. The letter dated November 23, 1990 from the Deputy Prime Minister and Minister of Finance and the President of the National Bank of Poland shall be attached to the stand-by arrangement for Poland, and the letter and memorandum dated December 22, 1989, as supplemented by the letter of August 20, 1990, shall be read as supplemented and modified by the letter dated November 23, 1990.

3. Accordingly, the performance criteria as specified in paragraph 4(a) of the stand-by arrangement shall be as set forth in Table 1 attached to the letter dated November 23, 1990.

4. The Fund decides that Poland may proceed to make purchases under the stand-by arrangement notwithstanding the nonobservance of the performance criteria for end-September 1990 specified in paragraph 4(a)(i) and (ii).

Table 1. Poland: Fund Position, 1989-91

	Oct.-Dec. 1989	Jan.-Mar. 1990	Apr.-June 1990	July-Sept. 1990	Oct.-Dec. 1990 1/	Jan.-Mar. 1991 1/
			(In millions of SDRs)			
Purchases	--	170.0	93.75	93.75	93.75	93.75
Ordinary resources	--	170.0	93.75	93.75	93.75	93.75
Borrowed resources						
Repurchases	--	--	--	--	--	--
Tranche policies	--	--	--	--	--	--
Special facilities	--	--	--	--	--	--
Net purchases	--	170.0	93.75	93.75	93.75	93.75
Total Fund credit outstanding (end of period)	--	170.0	263.75	357.5	451.25	545.0
Tranche policies	--	170.0	263.75	357.5	451.25	545.0
Special facilities	--	--	--	--	--	--
			(In percent of quota) 2/			
Total Fund credit outstanding (end of period)	--	25.0	38.8	52.6	66.4	80.1
Tranche policies	--	25.0	38.8	52.6	66.4	80.1
Special facilities	--	--	--	--	--	--

Source: IMF staff.

1/ Projections.
2/ Poland's quota is SDR 680 million.

Table 2. Poland: Performance Under the Stand-by Arrangement, June 30, 1990 to September 30, 1990

	Program 1/	Actual
Increase in wages charged to enterprises' costs 2/ (in percent)	14.0	25.8
Increase in consumer prices (in percent)	14.0	10.4
Change in net credit of the banking system to the general government (in trillions of zlotys)	4.30	-6.99
Deficit of the "core" general government (in trillions of zlotys)	3.90	-9.28 3/
Change in net domestic assets of the banking system (in trillions of zlotys)	14.22	18.83
Increase in net international reserves of the banking system (in millions of US dollars)	800	1,488
Contracting or guaranteeing of new external debt (in millions of US dollars)	700 4/	288 5/

Source: Data provided by the Polish authorities.

1/ Limits, except in the case of net international reserves, where the figure is a minimum target. For definitions, see Appendices to Memorandum of Economic Policies dated December 22, 1989 (EBS/90/3, 1/3/90).
2/ In the five main areas of the socialized sector.
3/ Negative sign denotes surplus.
4/ Limit applies to January 1-December 31, 1990.
5/ January 1 to September 30, 1990.

Table 3. Poland: Short-term Indicators, I

	1989	1990			
	Dec.	Jan.	Mar.	June	Sept.
Exchange rate					
Official rate (zloty per US$1), average	5,235	9,500	9,500	9,500	9,500
Parallel market rate (zloty per US$1), average	7,454	9,344	9,624	9,621	9,490
Real effective rate, price-deflated (Nov-Dec 1989=100)		77	98	113	115
Real effective rate, wage-deflated (Nov-Dec 1989=100)		52	61	69	74

	1990		
	QI	QII	QIII
Balance of payments and reserves			
In convertible currencies			
Exports (percent change) 1/	23	22	73
Imports (percent change) 1/	-23	-18	10
Trade balance (in millions of US dollars)	816	1,154	890
Current balance (in millions of US dollars)	181	948	712
Change in gross official reserves (in millions of US dollars)	333	1,020	1,496
Change in net international reserves (in millions of US dollars)	1,712	1,448	1,594
In transferable rubles with the CMEA			
Exports (percent change) 1/	11	15	-2
Imports (percent change) 1/	-36	-46	-29
Trade balance (in millions of TRs)	1,409	1,805	816
Fiscal, credit, and money			
General government balance (in percent of 1990 GDP)	0.7	2.6	1.4
Net credit to nongovernment (percent change in real terms)	-36	33	21
Money and quasi-money (percent change in real terms)	-44	5	13

Source: Data provided by the authorities.

1/ Over corresponding period of previous year.

2/ In terms of transferable rubles.

Table 4. Poland: Short-term Indicators, II

	1990 QI	1990 QII	1990 QIII
Economic activity (percent change over corresponding period of 1989, in volume terms)			
Sold production of socialized industry	-26.7	-30.8	-20.0
Consumption by industry of electricity 1/	-10.3	-12.6	-12.8
Production of socialized construction	-20.3	-24.4	-19.8
Average employment 1/	-8.3	-9.7	-12.0
Prices (within-quarter percent change)			
Consumer prices	131.9	16.3	10.3
Wholesale prices (sold production of socialized industry)	129.3	4.3	9.2
Wages 2/ (within-quarter percent change)			
Average wages, excluding premia from profit	18.7	17.6	31.8
Wage Fund, excluding premia from profit	14.6	12.6	25.8

Source: Data provided by the Polish authorities.

1/ Cumulative quarterly--i.e., the figure for QII is for the first half of 1990.
2/ In the five main areas of the socialized sector.

Table 5. Poland: Major Budgetary Aggregates

(In percent of annual GDP)

	1989	1990 HI	1990 HII 1/	1990 Year 1/	1990 Original Program
A. State budget					
Revenue	30.8	14.0	16.7	30.7	34.6
Income tax and dividends	10.2	6.3	7.9	14.2	14.5
Turnover tax	8.9	2.7	3.3	6.0	9.3
Other	11.7	5.0	5.5	10.5	10.8
Expenditure	37.0	12.7	16.8	29.5	35.4
Goods and services and wages	7.6	...	...	6.3	7.4
Subsidies	13.0	...	...	6.7	6.2
Other current expenditure 2/	12.2	...	...	13.3	18.7
Investment	4.2	...	...	3.3	3.1
Balance	-6.1	1.3	-0.1	1.2	-0.8
B. Balance of "Core" Extrabudgetary Funds 3/	-1.9	2.1	0.9	3.0	0.7
C. Balance of "Core" general government (A+B)	-8.1	3.4	0.8	4.2	-0.1
(in trillions of zlotys)	(-7.8)	(21.2)	(5.1)	(26.3)	(-0.5)
D. Balance of other Extrabudgetary Funds	0.7	--	-0.1	-0.1	--
E. Balance of general government (C+D)	-7.4	3.4	0.7	4.1	-0.1
(in trillions of zlotys)	(-7.1)	(21.3)	(4.5)	(25.8)	(-0.3)
Memorandum items:					
Financing of general government balance (in trillions of zlotys)					
Total	7.1	-21.3	-4.6	-25.8	0.3
Banking system	5.0	-16.7	-3.3	-20.0	--
Change in net arrears	1.9	-1.9	0.2	-1.7	...
Treasury bills and bonds	0.4	-0.3	--	-0.3	...
External	-0.2	-2.3	-1.5	-3.8	...

Sources: Staff compilation from data provided by the authorities; and staff estimates.

1/ Projection.

2/ Includes transfers to extrabudgetary funds.

3/ The eight largest funds and certain other budgetary units.

Table 6. Poland: Summary Monetary Program, 1990

	QI	QII	QIII	QIV
	Actual		Program	
Actual and Mid-Year Program				
	(In trillions of zlotys; end of period)			
Net international reserves	30.9	44.9	52.5	57.1
(In millions of U.S. dollars)	(3,248)	(4,725)	(5,525)	(6,015)
Net domestic assets	81.6	91.7	106.0	119.2
Net credit to government	2.2	-11.1	-6.8	-4.1
Net credit to nongovernment	48.1	74.5	87.4	99.3
Other assets, net	31.3	28.3	25.4	24.1
Money and quasi-money	112.4	136.6	158.5	176.4
	(Quarterly percentage change in real terms)			
Net domestic assets	-54	-3	3	8
Net credit to nongovernment	-36	33	5	9
Money and quasi-money	-44	5	4	6
Memorandum item:				
Inflation during quarter	131.9	16.3	11.9	4.6
Actual QIII and Proposed Revised Program QIV				
	(In trillions of zlotys; end of period)			
Net international reserves			59.0	62.8
(In millions of U.S. dollars)			(6,213)	(6,613)
Net domestic assets			110.6	125.6
Net credit to government			-18.1	-14.4
Net credit to nongovernment			99.9	111.2
Other assets, net			28.8	28.8
Money and quasi-money			169.6	188.4
	(Quarterly percentage change in real terms)			
Net domestic assets			9	0
Net credit to nongovernment			21	-2
Money and quasi-money			13	-2
Memorandum item:				
Inflation during quarter			10.3	13.6

Source: Data provided by the authorities, and staff projection.

Table 7. Poland: Balance of Payments in Convertible Currencies

(In millions of U.S. dollars)

	1989	Jan.-June 1990	Jan.-Sept. 1990	Proj. 1990
Exports	7,575	4,723	7,516	10,500
Imports	-7,335	-2,753	-4,656	-7,500
Trade balance	240	1,970	2,860	3,000
Nonfactor services (net)	-228	-155	-131	-192
Interest receipts	382	230	396	562
Interest payment obligations	-3,469	-1,906	-2,885	-3,910
Transfers (net)	1,232	990	1,601	2,025
Private	(1,144)	(796)	(1,375)	(1,775)
Official	(88)	(194)	(226)	(250)
Current balance	-1,843	1,129	1,841	1,485
Medium- and long-term capital (net)	-1,406	-1,299	-2,515	-2,594
Drawings	226	114	199	350
Loan repayment obligations	-1,668	-1,418	-2,720	-2,954
Export credits extended, etc.	36	5	6	10
Short-term capital (net) 1/	-125	-1,615 2/	-1,816 2/	-1,600
Overall balance	-3,374	-1,785	-2,490	-2,709
Debt relief	382	7,371	9,457	9,049
Balance of payments financing (net)	215	135	264	360
Of which: IMF	(--)	(350)	(479)	(595)
Change in arrears	3,192	-3,529	-3,364	-2,985
Of which: interest payments to banks	(--)	(367)	(572)	(775)
Change in gross official reserves (- increase)	-415	-1,353	-2,849	-3,715
Memorandum items				
Change in net international reserves of the banking system	356	3,159	4,754	5,205
Change in gross official reserves	415	1,353	2,849	3,715
Change in other foreign assets (net) of the banking system	156	1,941	2,169	1,850
Less: balance of payments financing (net)	215	135	264	360

Source: Data provided by the authorities; and staff projections.

1/ Includes errors and omissions.

2/ Reflects, in large part, a buildup in the foreign exchange holdings of commercial banks in Poland which was deposited with correspondent banks abroad.

Table 8. Poland: Balance of Payments in Nonconvertible Currencies

	1989	Jan.-June 1990	Jan.-Sept. 1990	Proj. 1990
A. With the CMEA in Transferable Rubles				
	(In millions of transferable rubles)			
Exports	11,320	6,217	8,741	11,090
Imports	-10,342	-3,003	-4,711	-6,790
Trade balance	978	3,214	4,030	4,300
Nonfactor services (net)	427	312	498	624
Interest receipts	3	14	21	35
Interest payments	-309	-251	-252	-265
Transfers (net)	5	5	2	15
Current balance	1,104	3,294	4,299	4,709
(in millions of U.S. dollars) 1/	(372)	(728)	(951)	(1,042)
Medium and long-term capital (net)	-721	-713	-744	-954
Credits received	-654	-624	-701	-925
Drawings	(107)	(66)	(71)	(75)
Repayments	(-761)	(-690)	(-772)	(-1,000)
Credits extended (net)	-79	7	11	25
Other 2/	12	-96	-54	-54
Balance	383	2,581	3,555	3,755
B. Under Bilateral Clearing Agreements				
	(In millions of U.S. dollars)			
Exports	538	459	759	...
Imports	652	161	454	...
Trade balance	-114	298	305	...
Net invisibles	35	6	13	...
Current balance	79	304	318	...

Source: Data provided by the authorities, and staff estimates.

1/ Converted at the official commercial cross rate between the transferable ruble and the U.S. dollar; for 1990 the cross rate effective January 1, 1990 (TR 4.52=US$1) was used.

2/ Including errors and omissions..

Table 9. Poland: Proposed Performance Criteria for September 30, 1990 to December 31, 1990 1/

	Existing Criteria for 1990 HII	Outturn During Q3	Implied Criteria for 1990 Q4 2/	Proposed Modified Criteria for 1990 Q4
Change in net credit of the banking system to the general government (in millions of zlotys)	7.00	-6.99	13.99	3.70
Deficit of the "core" general government (in millions of zlotys)	6.30	-9.28	15.58	4.10
Change in net domestic assets of the banking system (in millions of zlotys)	27.50	18.83	8.67	15.00
Increase in net international reserves of the banking system (in millions of zlotys)	1,290	1,488	-198	400 3/
Contracting or guaranteeing of new external debt (in millions of US dollars)	700 4/		...	...

Source: IMF staff.

1/ Limits, except in the case of net international reserves, where the figures are minimum targets. For definitions, see Appendices to Memorandum of Economic Policies dated December 22, 1989 (EBS/90/3, 1/3/90).
2/ After deducting outturn in the third quarter from the performance criterion for the second half of the year.
3/ Valued at January 1, 1990 cross rates.
4/ Ceiling for calendar 1990 as a whole. No modification is being proposed.

Table 10. Poland: Current Projections Compared with Original Program Projections for Selected Variables

(Percent change unless otherwise indicated)

	1989	1990	
		Original Program	Current Projections
Gross domestic product (in real terms)	0.2	-5	-10/-15
Consumer prices			
Period average	245	395	601
Within year	640	94	241
Average monthly wages in the socialized sector (period average)			
In nominal terms	275	240	376
In real terms	9	-31	-32
General government balance (in percent of GDP)	-7.4	-0.1	4.1
Money and credit (within year)			
Net domestic credit			
in nominal terms	221	122	152
in real terms	-57	15	-26
Money and quasi-money			
in nominal terms	239	87	117
in real terms	-54	-4	-36
External trade in convertible currencies (in terms of U.S. dollars)			
Exports	5	2	39
Imports	16	13	2
Trade balance (billions of US$)	0.2	-0.8	3.0
Current account (billions of US$)	-1.8	-3.0	1.5
Change in net international reserves (billions of US$)	0.4	0.2	5.2

Sources: Data provided by the authorities; and staff estimates.

ATTACHMENT

November 23, 1990

Dear Mr. Camdessus:

Since midyear, further progress has been made under the economic program launched in January. In particular, the external current account in convertible currencies has remained strong, with exports maintaining their upward trend. Also, the monthly inflation rate continued to decline through August and output has shown some signs of moderate recovery following its sharp fall in the first half of the year.

Despite these achievements, difficulties have recently been encountered in some areas and two quantitative performance criteria for end-September were breached. The target of 14 percent for the increase in the wage fund during the third quarter was exceeded by about 12 percentage points, an overrun that resulted mainly from a greater-than-anticipated utilization of the margin under the wage norm accumulated during the first half of the year. Over the same period, the program limit of Zl 14.2 trillion for the increase in net domestic assets of the banking system was exceeded by Zl 4.6 trillion, in part reflecting a rapid expansion in credit to the private sector. While we believe that the demand for money was somewhat stronger than expected during the third quarter, we also recognize that the expansion of money and credit has contributed with a lag to some upturn in inflationary pressures.

At the same time, the economy has been adversely affected by the sharp increase in international oil prices. We have moved promptly to adjust domestic prices to reflect the higher import cost, raising the retail prices of petroleum products by 32 to 54 percent between September 1 and early October. Partly reflecting these adjustments, the monthly inflation rate rose from 1.8 percent in August to 4.6 percent in September and 5.7 percent in October. While we estimate that with tight financial policies inflation will be lower by year-end, it will inevitably be higher in the fourth quarter than foreseen earlier, and we are now projecting an increase in the consumer price index of about 13 1/2 percent during this quarter.

We are aware of the threat posed by a continuation of the recent rapid growth in credit and wages to the objectives of the economic program, especially the achievement of price stability. Accordingly, we have taken the following measures:

1. Interest rates

In order to restore interest rates to levels that are positive in real terms and to signal the Government's clear intention to restrain inflation, the refinance rate was increased from the equivalent of 2.8 percent per month to 3.5 percent in early October and further to 4.4 percent with effect from November 21; the rediscount rate has been raised by a corresponding amount. In addition, the restriction limiting the lending rates of State-owned banks to no more than 2 percentage points above the refinance rate has been removed. At the same time, these banks will be required to set interest rates on six-month deposits at the same level as the prime lending rate. We believe that these steps will be effective both in restraining the demand for credit, particularly for consumption purposes, and in bolstering the demand for zloty deposits. It should also help to discipline wage awards.

2. Wage policy

Given the unutilized margin remaining under the wage norm, wage pressures are likely to remain strong during the last quarter of the year; in October, preliminary data indicate that the wage fund increased by 10.4 percent. With a view to moderating these pressures, we have announced (i) that a tax-based wage policy will be continued next year and that any unutilized margin under the norm at the end of 1990 can be carried over into 1991; and (ii) that under this policy the norm for the level of wages free of excess wage tax will be set independently of the actual level of wages in December. This latter provision implies that the January 1991 wage norm will be well below the actual level of wages in December. In line with the customary seasonal pattern following wage bonuses in December, total wage remuneration in nominal terms will decline significantly at the beginning of the year.

3. Credit program

We regard a tightening of monetary policy as necessary to prevent the present level of inflation from becoming entrenched. However, because of the impact of adjustments to the prices of petroleum products on the overall inflation rate, we believe that it is no longer feasible to adhere to the original credit program for the fourth quarter. Our revised credit program, which is designed to restrain inflation during the last quarter to the rate mentioned above, is consistent with a decline in the stock of real broad money. On this basis, and taking into account the revised target for the increase in net international reserves of US$400 million during the fourth quarter, we intend to allow an increase in net domestic assets of no more than Zl 15 trillion between end-September and end-December 1990.

In order to keep credit growth within this limit, we have--in addition to raising interest rates--taken the following measures: raised obligatory reserve requirements in two stages from 18 to 30 percent for savings deposits, from 7 to 10 percent for time deposits, and from 27 to 30 percent for sight deposits; required State and State- owned banks to cut their nonpreferential credit to socialized enterprises by 5 percent by end-December in relation to its level at end-September; and reduced the outstanding rediscount credit allowed for the Bank for Food Economy from some Zl 6 trillion in early November to Zl 4.2 trillion at end-December 1990. In addition, to absorb further the liquidity of the banking system, we intend to increase sales of National Bank of Poland bills so as to raise the outstanding stock from its level of Zl 3 trillion in early November to Zl 5 trillion by year-end.

Budgetary expenditure will also bear some of the burden of adjustment, and borrowing by the general government from the banking system will be limited to Zl 3.7 trillion between end-September and end-December 1990, substantially less than allowed under the existing program. Consistent with this, the deficit of the "core" general government will be limited to Zl 4.1 trillion between end-September and end-December 1990 (which will imply a "core" general government surplus for the year as a whole of some Zl 26 trillion, or about 4 percent of estimated GDP).

We believe that these policy adjustments will provide a solid foundation for the continuation of progress toward stabilization and sustained growth in 1991. We recognize that the economic outlook is uncertain and we stand ready to take additional measures as necessary.

Against this background, we request waivers for the nonobservance of end-September performance criteria with respect to wages and net domestic assets and also request that the performance criteria for end-December for net domestic assets, borrowing by general government from the banking system, the deficit of the "core" general government, and net international reserves be modified as described above and in Table 1.

Sincerely,

Leszek Balcerowicz
Deputy Prime Minister
and Minister of Finance

Wladyslaw Baka
President
National Bank of Poland

Mr. Michel Camdessus
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C., 20431

Table 1. Poland: Revised Performance Criteria for the Fourth Quarter of 1990 1/

	End-September to End-December 1990
Deficit of "core" general government (in trillions of zlotys)	4.1
Borrowing by general government from banking system (in trillions of zlotys)	3.7
Increase in net international reserves of the banking system (in millions of U.S. dollars)	400
Increase in net domestic assets of the banking system (in trillions of zlotys)	15
Contracting or guaranteeing of external debt (in millions of U.S. dollars)	700 2/

1/ Limits, except in the case of net international reserves where the figures are minimum targets. For definitions, see Appendices to Memorandum of Economic Policies dated December 22, 1989 (EBS/90/3, 1/3/90)

2/ Cumulative change from December 31, 1989; unchanged from existing program.

Poland - Fund Relations

(As of October 31, 1990)

I. (a) Date of membership: Poland was an original member of the Fund but withdrew from membership on March 14, 1950. Poland rejoined the Fund on June 12, 1986.

(b) Status: Article XIV.

A. Financial Relations

II. General Department (General Resources Account)

(a) Quota: SDR 680 million

(b) Total Fund holdings of currency: SDR 1,037.5 million (152.57 percent of quota).

(c) Fund credit: SDR 357.5 million, of which credit tranche SDR 357.5 million (52.57 percent of quota).

(d) Reserve tranche position: none

III. Stand-by Arrangement

Dates: February 5, 1990 - March 4, 1991

Amount: SDR 545 million

Amount drawn: SDR 357.5 million

IV. SDR Department

(a) Net cumulative allocation: none

(b) Holdings: SDR 73,567

V. Financial Obligations due to the Fund

(SDRs)	10/1/90- 12/31/90	1/1/91- 12/31/91	1/1/92- 12/31/92	1/1/93- 12/31/93
Repurchases	--	--	--	98,906,250
Interest charges (provisional)	7,753,622	49,895,377	53,716,877	51,925,028
Total	7,753,622	49,895,377	53,716,877	150,831,278

B. Nonfinancial Relations

VI. Exchange rate arrangements

The currency of Poland is the zloty. Exchange rates of the zloty to make payments and transfers for most current international transactions with the convertible currency area are set and monitored on the basis of a basket of convertible currencies the share of which in Polish external current account transactions are not lower than 1 percent. Buying and selling rates are set with margins of 0.5 percent around the middle rate (except for notes and coins, for which the margins are 2 percent), which on July 31, 1990 was Zl 9,500 = US$1. The cross rates of the U.S. dollar with other convertible foreign currencies are monitored closely with a view to adjusting the exchange rates of the zloty against these currencies whenever their exchange rates against the U.S. dollar in foreign markets move out of line with these cross rates. Individuals may make payments and transfers which are not eligible for foreign exchange at the official rate with foreign exchange acquired in a parallel market in which the exchange rate of the zloty is determined freely by supply and demand. On October 26, 1990 the middle rate of this exchange rate was Zl 9,475 per U.S. dollar.

Exchange rates for the transferable ruble and the clearing ruble--used for trade and financial settlements with CMEA member countries and settlements under some clearing arrangements, respectively--are set at the same level, with margins of 0.5 percent around the middle rate. On October 31, 1990 the middle rate for the transferable ruble was Zl 2,100 = TR 1. Exchange rates are also quoted for the zloty against the currencies of other CMEA member countries, Albania and the Democratic People's Republic of Korea for the purpose of noncommercial transactions; these rates are based on multilateral and supplemental bilateral agreements.

VII. The last Article IV consultation was concluded at EBM/90/15 (2/5/90). Poland is on a 12-month consultation cycle. The following decision was taken by the Board on February 5, 1990:

1. The Fund takes this decision relating to Poland's exchange practices subject to Article VIII, Sections 2(a) and 3, and in concluding the 1989 Article IV consultation with Poland, in the light of the 1989 Article IV consultation with Poland conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. Poland's exchange restrictions and multiple currency practices are maintained under Article XIV, Section 2, except that the multiple currency practices listed below, as well as restrictions on certain payments and transfers by enterprises are subject to approval under Article VIII, Section 2(a). The multiple currency practices that arise from the operation of the parallel exchange market, the convertible foreign exchange coupon scheme, and the

currency-specific surcharges on foreign exchange sales for travel to CMEA countries that are members of the Fund are subject to approval under Article VIII, Section 3. The latter practice constitutes a discriminatory multiple currency practice, which the Fund urges Poland to eliminate. The Fund also encourages Poland to take the necessary steps to avoid the emergence of broken cross rates. The Fund welcomes the Government's intention to reduce reliance on the other restrictions subject to Article VIII and on bilateral payments arrangements and hopes that early progress can be made in this respect. In the meantime, the Fund grants approval of the multiple currency practices that arise from the operation of the parallel market and from the convertible foreign exchange coupon scheme until May 15, 1990.

VIII. Technical Assistance

Over the past 18 months, the following technical assistance was provided:

Bureau of Statistics: A mission from the Bureau of Statistics visited Poland in October 1988 to discuss monetary and government finance statistics. A mission visited Warsaw in November 1990 to discuss monetary statistics.

Central Banking Department: Missions from the Central Banking Department visited Poland in May-June 1989 to assist the authorities in designing new monetary control procedures and strengthening banking supervision; in November 1989 to discuss earlier recommendations and the scope for further technical assistance to be delivered by several cooperating central banks; in December 1989 to discuss the development of research and statistical capabilities to implement monetary policy; in January 1990 to develop further and coordinate technical assistance efforts with the view to facilitating the effective implementation of monetary policy and modernizing the operations of the National Bank of Poland; and in March/April 1990 to assist with modernizing accounting and auditing procedures and reviewing foreign exchange operations. A follow-up mission on all technical assistance projects took place in May 1990. Periodic visits by experts from central banks cooperating in providing technical assistance to the National Bank of Poland under the coordination of the Central Banking Department took place throughout the year and continued after May.

Fiscal Affairs Department: Missions from the Fiscal Affairs Department visited Poland in September 1989 to advise the authorities on the implementation of a personal income tax system; in October-November 1989 to review the fiscal structure, to recommend structural fiscal reforms, and to assist the authorities in the formulation of the 1990 budget; in June 1990 to advise on the possible introduction of the value-added tax; and in August 1990 to review and improve the effectiveness of tax administration and to initiate preparations for the introduction of the value-added tax. A field expert is currently on a short-term assignment in Warsaw providing assistance on improvement in tax administration.

Legal Department: A mission visited Warsaw in June 1990 to advise the authorities on the establishment of an export credit insurance scheme.

Poland: Selected Economic Indicators, 1985-90

(Percentage change unless otherwise indicated)

	1985	1986	1987	1988	1989	Projected 1990
Domestic indicators						
(In real terms)						
Gross domestic product (SNA basis)	3.6	4.2	2.0	4.1	0.2	-10/-15
Net material product	3.4	4.9	1.9	4.9	—	...
Consumption (material)	2.9	4.8	2.8	2.9	-1	...
Gross fixed investment	4.4	4.5	4.1	6.1	-4	-13
Industrial production (gross)	3.8	4.3	3.2	4.6	-3	...
Agricultural production (gross)	1.1	5.2	-6.8	1.5	...	...
(In nominal terms)						
Consumer prices (period average)	15.1	17.7	25.2	60.2	245.3	601
Average monthly wages in the socialized sector (period average)	18.8	20.4	21.1	81.9	275 1/	376 1/
Household incomes 2/	18.7	22.4	25.9	83.8	...	...
Fiscal indicators (in percent of GDP)						
State budget revenues	40.4	39.9	34.2	35.5	30.8	30.7
State budget expenditures	41.6	41.0	37.7	37.0	37.0	29.5
State budget balance	-1.2	-1.1	-3.5	-1.4	-6.1	1.2
General government balance	...	-0.3	-0.8	—	-7.4	4.1
Monetary indicators (end of period)						
Domestic credit (net of general government deposits)	18.1	16.9	17.8	46.4	220.6	151.6
Money and quasi-money	26.7	34.1	58.3	133.0	239.4	117.1
External indicators in convertible currencies (in terms of U.S. dollars)						
Exports 3/	-3.8	3.8	15.9	17.6	4.5	38.6
Imports 3/	2.2	6.2	19.7	23.1	16.3	2.2
Trade balance						
In billions of U.S. dollars	1.1	1.0	1.0	0.9	0.2	3.0
In percent of GDP 4/	1.5	1.4	1.6	1.4	0.3	4.6
Current account						
In billions of U.S. dollars	-0.6	-0.7	-0.4	-0.6	-1.8	1.5
In percent of GDP 4/	-0.9	-0.9	-0.6	-0.8	-2.6	2.3
External debt (end of period) 5/						
In billions of U.S. dollars	29.7	33.5	39.7 6/	39.1	40.6	45.9
Ratio to exports of goods and nonfactor services in convertible currencies	5.2	5.7	5.8	4.9	4.9	3.9
External debt service ratio 7/						
Due	88	105	91	85	62	58
Paid	35	30	23	20	19	7
Commercial exchange rate depreciation (-) against U.S. dollar (period average)	-22.7	-16.0	-33.9	-38.4	-70.2	-84.8
External indicators in nonconvertible currencies (in terms of U.S. dollars) 8/						
Current account balance (in billions of U.S. dollars)	-0.6	-0.3	-0.2	0.3	0.3	1.0

Sources: Central Statistical Office, Rocznik Statystyczny; data provided by the authorities; and staff estimates.

1/ In the five main areas of the socialized sector.

2/ Income accruing from savings bonds issued in 1982 (to provide partial compensation to savers for the large increase in prices in that year) is distributed over the period 1982-85 even though the bonds and accumulated interest income could not be encashed before 1985.

3/ Balance of payments basis.

4/ Gross domestic product in zloty terms is converted into U.S. dollars at the commercial exchange rate.

5/ Including arrears.

6/ Includes an estimated US$0.5 billion of late interest due on certain rescheduled debt.

7/ In percent of exports of goods and nonfactor services in convertible currencies.

8/ Transactions in nonconvertible currencies were converted from transferable rubles into zlotys at the TR/Zl commercial rate, and then into U.S. dollars at the Zl/US$ commercial rate.