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RECENT ECONOMIC DEVELOPMENTS IN EASTERN EUROPE

Note by the Secretary General

The attached report, prepared by the Economic Committee, on the basis of national contributions and in the light of detailed discussions, analyses the repercussions of the Polish economic difficulties on other Eastern European CMEA member countries.

2. This report will be placed on the Agenda for the meeting of the Council in Ministerial Session as a reference document.

(Signed) Joseph M.A.H. LUNS

NATO,  
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This document includes: 1 Annex

N A T O C O N F I D E N T I A L

RECENT ECONOMIC DEVELOPMENTS  
IN EASTERN EUROPE

Report by the Economic Committee

PART I

ECONOMIC IMPACT OF RECENT ECONOMIC DEVELOPMENTS IN POLAND  
ON EAST EUROPEAN CMEA MEMBERS

1. The dominant feature of the structure of intra-CMEA trade is usually the dependence of each separate country on the USSR both as a main supplier of raw materials and fuel and as a market for the individual countries' exports. Especially in recent years, however, the interdependence of other European CMEA members(1) has grown. The inflexible nature of these planned economies, on the other hand, reduces their capacity to set up a regulating machinery to offset the effects of any developments not in line with the planners' intentions or expectations. Thus the recent developments in Poland, unexpected as they were, affected other European CMEA countries in varying degrees, depending on the scope and intensity of their bilateral trade and structure of their economies.

POLAND'S PLACE IN CMEA

2. Poland, whose geographical position makes it the centre of traffic between the USSR and its Warsaw Pact allies, is a leading CMEA country in Eastern Europe: it accounts for more than a third of the area's population, provides around a quarter of its gross national product and nearly a third of its electricity production. It accounts for 13% of CMEA total foreign trade turnover(2), more than 53% of Poland's total foreign trade is conducted with other CMEA countries, and nearly 60% of Poland's exports go to CMEA. 32% of its total foreign trade is with the USSR, and its indebtedness to that country can be covered by nearly one third of its exports to the Soviet Union in 1980. 86.5% of Poland's intra-bloc trade, however, is conducted with her most important trade partners: USSR, Czechoslovakia, GDR.

3. Poland is an important supplier to Eastern Europe of machines and equipment as well as raw materials such as coal, sulphur and copper. Its electricity production is sufficient to meet its own consumption unlike the other East European countries, except Romania, which have to rely on the USSR, in varying degrees for their electricity supplies. It is the second main producer of coal in CMEA after the USSR and accounts for half of East European coal production. It participates in common CMEA projects under the long term target programme and 15% of its machinery and

(1) Excluding Cuba, Mongolia, Vietnam and associated or affiliated states.

(2) Including intra CMEA trade, but excluding Vietnam.

N A T O   C O N F I D E N T I A L

C-M(81)23

-3-

equipment exports to CMEA falls under the specialisation and co-operation agreements. The overall share of specialised goods in exports in intra-bloc trade is estimated to reach 28% and in imports 21% in 1980(1).

4. As far as socialization and consumption are concerned, the socialized sector ratio is the lowest among all CMEA members in National Income, basic productive funds, gross agricultural production, agricultural land area. Particularly in the agricultural sector, the socialized sector accounts for only 22% of gross agricultural production and 23% of agricultural land area. When 1970 is taken as a base year (100), the greatest increase in real wages and salaries has been in Poland (150 versus 134 in Romania which is the nearest). Per capita annual consumption of meat and meat products at 77 kgs is only 6 kgs less than the GDR but 15 kgs more than Bulgaria and 20 kgs more than the USSR. Milk, butter and potato consumption is the highest in CMEA(2).

DIFFICULTIES ARISING FROM POLAND'S FAILURE TO COMPLY WITH EXPORT CONTRACTS

5. Although some reluctance is sensed on behalf of the CMEA partners to co-ordinate their five year plans with Poland because of the uncertainty of its situation, Poland has signed trade protocols with its CMEA partners. Despite the fact that over the first two months of 1981, Polish exports to socialist countries fell by nearly 17% and to the capitalist countries by 32% whilst the imports from socialist countries went up by more

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- (1) By the end of 1980 Poland had concluded about 100 multilateral and 220 bilateral specialisation and co-operation agreements with the other CMEA countries. However, the share of specialised products produced under such agreements in Poland's foreign trade with individual CMEA countries differed. Whereas the share of specialised products in Soviet-Polish trade was 18% in 1978, it had reached 41% for Hungary.
- (2) Figures are mainly taken from, or based upon information given in, CMEA Yearbook for 1978 (English version).

N A T O   C O N F I D E N T I A L

-3-

N A T O   C O N F I D E N T I A L

-4-

C-M(81)23

than 21%(1), the trade protocols concluded keeping the mutual trade more or less at its 1980 level. The 1981 trade protocol between Poland and the USSR (signed on 19th February 1981), aims at a turnover of 8.4 billion roubles. Poland's exports to the USSR, however, will be more than 4% lower than in 1980. Deliveries of coal, copper, sulphuric acid and other raw materials will be smaller than last year. The trade protocol with Czechoslovakia calls for a turnover of 1.27 billion roubles. According to the protocol consumer goods will take an "important place" in Czechoslovak exports to Poland.

6. There are, however, serious doubts about Poland's capacity to abide by its export commitments. The fall, as from August 1980, of industrial production combined with the need to abide by the government's pledge to increase the availability of certain consumer items inter alia by diverting goods earmarked for export towards the domestic market, has led to a reduction in some of Poland's deliveries to other CMEA states. Of most concern, because it is potentially most damaging, will be the reduction or loss of Polish exports, of coal, machines and equipment and other raw materials, as a result of disruption in Polish industries. Following greatly reduced coal output in the second half of 1980, Polish coal deliveries to the Soviet Union are reported to have ceased and deliveries of hard coal to other CMEA countries have been more than halved. The GDR is having to make up the shortfall by imports of coking coal from the Federal Republic of Germany and converting its furnaces to use domestic compressed lignite, which has a low heating value. Press reports in December stated that one of Romania's major steel plants was at a standstill because of shortages of Polish coal.

7. Poland also exports substantial quantities of copper, sulphur and other chemicals to her CMEA partners. Although none is critically dependent on Polish sources certain enterprises in these countries are particularly affected and this might have a knock off effect on other enterprises. Shortfalls in Polish deliveries of raw and intermediate materials may have caused some difficulties in other CMEA countries, particularly in the GDR which imports significant quantities of chemicals. Although only about 12% of Polish copper exports go to CMEA and they get most of their copper from the USSR, Czechoslovakia seems to be hit specifically because of a relative shortfall in Polish copper exports. The non-delivery of Polish copper is reported to have caused considerable difficulties in the heavy and armaments industry of Czechoslovakia, particularly the Skoda enterprises. Any substantial shortfalls in Polish deliveries of sulphur could increasingly affect Soviet production of sulphuric acid and all its derivatives including nitrogenous fertilizers. However,

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(1) PAP (Polish Information Agency) 2nd March 1981. PAP report also indicates a 17% decrease in imports from capitalist countries.

N A T O   C O N F I D E N T I A L

-4-

N A T O    C O N F I D E N T I A L

C-M(81)23

-5-

after suspending exports of sulphur on "force majeure" grounds last September, the Poles now appear to have production back on target(1).

8. Poland is an important supplier of components and equipment to CMEA industries under numerous long-term specialisation and co-operation agreements. In Eastern Europe, production shortages in one country cannot easily or quickly be compensated for by production in another. This is partly due to the constraints of CMEA specialisation and even more to the centralised planning system which does not permit flexible or rapid responses to changed conditions. The share of these specialised products in mutual trade with USSR was 18%, with GDR 25% (1980 plan) and with Hungary 41% in 1978. They range from Mining equipment to installations for nuclear power plants.

9. In the defence production field, any delay in the implementation of joint production projects now being finalised for the next 5 years would be quite serious. Some projects, such as the manufacture of the T-72 tank, involve substantial investment and collaboration between Warsaw Pact countries. On the civil side, Polish manufacturers include vehicle and aircraft components, earth-moving and mining equipment, chemical plants and sugar refineries, ships and pharmaceuticals. It is probable that deliveries of items for the Soviet vehicle industry are being delayed. In October, workers in a number of GDR factories were reportedly idle as a result of non-delivery of Polish goods. It is unlikely that there have been delays on many of the Polish-assisted construction projects in the USSR or Eastern Europe, although Polish labour as well as machinery and equipment are supplied for some of these.

10. In the agricultural sector, livestock and milk procurement fell sharply in the second half of 1980 and sugar production dropped dramatically. This situation persisted in the first quarter of 1981 and if forecasted to worsen in the second quarter. Poland, which until recently exported 300,000 tonnes of meat a year to the West against hard currency is expected to import meat in 1981, while domestic output is expected to drop by 20%. Some other foodstuffs are also in short supply which necessitates commodity assistance.

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(1) A Polish official disclosed that Poland earned hard currency in 1980:

350	million	US	\$	from	silver	exports
300	"	"	"	"	copper	"
200	"	"	"	"	sulphur	"

According to the same official output of copper is expected to fall by 5% but exports would be slightly higher.

N A T O    C O N F I D E N T I A L

-5-

N A T O C O N F I D E N T I A L

-6-

C-M(81)23

FINANCIAL ASSISTANCE

11. Bloc financial assistance to Poland in 1980, occasioned by the deteriorating balance of payments and market supply situation in the second half of the year, consisted of approximately \$700 million in hard currency credits (mostly from the USSR) but a little below \$100 million may have come from the GDR; about \$1.5 billion in soft currency (rouble) loans and credits from the Soviet Union in 1980-1981 to cover the deficit in Soviet-Polish trade and the cost of additional food and raw materials deliveries (although there may have been an element of double counting); and a reported \$150 million credit (from the GDR) for purchase of additional goods.

12. As for 1981 alone, press reports(1) quoting Polish sources, allege that the USSR has granted a hard currency credit of \$1.1 billion(2): this would cover only a part of the current account deficit which is bound to be greater than earlier years due to the fall in export levels of some hard currency earning Polish goods. At the same time, the USSR is said to have deferred up to 1985, repayment of credits granted between 1976 and 1980, possibly including the \$1.1 billion. Some reports indicate that the GDR has recently furnished a grant of 200 million marks (DDR) and Czechoslovakia pledged to provide a 500 million dollar hard currency loan spread over a longer period. The USSR reportedly had put pressure on Czechoslovakia, the GDR and Hungary to grant further aid to Poland during the recent CMEA Executive Committee meeting (13th-15th January 1981, Moscow). During this meeting it seems that the GDR and Bulgaria had resisted providing increased aid invoking the negative attitude of their own populations. Czechoslovakia, however, had agreed to provide some help. The outcome of the discussions was that Poland should seek additional aid from the West. It seems therefore Poland could only rely upon its partners for aid on a limited scale. Even for the Soviet Union, which is at present in a relatively favourable hard currency position, granting Poland hard currency credits placed a certain financial constraint on the Soviet Economy. Aid however could come in an indirect way by exempting Poland from some of its export commitments such as coal and some other raw materials. This would only be involuntary in the case of some East European countries. Another form of indirect aid would be letting Poland run a deficit in mutual trade like the 1.4 billion rouble deficit foreseen in the Soviet Polish trade agreement.

COMMODITY ASSISTANCE

13. Under an aid package agreed in September 1980, the Soviet Union undertook to supply Poland with 500,000 tonnes of wheat (now mostly delivered), other foodstuffs and industrial consumer goods

(1) Financial Times, 2nd December 1980

(2) A Polish official disclosed that only US\$ 300 million of that sum was fresh credits in hard currency and the total included consolidation of earlier loans

N A T O C O N F I D E N T I A L

-6-

N A T O C O N F I D E N T I A L

C-M(81)23

-7-

and fertilisers. Under a second aid package agreed in December, the Russians will provide foodstuffs, raw materials (cotton and synthetic rubber), farm machinery, consumer durables and more fertilisers. The one-and-three-quarter million tonnes of fertilisers the Soviet Union is to provide in all amounts to less than 2% of Soviet output in 1980, but will nevertheless represent a significant loss to Soviet agriculture which badly needs additional inputs. The same applies to deliveries of Soviet farm machinery.

14. Little aid appears to have been forthcoming from Bulgaria and Romania. Like the Soviet Union, the other East European countries have concentrated their aid on food and consumer goods. Although these extra supplies appear relatively meagre, their loss will be felt either on the home markets of the supplier countries or in their exports.

TRANSPORT

15. Poland's transport system, particularly its rail network, is important to the economies of the USSR and Eastern Europe. Routes on an east-west axis serve traffic between the Soviet Union, Poland and the GDR; other routes on a north-south axis serve traffic between Czechoslovakia, Hungary, Poland and the Baltic ports. During the latter half of 1980, there seems to have been little disruption to surface transport in Poland. Although temporary interruptions to traffic were reported at border crossings and a number of ports, we have seen little evidence so far to suggest that intra-CMEA trade in general has been affected. Czechoslovakia is believed to have incurred additional convertible currency costs through using Federal German ports because of congestion at Polish ports. However, since the mid-1970s, Czechoslovakia has been switching part of its trade (particularly bulk cargoes) away from the Polish Baltic ports in favour of Hamburg and Rostock, apparently because of shortcomings in Polish rail transport, coupled with Poland's increasing use of its own ports.

CONCLUSIONS

16. Poland's economic problems have affected its CMEA European partners in varying degrees. So far, the shortfall in Polish coal production seems to have been the most damaging. Further disruption in Polish industry and other sectors of the economy is bound to affect intra-CMEA trade. If the Polish economy does not recover fast, the losses of Eastern Europe might be considerable. Even in the unlikely event of any speedy recovery of the Polish economy, East European losses are bound to accumulate. The situation in Poland, moreover, might affect the pattern of intra-CMEA trade.

N A T O C O N F I D E N T I A L

-7-

N A T O   C O N F I D E N T I A L

-8-

C-M(81)23

which would create a self perpetrating process which in turn would affect Polish prospects. It has been reported that Romania has promptly offered to supply to Czechoslovakia machine tools which Poland can no longer deliver. Such moves could change the international division of labour within the CMEA. The gravity of the Polish situation or the public reaction to it on the other hand, has already affected the public mood and leaders' attitude in other CMEA countries. A recent example of this is the obligation the Romanian Government felt to acknowledge publicly the shortages of foodstuffs and generally depressed living standards admitting to past errors of policy.

17. The burden of aid to Poland, both in financial and commodity form, constitutes another facet of the problem: continuation of the present situation in Poland will call for substantial aid, but denial might result in a worsening of the situation whilst continuing it adds an extra burden to the already strained East European economies. The problem will be exacerbated if Poland cannot successfully reschedule its hard currency debt with western creditors, and obtain fresh credits from them. So far the East European CMEA countries appear to have adopted to some extent a concerted approach to easing the Polish economic difficulties.

N A T O   C O N F I D E N T I A L

-8-



N A T O   C O N F I D E N T I A L

C-M(81)23

-9-

PART II

THE POLISH ECONOMY

18. The work stoppages in Poland during the Summer of 1980 further illustrate the failure of the strategy combining intensive economic growth with big pay increases implemented by the authorities in the early 1970s. While the need for measures intended to decrease the very high level of State subsidies in the consumer market appeared justified from the economic point of view (in this connection the rise in meat prices should have been followed by a rise in other commodities), their sudden introduction exacerbated the resentment felt by a large proportion of wage earners over the many, serious and varied social inequalities existing in Polish society (the scale of these inequalities partly explains the extent of the government's concessions granted with little delay), concessions which were striking for a socialist régime.

19. Perhaps one of the most important aspects of the protest movement has indeed been the outright refusal of a large part of the population to accept the introduction of an austerity programme designed, inter alia, to help correct the imbalances in the consumer markets by reducing demand. The government, faced by this attitude and by the strength of the free trade unions, which now makes widespread social conflict possible, has a very limited range of options. A return to a balance between supply and demand on the consumer markets has become more difficult to achieve because of the increased purchasing power injected into the economy through the wage rises conceded by the government, and, in any case, is conceivable only through an increase in supply. In the short term, this increase could come up against the negative consequences of various factors such as a persistence of the constraints arising from the convertible currency payments deficit, which limit the possibility of an adjustment through trading, the unsettled state of certain consumer markets, compounded by the poor 1980 harvest and poor prospects for 1981, which has worsened the shortage of foodstuffs, or, again, the uncertainty surrounding the development of industrial output.

RECENT ECONOMIC TRENDS

(i) CONVERTIBLE CURRENCY PAYMENTS DEFICIT

20. Poland's convertible currency indebtedness probably constitutes the greatest constraint on its economy. The country has had to draw extensively on Western financial facilities to fund its successive current account deficits and to repay its

N A T O   C O N F I D E N T I A L

-9-

N A T O C O N F I D E N T I A L

-10-

C-M(81)23

existing debt. In 1978 and 1979 alone, the gross capital inflow (new drawings) came to \$5.8 billion and \$8.2 billion respectively (1). As a result, indebtedness has soared (in net terms, the total, including short-term debt, was between \$24 billion and \$25 billion at the end of 1980) and, above all, the drain represented by debt servicing has grown enormously: payment of principal plus interest accounted in 1979 (2) for 92% of earnings from merchandise exports to the non-Communist countries. The debt service ratio has thus reached excessive proportions which have forced Poland to refinance a growing proportion of its repayments. The fact that the ratio between the actual transfer of resources (3) and the gross inflow of capital (drawings) was only 15% in 1979 (as compared with 35% in 1977-78 and 60% in 1976), serves to illustrate this. Paradoxically, therefore, only 15% of the new debts contracted by Poland in 1979 was used to finance imports, whereas 85% was used to refinance the debt.

21. The external payments situation further deteriorated in 1980. The upward trend in trade which had been noted during the first half of the year (4) was later reversed and by the end of the year Poland was running a deficit of \$0.8 billion in its trade with the non-Communist world. Although this is an improvement on the previous year (when the deficit was \$1.7 billion) it is still further proof of Poland's inability to balance its foreign trade.

22. The persistence of a large trade deficit is admittedly due in part to the economic and social climate reigning during the second half of 1980, and in particular to the drop in certain exports because of the strikes and the production losses in certain industrial branches and the increase in imports made necessary by the poor harvest. But, generally speaking, Poland is faced with a twofold difficulty in its efforts to improve its convertible currency trade balance. On the one hand, greater selectivity in imports of equipment and semi-finished goods may place severe constraints on industrial output, while a reduction in the purchase of consumer goods would be incompatible with the government's

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(1) Source: Bank Handlowy

(2) Including the short-term debt. As a proportion of total gross receipts on current account, the debt service ratio accounted for a slightly lower figure, i.e. about 70%.

(3) By actual transfer of resources is meant the gross inflow of capital (drawings) less the amount represented by the debt service (principal plus interest).

(4) During the first six months of 1980, Poland had a small convertible currency trade deficit of 87 million.

N A T O C O N F I D E N T I A L

-10-

N A T O   C O N F I D E N T I A L

C-M(81)23

-11-

promise to increase supplies of these items. On the other hand, opportunities for increasing exports of manufactured goods are limited, partly it is true because of the weakness in the growth of Western demand, while a further channelling of raw materials away from the domestic market would have a serious effect on economic activity and compound the already existing bottlenecks.

23. The reduction of the trade deficit with the West(1) in 1980 probably had no effect on the level of current payments because of the increase of interest payments; in all probability the convertible currency deficit on current account was at least equal to that recorded in 1979 (some \$3.1 billion). Poland was successful in obtaining sufficient resources to cover its financial requirements for 1980 (in the region of \$9 billion). This achievement will nevertheless highlight the Poles' declining room for manoeuvre inasmuch as additional sources of credit seem to have dried up, as evidenced, for example, by the fact that the National Bank has apparently intervened for the first time on the six-month eurodollar market, the conditions for the transfer of promissory notes subject to forfeiting have been relaxed and the convertible currency reserves have been drawn on.

24. So far, and despite some signs of hesitation(2), Western banks seem to have retained some confidence in Poland, although it seems that many of them have simply refinanced payments falling due and have attempted not to increase the present value of their outstanding commitments to the country. It also seems that the increase in net terms of Poland's debts with banks reporting to the BIS has slackened; between January and September 1980 it amounted to \$0.7 billion, whereas during the first nine months of 1979 the increase was \$1.9 billion. At the same time there has been an increase in the relative importance of Western government support, mainly through the granting of credit guarantees. In this respect it is worth noting that, according to official Polish data(3) two-thirds (\$4.6 billion) of a total of \$6.95 billion in loans already obtained by the country in 1980 represented credits officially backed by a Western public institution(4)(5).

- (1) On the other hand, Poland's trade with its Communist partners worsened from a surplus in 1979 of \$0.3 billion to a big deficit of \$0.9 billion in 1980.
- (2) For example, the medium-term syndicated loan signed on 22nd August 1980 after lengthy negotiations was for \$325 million (a figure which included contributions from Soviet and East European banks established in the West) as compared with the \$500 million which Poland originally hoped to get.
- (3) Figures obtained from the Handlowy Bank.
- (4) Including \$3.8 billion tied to the performance of commercial contracts.
- (5) In 1979, drawings on officially-backed Western credits were estimated at \$2.0 billion (see C-M(80)84 table VII).

N A T O   C O N F I D E N T I A L

-11-

N A T O   C O N F I D E N T I A L

-12-

C-M(81)23

25. Be that as it may, since Poland is unable in the short term to redress its convertible currency balance on current account (and, in the first instance, its trade balance) it will probably be faced this year with even greater difficulties than in 1980, partly because of the increased value of maturing debts and probably because of greater reluctance on the part of certain Western lenders to extend new credits. According to information received recently, the Polish authorities are planning on a convertible currency trade deficit of \$0.8 billion in 1981 and net payments and interest on the debt of \$2.6 billion(1). Bearing in mind scheduled repayments on capital (\$7.5 million), Poland's total convertible currency capital requirements will, according to these forecasts, amount to \$10.9 billion(2). As things stand, it is highly unlikely that Poland will be able to cover its financing needs and the maintenance of solvency will depend entirely on the granting of specific financial support by its creditors.

26. After first having attempted to conclude bilateral agreements mainly for the refinancing of certain officially-backed export credits(3), Poland later became obliged to take part in multilateral negotiations to work out conditions and procedures for consolidating its debt. For officially-backed credits(4), preliminary discussions were held late in February 1981 within a

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- (1) Furthermore, the aim of achieving a surplus on current account initially planned for 1983 has been postponed until 1986.
- (2) Source: Financial Times, 6th March 1981. The figure given for net interest payments should, in all probability, be taken as a minimum but these forecasts do not refer to the traditional surplus (some \$500 million in 1980) under other services and net transfers.
- (3) For example, France agreed to refinance \$310 million worth of officially-backed export credits with an additional four-year period of grace.
- (4) At end-1979, the gross total debt (including short-term debts) on the basis of convertible currency drawings by Poland was estimated at \$21.1 billion (C-M(80)84). Of this figure, \$5.1 billion represented officially-backed Western credits which had actually been drawn. But for the Club de Paris negotiations, undrawn credit commitments must also be taken into account, in which case the Polish debt for guaranteed credits (based on all outstanding commitments and including interest) amounts to between \$12.5 and \$13 billion (figures derived from the statistics of the Berne Union and the ex post facto half-yearly notification procedures used by the Economic Committee).

N A T O   C O N F I D E N T I A L

-12-

N A T O   C O N F I D E N T I A L

C-M(81)23

-13-

framework similar to the Club de Paris(1). According to the information available to the International Staff, it would seem that an agreement in principle has been reached on the rescheduling of part of the Polish debt and that further multi-lateral consultations are to take place in April at which the decision on rescheduling could be taken officially. Later, and probably until July, technical negotiations between Poland and the different Western countries concerned would take place to define the rescheduling arrangements(2). In the meantime, it has been agreed to adopt interim measures which would consist of the granting of bridging credits in the form of financial loans granted by public bodies for, apparently, a duration of six months (February-July).

27. Concurrently with the negotiations with Western governments, Poland has started discussions with a group of seventy Western banks on, by all accounts, the rescheduling of \$3.1 billion representing what are probably medium-term unguaranteed bank credits maturing in 1981(3). In all likelihood, the response by the international banking circles to this request will depend on its assessment of the Polish economic recovery programme and also on Western governments' financial attitude towards Poland.

28. Reference should also be made to the assistance granted to Poland by the European Community: on 16th December 1980, the EEC Foreign Ministers approved the Commission's programme for the supply at reduced prices of a certain number of foodstuffs taken from Community stocks. These include, among other things, 175,000 tonnes of barley, 25,000 tonnes of rye, 50,000 tonnes of sugar, 30,000 tonnes of butter, 50,000 tonnes of meat (pork and beef) and 3,000 tonnes of powdered milk. The prices are between 10% and 15% below those obtained on world markets. Furthermore, several EEC member countries will grant Poland officially-backed

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- (1) In addition to Poland, the following countries took part in the meeting: Federal Republic of Germany, Austria, Belgium, Canada, Denmark, Finland, France, Italy, Japan, Norway, Netherlands, Sweden, Switzerland, UK and USA.
- (2) The Poles recently presented a financing programme for 1981 which provides for the rescheduling of \$4.4 billion associated with the granting of new, officially-backed export credits worth \$3.4 billion. But it is not certain that this scheme will be approved by the Western creditors.
- (3) On 30th September 1980, Poland's total net debt with the banks reporting to the BIS was \$14.7 billion (source: BIS).

N A T O   C O N F I D E N T I A L

-13-

N A T O   C O N F I D E N T I A L

-14-

C-M(81)23

export credits to cover the cost of these deliveries. The possibility of further substantial aid to Poland from the Community remains however uncertain if only because of the possible reactions it might entail among certain Third World countries. But the Community does seem to be considering the question.

(ii) TREND OF INTERNAL IMBALANCES ON CERTAIN CONSUMER MARKETS

29. The full effects of the pay increases granted to the 12 million wage earners in the socialised sector will hit the market in 1981. The authorities anticipate an increase in income of 17% (i.e. 290 billion zlotys) over the full year, whereas the value of goods and services offered for sale is only expected to rise by 3%. According to the Ministry of Internal Trade the market supplies in January and February 1981 increased by 1.6% while purchasing power rose by 12.5%.

30. In the absence of genuine corrective mechanism (despite government endeavours to encourage savings, the latter will probably mop up only a small fraction of surplus spending power), the problem of imbalance between the supply of and demand for consumer goods could become even more acute in the short term. Regardless of whether or not these imbalances are camouflaged by an increase in inflationary pressures, they will mean either more imports<sup>(1)</sup> or the extension of existing shortages (and their corollary, the black market) with the adverse effects which the latter have for the consumer.

31. The problem of the imbalance between supply and the demand for consumer goods is heightened by the physical shortage of certain foodstuffs for which the poor harvest results provide the main explanation. Following a drop of 1.4% in 1979, overall agricultural output fell back sharply in 1980 (-9.6%) mainly as a result of bad weather. The grain harvest in particular (18.3 million tonnes) was 19% below the plan targets and the potato crop (used extensively as a substitute for animal fodder) proved disastrous (45% below 1979 levels) while the sugar beet crop was one third below the levels of the previous year. The shortage of fodder will have led to an increase in the number of animals sent for slaughter and this, after a fleeting improvement, will mean a greater shortage of meat supplies on the consumer market. According to official forecasts, meat production could drop by about 20% in 1981 (representing a fall in volume terms of between 400 and 450,000 tonnes) to no more than 1.9 million tonnes.

(1) The authorities are already expecting an increase of \$600 million in imports of foodstuffs during 1981 (source: report by the commission on the implementation of the Szczecin Agreements, Trybuna Ludu 30th January 1981).

N A T O   C O N F I D E N T I A L

-14-

N A T O   C O N F I D E N T I A L

C-M(81)23

-15-

32. Apart from meat, certain other foodstuffs are also in short supply (oil, butter, salt, sugar and vegetables in particular). According to information from Western sources gathered in Poland, the food supply situation which had improved somewhat in January 1981 has since deteriorated and in early March was even worse than in November and early December 1980 when the previous consumer "low" was recorded. The population is still able to feed itself but only at the cost of enormous effort and inconvenience. Although minor differences may exist from one town to the next, the country as a whole seems to be suffering from shortages of more or less the same magnitude. There is little likelihood of improvement in the short term except as regards butter (as a result of imports from the EEC) and the hope that the introduction of the meat rationing scheme will at least reduce the time spent on buying this item(1)(2).

33. An additional factor in the growing scarcity of consumer goods, which is hard to quantify but probably far from negligible at regional level and for quality items, is the closure of German markets to visitors from Poland.

34. One of the consequences of the growing number of food items (as well as of other consumer goods) in short supply is the apparent return of speculation (one of the features of which is the exorbitant level of prices charged on authorized private markets) and the expansion of parallel markets(3). This development of the black market, coupled with the adverse effects of the systematic hoarding probably being practised by certain individuals, could lead to even greater shortages fuelled by the holders of scarce items as well as to the disruption of the marketing networks and of the distribution of everyday consumer items.

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- (1) After repeated delays, meat rationing (which was part of the packaged demanded by the Gdansk strikers) will be introduced on 1st April 1981, in principle for three months.
- (2) Time spent queuing for everyday items has also contributed to the fall in individual productivity.
- (3) Official concern over the growth of speculation and the determination to keep it in check has been widely reported recently (early March) in the Polish press. Given the persistence of shortages, however, the margin for official manoeuvre is limited. For example, tighter controls on the prices charged on authorized private markets could well lead, in the first instance, to a drop in the activity of the latter which, in turn, would benefit the black market.

N A T O   C O N F I D E N T I A L

-15-

N A T O   C O N F I D E N T I A L

-16-

C-M(81)23

35. In view of these difficulties, the authorities appear determined to make a further effort on behalf of agriculture, particularly by reducing investment in this sector apparently at a slower rate than total investment(1). Given the complexities of the issue, however (e.g. small size of private plots), agricultural recovery will only be feasible in the long term and at great cost. In the shorter terms, ad hoc measures may be adopted with a view to encouraging private production. For instance, producer prices of a number of items (meat, milk, vegetables) have recently been raised by a significant margin.

(iii) TREND OF INDUSTRIAL ACTIVITY

36. Industrial production in volume terms (quantified by industrial sales at constant prices) dropped by 1.3% in 1980(2). This is mainly the consequence of the social unrest last Summer: apart from the production losses stemming directly from the work stoppages, there is also the fact that the strikes contributed to the disruption of the economy and the exacerbation of some of its chronic problems. Thus, in some instances delivery delays have not been fully offset by the stock change adjustment mechanism and in several cases shortages of both domestic and imported raw materials as well as intermediary goods have accentuated traditional bottlenecks. Likewise, disruptions in the transport system can only have made the difficult situation in this sector even worse. A source of perhaps even greater concern is the continuing deterioration of the country's industrial activity: in the first quarter of 1981 output dropped in real terms by 10% in comparison with the corresponding period of 1980.

37. This continuing negative growth rate at a time when work stoppages were almost completely over could point to disorganization within the economy and would seem to be due to a combination of factors. To begin with, a number of enterprises are finding it difficult to keep going owing to the lack of raw materials, energy and intermediate items which, in turn, may be aggravated by excessive stock-piling by other industrial establishments in anticipation of what is regarded as a possible period of crisis. Furthermore, the expansion of economic activity continues to be hampered by the shortcomings of the transport system: this sector continues to be in trouble mainly because of inadequate maintenance and a shortage of spare parts. The failure to offset the reduction in working hours by productivity gains in certain areas is also a source of production losses.

(1) According to official Polish sources, agriculture's share of investment expenditure should rise from about 20% between 1976 and 1980 to 30% during the period 1981-1985.

(2) In 1979, the same aggregate rose by 2.8%.

N A T O   C O N F I D E N T I A L

-16-



N A T O C O N F I D E N T I A L

C-M(81)23

-17-

38. A case in point is coal production trends. Since September 1980, Poland has been having the greatest difficulty in obtaining a sufficient level of output in the mines mainly following the abolition of the four-shift system and work on Sundays and public holidays, the effects of which were exacerbated by a fall in productivity which in itself perhaps was partly generated by the switch-over to a new shift system and the ensuing disruption of work. Total output for the whole of 1980 totalled only 193 million tons compared with 201 million tons in 1979 and the 207 million tons provided for in the plan. Given the priority assigned by the government to the satisfaction of domestic demand (industry and heating), this drop in production has hit exports and called into question the country's ability to fulfil certain supply contracts as well as leading to a loss of earnings mainly in convertible currency(1).

39. The outlook for coal mining in 1981 is uncertain to say the least. The recent adoption of a decree introducing a 37½ hour working week for miners working below surface may have an even worse impact on ore output unless the tendency noted in February 1981 for voluntary work to be done on Saturdays at double normal rates becomes more marked. Be that as it may, extrapolation of average output at the end of February would give a yearly figure of about 171 million tons(2) which is only 4 million tons higher than the projection of domestic consumption provided for in the plan(3). Should this downward movement (by comparison by 1980) continue, it will undoubtedly lead not only to a loss of earnings in terms of exports but also to new constraints on industry as a consequence of the increased difficulty of obtaining an essential intermediate item. The fall in Polish coal deliveries will likewise hamper production in other COMECON countries.

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(1) In 1979, Poland exported 41.4 million tons of coal of which 26.5 million tons worth \$1.1 billion, went to the West. Statistics available for 1980 indicate that deliveries totalled 31 million tons, which is 10.1 million tons down on the previous figure.

(2) 155 million tons during the 5-day working week and 16 million tons on Saturdays.

(3) The plan targets for 1981 are believed to be 177-178 million tons (including 16 million on Saturdays). Forecasts of internal demand are for 167 million tons.

N A T O C O N F I D E N T I A L

-17-

N A T O C O N F I D E N T I A L

-18-

C-M(81)23

40. Generally speaking, it would appear that the return to work and the initial implementation of the government's concessions have not been followed by productivity increases; in fact the opposite seems to be the case if current levels are set against those obtaining before the start of the protest movement in the Summer of 1980. This drop is probably due in part to disruptions in patterns of work created by changes in the organization of production (e.g. following a reduction in working hours). There is also the question of whether there is a greater inclination among certain wage-earners to work harder now that the strikes are over or whether, on the contrary, they are spending more time in discussing within their new trade unions. Last but not least, the impact (which is hard to assess) of certain psychological attitudes of part of the working population cannot be overlooked. It is not unlikely that certain of the values inherent in the system are being called into question by the man in the street and this could have a negative influence on productivity.

GOVERNMENT ECONOMIC POLICY

41. The Government's economic strategy does not appear to have been worked out in full. As far as 1981 is concerned, the intention seems to be, inter alia, to reallocate resources by means of a 15% reduction in investments. Agriculture will apparently be given priority mainly in the form of an increase in the supply of fertiliser and equipment; privately owned farms will be encouraged and credits have been set aside to allow them to increase capital expenditure by 20%. Successful implementation of the target of a 16% increase in agricultural output will depend extensively, apart from favourable weather conditions, on the ability of other sectors to supply fertiliser and equipment and on the farming community's confidence in the government. The volume of industrial output will probably be on a par with 1980 levels; a downward trend is expected in the mining sectors but a 4-5% increase is hoped for in the production of consumer goods. A less optimistic view expects national income to decrease by at least 4% in 1981.

42. The introduction of reforms in the system of economic production and management could in theory help reduce Poland's economic difficulties. A series of measures effective as from 1st January 1981, which come within the framework of the "little reform", point to the government's awareness of the need to loosen the centralized hold on directives and on the controls exercised over the various enterprises country-wide. These measures should, inter alia, give enterprises greater autonomy in deciding on the size of the work force and the apportionment of wages; if they are

N A T O C O N F I D E N T I A L

-18-

N A T O   C O N F I D E N T I A L

C-M(81)23

-19-

actually applied and if managers are able to make the most of liberalization regardless of chaotic conditions, the above-mentioned measures should have a favourable effect on productivity. The Poles themselves admit, however, that January's small economic reform has had little impact so far this year because of the enterprise's lack of preparation and disregard of the reform by many enterprises. It is furthermore believed that a decentralization of the economy at a time of economic crisis could result in even more chaos.

43. For the longer term, a broader programme of reform geared, inter alia, to a three year stabilization plan (1981-83) is being contemplated. Among the most important aspects of this programme are the decentralization of economic decision-making for the benefit of enterprises and the assignment of greater importance to economic variables, such as prices and taxes, in the choice of these economic decisions. The application (which is still hypothetical) of such a programme would not seem feasible however until 1982-83. Furthermore, the effects on the economy of these future measures would not be felt immediately. The possibility of implementing a full range of genuine economic reforms remains uncertain for a number of reasons, among them the divergence of views at leadership level and a shortage of economists of the "Kania school" capable of implementing the reforms and preventing them from running out of steam.

CONCLUSIONS

44. The economic situation in Poland remains problematical. The size of the problems facing the country results from the accumulation during the 1970s of a series of economic management errors, in particular at the level of resource allocation, and of which the bad consequences can only be eliminated by a long term process. The authorities are conscious of the need for thorough reforms but, in spite of a large number of proposals, they do not appear so far to have been able to establish a long term cohesive plan aimed at improving the economic structures. This absence is explained largely by the difficulty of reconciling the vital re-establishment of the economy and the satisfaction of social claims to which the leaders appear to have given priority until now. In any event the practical application - which still remains hypothetical - of a complete set of reforms will require time and, moreover, its positive effects will be felt only after a certain delay.

N A T O   C O N F I D E N T I A L

-19-

N A T O   C O N F I D E N T I A L

-20-

C-M(81)23

45. In the short term, there are therefore few elements indicating an improvement in the country's economy. In fact, the only way of reducing the difficulties seems to be a combination of the two following conditions: on the one hand that the leaders of the free trade unions manage to convince the work force that immediate sacrifices are the only possible way of ensuring a re-establishment of the economy in the medium term, and on the other, that the government be successful in obtaining a substantial rescheduling of the convertible currency debt so that the constraints from repayments do not inhibit the establishment of machinery to re-adjust internal equilibrium.

(Signed) J.-N. GIBAULT  
Chairman

N A T O   C O N F I D E N T I A L

-20-

N A T O   C O N F I D E N T I A L

-1-

ANNEX to  
C-M(81)23

Table 1

Poland's Foreign Trade with the COMECON Countries

Regional structure:

	Share in % in Poland's overall COMECON exports		Share in % in Poland's overall COMECON imports	
	1970	1979	1970	1979
Bulgaria	3.1	3.4	3.4	3.6
CSSR	12.3	12.5	13.1	11.2
GDR	15.3	12.6	16.9	14.8
Romania	3.7	3.7	3.0	3.5
USSR	58.1	61.2	57.4	60.8
Hungary	6.6	5.4	5.8	5.4
Cuba	0.1	0.7	0.2	0.4
Mongolia	0.2	0.1	0.1	0.1
Vietnam	0.7	0.4	0.1	0.2

Source: Statystyka Polski, Rocznik Statystyczny Handlu Zagranicznego  
(various years)

N A T O   C O N F I D E N T I A L

-1-

N A T O   C O N F I D E N T I A L

-2-

ANNEX to  
C-M(81)23

Table 2

Poland's Foreign Trade with the COMECON Countries

Goods structure:

	Export (%)		Import (%)	
	1970	1979	1970	1979
Fuel, Energy	11.4	10.1	9.6	21.7
Metallurgical industry	6.8	3.6	19.0	10.8
Electro-technical and engineering industry	56.3	63.1	46.0	48.8
Chemical industry	8.2	7.8	7.7	7.3
Non-ferrous metals industry	0.4	0.3	1.6	1.1
Wood and paper industry	1.7	1.2	2.4	2.2
Light industry	9.6	9.4	5.7	3.4
Food industry	2.1	2.1	2.2	1.8
Agriculture	2.7	1.6	4.3	1.7
Forestry	0.1	0.1	0.3	0.1
Other products	0.7	0.7	1.2	1.1

Source: Statystyka Polski, Rocznik Statystyczny Handlu Zagranicznego  
(various years)

N A T O   C O N F I D E N T I A L

-2-

N A T O   C O N F I D E N T I A L

-3-

ANNEX to  
C-M(81)23

USSR: Imports from Poland

Table 3

1979	in million rubles	Share in overall imports of these products (%)
Machines, equipment and means of transport	1,701	11.8
of which:		
Electro-technical equipment	137	28.3
Electric motors		4.0
Equipment for the food industry	55	16.6
Equipment for the textile industry	46	11.8
Equipment for the chemical industry	110	6.3
Equipment for the wood, pulp and paper industries	33	15.5
Equipment for the building material industry	12	12.5
Equipment for engineering and road construction	78	34.0
Agricultural machinery and equipment	77	11.5
Rolling railway stock and auxiliary equipment	152	26.7
Ships and ship's equipment	283	23.0
Iron rolling stock	36	3.1
Non-ores, clay minerals and alumina	34	30.2
Chemical products	11	1.2
Lacquers and paint	50	23.4
Clothing	215	27.5
Drugs	139	28.5

Source: Vneshnyaya Torgovlya SSSR, Statisticheskiy Sbornik 1979

N A T O   C O N F I D E N T I A L

-3-

N A T O   C O N F I D E N T I A L

ANNEX to  
C-M(81)23

-4-

Table 4

USSR: Exports to Poland

1979	in million rubles	Share in overall exports of these products (%)
Machines, equipment and means of transport	985	13.2
of which:		
Underground and surface equipment	28	13.1
Equipment for the textile industry	34	21.8
Rolling bearing	29	31.9
Tractors	57	21.0
Rolling railway stock	91	43.1
Trucks and complete assembly parts	124	30.1
Oil and oil products	1,109	7.6
Gas	198	9.5
Iron ore (13.4 million tons)		34.4
Non-ores, clay minerals and alumina	45	6.1
Crude iron	79	31.1
Iron rolling stock	137	10.9
Chemical products	25	4.3
Potassium salts (1 537,000 tons)		32.2
Cellulosis (95,500 tons)		14.0
Cultural and household goods	109	22.9

Source: Vneshnyaya Torgovlya SSSR, Statisticheskiy Sbornik 1979

N A T O   C O N F I D E N T I A L

-4-



N A T O   C O N F I D E N T I A L

-5-

ANNEX to  
C-M(81)23

Table 5

GDR: Imports from Poland

1978	in million rubles	Share in overall imports of these products (%)
Hard coal including anthracite (1 278,000 tons)		21.5
Hard coal coke (494,000 tons)		19.0
Steel pipe 2nd processing stage (217,200 tons)		65.2
Building machinery	17.6	21.5
Cutting machine-tools	4.7	4.3
Machines and equipment for the textile, clothing and leather industries	6.2	7.8
Passenger cars (982 ea)		10.4
Hoists and conveyors	11.1	8.3
Products of the knitting, hosiery and clothing industry	16.3	17.3

Source: Calculated on the basis of the Statistical Yearbook of  
the GDR 1979

N A T O   C O N F I D E N T I A L

-5-

N A T O   C O N F I D E N T I A L

ANNEX to  
C-M(81)23

-6-

Table 6

GDR: Exports to Poland

1978	in million rubles	Share in overall exports of these products (%)
Cutting machine-tools	28.1	8.4
Machines and equipment for the textile, clothing and leather industries	25.0	11.6
Machines and equipment for the food industry	21.5	15.9
Passenger cars (13,500 ea)		14.6
Agricultural machinery and tractors	26.2	5.5
Pesticides and insecticides	3.1	5.7

Source: Calculated on the basis of the Statistical Yearbook of the  
GDR 1979

N A T O   C O N F I D E N T I A L

-6-

N A T O   C O N F I D E N T I A L

-7-

ANNEX to  
C-M(81)23

Table 7

CSSR: Imports from Poland

1979	in million rubles	Share in overall imports of these products (%)
Raw materials and mineral fuels	103	3.3
of which:		
coal, coke, briquets	71	40.0
Machines and vehicles	501	14.6
of which:		
electr. machines and switching equipment	152	51.9
motor vehicles	41	10.8
Chemical products	15	2.1

Source: Calculated on the basis of the Yearbook of Foreign Trade  
of the CSSR 1980

N A T O   C O N F I D E N T I A L

-7-

CSSR: Exports to Poland

1979	in million rubles	Share in overall exports of these products (%)
Raw materials and mineral fuels	15	0.6
Rolling material		5.7
Thick and thin plate		7.3
Electric energy		13.7
Machines and vehicles	459	10.3
of which:		
trucks		14.0
motorcycles		20.7
rolling bearing		20.4
Chemical products	28	5.6
Woollen fabrics		6.6
Shoes		2.3

Source: Calculated on the basis of the Yearbook of Foreign Trade of the CSSR 1980