

3 Internationalization of a Post-Communist Economy – Opportunities and Threats: The Case of Poland

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Introduction

Until 1990 when the transition towards market orientation began, the Polish economy had been to a large extent closed as regards to its ties with the external environment. Development processes occurring in Poland after World War II bore many signs of autarchy. Economic cooperation with foreign countries outside the Council for Mutual Economic Assistance (CMEA) was very limited and unsatisfactorily used to accelerate the economic growth and increase economic effectiveness. Potential advantages from the international division of labor were not used properly. Poland's share in the world exports and imports was very low. The structure of foreign trade was distorted. The exports of Poland and other Central and Eastern European (CEE) countries to the OECD were much below the level determined by economic factors, while the exports to the CMEA countries were much higher.

One of the characteristic features of the market transformations of the Polish economy is the fact that it is becoming more and more open, i.e., the economic ties with foreign partners are being developed very quickly. There are many forms of internationalization of the Polish economy. Two of them deserve particular attention: trade exchange and foreign direct investment (FDI). Their dynamic development offers many advantages to the Polish economy. At the same time, however, there exist certain threats that, in extreme case, may undermine or destroy the advantages coming from the open economy.

In the post-communist countries the processes of internationalization are of specific nature as they occur in the conditions of very deep restructuring of the internal system of regulation from the administrative-bureaucratic to market oriented. The following problems are touched upon in this chapter:

- Premises for deeper internationalization of competitive relations.
- Most important problems of the development of Polish foreign trade in the period of market transformation of the economy.
- Main aspects of FDI in Poland.

Internationalization of Competition versus Transformation of a Post-Communist Economy

Internationalization of competition is not a new process. One can say that it begins when enterprises traditionally functioning on the internal markets in their home countries start economic operations (trade, production) abroad. These processes began to appear on a larger scale in this century. Internationalization of competition also embraced, although for obvious reasons to a limited extent, the Polish enterprises operating in the whole post-war period when foreign trade was a state monopoly. From the viewpoint of the Polish enterprises the beginning of market transformation of the Polish economy resulted in much wider and more extensive processes of internationalization of competition. In the above-mentioned context one may ask a question – what kind of premises influence the range and acceleration of internationalization of competitive behavior of Polish enterprises. It seems that these premises belong to two categories: the premises of specific character for Poland and other post-communist countries, and non-specific premises, generally pertaining to the evolution of international economic relations on a global scale. Specific premises of internationalization are as follows: opening of the post-communist economies, liquidation of the CMEA, and tendencies towards economic integration with Western industrialized countries. The second group of premises covers various aspects of the progressive globalization of economic activities and attempts of a more liberal organization of economic relations between all the countries in the world.

The concept of opening of the economy is being implemented in most post-communist countries. The programs of fiscal and monetary stabilization are carried out along with liberalization of a broadly defined foreign policy. The main measures in this field include: introduction of (limited) convertibility of the national currency, introduction of relatively liberal customs tariffs, abolishment (to a considerable extent) of non-tariff instruments of exports and imports regulation, demonopolization of foreign trade, implementation of the principle of economic freedom in the sphere of economic relations across national borders (Gorynia and Otta, 1995a; Gorynia and Otta, 1995b).

Abandoning the instruments of central regulation, a typical characteristic of command economies, resulted in the fact that home exporters and importers 'got closer' to the foreign markets. For the exporters this meant above all full self-financing with no possibility of subsidies. On the other hand, imports became a real threat for the home producers who frequently lost their share in the home market because of the free access to convertible currencies for financing imports.

Moreover, the liquidation of CMEA contributed to the internationalization of competition of formerly existing and new businesses. CMEA can be defined as an enclave of non-market behaviors of supranational scale. On the one hand, CMEA brought to member countries among other benefits access to massive, secure markets, and access to 'cheap' raw materials. On the other hand, there was no motivation to introduce innovation, to develop new products, and improve their quality. At the same time the binding principles of exchange (procedure of determining the lists of commodities, yearly protocols, way of establishing prices, exchange rates, etc.) led to a completely blurred calculation of effectiveness of the economic ties between member countries. Thus, one can state that the liquidation of CMEA facilitated the transition to market orientation and the introduction of competitive economic relations by firms in the former communist countries.

A very significant premise for the internationalization of competition of post-communist enterprises is the attempt for economic integration with the European Union (EU). This integration means a quicker and more complete opening of the national CEE economies towards EU partners. It creates both great opportunities and immense threats for the enterprises in the countries that strive for this integration. Some of these opportunities are already experienced by Polish enterprises. Hypothetically, the access to the immense EU market should be easy. However, the abolishment of administrative barriers and customs barriers does not necessarily guarantee success. The rest belongs to the enterprises themselves. They have to develop and rely on their competitive advantage. Threats stem from the resignation of the protection of home producers and their exposure to a direct rivalry with EU competitors. The effects of such a procedure will probably be of twofold. The new competitive challenges will enforce some Polish companies to become more competitive. Others will not be able to cope with the strong competitive pressures that will not positively affect their international competitiveness.

As mentioned above, the general non-specific premises for the internationalization of competition are, among others, connected with progressive and more intensive globalization processes. Globalization of markets results from the fact that some firms, operating on an international

scale, carry out global strategies the implementation of which is a result of the changing conditions of international competition leading to a fiercer competitive struggle (Gorynia and Otta, 1989). Globalization is basically connected with demand premises. The main premise of this kind is an idea of 'the global product' according to which, at least in economic sectors, we deal with the uniformity of needs on the international scale (Levitt, 1983). The uniformity of needs creates the grounds for the uniformity of product that in turn provides an opportunity to achieve advantages of scale. In this way the demand premises of globalization are linked with the premises of effectiveness. The following factors are most frequently mentioned among those that favor globalization: the possibility of advantages of scale, necessity to allocate large outlays for research and development and low costs of transport (Hout, Porter and Rudden, 1982). The global strategy is defined as a strategy thanks to which a firm operating internationally tries to achieve competitive advantage either through concentrated configuration (distribution, location of particular kinds of the firm's economic activity) or coordination (a way of coordination of similar or related types of the firm activity). Both ways may be applied simultaneously (Porter, 1986).

Internationalization of competition has been and will be favored by the regulations of international economic relations determined by the General Agreement on Tariffs and Trade (GATT) at the Uruguay Round and recently by the World Trade Organization (WTO) (Kaczurba and Kawecka-Wyrzykowska, 1995). Their aim is a full liberalization of the international economic and trade cooperation. Successive lifting of barriers in the turnover will result in a wider range and more intensified processes of the internationalization of competition.

Foreign Trade in the Polish Economy under Transformation

Sphere of Regulation

Until recently Poland's foreign economic policy, and more specifically foreign trade policy, has been linked to the program of stabilization. The main aim of the stabilization program was to curb inflation.

The aim of the changes introduced in the sphere of regulations in the years 1989–1997 was to transform the Polish economy from a basically closed one into an open one.

The foreign trade policy in the above-mentioned period was not uniform. The following stages can be identified (Płowiec, 1997):

- Stage I (from the beginning of 1990 until August 1991) was characterized by liberalization of commodity prices, lifting of subventions (including export subventions), strong devaluation of the zloty, introduction of its external convertibility and a wide liberalization of imports.
- Stage II (from September 1991 until the end of 1993) when adjustment to be associated with the EU was commenced, despite the lack of positive changes in the structure and volume of the existing production capacities.
- Stage III (commenced in 1994) is marked by a clearly more active trade policy and the stimulation of restructuring of production and exports.

In the economic policy carried out in the years 1990–1997 four main trends can be differentiated (Otta and Gorynia, 1993):

- Fiscal and monetary stabilization.
- Liberalization of trade.
- Institutional transformation.
- Restructuring.

The most significant changes in the sphere of foreign trade regulations are enumerated below in chronological order:

- Liberalization of most prices, elimination of subventions (1990).
- Substantial devaluation of the zloty and introduction of its internal convertibility (1990).
- Extreme liberalization of imports (1990).
- Introduction of a new customs tariff based on terminology used by the EU (1991).
- Introduction of the principle of crawling devaluation of the zloty (1991) and simultaneous jumping devaluations (1991–1993).
- Implementation of transition agreement with the EU on the creation of free trade zones concerning industrial goods (1992). This agreement anticipated that the process of reduction of customs rates on industrial goods would last 10 years. The agreement contained an asymmetric schedule of the reduction of customs rates favorable for Poland.
- Implementation of other agreements similar to that with the EU with EFTA and CEFTA countries (1993).
- Replacing the turnover tax imposed, among others, on imported goods with VAT (1993); the basic rate of this tax amounts to 22% and the preferential rate – to 7%.

- From the beginning of 1993, due to difficulties with the balance of payments, temporary introduction of 6% import tax was agreed on with GATT (this tax was lifted at the beginning of 1997).
- In order to facilitate the restructuring of industry, from the year 1993 the suspension of duties and customs quotas (particularly for raw materials) was applied.
- Introduction of incentives for investment – a possibility to deduct part of investment outlays from taxable income (1994).
- Systematic slowdown in the rate of devaluation of the zloty (1994–1998).
- Poland has gained the status of a market economy country and starts participating in the process of reduction of customs and non-customs barriers in trade relations with WTO member countries.
- February 1, 1994 – Implementation (after a two-year period of ratification) of the European Agreement determining the principles of Poland's association with the EU; unilateral protective clauses for Poland as a weaker partner deserve attention. They include: the clause of the restructuring of industry, a protective clause as regards the establishment of EU enterprises in Poland and the clause enabling Poland to apply restrictions in hard currency turnover until the Polish currency is fully convertible.
- Liberalization of the import of goods caused by a simultaneous implementation of the resolutions of the Final Act of the Uruguay Round, European Agreement, agreements with CEFTA and EFTA (in the period 1995–1998).
- Liberalization of hard currency turnover including, among others, the introduction of convertibility of the zloty (June 1995) according to the standard of the article eight of the IMF Statutes and abandoning of the obligatory reselling of hard currency to banks by the exporters (1995) as well as liberalization of the export of capital from Poland.
- Application of export supporting instruments, such as export credits and insurance of export credits (the range of application of these tools is very narrow).
- Flexibility of the exchange rate policy, i.e., replacing the official exchange rate with the central exchange rate that fulfills the function of a preferential rate while determining the limits of fluctuations (1995).
- Poland's membership in the OECD thanks to which the conditions of access of foreign capital to the Polish market were eased (1996).

Generally, the stated changes in the sphere of regulation should be evaluated as positive. These changes created a basis for Poland's larger

participation in the international division of labor. Polish economy became more open to international economic cooperation. This creates many opportunities for Polish companies simultaneously posing some threats.

Dynamics of Turnover against the Background of the Economic Situation

Table 3.1 presents the indicators of the dynamics of exports, imports, GDP, industrial production and unemployment in the years 1990–1997. In this period exports (after a considerable initial growth in 1990) declined in the years 1991–1993 by 2.5% annually. However, from the beginning of 1994 the indicators of export dynamics were already positive.

Throughout the whole analyzed period imports grew dynamically. It should also be underlined that in the period 1995–1997 the turnover of the Polish foreign trade increased much quicker than the turnover of the world economy or of the EU.

Geographical Structure of Trade Exchange

Table 3.2 presents the geographical structure of Poland's foreign trade turnover in 1989–1997.

A characteristic feature of the Polish foreign trade in the 1990s was a strong reorientation of trade from East to West. In 1988 exports to CEE countries constituted about 40% of the total exports, and in 1993 – only 13%. From 1994 this share was steadily growing and amounted to 24% in 1997. In 1988 the share of exports to the EU countries amounted to approximately 28% and in 1993 it reached over 63%. In 1995 these exports amounted to as much as 70% and afterwards they started to decline. It is also easy to notice a steady declining tendency in the share of the developing countries in the Polish exports.

As regards imports, there was a visible growth trend in the share of imports from EU countries in the total imports. This tendency broke down in 1996. On the other hand, the share of CEE countries in Polish imports was declining until 1993 and afterwards it began to increase.

Numerous articles referring to the so-called gravitation model indicated the necessity for a strategic turn in the Polish foreign trade (reorientation from East to West). Political factors were responsible for the fact that the volume of Polish trade with CMEA countries before 1990 was too large, while that with the OECD countries was too small as compared with the level determined by economic factors (Winters and Wang, 1994).

Table 3.1 Dynamics of the volume of Polish exports and imports, GDP and industrial production (previous year=100), and unemployment rates (in %)

Specification	1990	1991	1992	1993	1994	1995	1996	1997
Exports	113.7	97.6	97.4	98.9	118.3	116.7	109.7	113.7
Imports	101.5	137.8	113.9	118.5	113.4	120.5	128.0	122.0
GDP	92.9	93.0	102.6	103.8	105.2	107.0	106.1	106.9
Industrial production	76.8	92.0	102.8	106.4	112.1	109.7	108.3	110.8
Unemployment rate	6.5	12.2	14.3	16.4	16.0	14.9	13.2	10.5

Sources: Assessment of social-economic situation in 1997 along with elements of the forecast for 1998, Government Center for Strategic Studies, Warsaw, February 1998; Polish foreign trade in 1997, Annual Report, Foreign Trade Research Institute, Warsaw, 1998.

Table 3.2 Geographical structure of Poland's foreign trade turnover in the years 1989–1996 (calculated on the basis of current prices expressed in zlotys, shares in %)

Specification	1989	1990	1991	1992	1993	1994	1995	1996	1997
Total exports	94.7*	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Highly developed countries:	49.1	67.1	73.8	71.9	75.1	75.4	75.0	71.7	69.0
• EU countries	32.1	45.6	55.7	58.0	60.2	62.7	70.0	66.4	64.0
• EFTA countries	10.9	16.8	14.1	10.3	7.9	8.2	1.6	2.2	1.5
Developing countries	10.3	10.6	9.4	12.7	11.6	10.1	7.7	7.8	6.6
CEE countries and ex-USSR	35.1	22.3	16.8	15.4	13.3	14.5	17.3	20.5	24.4
• including CEFTA	7.1	5.1	5.3	5.1	4.8	4.8	5.4	6.1	6.8
Total imports	92.7*	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Highly developed countries:	53.0	65.3	68.4	72.4	76.2	75.1	74.3	73.6	73.5
• EU countries	33.8	47.2	49.7	53.2	57.2	57.5	64.6	63.9	63.8
• EFTA countries	14.7	13.8	14.8	12.9	11.2	11.2	3.1	2.5	2.5
Developing countries	6.9	13.3	12.3	11.3	10.3	10.6	10.3	10.9	11.6
CEE countries and ex-USSR	32.7	21.4	19.3	16.3	13.5	14.3	15.4	15.5	14.9
• including CEFTA	7.3	4.5	4.0	4.1	3.6	4.3	5.6	5.8	6.3

* Excluding the former communist countries.

Sources: Perczyński, 1997; Statistical Yearbooks of the Central Statistical Office.

It must be underlined that the gravitation model makes it possible to measure only distortions in the geographical structure of foreign trade. This model, however, gives no suggestions about the extent of the inherited deformations in the commodity structure of trade exchange with foreign countries.

Commodity Structure of Trade Exchange

Table 3.3 presents the structure of Polish exports and imports in terms of economic sectors. However, the data of such a high level of aggregation are difficult to interpret.

More detailed articles on the changes in commodity structure of the Polish foreign trade in the years 1990–1997 indicate two main factors (Płowiec, 1997):

- Primitive character of the commodity structure of exports.
- Growth of import penetration in certain groups of commodities.

The phenomenon of the so-called backwardness of the structure of exports is obvious. It means that the significance of highly processed export goods and the share of added value were lower in comparison to the value of material and energy intensive export products of relatively low technological level (Perczyński, 1997).

According to the most recent data the share of electromechanical goods in Polish total exports declined to 22.4% in 1997. In the same year growth dynamics higher than the average for all Polish exports were reached in the groups of agricultural-food products, furniture, wood and wood products as well as chemical and metallurgical products (Piotrowski, 1998).

Moreover, some attention should be paid to a positive phenomenon in the structure of imports. Recent years have witnessed a high dynamics of growth in investment import. In the structure of imports according to ways of their use the share of investment import went up from 13.0% in 1995 to 15.3% in 1997.

Trade Balance

Table 3.4 presents the development of Polish trade balance and the relations between repayment of debts and revenues from the export of commodities in the period 1990–1997.

Table 3.3 Structure of exports and imports according to branches in current prices in the years 1989-1997

Specification		1989	1990	1993	1994	1995	1996	1997
Fuels and power	I	12.4	20.7	12.6	10.5	9.2	9.2	8.8
	E	9.6	10.1	9.5	8.9	8.0	6.7	6.5
Metallurgical industry	I	8.8	6.9	4.6	4.9	5.8	5.1	5.0
	E	10.5	14.6	14.6	13.8	12.2	10.4	10.9
Electromechanical industry	I	36.3	39.8	34.4	33.8	35.1	38.2	41.6
	E	38.4	29.3	25.8	25.8	27.6	29.6	27.7
Chemical industry	I	15.2	11.6	17.5	19.2	19.2	18.0	18.0
	E	10.5	12.0	9.8	10.0	11.4	11.4	11.6
Extractive industry	I	1.3	1.3	2.1	2.4	2.6	2.5	2.6
	E	1.3	1.7	3.3	3.4	3.2	3.3	3.1
Wood and paper industry	I	1.9	1.6	3.6	3.9	4.7	4.4	4.5
	E	2.9	4.1	8.3	9.9	11.3	11.4	12.1
Light industry	I	7.6	6.1	10.0	10.6	10.0	8.6	7.9
	E	5.5	6.4	15.3	14.8	14.1	14.0	12.9
Food industry	I	9.5	7.8	7.7	7.8	6.8	6.6	6.1
	E	9.6	10.0	9.1	9.7	8.5	9.6	11.3
Other branches of industry	I	1.7	2.1	3.0	3.0	2.7	2.6	2.5
	E	0.6	0.6	0.8	0.8	0.9	1.2	1.2
Agricultural products	I	4.9	2.0	4.2	3.3	3.5	4.2	2.7
	E	4.1	5.4	3.0	2.5	2.5	1.9	1.7

Sources: Statistical Yearbook of Foreign Trade 1997, Warsaw, 1997; Statistical Yearbook of Foreign Trade 1998, Warsaw, 1998.

The trade deficit, worsening from year to year, has been the main factor influencing the balance of current turnover. In 1997 this balance amounted to US\$ – 4.3 billion that constituted 3.2% of the GDP. The factor which smoothes the effect of high deficit in the trade exchange is the revenues from the so-called cross-border trade.

Negative trade exchange balance is created mainly through the exchange with the EU countries. According to customs statistics, which register the flow of goods, not the actually made payments, the deficit in trade with the EU increased from US\$ – 7.3 billion in 1996 to US\$ – 10.5 billion in 1997. It should also be underlined that a significant factor influencing the Polish trade exchange balance is the balance of exchange of FDI in Poland with export activities. In the period 1994–1997 it amounted to US\$ – 2.8 billion in 1994, US\$ – 3.9 billion in 1995, US\$ – 7.4 billion in 1996, and US\$ – 10.0 billion in 1997. Substantial import requirements of the firms with foreign capital result from modernization of their production potential (investment import) and a high demand for the import of materials (Durka, 1998).

The high and still worsening deficit in the balance of current turnover is the biggest threat for the further steady economic development of Poland. Official publications show that the countries which opened their economies and joined the European Union (Spain, Portugal, and Greece) also noted a considerable worsening of their current trade balance. Similarly, they have also financed the current balance deficit with the surplus of the capital balance (Nowicki 1997). Implementation of an appropriate macroeconomic policy is necessary in such a situation to prevent overheating of the economy and inflation related tensions.

Foreign Direct Investment – Regulations, Inflow, Effects

Evolution of the Legal Institutional Conditions for the Inflow of Foreign Capital

A major feature of the Polish economic transition is the systematic opening of the economy to foreign investment. This is favored by the changes in regulations on this sphere of economic cooperation with foreign countries.

The following factors had the most powerful influence on the opening of the country to inflows of foreign capital in the form of FDI (Kubiela, Monkowski and Jackson, 1996):

- Liberalization of legal regulations concerning the inflow of FDI.

Table 3.4 Commodity payments and relation between debt repayment and export revenues in the years 1990–1997

Specification	1990	1991	1992	1993	1994	1995	1996	1997
Commodity payments in billion USD								
• Exports revenues	10,863	12,760	13,997	13,585	16,950	22,878	24,420	27,233
• Payments for imports	8,649	12,709	13,485	15,878	17,786	24,705	32,574	38,522
• Balance	2,214	51	512	-2,293	-836	-1,827	-8,154	-11,289
Relation between debt repayment and export revenues in %	6.8	10.5	11.0	13.2	8.7	9.0	10.2	8.3

- Liberalization of international trade exchanges and of the principles of currency convertibility.
- Privatization of state-owned enterprises.

Before the beginning of Polish transition to market, there existed a so-called enclave model concerning FDI's preferential treatment vis-à-vis the other types of investment (Samonis, 1992). The legal-institutional changes in the conditions for the inflow of foreign capital meant abandoning this model in favor of treating FDI in the same way as the domestic investments.

The enclave model functioning in Poland had the following characteristics:

- Participation of foreign capital was permitted only for small foreign businesses or in larger joint venture companies with a minority share of foreign capital in the ownership structure.
- Complicated procedure of granting licenses.
- Wide range of sectors where the penetration of foreign capital was forbidden or restricted.
- Obligation to resell foreign currency revenues from exports to hard currency banks.
- Restrictions on foreign profit repatriation.
- Restrictions in the purchase of real estate.
- Tax holidays in terms of income tax.

The 1991 Act on the activities of economic entities with foreign capital created identical treatment of FDI companies and firms with domestic capital. The most important features of the Act regulating foreign investments are as follows:

- No restrictions to the amount of invested capital and the transfer of profit.
- Necessity to obtain licenses from the state when the property of state owned legal entities is made available to companies with FDI. Licenses are granted by the minister of State Treasury in response to the application of an economic entity.
- Abandoning of the principle of automatic three-year tax holidays.
- Full guarantee of compensation in case of expropriation.
- Foreign entities can start their activity in two major forms: limited liability companies and joint stock companies (this is an exception to the principle of national treatment approved by the OECD).
- In the field of lotteries and betting FDI is impossible.
- Other restrictions in observing the national treatment principle refer to the maximum share of foreign capital in the initial capital of the

company, for example in telecommunication services the limit is up to 49%, in other communications – up to 33%, and in radio and television industries – up to 33%.

Volume and Structure of Foreign Direct Investments

The data on the value of FDI in Poland are presented in Table 3.5. These data show that in the first half of the 1990s the volume of investment in Poland was by no means impressive.

Table 3.5 Stock of FDI in Poland in 1989–1997 (in US\$ million)

Year	Investment above 1 million US\$	Investment below 1 million US\$	Joint investment
1989	8	1	9
1990	105	15	120
1991	324	45	369
1992	1,408	197	1,605
1993	2,828	396	3,224
1994	4,321	605	4,926
1995	6,832	956	7,788
1996	12,028	1,999	14,027
1997	17,705	2,882	20,587

Source: Olesiński and Pac-Pomarnacki, 1998.

Recently Poland has become a leader among the countries of Central and Eastern Europe in terms of the FDI inflow and stock, overtaking Hungary (see Table 3.6). However, it must be kept in mind that in the calculation of the value of foreign investment per capita, Hungary, Slovenia and the Czech Republic rank before Poland.

Table 3.6 Inflow of foreign direct investment in the chosen countries of CEE in the years 1993–1996 (in US\$ million)

Country	1993	1994	1995	1996
CEE	6,287	5,882	14,317	12,261
Albania	58	53	70	72
Belarus	10	15	7	18
Bulgaria	55	105	90	150
Czech R.	654	878	2,568	1,200
Estonia	162	215	202	138
Lithuania	30	31	73	152
Latvia	45	214	180	152
Moldova	14	12	67	292
Poland	1,715	1,875	3,659	5,196
Russia	700	638	2,017	1,800
Romania	94	341	410	624
Slovakia	199	203	183	150
Ukraine	200	159	267	440
Hungary	2,350	1,144	4,519	1,982

Source: Olesiński and Pac-Pomarnacki, 1998.

Table 3.7 Entities with the share of foreign capital against the total number of entities registered in the REGON system in the years 1991–1997 (the state as of December 31)

Year	Number of entities with foreign capital*	Share in total number of national economy entities (%)
1991	5,583	4.1
1992	10,817	6.9
1993	15,814	8.6
1994	20,324	10.4
1995	24,635	11.7
1996	29,157	12.2
1997	33,459	12.8

* Includes commercial law firms with foreign capital and foreign small businesses.

Source: Chojna, 1998.

According to the data from the end of 1997 in the recording system REGON, there were jointly registered 33,459 entities with FDI, of which 32,941 were commercial law companies and 518 were small foreign businesses (Chojna, 1998). The FDI entities constituted 12.8% of the total number of the registered businesses in the national economy (excluding investments made by individuals and civil associations), against 12.2% in the end of 1996, 10.4% in the end of 1994 and merely 4.1% in the end of 1991 (see Table 3.7). However, it must be underlined that the very fact of registering the company in the REGON system does not mean engaging in a sustained economic activity. A part of the registered entities have not undertaken any economic operations, others have suspended their activities, while some have been liquidated or gone bankrupt. Foreign investors who have put in capital of at least US\$ 1 million have been monitored by the State Agency for Foreign Investment (PAIZ). Table 3.8 presents the number of investors originating from a country that has made more than ten investments in Poland. The table shows that the investors from Germany, the USA, France, and Italy occupy the leading positions.

Table 3.8 The number of largest foreign investors in Poland in the years 1993–1997 (the state for the end of the year)

Countries	1993	1994	1995	1996	1997
USA	45	53	62	77	91
Germany	34	53	79	113	134
International concerns	8	11	14	15	15
Italy	3	6	17	29	44
France	19	20	29	42	51
Holland	9	11	13	32	34
Great Britain	12	15	21	21	26
Austria	10	18	23	30	34
Sweden	8	9	16	30	36
Denmark	5	10	13	16	22
Finland	4	5	6	9	11
Belgium	0	11	13	14	15
Canada	12	13	18	19	19

Source: Olesiński and Pac-Pomarnacki, 1998.

When considering the value of the capital invested by the end of 1997, the list of foreign investors with at least US\$ 1 million invested capital is dominated by US firms, followed by German and multinational corporations (Table 3.9).

Table 3.9 List of the largest foreign investors in Poland in the period 1993–1997 considering the actual investments made – as of year end status

Countries	1993	1994	1995	1996	1997
USA	1,028.00	1,413.70	1,698.00	2,965.60	3,981.80
Germany	212.00	386.40	683.00	1,524.40	2,104.90
Multinationals concerns	290.00	808.30	1,101.00	1,493.00	1,654.00
Italy	270.00	365.80	495.00	1,223.80	1,636.30
France	177.00	268.10	574.00	899.90	1,616.40
Holland	233.00	240.40	408.00	9,512.70	1,213.60
South Korea	5.00	5.00	69.00	184.50	1,077.80
Great Britain	68.00	112.20	368.00	509.00	1,002.00
Austria	195.00	159.70	248.00	315.30	660.30
Sweden	71.00	86.70	179.00	361.30	565.80
Switzerland	51.00	112.00	196.00	357.70	445.30
Australia	5.00	6.30	298.00	328.10	354.10
Denmark	24.00	60.20	124.00	238.20	306.80
Norway	42.00	46.90	29.00	80.10	240.00
Ireland	7.00	7.00	47.00	105.70	191.20

Source: Olesiński and Pac-Pomarnacki, 1998.

The list of most significant foreign investors is presented in Table 3.10. It must be underlined that from 1994 the first ten most important investors have not changed. FIAT, EBOR, Polish/American Entrepreneurship Fund, IPC, Coca-Cola and ABB are undisputed leaders. The new firms on the list are Daewoo, PepsiCo, ING Group and Philip Morris.

Table 3.10 The largest foreign investors in Poland – actual investments made by the end of 1997

Investor	US\$ Million	Branch
FIAT	1,141.9	Car industry
Daewoo	1,011.3	Car industry
EBOR	616.5	Banking
PepsiCo	412.0	Food industry
IPC	370.0	Paper industry
ING Group	350.0	Banking
Coca-Cola	285.0	Food industry
ABB	282.0	Engineering industry
Philip Morris	282.0	Tobacco industry
IFC	277.3	Financial intermediation
Nestle	248.0	Food industry

Source: Raport o inwestycjach zagranicznych w Polsce, "Rzeczpospolita" nr 157, 7 lipca 1997.

In terms of economic sectors the structure of foreign investment in Poland looks interesting. At the end of 1997 there were three dominating sectors: manufacturing, financial intermediaries and services (see Table 3.11).

Significance and Effects of Foreign Direct Investment

The role of foreign direct investment can be defined through:

- The share of these investments in the GDP and the total number of investments.
- Creation of new jobs and labor productivity.
- The share of entities with foreign capital in Polish foreign trade.

Table 3.11 Foreign investment in economic sectors as of the end of 1997 (in US\$ million)

Economic sectors	Investments	Investment plans
Manufacturing including:	11,042.0	5,782.6
• Food products, beverages, tobacco	3,276.9	1,109.4
• Means of transport	2,510.5	1,969.5
• Paper, publishing and printing activity	1,158.4	293.3
• Chemicals, chemical products	1,087.4	518.0
• Other non-metallic raw materials	971.4	864.5
• Optical and electrical appliances	667.4	260.8
• Metals and processed metallic products	375.3	184.3
Financial intermediation	3,130.4	422.0
Trade and repairs	1,408.5	2,033.8
Transport, storage and telecommunications	734.5	299.4
Construction	554.9	511.8
Service and municipal activity	354.6	232.0
Hotels and restaurants	305.5	431.0
Electricity, gas and water supply	96.5	1,040.0
Real estate servicing	38.3	24.5
Mining and extraction	16.2	0.0
Agriculture and fisheries	15.0	0.0
Total	17,705.4	10,777.1

Source: Olesiński and Pac-Pomarnacki, 1998.

- Comparison of invested capital in FDI companies with the investment volume in other enterprises.
- Comparison of the financial performance of FDI entities vis-à-vis other entities.
- Contribution of FDI to the privatization of the Polish economy.

The share of foreign direct investments in the GDP and in the total number of investments is presented in Table 3.12. In the period 1994–1996 this share constantly increased and in 1997 started stabilizing.

Table 3.12 Relations between the inflow of FDI^a in the GDP value and the total investment made in the period 1994–1997 (in %)

Specification	1994	1995	1996	1997 ^b	1994-1997 average
FDI/GDP	1.6	2.1	3.9	4.2	3.1
FDI/total investments	10.0	12.9	21.3	20.6	17.2

^a Include foreign direct investments exceeding the value of 1 million USD.

^b Estimates.

Source: Chojna, 1998.

The data on employment in the companies with foreign capital (Table 3.13) show that the share of these entities in the overall employment is not high although it is steadily increasing. This may mean a much better utilization of labor resources in the FDI companies.

Firms with FDI have a clear advantage over other companies in terms of labor productivity measured by revenues calculated per one employee. In 1996 labor productivity in the firms with foreign capital was twice as high as the average in the total number of entities in the Polish economy.

It should be stated that the contribution of FDI companies to the revenues from all economic entities in Poland is steadily increasing. In 1996 this share amounted to approximately 20% of the revenues of all the entities that submitted their statistical annual reports. In the period 1994–1995 this index amounted to 12.4% and 16.6% respectively.

FDI companies are more likely to export their produce than firms with domestic capital. In 1996 the share of export revenues of FDI companies amounted to 13.9% from their total revenue, whereas the one for companies with domestic capital was 8.8%. However, it should be

mentioned that in the period 1994–1996 the foreign revenue of FDI companies showed a slightly declining trend from 15.6% to 13.9%.

The share of firms with foreign capital in the total Polish exports in 1997 amounted to 43.0%. In terms of import the share was 49.9% (Durka and Chojna, 1998).

Intense international trade activities of FDI companies resulted in a negative trade balance on company level. This negative value was steadily growing from US\$ – 2.8 billion in 1994 to US\$ – 10.0 billion in 1997.

Table 3.13 Employment in FDI companies in the period 1991-1996 in relation to total employment in the Polish economy^a as of December 31

Year	Number of employees (in 1000s)	Share in total employment (in percentages)
1991	117.6	1.3
1992	230.0	2.0
1993	310.2	2.8
1994	373.9	3.3
1995	495.3	4.4
1996	525.9	4.6

^a Excluding individual firms, national defense and internal affairs sectors.

Source: Chojna, 1998.

The share of imported elements of the supply chain (raw materials, parts and components) in the total imports of FDI firms amounted to approximately 60% of all inputs while the same in the firms with Polish capital was approximately 70% in 1997.

Companies with FDI are characterized by high investment activities. The contribution of FDI companies to the overall volume of investment increased from 11.6% in 1994 to 20.1% in 1996.

When considering the financial results of FDI companies, a positive trend can be observed. In the period 1994–1997 profitability rates were considerably improved and from negative indicators in 1994 they became positive. It should be emphasized that in companies with FDI the profitability indicators look particularly good compared with those of domestic companies.

The share of foreign capital in the privatization of the Polish economy also deserves attention. Out of 203 companies that underwent FDI privatization in 1990–1997, 104 strategic investors who purchased their

shares were Polish and 83 were foreign investors, whereas in 16 companies the shares were bought by foreign and Polish investors (Włodarczyk, 1998). In the course of direct privatization of small and medium sized enterprises (the so-called selling path) 80 enterprises were sold to foreign investors. Under the Program of the National Investment Funds, out of 93 portfolio companies 32 were sold to foreign entities.

Opportunities and Threats of Internationalization

International trade and the inflow of FDI are considered to be the two most important forms of internationalization of the Polish economy. The extension of both forms of international economic ties offers a number of advantages and creates many opportunities. However, one must not overlook the threats related to the progressive internationalization.

Internationalization opportunities and advantages have been well identified by the theories of international trade and the theories of foreign direct investment. Here, we shall only indicate these factors that are particularly significant in the case of Poland.

The opportunities and advantages resulting from the development of international trade in the period of transformation are as follows:

- Export is one of the significant factors stimulating the economic growth. Achieving a much higher increase of the GDP is a condition for the overcoming of the so-called product gap that separates Poland from highly developed countries.
- Revenues from export are an important source of the financing of foreign purchases.
- Exports make it possible for the enterprises to achieve advantages of scale against limited extent and demand on the domestic market.
- Exports force the producers to improve the quality of production to meet the high quality expectations of foreign markets.
- Thanks to imports the economy has an access to modern machines and equipment as well as to high quality materials. This is particularly important during a period of rapid economic growth which is expressed in the high rate of GDP growth and the high rate of investment.
- Making part of import purchases on credit increases the country's accumulation capacities that are insufficient to finance the high rate of economic growth.
- Import discipline home producers in terms of pricing and quality assurance and is also the means of diffusion of foreign investments in the Polish economy.

- Imports facilitate the maintenance of equilibrium on the home market.

A rapid growth of foreign trade in the period of transformation is also a source of the following threats:

- Persistence and worsening of foreign trade deficit which in the long run may break down the balance of payments.
- ‘Backwardness’ of the structure of exports – smaller importance of the high-tech products and the smaller share of the so-called added value in favor of material- and energy-intensive products of relatively low technological level.
- There are no good prospects for development of external demand in the economic sectors where Polish export capacities are most important and in which the development is most dynamic, whereas in the economic sectors where growth of foreign demand is expected Poland has limited possibilities to increase supply.
- Trespassing in some economic sectors, particularly the most technologically advanced, the critical threshold of the penetration of imports in relation to the home production that leads to elimination of certain fields from the Polish industry.

The positive effects of FDI inflow into the Polish economy are unquestioned. They provide Poland with an opportunity to bridge the civilization gap separating the country from the highly developed economies relatively quickly. Advantages resulting from the inflow of foreign investments can be listed as follows:

- Increased accumulation of capital and opportunities for new investments.
- Modernizing and restructuring the industry through the transfer of modern technologies, know-how, and management methods.
- Improved quality of products made by FDI and domestic companies – pressure on the local suppliers for new quality standards of products, materials, components and servicing.
- Creating demand for new products.
- Access to organized networks of sales in the foreign markets.
- Acceleration of privatization processes.
- Creating new jobs and increasing employees’ qualifications.

Experiences of the countries that receive foreign investments on a wide scale also show some threats:

- Locating environmentally unfriendly production in the host country.

- Use of obsolete production technologies in the host country.
- Transfer of incomes in the form of transfer prices.
- Limitation of investment duration – an attitude to ‘skim the cream’ in a short period of time, not re-investing the profits followed by a rapid divestment.
- Investments ‘blocking’ the local competitors in order to increase import penetration on the market of the host country.

In the context of the opportunities and threats connected with a wider opening of the transformed Polish economy to internationalization, a question is raised about the appropriate economic policy that should be adopted.

Maintaining the high rate of economic growth and also the necessity to service a considerable foreign debt are responsible for the fact that rapid development of export is a must for the development of the Polish economy. Therefore, a pro-export policy is a high priority for the national economy. Such a policy should be a part of the overall economic policy, non-contradictory and coherent with all state economic activities. The fact that Polish exports must grow is generally unquestioned. This, however, does not mean that the export sector should be a kind of enclave strongly subsidized by the non-export sector. This kind of solution was frequently tested in the period of communist economy and its results were unsatisfactory.

The pro-export policy should not be of segmental character. The best pro-export policy is a comprehensive economic policy oriented towards the improvement of effectiveness, efficiency, and growth of international competitiveness of the Polish economy. The economic policy, which concentrates on stabilization measures, is not sufficient to achieve this objective. It should be supplemented with the policy of institutional transformation and restructuring.

In the present reality of Poland and its external environment, the growth of competitive production of goods and services marketable both on internal and external markets is the fundamental strategic problem (Płowiec, 1997).

Thus, two general recommendations to economic policy makers can be made (Gorynia, 1996):

- The state’s economic policy should support competitiveness of enterprises.
- The economic policy should favor competitiveness in an integral way, i.e., it should not differentiate in an unjust way the instruments that favor competitiveness in two dimensions – competitiveness of

exporters to foreign markets and competitiveness of producers in the home market.

The above-mentioned criteria are fulfilled by the concept of liberal-institutional industrial policy (Gorynia, 1995). The essence of the liberal-institutional industrial policy is in promoting a widely understood growth and entrepreneurship. Four main trends can be distinguished in the liberal-institutional policy:

- The policy promoting development.
- The policy of supporting competition.
- The policy of privatization.
- The policy of promoting economic self-governance.

The following groups of activities can exemplify the policy of promoting development:

- Promotion of investment.
- Promotion of innovation, research and development.
- Supporting education and training.
- Distribution of economic risk.
- Supporting the construction of the systems of information and its diffusion.

The above-mentioned main directions of the impact of economic policy, defined as the liberal-institutional industrial policy, are characterized by a general, universal approach, which basically does not provide for individualization of the policy measures according to particular economic mezzo systems. However, it seems that in some cases selective application of the chosen instruments can be admissible (Gorynia, 1995). Such cases can be listed as follows:

- Market failure.
- Occurrence of the second-best situation.
- Protection of infant industries.

Some concepts of the economic policy identify the pro-export policy with a selective industrial policy. Some economists put forward a concept of deliberate construction of comparative advantages in the chosen fields of advanced technology and strategic integration with the world market, not the integration with the world market based on the current premises which are unreliable while making decisions of strategic character (Hubner, 1994).

In the discussions concerning the borderline of the pro-export policy and the selective industrial policy there appears the concept of the so-called strategic trade policy (Brander and Spencer, 1985). According to this concept export subsidies may seem to be an attractive measure of the policy because they improve a relative position of home producers in non-cooperative competition with foreign firms, thus enabling them to get a bigger share of the market and to increase profits. The subsidies change the initial conditions of competition. The terms of trade in the subsidizing country get worse but their welfare can increase because under imperfect competition the price exceeds extreme costs.

Numerous arguments can be listed against the strategic trade policy understood in the above-mentioned way. The most important arguments are as follows:

- The governments of rival countries may also start subsidizing. 'The war of subsidies' will result in the decline of prices in the international market and may lead to a decline of welfare in the countries using subsidies.
- A target country of the subsidized exports can take up some retaliation measures (customs, compensation charges, quotas, embargoes, etc.).
- Subsidies granted simultaneously in several countries can lead to over-investment in the subsidized economic sectors.
- Low prices of the subsidized goods on the international market can be a false signal for the potential investors from third countries.
- Ensuring means for the subsidies is an essential problem for the countries with an unbalanced budget.
- According to the binding international agreements export subsidies are forbidden. Such is the attitude of the Code on Subsidies of the GATT Tokyo Round. Agreement on Subsidies and Compensative Duties from the Final Act of the Uruguay Round binding under the WTO introduces quite a precise and extended definition of subsidies.

The Polish policy of foreign trade should, therefore, develop in the following directions (Płowiec, 1997):

- Lifting barriers for exports development: barriers related to the quality of production, barriers related to the terms of payment offered (export credits, insurance of export transactions), barriers of infrastructural character.
- Development of non-tariff forms of the protection of producers against dishonest competition or against excessive imports.

The economic policy should also concentrate on creating the economic climate that attracts foreign investors. Foreign direct investments should prove particularly useful in the development of managerial staff and operational personnel; improvement of the professional level of management; transfer of production and marketing technologies as well as management techniques; introduction of energy and material-saving technologies, friendly to the natural environment; further privatization of the economy and in the long run they should also improve the balance of trade.

Those policies to international trade and FDI into Poland will increase the degree of internationalization of the Polish economy and its competitiveness in the international marketplace.

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