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Impact of Financial Deregulation on Monetary and Economic Policy in the Czech Republic, Hungary and Poland: 1990-2003

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Abstract

The three countries took different stances in regards to economic policy; the Czech Republic pursued a shock therapy regime which aimed to stabilise the economy, Hungary's policy was more relaxed whilst Poland had an aggressive reform programme. Regarding monetary policy the Czech Republic used the discount rate as a tool for monetary policy, Hungary used indirect monetary policy and Poland had strict monetary policies which raised interest rates and devalued the zloty. After financial deregulation the impact of economic and monetary policy led to positive economic growth in the Czech Republic year on year. Hungary had a similar experience whilst Poland had an initial high increase in economic growth. This reduced over time but they still recorded positive economic growth over the period studied.

Keywords: Transition Economies, Financial Deregulation, Economic Growth, Eastern Europe.

JEL CODES:

E Macroeconomics and Monetary Economics

E2 Macroeconomics: Consumption, Saving, Production, Employment, and Investment

E4 Money and Interest Rates

E5 Monetary Policy, Central Banking, and the Supply of Money and Credit

G Financial Economics

G15 International Financial Markets

G21 Banks; other Depositary Institutions, Micro Financing, Mortgages.

1.0 Introduction

By the early 1990's all three countries had moved from centrally planned economies to market driven economies. Though the three countries had similar experiences under socialism, there were also marked differences between them. Poland which had the largest population, recorded the lowest income per capita of the three countries[1]. Whilst all three countries income levels were high for CEEC's (Central and Eastern European Countries) they represented between one quarter and one third of that of the advanced Western countries. The Czech Republic at the onset of restructuring, was the most politically stable with both Hungary and Poland experiencing significant political instability. Hungary was the first country to introduce economic reforms as far back as 1968. In 1982 Poland began to liberalise whilst the Czech Republic waited until the early 1990's before they undertook any move from central planning. Since mid 1990 Hungary accelerated its gradualist approach to reform whilst Poland launched a radical plan of transformation in 1990. The Czech Republic's approach resembled Poland's fast track plan and both countries implemented large adjustments to prices. Hungary's approach to price liberalisation was again a gradual one. Poland had the higher monetary overhang and the highest inflation rates. Though the other two countries experienced higher inflation than previously, the Czech Republic had moderate inflation with price liberalisation. Hungary already had high inflation rates in the 1980's which peaked in 1990-1991. Their approach of gradual liberalisation meant that there was constant pressure on prices and expectations of high inflation rates in the future.

This paper outlines the economic and monetary policies followed by the Czech Republic, Hungary and Poland from 1990-2003. It examines the impact of financial liberalisation on economic and monetary policies and vice versa. Further it questions the effect of credit
growth on economic growth and development. The paper is organised as follows:

Section 2 examines economic and monetary policies following by the three countries and the resulting impact on economic growth

Section 3 investigates credit policy in the three countries and the impact on economic growth and development

Section 4 summarises and concludes the paper

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[1] Anderson, R.A. and Kegels, Chantal. *Transition Banking, Financial Development of Central and Eastern Europe*, Oxford, Clarendon Press, 1988

2.0 Policies pursued by the three countries

2.1 Economic Policy in the Czech Republic

The Czech Republic pursued a shock therapy regime[2]. Whilst they did not suffer from major macroeconomic imbalances they still actively followed a policy of stabilising the economy. Real wages decreased by 6.3% in 1990 and 40% in 1991. By the end of 1991 most prices had been deregulated and most controls and imports and exports had been eliminated. Liberalisation of trade and capital led to trade increasing in the Czech Republic from 66.9% of GDP to 104.2%[3]. At the end of 1993 the private sector accounted for 52.8% of total employment[4]. Between 1993-1995 there was a large net surplus on both the current and financial accounts and by 1995 official foreign reserves rose to $13.8 billion[5]. In 1995 the Czech Republic exported 36.6% of total exports to Germany[6]. They imported 30.3% of total imports from Germany with 10% from Slovakia and 7.3% from Russia and 6% from Austria. They received 16% of total FDI (Foreign Direct Investment) to CEEC's in 1996. Most of this was from German investors who were the largest investors in the Czech Republic from 1990-1996. Official foreign reserves rose to $13.8 billion by 1995 though by the end of 1997 they had fallen to $9.7 billion[7]. FDI was $1.4 billion in 1996, $1.3 billion in 1997 and $2.6 billion in 1998. Imports included communications equipment, metalworking machinery, chemicals and transport equipment. 1998 import figures were: machinery and transport 39%, other manufactured goods 21%, chemicals 12%, raw materials and fuels 10% and food 5%. By 1999 the ratio of FDI to GDP was 9% and 5.3% in 2000. The private sector's share of GDP was 70.8% in 2001[8]. (See Appendix A: Tables 1.1 and 1.2 for

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[2] King, Lawrence P. "Explaining Postcommunist Economic Performance", William Davidson Institute, University of Michigan Business School, Working Paper No. 559, May 2003

[3] Estrin, Saul. "Competition and Corporate Governance in Transition", William Davidson Institute, University of Michigan Business School, Working Paper Number 431, December 2001

[4] Op. Cit. Anderson, R.A. and Kegels, Chantal. 1988

[5] Zoubir, Y. and Lhabitant, F.S. *Doing Business in Emerging Europe*, Palgrave, Macmillan, 2003, pp1-52

[6] Kurz, Constance and Wittle, Volker. "Using Industrial Capacities as a Way of Integrating the Central and East European Economies", edited by Homi Katrak and Roger Strange, in *Small Scale Enterprises in Developing and Transitional Countries*, Basingstoke, Palgrave, 2002, pp63-95

[7] Op. Cit. Zoubit, Y and Lhabitant, F.S. 2003

[8] www.economist.com/countries.CzechRepublic/profits.cfm

Current Account figures and External Debt).

The Czech Republic which favoured a mass privatisation approach, had overtaken Poland by the mid 1990's[9]. However by 1998 they saw a collapse in the capital markets and bank finance. There was widespread insider trading and non-performing loans increased. The Czech government was criticised for maintaining too strong a boundary between the state and society and this was believed to have impeded development. A powerful central policy making apparatus remained whilst there were too rapid attempts to privatise firms. Kogur and Spicer[10] found that capitalist economies do not work without the development of capital markets. There was failure to built deep capital markets in the Czech Republic and no reliable networks existed. There were no developed bank ties, and no markets or institutional experience for trading stocks. They did not have transparent market exchange of ownership of rights and most trading took place outside formal markets. This contributed to the economic stagnation of the Czech Republic.

Table 1.1

Industrial Production in the Czech Republic 1994-2003[11]

1994	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
91.347	90.51	92.3	96.42	96.01	94.87	100	106.53	116.61	123.43

The Czech Republic recorded growth in years 2000 and 2001[12]. In 2001 growth reached 3.6% with no significant effects on inflation which varied between 4-6%. Annual growth rates of exports and imports fell due to the slowdown in economic growth abroad. The Czech's economy grew by 2.9% in 2003 and the main driving force was private consumption (mainly households) and exports[13]. Private consumption grew by 5.4%,

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9 McDermott, Gerald. A. "Institutional Change and Firm Creation in East-Central Europe: an Embedded Politics Approach", William Davidson Institute, University of Michigan Business School, Working Paper No 590, 2003

10 Kogur, Briuce and Spicer, Andrew. "Institutional Technology and the Chains of Trust: Capital Markets and Privatisation in Russia and the Czech Republic", William Davidson Institute, University of Michigan Business School, Working Paper Number 291, March 1999

11 International Financial Statistics, International Monetary Fund

12 Czech National Bank, Annual Report 2001, IV Macroeconomics and Monetary Developments

13 European Economy, European Commission, Directorate General for Economic and Financial Affairs, Economic Forecasts, Spring 2004, No 2/2004

exports grew by 6.7% whilst government consumption was 0.0%. Real disposable income had increased and along with low nominal interest rates this led to an expansion of consumer credit, despite rising unemployment at 7.8%. Inflation was -0.1%

Table 1.2
Imports of Goods and Services at 1995 prices in the Czech Republic (national currency, annual % change)[14]

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
3170	3286	3792	4644	6894	8172	9676	10691	11693	12655	13583

Increases in wages were recorded once the economy was restructured. Between 1990 and 1994 there was 100% increase in gross nominal wages reflecting the need for wages to move with prices increases following liberalisation. By 2000 this wage level had increased by another 97%.

Table 1.3
Real Wages Per Head in the Czech Republic (annual % change)[15]

1995	1996	1997	1998	1999	2000	2001	2002	2003
9.3	7.8	-0.2	-0.4	2.9	3.4	3.4	6.6	6.5

In real terms the wages were more modest when inflation rates are taken into account. Minus figures were recorded in 1997 and 1998 with low figures recorded in 1999-2001 and rising figures to over 6% in 2002-2003.

Table 1.4
Growth of GDP/Components in the Czech Republic[16]

	92	93	94	95	96	97	98	99	00	01	02	03
Exports of goods and services	9.5	15.8	1.7	16.7	8.2	9.2	10	6.1	17	11.9	2.8	4.9

14 European Economy, European Commission, Directorate General for Economic and Financial Affairs, No 6, 2003
15 Ibid, European Economy, 6/2003
16 Ibid, European Economy, 6/2003

Imports of goods and services	29.7	23.8	14.7	21.2	13.4	8.1	6.6	5.4	17	13.6	4.3	4.8
GDP	-0.5	0.1	2.2	5.9	4.3	-0.8	-1.0	0.5	3.3	3.1	2.0	2.2

Exports fluctuated and then overtook the amount of imports in 1997-1999. They reached a high of 17 in 2000 but fell between 2001-2003 reflecting difficult economic situations in other countries, especially in the rest of the EU.

Table 1.5

Persons in Employment in the Czech Republic (annual average)[17]

1995	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
4959	4968	4933	4863	4761	4728	4724	4760	4731

The Czech Republic did not suffer from employment problems like other former CEEC countries. Employment levels remained steady during the economic restructuring with a small increase in unemployment being experienced from 1997 onwards. This reflected the change in employment patters once the large state owned enterprises were restructured and privatised.

2.2 Monetary Policy in the Czech Republic

Throughout the nineties the Czech Republic's prices remained fairly stable but increased at the beginning of 1991 following price liberalisation. There was a tax on wage increases which stabilised the economy. In 1991 inflation was a massive 56.6% which fell to 10.7% by 1998[18]. In 1991 all credit ceilings were removed leaving banks to set their own deposit and lending rates[19]. In 1991 and 1992 the discount rate was used extensively as a tool for monetary policy and after 1993 an interbank money market and a secondary market for government securities emerged. By 1993 inflation accelerated with the introduction of VAT (see table 1.6 below). However by the following year inflation had halved with further reductions until 1997. 1998 saw an increase in inflation

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17 European Commission, Eurostat Yearbook 2004, The Statistical Guide to Europe, Data 1992-2002

18 Op. Cit. Zoubir, Y. and Lhabitant, F.S. 2003 PP1-52

19 Borish, Michael.s. et al, "On the Road to EU Accession, Financial Sector Development in Central Europe", World Bank Discussion, Paper No. 345, 1996

but there were large reductions in 1999-2000.

Table 1.6

Inflation in the Czech Republic

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
9.6	56.6	12.7	20.8	10	9.1	8.8	8.5	10.7	2.1	3.9

Source: World Bank Development Indicators, EBRD Transition Report 2000, William Davidson Institute at the University of Michigan Business School

In 2001 the Czech Republic experienced some inflation pressures in the middle of the year but they eased off towards the end of 2001 due to a fall in the major world economies.

Table 1.7

Interest Rate Spread in the Czech Republic

1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
7.038	6.0475	5.8375	5.75	5.489	4.7277	4.203	3.74	4.323	4.726	4.616

Source: International Financial Statistics, International Monetary Fund
Once the banks were permitted to set their own interest rate the spread began to fall. This reduction continued year on year though there was a slight increase in 2001.

2.3 Economic Policy in Hungary

Between 1990-1993 the economy declined by 18% but by 1994 growth had stabilised at 2.9%. 1.5% was recorded for 1995 and 1% in 1996. By 2000 GDP growth reached 5.5%[20]. Once trade and capital were liberalised Hungary's GDP increased. By 1991 it had increased by 38.9%[21] (from 54.9% to 93.8%). 30% of Hungarian exports went to Germany in 1995, 10.7% went to Austria and 8% to Italy. They imported 23.5% from Germany, 12.3% from Russia and 9.7% from Austria. In 1993 the private sector accounted for 59.4% of employment[22]. Hungary received the bulk of FDI for CEEC's in 1996 (40%). There were strong FDI inflows in 1999 but there were offset in 2000 by substantial portfolio equity outflows[23]. By 2000 net external debt as a percentage of

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20 Op. Cit. Zoubir, Y and Lhabitant, F.S. 2003

21 Op. Cit. Estrin, S. 2001

22 Op. Cit. Anderson, RA. And Kegels, C. 1998

23 IMF concludes Article IV Consultation with Hungary, International Monetary

GDP was half the 1995 level though it still remained high at 60%. By 2000 FDI was $27.4 billion[24]. Strong external demand boosted economic activity making Hungary one of the strongest performers in the CEEC region[25]. In 2001 Hungarian per capita GDP was 53% of the EU average[26]. Industrial output increased in 2002 with a 9.3% rise in food, drink and tobacco manufacturing and a 40% rise in machinery and equipment manufacturing[27]. In 2003 real GDP was 2.9% as investment was sluggish and there was a negative contribution from net exports.[28] The fiscal deficit reached 5.9% of GDP due to high current expenditures (social benefits and interest payments), weaker tax revenues (personal income and corporate taxes). The current account deficit reached 5.7% of GDP. Inflation reached 4.7%. The unemployment rate was 5.8%. See Appendix A Tables 1.3 and 1.4 and 1.5 for figures for Current Account Balance, External Debt and Foreign Debt.

Table 1.8

Industrial Production in Hungary 1990-2003[29]

90	**91**	**92**	**93**	**94**	**95**	**96**	**97**	**98**	**99**	**00**	**01**	**02**	**03**
65	53.4	49.7	51.6	56.4	59.9	61.5	68.1	76.5	83.9	100.2	104.2	107	113

Table 1.9

Imports of Goods and Services in Hungary at 1995 prices (national currency, annual % change[30])

91	**92**	**93**	**94**	**95**	**96**	**97**	**98**	**99**	**00**	**01**	**02**	**03**
5.4	0.7	20	8.8	21.2	10.4	23.1	25.2	13.3	19.4	6.1	6.1	8

Imports decreased by 20% in 2003 though this reduced to single figures by 2001

Fund, Public Information Notice (OIN), No 01/47, May 18 2001

24 Monthly Report, National Bank of Hungary, Statistical Department, 5/2002

25 IMF concludes Article IV Consultation with Hungary, International Monetary Fund, Public Information Notice (PIN), No 01/47, May 18 2001

26 Csajbok, A. and Scermely, A. “Adopting the Euro in Hungary: Expected Costs, Benefits and Training”, NBH Occasional Papers 24, 2001, Magyar Nemzeti Bank

27 Monthly Report, National Bank of Hungary, Statistical Department, 5/2002

28 Op. Cit. European Economy, 02/2004

29 Op. Cit. International Financial Statistics, International Monetary Fund

30 Ibid, IMF

reflecting the reduced need for Hungary to buy from abroad. As new companies emerged in Hungary there was increased scope of operations and increased domestic activity.

Table 1.10

Gross Nominal Wages in Total Economy in Hungary, Annual[31]

90	91	92	93	94	95	96	97	98	99	00
10571	13446	22294	22294	29173	33309	38900	46837	57270	67764	77187

Gross nominal wages increased almost threefold between 1990 and 1994. By 2000 it had more than doubled again.

Table 1.11

Net Nominal Wages in Total Economy in Hungary[32]

90	91	92	93	94	95	96	97	98	99	00
10108	12948	15628	18397	23049	25891	30544	38145	45162	50076	55785

Table 1.12

Real Wages per head in Hungary (annual % change)[33]

1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
2.1	-1.3	-4.8	-2.2	2.4	`0.3	-4.8	6.1	7.0	10.1	5.8

Above real wages fell in years 1994-1996, and 1999. Increases are recorded in other years with a 10% increase in 2002.

Table 1.13

Growth of GDP/Components in Hungary[34]

	92	93	94	95	96	97	98	99	00	01	02	03

31 Op. Cit. European Economy, 6.2003
32 Op. Cit. European Economy, 6/2003
33 Ibid. 6/2003
34 Ibid. 6/2003

Exports of goods and services	2.7	-10.3	13.6	47.5	12.6	22.3	18.9	12.4	21	8.8	3.8	4.1
Imports of goods and servics	0.7	20	8.8	21.2	10.4	23.1	25.2	13.3	19.4	6.1	6.1	8
GDP	-2.1	-0.6	2.9	1.5	1.3	4.6	4.9	4.2	5.2	3.8	3.3	2.9

Exports fluctuated over the years with large increases recorded in 1995. Imports also fluctuated with the level falling to 6% in 2001-2002.

Table 1.14

Persons in Employment in Hungary (annual average in 000)[35]

1995	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
3623	3605	3611	3675	3792	3829	3845	3856	3969

Employment increased year on year from the mid nineties onwards.

2.4 Monetary Policy in Hungary

The National Bank of Hungary's main instrument was the two week central bank deposit rate[36]. This rate was the policy rate that reflected the monetary policy stance. They also used the secured loan/deposit rate and the reserve rate. They NBH bond was sold along with the sale and purchase of government papers, and the active and passive repo. Potential instruments included the interest rate ceiling and floor, the Lombard loan, and refinancing facilities and rediscounting.

By 1991 Hungary had liberalised interest rates fully[37]. The National Bank of Hungary used indirect monetary policy from 1990 onwards and in 1993 repurchase and reverse repurchase agreements based on government securities were introduced. In January

35 Eurostat Yearbook 2004, European Commission, The Statistical Guide to Europe, Data 1992-2002

36 MNB, The Instruments of Monetary Policy, http://www.english.mnv.hu/module

37 Op. Cit. Borish et al, 1996

1991 Hungary's programme of restructuring included a devaluation of 15%, further liberalisation of prices (90% of the consumer basket) and restrictive fiscal, monetary and incomes policies[38]. Price liberalisation was extended at the end of 1990 and prices increased though subsequent inflation fell. In 1991 there was a tax placed on wage increases in excess of 28% in an effort to stabilise the economy.

On May 4th 2001 the intervention band of the forint was widened to +-15%. The exchange rate fluctuated from that time onwards within a narrow range. The National Bank of Hungary cut interest rates five times since 2001. Inflation in Hungary was 5.4% in 2002 and 5.2% in 2003[39]. The National Bank kept its key policy at 9.5% in 2002 and the exchange rate moved within its range of 240-245 forints per euro that year.

Table 1.15

Inflation in Hungary

90	**91**	**92**	**93**	**94**	**95**	**96**	**97**	**98**	**99**	**00**
33.4	32.3	21.6	21.1	21.2	28.3	23.6	18.3	14.3	10.1	9.5

Source: World Bank Development Indicators, EBRD Transition Report 2000, William Davidson Institute at the University of Michigan Business School

Table 1.16

Interest Rate Spread in Hungary

90	**91**	**92**	**93**	**94**	**95**	**96**	**97**	**98**	**99**	**00**	**01**	**02**	**03**
4.1	4.7	8.6	9.7	7	7.6	7	4.23	4.14	3.87	3.568	3.21	2.95	1.77

Source: International Financial Statistics, International Monetary Fund

The interest rate spread increased initially but by 1997 it had fallen to below 5%. This reduced further to under 2% as the Hungarian economy operated to meet the standards set out by the EU for entry in 2004.

38 Op. Cit. Anderson, R.A. and Kegels, C. 1988
39 Quarterly Report on Inflation, Magyar Nemzeti Bank, November 2002

2.5 Economic Policy in Poland

Poland implemented one of the more aggressive reform programmes after the collapse of the communist government in 1989[40]. It included macroeconomic stabilisation, microeconomic liberalisation and reform of the institutional structure of the economy. Poland experienced a post transformation slump between 1989-1991 (7.5% and 7% decreases in GDP in 1990 and 1991 respectively) though GDP growth reached 6.9% in 1997 and then fell to 4.8% in 1998[41]. In 1991 when trade and capital was liberalised Poland saw an increase from 32.7% of GDP to 43.6%[42]. Poland's private sector accounted for 57.6% of total employment in 1993[43]. By 1994 private enterprise accounted for more than 50% of national output and nearly 60% of employment. FDI increased rapidly and trade moved from CMEA (Council for Mutual Economic Assistance) to the West. The inflation rate declined by a factor of 20 to 38%. By 1994 Poland was the first country in the region to see real GDP exceeding the GDP level of 1989[44]. Also by the mid 1990's there were concerns that the economy was overheating. Prior to 1995 growth was export led and there was moderate growth in domestic consumption and investment. Investment then increased by over 20% between 1995 and 1997 then fell to 15% in 1998 and 1.4% in 2000. 38.5% of Polish exports went to Germany in 1995 and 5.6% to Russia and 4.9% to Italy[45]. 26.6% of Polish imports were from Germany with 8.5% imported from Italy and 6.7% from Russia. Poland received 25% of FDI for CEEC's in 1996 and this rose in 1997. By 1999 policy had shifted to boost domestic demand with interest rate cuts and real wages growth. By the end of the nineties Poland had reduced most of its trade links with Russia and was not duly affected by the 1998 rouble collapse. They had increased trade with Germany and the rest of the EU.

By 1998 Poland was one of the more robust East European economies which was accredited to the transparency in banking and finance and in the overall privatisation process. By 1998 the trade share of GDP was 47%[46]. At the end of 1998 Poland

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[40] Ghemawat, Pankaj and Kennedy, Robert E. "Competitive Shocks and Industrial Structure: the Case of Polish Manufacturing", William Davidson Institute, University of Michigan Business School, Working Paper No. 53, May 1997

[41] Blazca, George. "The Policy Business Scene in the Millenium", European Business Review, Vol 12, Issue 5, 2000, pp265-273

[42] Op. Cit. Estrin, S. 2001

[43] Op. Cit. Anderson, R.A. and Kegels, C 1988

[44] Lill, Bruno. "Economic Growth - GDP, Center for Markets in Transition", HSE, October 2001, http://www.balticdata.info/poland/macro-economics/poland/

[45] Op. Cit. Kurz, C and Wittle, V. 2002

[46] Angelucci, Manueal. Et al, "The Effect of Ownership and Competitive Pressure on

experience a deep depressed trade and current account and this continued in 1999. However by the end of the 1990's Poland was the economic leader of the three countries. It was argued that Poland's approach which included bank restructuring and support for new firms, facilitated negotiated restructuring and risk sharing[47] They created political conditions which were more conducive for institutional experimentation. Their economic policies included gradual ownership change with institutional policies that allowed the government to monitor each other's actions. Also they witnessed a decline of 20% in non-performing loans. Poland experienced a difficult year in 2001 and there was a large increase in the deficit[48]. There were large increases in non-interest State spending with increases in transfers and subsidies to households, the agricultural sector and state enterprises and wages. The cash deficit was around 5% of GDP, up 2.8% from 2000. After the slowdown of 2001-2002 Poland experienced a recovery in 2003[49]. Growth in 2003 was 3.75%, up from 1.4% in 2002. Growth was led by net exports and a depreciation of the zloty. The unemployment rate was 19.8%. By 2003 investment was stronger[50]. Interest rates fell and a depreciation of currency created a competitive position for Poland. See Appendix A Table 1.6 and Table 1.7 for figures for Current Account Balance and External Debt.

Table 1.17

Industrial Production in Poland 1994-2003[51]

1994	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
90.426	69.724	76.275	84.87	88.811	93.018	100	100.443	101.845	110.756

Table 1.18

Imports of Goods and Services at 1995 Prices in Poland (national currency, annual %

Firms Performance in Transition Countries: Micro Evidence from Bulgaria, Romania and Poland", William Davidson Institute, University of Michigan Business School, Working Paper No. 434, January 2002

47 McDermott, Gerald. "Institutional Change and Firm Creation in East-Central Europe: an Imbedded Politics Approach", William Davidson Institute, University of Michigan Business School, Working Paper No 590, 2003

48 Poland - 2002 Article IV Consultation Concluding Statement of the IMF Mission, IMF, March 14 2002, http://www.imf.org/external/np.ms/2002/031402.htm

49 Op. Cit. European Economy, 02/2004

50 Poland, Concluding Statement of the IMF Staff Mission, IMF, Warsaw, November 20, 2003, http://www.imf.org/external/np/ms/2003/112003.htm

51 Op. Cit. International Financial Statistics, IMF

change)[52]

91	92	93	94	95	96	97	98	99	00	01	02	03
29.7	1.8	13.1	11.3	24.2	28	21.4	18.5	1	15.6	16.1	-0.1	2.6

The level of imported fluctuated over the time period with a negative figure of change recorded for 2002 reflecting difficult conditions world wide. By 2003 imports had recovered to a positive figure.

Table 1.19

Gross Nominal Wages in the Total Economy in Poland[53]

1992	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**
289.7	390.4	525	690.9	874.3	1065.8	1232.7	1386.8

Gross nominal wages increased with liberalisation along with net nominal wages (see table 1.20)

Table 1.20

Net Nominal Wages in the Total Economy in Poland[54]

1990	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**
103	175.6	243.9	320.2	425.5	560.6	720.5	877.3	1026.7

Table 1.21

Real Wages Per Head in Poland (Annual % Change)[55]

92	**93**	**94**	**95**	**96**	**97**	**98**	**99**	**00**	**01**	**02**	**03**
20.1	1.1	1.8	5.37	7	5.1	4	5.8	1.5	8.1	2.8	2.4

1992 recorded a large increase in real wages but there was a marked reduction in this increase over the next few years. Moderate increases were recorded for years 2002-2003 which were more in line with changes in the rest of the EU.

Table 1.22

Growth of GDP/Components in Poland[56]

52 Ibid. IMF
53 Op. Cit. European Economy, 6/2003
54 Op. Cit. European Economy, 6/2003
55 Ibid. European Economy, 6/2003

	92	93	94	95	96	97	98	99	00	01	02	03
Exports of goods and services	10.8	3.2	13.1	22.9	12	12.2	14.3	-2.6	23.2	10.3	4.8	6.5
Imports of goods and services	1.8	13.1	11.3	24.2	28	21.4	18.5	1.	15.6	-0.1	2.6	4.3
GDP	2.5	3.7	5.3	7	6	6.8	4.8	4.1	4	1	1.4	3.3

The level of exports and imports increased by the mid nineties and fell considerably by 1999. 2000 saw a recovery in overseas trade with reduced figures for 2002-2003.

Table 1.23

Persons in Employment in Poland (annual average in 000)[57]

195	1996	1997	1998	1999	2000	2001	2002	2003
14791	14969	15177	15354	14757	14526	14207	13782	13627

Employment fell between 1995 and 2003 reflecting the change in employment levels as the impact of the restructured state owned enterprises affected the whole economy.

Table 1.24

Foreign Investment in Poland

	No of Registered Companies	Value of Foreign Investment ($ millions)
1990	2799	105
1991	4797	324
1992	10131	1408
1993	15167	3041
1994	19737	4321

56 Ibid. European Economy, 6/2003

57 Op. Cit. European Economy, 6/2003

1995	24086	6832
1996 (June)	25000	10155

Source: Polish Agency for Foreign Investment (PAIZ)

The number of registered companies involved in FDI in Poland increased eight fold by the mid nineties with the value of foreign investment increasing ten fold.

2.6 Monetary Policy in Poland

In Poland by 1990 interest rate ceilings were abandoned and banks set their own interest rates[58]. Direct controls over credit were replaced by indirect monetary instruments though inflation remained high and volatile. In 1991 Poland had strict monetary and fiscal policies. Interest rates were raised and the zloty devalued. Prices were liberalised along with the trade and foreign exchange system[59]. Banks used the National Bank of Poland's refinancing rate to determine their own interest rate though by 1992 market signals were used as a basis for interest rates. Open market operations grew and developed. In the 1990's the rate of inflation declined overall though it increased from 8.4% in 1999 to 11.6% in 2000[60]. Tight monetary policy leading to reduced domestic demand and investment and slow export growth, slowed economic growth to 4% in 2000. Economic growth was only 1.1% in 2001 and 1.3% in 2002.

Table 1.25

Inflation in Poland

90	**91**	**29**	**93**	**94**	**95**	**96**	**97**	**98**	**99**	**00**
555.4	76.7	45.3	37.6	29.5	19.9	14.9	11.8	7.3	9.9	

Source: World Bank Development Indicator, EBRD Transition Report 2000, William Davidson Institute at the University of Michigan Business School

The inflation rate fell from a high of over 500% in 1990 to under 20% by 1996. It then fell further to single digits which was more in line with rate in the rest of the EU.

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58 Op. Cit. Borish et al, 1996

59 Foley, Paul et al, "Economic Development in Poland: a Local Perspective", European Business Review, MCB University Press, Volume 96, Number 2, p23-31

60 Op. Cit. Zoubir, Y. and Lhabitant, F.S. 2003

Table 1.26

Interest Rate Spread in Poland

90	91	92	93	94	95	96	97	98	99	00	01	02	03
462.1	1.08	1.25	-1.124	.116	6.66	4.56	5.6	6.29	5.71	5.83	6.56	5.82	3.59

Source: International Financial Statistics, International Monetary Fund

Poland’s interest rate spread fell dramatically once interest rate ceilings were abandoned. They are now similar to other EU countries.

2.7 The Impact of Economic and Monetary Policy on Economic Growth

Czech Republic

Table 1.27

GDP Growth 1990-2003

91	92	93	94	95	96	97	98	99	00	01	02	03
12	16	11	34	15	14	7	6	3	12	8	3	6

Source: International Financial Statistics, International Monetary Fund

The Czech Republic experienced positive growth, year on year after financial deregulation took place. Although prices increased and unemployment also increased, the liberalised environment allowed the private sector to become more involved in all economic activity. Research suggests that the private sector is one of the most important instigators of economic activity and growth. The Czech Republic did not suffer as much as other countries with high unemployment rates. Trade had increased and the amount of FDI increased. While liberalisation helped the Czech Republic to develop, the government also continued to be involved in industry. Rapid privatisation helped the country to move forwards from central planning but it was hindered by the continuing state presence. By the mid 1990’s the Czech Republic was the most advanced of the CEEC countries. However by the end of the 1990’s this changed as the undeveloped banking system and lack of deep capital markets hindered further progress. 2000 was a positive year for economic growth but later years showed the difficulties the Czech Republic encountered as it became more dependent on the rest of the EU which was experiencing a downturn. Overall financial liberalisation helped the Czech Republic to move ahead with a market based economy. Inflation fell from large double digit figures to that similar to the rest of the EU. The interest rate spread also fell over time down to 4%. The Czech economy made good progress in meeting conditions for EU entry whilst further progress needs to be made on reducing government involvement in industrial enterprises. Overall the liberalisation of financial markets allowed industry to thrive without any great negative impact on unemployment levels. This encouraged economic growth.

Hungary

Table 1.28

GDP Growth 1990-2003

1996	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
25	25	17	15	14	13	12	10

Source: International Financial Statistics, International Monetary Fund

GDP growth increased year on year for Hungary once liberalisation was effected. Whilst prices increased initially inflation came under control as the government intervened directly to ensure economic stability. Hungary benefited from large FDI inflows more than other CEEC's. Inflation levels quickly fell to acceptable levels, down to 5%. The spread of interest rates increased in the mid nineties though it later fell to under 25%. Hungary met the conditions necessary for EU entry and the overall impact of the financial liberalisation programme was positive.

Poland

Table 1.29

GDP Growth 1990-2003

1996	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
30	23	15	14	9	3	2	5

Source: International Financial Statistics, International Monetary Fund

GDP in Poland increased once financial markets were liberalised. Whilst the levels of GDP increases fell over time there was still positive growth throughout the time period studied. Poland had one of the most aggressive reform programmes and they quickly began to increase trade wit the West once CMEA collapsed. By the mid nineties the country was experiencing growth levels similar to pre-reform days and there was concern that the economy was overheating. Inflation was a prime problem for Poland initially though rates have fallen to single digit figures. Interest rate spreads reduced to levels seen in other countries of the EU whilst unemployment remained high. Poland's massive transformation was one that showed real results. Banks were restructured along with state owned industry. Considering the size of this country and the scale of the restructuring process Poland managed to turn around its economy relatively quickly. Financial liberalisation was needed by Poland to reduce inflation rates and interest rate spreads in order to encourage increased industrial activity.

3.0 Credit Policy

Previously there has been debate over causes of economic growth in different economies but we now have acceptance that financial liberalisation is one of the prime determinants. More specifically the availability of credit has been the focus of recent studies[61]. Kelly and Everett found that where credit expanded rapidly, high growth followed. Financial liberalisation for the three countries in this study mean abolition of: exchange controls, interest rate fixing and credit rationing. The state sector had been the prime receiver of credit up to the early nineties but from then onwards there was a rapid decline in lending by financial institutions to the government. The private sector became the net benefiter of credit and the experience of each country is now examined.

Czech Republic

Table 1.30

Total Credit in the Czech Republic, annual average[62]

1993	1994	1995	1996	1997	1998	1999	2000
647.2	759.5	873.5	973.2	1074.8	1122.7	1080.7	1022.5

Table 1.31

Total Credit in the Czech Republic: Share in GDP[63]

1993	1994	1995	1996	1997	1998	1999	2000
63.4	64.2	63.2	62.1	64.0	61.4	59.0	53.5

61 Kelly, John and Everett, Mary. "Financial Liberalisation and Economic Growth in Ireland," Quarterly Bulletin, Central Bank, Autumn 2004, pp91-112

62 World Bank Indicators, EIU and EBRD Transition Indicators

63 Ibid. World Bank Indicators

Table 1.32

Credit to Government in the Czech Republic[64]

1995	1996	1997	1998	1999	2000	2001
100.2	116.8	428.6	804.1	914.1	1537.9	5451.6

Table 1.33

Credit to Other Sectors in the Czech Republic (in €million)[65]

1995	1996	1997	1998	1999	2000	2001
23544.6	25979.0	29321.4	30547.9	28637.5	29023.9	24260.7

Table 1.34

Domestic Credit in the Czech Republic, in % of GDP[66]

1989	1990	1991
72.7	74.7	72.1

Table 1.35

Credit to Enterprise and Household Sectors in the Czech Republic

1989	1990	1991
76.5	71.0	66.0

64 Statistical Yearbook on Candidate and South-East European Countries, data 1996-2000, 1995-1999, European Commission, Eurostat Theme 1, General Statistics, Yearbook 2002/01/03

65 Ibid. Statistical Yearbook on Candidate and South-East European Countries

66 Ibid. Statistical Yearbook on Candidate and South-East European Countries

Table 1.36

Credit to Non Financial Public Enterprises in the Czech Republic

1989	**1990**	**1991**
70.3	65.1	62.0

The tables above show that total credit in the Czech Republic increased up to 1997 and fell from 1998 onwards. The government continued to receive increasing amounts of credit year on year. GDP showed positive growth each year (see table 1.27 earlier) though it fell to single figures for years 1997-1999 and 2001 onwards. This pattern was similar to private sector credit figures which increased from 1995-1998 and then fell over the following years.

Table 1.37

Bank Lending to Households in Euro Member Countries in 2000 (as a % of GDP)[67]

	Households	**Of which:**	
		Real Property Loans	Consumer Credit
Euro Area - average	45.9	29.1	7.3
Czech Republic	6.3		

Source: ECB

When lending to households in the Czech Republic is compared to the average in euro member countries, the figure is well below average. Household credit is a large determinant of economic growth and Kelly and Everett's study cited previously, shows how private sector credit was a major factor in explaining the large economic growth experienced in Ireland in the 1990's.

Borish discovered that lending to enterprises in the Czech Republic in 1995 was around 60-70% of total credit[68]. Lending to the private sector was 34% of GDP in 1992 and 52% in 1995 showing a positive move. Lending to the government declined from 7% in 1992 to 2% in 1995, reflecting the reduced role of the government in industrial activity.

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67 Czsjbok, A. and Csermely, A. "Adopting the Euro in Hungary: Expected Costs, Benefits and Timing", <u>NBH Occasional Papers 24</u>, 2001, Magyar Nemzeti Bank

68 Op. Cit. Borish, 1996

Between 1992 and 1995 domestic credit increased two thirds, running parallel to GDP growth. Most of the increased lending was to the private sector though there was some increase in lending to public functions like health and education. The biggest reduction in credit has been to the state owned enterprises. Whilst lending rates stabilised there was upward pressure due to the high levels of non performing loans.

Table 1.38

Total Credit to the Economy in the Czech Republic (in €millions)[69]

1995	1996	1997	1998	1999	2000	2001
236543.7	26095.8	29750	31352	29551.6	30561.8	16503.2

Credit level increased from 1995-1998 with a fall in 1999. Whilst there was increased credit allocation in 2000 this fell in 2001 reflecting the reduced inward investment into the country.

Table 1.39

Allocation of Credit by Sector in the Czech Republic ($ million)

Government, net	1834	1041
Enterprises	16750	24249
SOE's	9816	5179
Private	6935	19067
Household	2525	3828
Other	91	5921
Domestic Credit	21201	35039

The financial institutions changed their lending habits and began moving away from the government and state owned sectors to increase credit levels to enterprises, households and the private sector.

Hungary

Table 1.40

Total Credit in Hungary, annual average[70]

[69] Statistical Yearbook on Candidate and South-East European Countries, data 1996-2000, 1995-1999. 1997-2001, European Commission, Eurostat Theme 1, General Statistics, Yearbook 2002/01/03

[70] Op. Cit. World Bank Development Indicators, EIU and EBRD Transition Indicators

1993	1994	1995	1996	1997	1998	1999	2000
942.9	1068.8	1220.3	2495.3	1775.5	2253.8	2614.8	3418.3

Table 1.41

Total Credit: Share in GDP in Hungary[71]

1993	1994	1995	1996	1997	1998	1999	2000
26.6	24.5	21.7	36.2	20.8	22.3	22.9	26.2

Total credit fluctuated slightly over the time period but was positive whilst the credit share of GDP fluctuated also.

Table 1.42

Credit to Government in Hungary (in €millions)[72]

1995	1996	1997	1998	1999	2000	2001
9992.5	19615.6	17040	16255.7	13362.4	12862.6	12961.5

Table 1.43

Credit to Other Sectors in Hungary (in €millions)[73]

1995	1996	1997	1998	1999	2000	2001
6915	7351.1	9243.1	9673.4	11651	15095.1	19293.5

Credit to government fell whilst credit to other sectors increased. Hungary recorded positive economic growth from 1994 onwards (see Table 1.13 earlier) showing a positive relationship between credit to non-government and GDP.

Table 1.44

Domestic Credit % of GDP in Hungary[74]

1990	1991	1992

71 Op. Cit. World Bank Indicators, EIU and IBRD Transition Indicators
72 Op. Cit. Statistical Yearbook on Candidate and South-East European Countries
73 Ibid. Statistical Yearbook on Candidate and South-East European Countries
74 Op. Cit. Calvo et al, 1993

83.4	78.6	77.6

Table 1.45

Credit to Enterprise and Household Sectors in Hungary[75]

1989	1990	1991
49.3	42.7	42

Table 1.46

Hungary: Banking Survey 1994-1996[76]

		1994				1995			1996
	Mar	Jun	Sept	Dec	Mar	Jun	Sept	Dec	Mar
Domestic Credit	2468	2659.4	2666.2	2792	2974.1	2973.9	3057.6	2770.7	2816.6
General Government, net	1413.1	1552.2	1519.8	1579.3	1697.3	1705.4	1763.9	1442.9	1522.1
Central Government, net	1138	1189.9	1163.6	1217.8	1326.8	1342.8	1324.7	1247.8	1020.6
Enterprises	700.4	747.3	775	780.5	868	875.6	915.6	928.6	920.4
Households	231.7	226.4	230.1	273.8	261.5	248.4	237	253.8	231.1
Small Enterprises	86.6	91.2	91.1	89.2	82.6	78.6	71.1	70.8	67.9
Other Financial Institutions	0.4	0.4	0.1	0.1	0.5	0.5	1.9	1.5	1.1

75 Ibid. Calvo et al, 1993

76 MNB, Data provided by Hungarian Authorities

Table 1.47

Bank Lending to Households in Euro Member Countries in 2000 (as a % of GDP)

	Households	Real Property Loans	Consumer Credit
Euro Area - average	45.9	29.1	7.3
Hungary	4.7	1.5	3.2*

*Consumer credit and other loans   Source: ECB, NBH

Above, Hungary's level of funding to household is well below that of the EU average. Borish's studies found that lending to enterprises to Hungary in 1995 was around 50% of total credit[77]. Domestic credit decreased by 21% between 1990 and 1995 which meant that Hungary was the only CEEC to experience a decline in credit during this time[78]. Domestic credit (as % of GDP) fell from 83% (one of the highest in Europe) to 54%. Lending to the government remained steady with a fall rate for both the enterprise and household sectors.

Table 1.48

Total Credit to Economy in Hungary (in € millions)[79]

1995	1996	1997	1998	1999	2000	2001
16907.5	25966.7	26283.1	25929.1	25013.4	27957.7	32255

Table 1.49

77 Op. Cit. Borish, 1996

78 Ibid. Borish, 1996

79 Statistical Yearbook on Candidate and South-East Euroean Countries, data 1996-2000, 1995-1999, 1997-2001, European Commission, Eurostat Theme 1, General Statistics, Yearbook 2002/01/03

Allocation of Credit by Sector in Hungary ($ millions)

	1990	**1995**
Government, net	12243	12381
Enterprises	9671	6861
SOE's	na	na
Private	na	na
Household	6086	2351
Other	20	111
Domestic Credit	28020	22141

The above table shows a reduction of credit to enterprises and households and lower levels of domestic credit reflecting an overall reduction in credit between 1992 and 12005 in Hungary. The government received a small increase in credit.

Table 1.50

Net Financial Saving of Households 1991-1996 in Hungary (billion of forint: end of period)

	91	**93**	**93 q4**	**94 q1**	**94 q2**	**94q 3**	**94 q4**	**95 q1**	**95 q2**	**95 q3**	**95q 4**	**96q 1**
Saving	888	1171	1378	1459	1532	1626	1717	1783	1879	1990	2109	2221
Cash	205	270	322	348	356	363	363	345	363	377	386	362
Deposits	432	582	696	716	756	815	866	917	966	1021	1079	1125
Foreign Deposits	303	430	491	497	520	543	573	568	584	610	640	669
Foreign Currency Depotis	130	153	205	219	273	273	294	3483	382	411	439	455
Securities	214	280	308	44	364	392	430	459	484	525	575	659
Credits:	241	252	283	286	290	305	317	313	309	307	30	292
Of which From Financial Institutions	202	209	240	243	248	262	274	270	266	264	254	249
Net Savings position	647	647	1096	1173	1173	1322	1400	1470	1570	1683	1812	1929

Source: National Bank of Hungary

The above table shows that savings increased each year over the period studied thus allowing increased investment opportunities for industry.

Poland

Table 1.51

Total Credit in Poland, Annual Average[80]

1993	1994	1995	1996	1997	1998	1999	2000
30658.4	37406.7	48904.4	66132.7	95889	125752.8	159088.6	186188.7

Table 1.52

Total Credit in Poland: Share in GDP[81]

1993	1994	1995	1996	1997	1998	1999	2000
19.7	16.6	15.9	17.1	20.3	22.7	25.8	27

Table 1.53

Total Credit to Economy in Poland (in € millions)[82]

1997	1998	1999	2000	2001
46230.5	52873.5	62937.4	73519.4	89984.3

Table 1.54

Credit to Government in Poland (in € millions)[83]

1997	1998	1999	2000	2001
18341.8	19037.2	20633.2	19919.2	26482

Table 1.55

Credit to Other Sectors in Poland (in € millions)[84]

1998	1999	2000	2001

80 Op. Cit. World Bank Development Indicators, EIU and EBRD Transition Indicators
81 Ibid. World Bank Development Indicators, EIU and EBRD Transition Indicators
82 Op. Cit. Statistical Yearbook on Candidate and South-East European Countries
83 Ibid. Statistical Yearbook on Candidate and South-East European Countries
84 Ibid. Statistical Yearbook on Candidate and South-East European Countries

33836.3	42303.2	53600.2	63502.3

Table 1.56

Domestic Credit in Poland, in % of GDP[85]

1989	1990	1991
26.1	12.5	23.8

Table 1.57

Credit to Enterprise and Household Sector in Poland[86]

1989	1990	1991
22.6	12.7	18.8

In Poland total credit sector grew steadily from 1993-20003 whilst GDP showed positive growth each year (see Table 1.22 earlier) indicating a positive relationship between the two variables. Credit to the government fluctuated during the time period studied and the positive growth in GDP can be attributed to the private sector selecting projects that had high returns.

Borish's[87] studies found that lending to enterprises in Poland was 3% of GDP in 1990 and 13% in 1995. Domestic credit increased by 250% between 1990 and 1995. By 1995 it stood at 34% of GDP which was low. Lending to government increased significantly and the government moved from being a ned lender in 1990 to accounting for 43% of domestic credit. By 1995 credit to the private sector and households increased. The SOE's had a fall in credit from 93% in 1990 to 21% of total credit in 1995. The private sector (households and enterprises) received 37% of total credit in 1995 compared to 15% in 1990. Lending rates remained high as provision for loan losses were already made.

Table 1.58

Allocation of Credit by Sector in Poland[88]

	1990	1995

85 Op. Cit. Calvo et al, 1993

86 Ibid. Calvo et al, 1993

87 Op. Cit.Borish, Michael. S. et al, 1996

88 Op. Cit. Csajbok, A. and Csermely, A. 2001

($ Millions)		
Government, net	-964	16973
Enterprises	11827	20507
SOE's	10637	8244
Private	1191	12263
Household	619	2277
Other	0	0
Domestic Credit	11483	39758

Above the government moved from being a net lender to benefiter of credit between 1992 and 1995. Enterprises, the private sector and households also received higher levels of credit over time with a reduction in the amount lent to the private sector.

Table 1.59

Bank Lending to Households in Euro Member Countries in 2000 in Poland (as a % of GDP)[89]

	Household	**Of which:**	**Consumer Credit**
Euro area - average	45.9	29.1	7.3
Poland	7.0		

Poland's lending to households compared to the EU average was low.

3.1 The Impact of Credit Growth on Economic Growth and Development

Czech Republic

The Czech Republic initially saw an increase in credit to the private sector which fell

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89 Op. Cit. Csajbok, A and Csermely, A. 2001

over time. This was in contrast to credit to the government which took the opposite direction i.e. as credit to the private sector fell, credit to government increased. Studies have shows that increased levels of credit to the private sector is one of the main determinants of economic growth. For countries to pursue this path of growth there must be sufficient investment in the country for funds to be available for investment. The Czech Republic received FDI from the West and households saved funds in the banking system (once they got used to liberalisation and the increased amounts and variety of goods and services). However the amount of funds available within the banking system was insufficient for higher levels of credit to be given to the private sector. This will change as increased liberalisation of markets results in EU entry and will lead to increased trade with the West and the former CEEC's. FDI will increase further and it more indigenous businesses will set up thus increasing investment opportunities and attracting capital from within and outside the country.

Hungary

Hungary increased levels of credit to the private sector whilst it reduced levels to the government. This encouraged economic growth. Hungary received the largest share of FDI to the former CEEC's and they were able to take advantage of this increased investment and increased levels of credit to the private sector. Studies reveal that the private sector is best placed to deal with credit as they are in a position to select high return projects. These projects then generate further income which can be reinvested in the banking system, thus increasing levels of credit further. Previous habits of lending large amounts to the state sector meant that initially the private sector was crowded out to a large degree. A lot of investment funds were used to prop up inefficient industry.

Poland

Poland experienced growth in GDP and also strong increases in levels of credit to the private sector. Of the three countries studied Poland had the longest tradition with private enterprise and long before the market was restructured there were many small enterprises operating in Poland. This escalated in 1989 with large and small enterprises being set up by private individuals. Credit to the government fell over time as state involvement was reduced with the large privatisation programme. The increase in private sector credit contributed to economic growth and with EU entry levels of investment into Poland will increase. This will lead to increased access to credit for all industry thus boosting economic growth further.

4.0 Summary and Conclusion

Price liberalisation for all three countries led to increased inflation though stabilisation measures were introduced to induce stability. All three countries experienced major economic shocks with the break up of CMEA trade, removal of direct subsidies to enterprises, trade and price liberalisation and increases in energy prices. Each country managed to turn around its economy by 1995 though employment levels were lower than that experienced in 1990. Whilst private enterprises contributed enormously to an increase in employment levels it was not enough to make up for the fall in employment from the structuring of state owned enterprises.

All three countries have low household credit levels that fall well below the credit levels of the average country in the EU. Increased household credit should lead to increased demand for goods and services which will boost economic demand. Increased access to loans by small and medium businesses will increase domestic production and again raise economic output and growth. Whilst all three countries received increasing amounts of FDI there were still barriers to entry for firms in the West given the geographical and economic stances of these countries. Since May 2004 this has changed as the three have joined the EU though they still hold their own currency and have individual monetary policies. All three countries have agreed to join the euro and adopt a common monetary policy. This will open up markets further and allow easier entry of FDI. Strong levels of credit with affordable rates of interest will allow households and enterprises easy access to loans and levels of credit available in Western Europe. High economic growth is likely to follow though all three countries will have to monitor inflation levels to ensure they do not rise above acceptable levels and negate any advancements made.

Appendix A

Table 1.60

Current Account Balance in the Czech Republic (as % of GDP)[90]

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
-3.9	-4.2	-1.0	0.3	-0.1	-2.6	-7.4	-6.1	-2.4	-2.0	-2.0

Table 1.61

90 World Bank Development Indicators, EBRD Transition Report 2000 and WDI Staff Calculations, William Davidson Institute at the University of Michigan Business School

External Debt in the Czech Republic (as % of GDP)[91]

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
20.3	33.1	23.7	24.7	26	31.8	36	40.6	43.1	42.3

External debt doubled between 1990 and 1999 reflecting the Czech Republic's increasing external debt.

Table 1.62

Current Account Balance in Hungary (as % of GDP)[92]

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
1.1	0.8	0.9	-9.0	-9.4	-5.6	-3.7	-2.1	-4.9	-4.2	-5.4

Table 1.63

External Debt in Hungary (as % of GDP)[93]

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
64.4	67.7	58.1	63.7	68.7	70.4	61.1	51.9	56.9	59.9

Table 1.64

Hungary: Foreign Debt, 1990-1995[94]

	1990	1991	1992	1993	1994	1995
Total Debt	21205	22812	21655	24556	28526	31660

Table 1.65

Current Account Balance in Poland (as % of GDP)[95]

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91 Op. Cit. World Bank Development Indicators, EIU and EBRD Indicators

92 Op. Cit. World Bank Development Indicators, EBRD Transition Report 2000 and WDI Staff Calculations,

93 Op. Cit. World Bank Development Indicators, EIU and EBRD Indicators

94 National Bank of Hungary

95 Op. Cit. World Bank Development Indicators, EBRD Transition Report 2000 and WDI Staff Calculations

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
5.2	-2.6	1.1	-0.7	2.5	4.6	-1.0	-3.2	-4.4	-7.6	-6.0

Table 1.66

External Debt in Poland (as % of GDP)[96]

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
83.7	69.9	56.4	54.9	47.1	38	35.2	36	36.2	38.3

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