

A quarter century of reforms

This year Poland celebrates the 25th anniversary of the post-socialist transformation. On their results, there are different views in the society. For example, according to a venerable 92-year-old professor of one of Polish universities, during that time, no change took place, and Poland's accession to the EU is the biggest mistake resulting in the nation's plunge in the neo-colonial capitalism. But a young scientist, my graduate who works at the World Bank, says that this was the most successful period in Poland over the last 600 years. That all depends on perspective. I think that, during those years, we did make some progress, but not such as we would like - about two-thirds of the possible.

Today, per capita GDP adjusted to purchasing power parity in our country is \$21 th., which is almost three times more than in Ukraine. And 25 years ago this figure in our countries was virtually identical. We seem to have done everything right, but GDP could be over \$30 th. per person, and Poland would take place somewhere near Portugal. Thus, there were mistakes, which, incidentally, can be a lesson for Ukraine. The government should provide more support for the development of the social market economy.

We made a big error because of our adherence to the recommendations of the Washington Consensus and the so-called shock therapy - lost 25% of GDP, 35% of industrial production, had considerable unemployment. Analysts believe that economic dynamism is largely dependent on political factors and political will. When I was a deputy prime minister and minister of finance in 1994-97, average annual economic growth in Poland was 6.5%, and now it is 2.5%, and some say that this is a significant success since the end of 2001, when, as a result neoliberal policies, the growth rate was at 1.2%. A worldwide discussion is going on what to expect in the context of economic development?

Yesterday I was at a conference in London devoted to inclusive capitals. («Inclusive» means all active economic actors should take appropriate participation in the distribution of economic assets.) Among the speakers were former U.S. President Bill Clinton, head of the IMF, Michel Lagarde, head of the Central Bank of England and other prominent persons. The topic was the urgent issues of the global economy. Everyone understands that the economic situation should change for the better. But what is now happening in the European Union? In particular, the French response to the crisis has been the rise to power of the extreme right-wing parties. The discussions about the crisis continue: what kind of crisis is this, the crisis of what?

I believe it is a crisis of neoliberal capitalism that offers inadequate economic policy instruments and produces rising inequality when the rich get richer at the expense of the poor. Politically, the European countries respond to the crisis in different ways: in Greece, for example, with a move towards the extreme leftists, in others towards the far rightists, such as Marine Le Pen's National Front in

France. Thus, it is a big problem to coordinate policies of individual countries within the EU. All these questions are quite relevant for Ukraine. Only you decide: whether to go to the European Union.

In Poland, there are enough skeptics too, we call them "the new rightists." But most people, including professional economists and other experts believe that membership in the European Union is the right thing for our country, in particular, to strengthen and support the national economy. Economic analysis shows that each year we have more than 1-1.5% economic growth just because our membership in the EU, otherwise our GDP would have been by 15-20% lower.

We have been 10 years in the EU and during previous 10 years we were preparing to access. The process of preparation helped us improve the quality of economic institutions to improve the competitiveness, first of all, of private enterprise. If Ukraine had the European quality of institutions, then your level of GDP already would be twice as high. The question is why we have at least a two-thirds success, and you have not? Similar is the situation in other countries, such as Turkey, which has a very long lasting conversation regarding EU integration. But, as I understand it, Turkey will not take part in the EU. While many politicians, businessmen, scholars believe that EU membership is a powerful support for a market economy.

So, I think it would be good if the new government of Ukraine and the new government of EU sign the EU Association Agreement. This will secure the support of the Ukrainian economy, and will increase the quality of Ukrainian institutions, bringing them closer to European standards.

Let us return to our error to find out what we did wrong. Within the neo-liberal policy regulation macroeconomic management was not always appropriate. These activities need special scientific justification, in my book, I call it new pragmatism. In my opinion, neither neo-liberal nor state capitalism will not do any good to us in the future. But I do not believe either that the so-called Beijing Consensus, as opposed to the Washington consensus, will prepare a receipt for the former Soviet republics. Ukraine needs to find ideological, political and practical answer to the question: how, given national traditions, to develop a system of institutions, values and policy instruments functioning as a reliable support for the social market economy.

And the economy should be market oriented and social. Of course, it will not happen just now, perhaps after one or two generations, maybe after 100 years, as was the case in Canada. But the economy should always grow. I think you have a potential to average growth rate within 5% for the next 20-25 years. It is also necessary to improve the regulation of institutions. First of all, state officials should have long-term socio-economic vision, not an illusion, and should be interested in supporting the economy. President and Parliament should develop a strategy for 20-25 years, not just for tomorrow or next month.

My program "Strategy for Poland" is a vision of public, social and market economy. Then I developed a specific program of economic reform involving the creation of market institutions and solution of many other problems. You need to look to the future in the light of a specific triangle: sustainable long-term social, environmental and economic development. The first point of the triangle should be of value. What values is the basis, the foundation of society and economic activity? United States and Canada have different values, as well as China and Japan. But, for example, in the United States or China, there will be no growth and they will not be able to overcome the crisis if they do not change the values. Americans should realize what a social market economy is, and the Chinese should learn individualism, and their leaders must understand the neo-liberal values. Also different are the visions of politics and economics in Poland and Ukraine.

The second point of the triangle is *the institutions*. First you need to determine where Ukraine is going, and then advance in accordance with the guideline. I cannot imagine Ukraine's development without normal cooperative relationship with Russia, but I cannot give an answer how to solve this issue now. I think that you need to make contact with Russia, and then develop relationships with the EU. This is necessary to avoid Russia from perceiving Ukraine's aspirations for European integration as a movement against it. Unfortunately, in the West, including in Poland, today many politicians consider such orientation as anti-Russian. We must find a strategic response to the question of how to build institutions so that they become the basis for market competitiveness of the economy, as they are in the EU. Of course, that will not become similar to the EU institutions at once, but their quality should increase.

25 years ago, when we decided that we would go to the EU and were just beginning to build a market economy, we sent 2080 pages of instructions on how to overcome the transition from the Soviet economy to a free market. And with those instructions we worked 10 years. Then, on May 1, 2004, we ascended the European Union, and now have a free country with a market economy. However, not all believe that our market economy is a free country, they say, this is the same Soviet Union, only called the European Union.

When we decided to move to the EU, we clearly knew where to go. We had a strategic vision and political ambitions. We clearly imagined what is competitiveness, capital markets, labor protection etc., and sought to make everything as in the EU.

So we knew where to go. And you don't. And Russia either doesn't. However, you have more choice, you can build institutions as in Japan or as in Canada, or by your own choice. We did not have a choice because we were moving exactly towards the European Union. Which is better? I think it is better when you have less freedom, then you know exactly what to do. You have a big variety of choice: there are a lot of ideas, there is democracy, there are special interest groups, ideology, the West, Russia,

Washington... You can join the EU in 20-25 years. Or maybe, at least I think so, develop without the EU, but through co-operation in terms of institutions. Today it is more a political issue than an economic one. It is exactly *policy* that is the third point of the triangle.

As for the World Bank, it seems to me, it is worth listening to their advice and perform better their requirements concerning capital, technology, and strategic positions. If a year ago I had been asked if I considered Ukraine's geopolitical position good, I would call it good: between Poland and the European Union, Russia and CIS countries. And now I see that it is very bad from a political point of view. If I were an economic politician in Ukraine, not in Poland, the most important question that I would seek to answer would be how best to use this geopolitical position for the development and strengthening of the state. And, as the second question, I would call how to build good relations with neighboring states. These questions, in my opinion, are paramount. And only then Ukraine should solve the problems of long-term development of the social market economy with Ukrainian specificity.

Professor G. W. Kolodko's responses to questions.

A. Radzievskyi:

- Historian Igor Froyanov, in a magazine, talks about globalization. He says that sooner or later will come a time when the Antichrist will reign over the world. This will be the result of the policies of globalization. What is your philosophical attitude to the challenges of globalization?

G. W. Kolodko:

- The economy, social and political sciences are categories of constantly ongoing discussion. Globalization is just such a concept. For example, I am a professor, and you are students. All have paper and pen, so write what globalization is. And then Professor Heyets will give you marks. You will find that globalization is virtually all. The answer depends on who is responsible. Globalization is not inflation, not unemployment, not competitiveness, and not economic growth. There is no clear definition of the term "globalization" because there are many. They belong to politicians, sociologists, anthropologists, economists. What is globalization in economic terms?

My definition is that globalization is a historical long-term chaotic process of liberalization and integration. Those who work in the national economy and in capital, goods, and labor markets are interconnected in a global world market and therefore globalized. There are three critical concepts: liberalization, integration and interdependence. They determine, for example, what is happening in Ukraine, or China, and what, in turn, affects what is happening in Poland and other countries. Fluctuations in China, for example, depend on what has happened at the labor exchange. From whatever point of view, is it good or bad for the country? Strategy of national development can be

implemented considering both bad and good effects of globalization. With respect to Poland, I thought that globalization would give us a new chance (in terms of trade, direct investment, technology and so on). It is also a great opportunity of risk management. Some people are in favor of anti-globalization. Why? Because they are anticapitalists and antiimperialists. And globalization is not capitalism or imperialism, it is not related to them. It is necessary that society form a different strategy. China, for example, uses globalization to accelerate economic growth and social development. They know how to do it. In Russia, they do not know that because they have gas and oil.

Y. Bersheda:

- What was the system of prioritization in the process of adapting Polish law to EU requirements? How do we start? How to build a training system in Ukrainian legislation that would meet the requirements of the EU? We are behind you, which has its advantages: we will learn on your achievements and your failures.

G. W. Kolodko:

- I think that Ukraine's priority should be the policy of competitiveness. It should begin with reform of the Antimonopoly Committee. Make it the country's most influential and organized agency. Not National Bank, not the SBU, not the army, but exactly the Anti-Monopoly Committee is the institution that fights for the consumer. A particular case is the judiciary. I do not mean criminologists, and much less the courts as part of economic relations. For example, if I asked a Polish businessman: what is the most important thing when you negotiate with other parties, other businessmen and sign a contract, he would say: the main thing that I will not be defrauded. Even after 25 years of building a market economy, most businesses are afraid of being deceived, "duped." So, here we somewhere made a mistake or failed to complete the job. It is necessary to strengthen the regulation of the market system. From the technical point of view, we know how to do it. Good experience in this regard is in the countries of former Yugoslavia. As for Ukraine, I would start with the revival of institutions aimed at demonopolization of the economy, and strengthening competitive market principles to support the competitiveness of SME.

V. Heyets:

- You know that we had two revolutions. Let someone says they were not real revolutions, but a lot of people stood for freedom. However, judging from your words, one can think that lack of freedom is better than freedom.

G. W. Kolodko:

- Of course, I believe that freedom is very important, perhaps the most important thing that might be. But the market does not preclude negligence, and democracy does not preclude stupidity. It also happens that there is freedom, and people do not know from where to start. And the ongoing public debates may last five years or 25, or indefinitely.

The restrictions that we had determined the guidelines to solve the problems through the use of democratic, technical and other instruments. I will speak about freedom in Krakow at the conference on "Freedom, Economy, Competitiveness." I believe that freedom is a value in itself. But we cannot say that there is more freedom when this freedom is not contributing to economic growth. This is not true. It is politically incorrect to say that democracy is always the best environment for economic growth. Not always. The United States have democracy, but today it does not contribute to the pragmatic development of the economy because the Democrats say one thing, and Republicans say a different thing. It is not democracy that works in China now and at one time worked in South Korea.

In Poland, the long-term civil relationship is a support for economic and social development. When I was invited to be deputy premier and minister of finance, I thought that 95% of my activities I would reflect how to solve problems of economic development, and 5% would be spent to political struggle, media and more. But the reality appeared to be quite the opposite. Only during 5% of my working hours I worked as a scientist, and during the rest of time I tried to prove my own associates that two plus two is four. Imagine, I come to the Verkhovna Rada and say: Sirs, we need to adopt the Law number 1, two plus two is four. Some say, not four, but three, others - no, five. I had to make great efforts to prove the simple truth. And the important thing was not only that I confidently maintained my position, but also that I had more supporters. It is very important that in Ukraine the majority know and perceive that two plus two is four.

A. Danylenko:

- We now have a very big problem with decentralization of financial resources. After you had conducted budgetary reform in Poland, how were the central and district budgets distributed? To what level did you bring the limits: to regional and district or to the communities?

G. W. Kolodko:

- We went down. But perhaps politically in Ukraine you should not do so. Our country is divided into provinces, districts and gminas (communes). At the time I had been the deputy prime minister and minister of finance, I paid special attention to the so-called special administrations. They were 52 and all were centralized. They covered fire brigades, diplomats, veterinarians, doctors and others. There are administrations that should be centralized, and there are such that can be either centralized or decentralized. It is necessary that the money be where it is advisable to use. Power, responsibility and

money were brought down to the lowest level in order to attain financial equilibrium. I think the more power is brought down, the better. Today, the situation in Poland is much better than in other countries because we have successfully solved the issues of administration decentralization, public finance and others. Recently many problems are solved at the level of communes.

O. Borodina:

- Within the program of agricultural development, Poland received 50% of the funds allocated to all new EU member countries that joined the EU together with Poland. Please tell me how you managed to get so much support.

G. W. Kolodko:

- I believe that we get from the EU more than we give them, something around 1.9% of GDP annually. That's a lot - 7.8 billion euros, and the bulk of this money is spent to support agriculture. Traveling the country, you can see how the Polish village has changed. When I was traveling by train from Dnepropetrovsk to Kharkov, I saw that in your country almost nothing had changed. There no new buildings like those in Poland, which were built in cooperation with the EU. How did we do it? Thanks to the work of institutions concerned with obtaining funds for investment and support of farmers and agriculture. Common Agricultural Policy is good if it serves the interests of agriculture. In terms of the rationality of EU expenditures, it is not the best macroeconomic policy, and in future it will not be conducted any longer. It is necessary that money be spent on infrastructure: in this sense, successful policy in itself is a success .. In the EU, it is the policy of supporting regional development. It is being conducted in Greece, Spain, southern Italy, Western Europe and Poland.

You should understand what expects you there. Some politicians in Europe think that if they are in favor of Ukraine, it means that they are against Russia. If a referendum were conducted now in the EU whether to take Ukraine and Turkey to the EU, the majority would say "no." Because their values are different than, for example, ours. If you just ask Europeans if they agree with the integration of Ukraine with the EU, they will say "yes." But, if it involves increased taxes - then they are against.

Yu. Prozorov:

- You have been to many countries, you know the characteristics and nuances of economic policy. What should we learn from other countries, what kind of economic policy other than European? The second question relates to technology development, which you mentioned: you did not very clearly outline the third point of the development triangle.

G. W. Kolodko:

- Yes, I have been to many countries, more than 160. There are such countries that, compared with them, Ukraine is the most successful. You are a big country, you have almost everything. But what is the specific feature of Ukrainian economy? That you know better than me, you have a huge corruption. And it is impossible to plan development. A very important factor in economic development is culture. And it is up to you how to use the values of Ukrainian culture.

Regarding the second question, the third point of the triangle is policy. A lot depends on the policies, on the personalities of those people who are in power. For example, having arrived in Ukraine, I have to respect the local values. If these values are not conducive to economic development, it is necessary to carry out corresponding educational work through public institutions and regulatory mechanisms. Institutions must change. Should we change interest rates or not? Should we change the exchange rate system or not? I would say that you should move towards floating exchange rate, not the one you had. And all that is policy on which much depends.

V. Heyets:

- We often discuss with our guest. One of the topics of discussion is the social order, social harmony. For us, it is a big problem today. We study public opinion, we wonder what public order they would like to have regardless of EU membership. The population wants the state provided jobs, decent health care, insurance, education, etc. They want the state to provide all those things.

G. W. Kolodko:

- In Poland, there is an ongoing debate about what should be done by society and business, and what should be done by the state. Here the basic principle of success is knowing what to seek. Before joining the EU, Poland has joined the OECD, Organization for Economic Cooperation and Development. I ran this process. It was not a struggle with the opposition but with my fellow ministers, my administration and bureaucracy. I said that I did not need the opposition, I had enough of my coalition in the government. I worked six days a week to improve the functioning of health, economy, foreign trade, etc., to gradually move toward EU membership. It was a struggle for success and positive synergy between the market and government. But the government should not be corrupt, such as in Egypt, or, unfortunately, in Ukraine. The government should understand and do what is good for long-term public support.

V. Heyets:

- About the policy of demonopolization: The level of capital concentration and monopoly in Ukraine is among the highest in the world. We have the largest proportion of dollar billionaires. So I agree with the idea that differentiation and demonopolization of capital use is a key issue that we are

not even discussing today, because it is impossible to overcome it so far. The gap between the living standards of the richest and the poorest is close to that of the eighteenth century. Such data have been made available to society through a research of French economists. That should be overcome as well. But we do not want to bring the situation to another October Revolution, which is quite possible. We are beginning to think about wealth tax and other effective tools.

G. W. Kolodko- We must find a solution before these rich escape with their money to other countries. When there is no solution, there will be no money. But it is quite a challenge.

V. Heyets:

- They got the power. Among the deputies elected to the Kiev City Council, there are a lot of millionaires.

G. W. Kolodko:

- You have a situation similar to the United States. There are too many millionaires in the Senate..

V. Heyets:

- But the per capita incomes are very different. That is why they agree to such a democracy. And our people will not. This is a big problem.

G. W. Kolodko:

- You already had two revolutions. If you do not avoid the third one, I wish it will be only intellectual and institutional revolution.

V. Heyets:

- We agree. Thank you very much.