

Dr. Joseph J. Penbera on the Polish Transformation

Andrzej Wilk*

Abstract

On the basis of his personal observation Dr. Joseph Penbera has made an assessment both positive results and shortcomings of the transformation of the Polish economy during the period 1990-2006. He also offered some advice concerning the process in the years to come.

Dr. Joseph J. Penbera has accumulated rich experience, both in academia as in business. He had served as dean of two U. S., business schools, the national program chairman of the international accrediting agency (AACSB) and a Fellow of Economics in the first think-tank in the California State University system. He has been a Professor of management and former dean of The Craig School of Business at California State University, Fresno.

In business he has served as a director or senior adviser to several U. S., publicly traded companies, including two of the largest in the world in their respective industries – Vendo, International and Rug Doctor Inc. – and more recently, to one of the largest auto manufacturers in the world. He also served as a director of publicly listed (NY Stock Exchange) retailer, Gottschalks Inc., and relatively new oil drilling company, Verdisys (OTC). He has been the senior economic advisor to five banks.

He first visited Poland in 1991 at the request of the U. S., Department of Commerce, and as a part of team consisting of accounting firms and professionals, government officials, and university-based consultants to evaluate the transformation of Polish state enterprises to private firms. The focus of his work at that time was to assess which state enterprises were likely candidates for both survival and, in several cases, eventual listing as publicly traded companies on a newly formed stock exchange.

In 2005 Dr. Penbera visited Poland as a Fulbright Senior Specialist. In his capacity he talked to the Polish government officials, business executives and young entrepreneurs, traveled throughout Poland, visited numerous companies and research institutions.

Owing to the two missions as well as his personal knowledge and skills Dr. Penbera enjoys a unique position of a well informed independent outsider, who – in his recent report – offers thoughtful observations and recommendations for post-transformation improvement.

In his report Dr. Penbera recalled:

In the early 1990's, when I first visited Poland, things were quite cloudy economically and politically. Solidarity has extended a union-activism tradition of resistance that exploded into Polish consciousness in 1956, but no one seemed all together sure of what Solidarity's leadership really knew about running a country in the 1990's, or how to transform hundred of state-owned enterprises into an economy based upon some notion of an American-style free market capitalist society. Pope John Paul's words "don't be afraid" rang loud and clear, it seemed, both politically and economically.

During this first visit, I spent the better part of my time in Poland poring through books and

* Andrzej Wilk, PhD., eng. – University of Management and Law, Warsaw

records of state-owned enterprises with other consultants, and attempting to communicate effectively with officials in government charged with “transformation” responsibilities. In my report to the U.S. Department of Commerce, I offered two cautionary pieces of advice: Poland should not under-price its state-owned industries, and Protections for small and medium-sized businesses should not be removed all at once, but, rather over a 3-5 year period.

A big storm could be brewing, I reasoned, when one combines the tremendous power of a new government with the forces of new wealth – and Poland was, well, without an umbrella. In the U.S., we have various checks and balances to guide the relationships between government and business. These include micro-type policies such as anti trust rules, and regulatory requirements on the independence of auditors, corporate director conduct, and exchange codifications regarding analyst, broker and director behavior and prohibitions. In the early 1990’s Poland, these checks-and-balances were not yet formed.

During his mission in 2005 Dr. Penbera came to the conclusion that:

The Polish economic transformation process is now in a second phase. Phase 1 involved the privatization of state-owned enterprises through a process of foreign or domestic private purchase, restructuring, change of control, or some combinations of the above. Phase 1 is, essentially, over with some exceptions.

Phase 1 lasted for about 10 years. The results are mixed. Many of Poland’s potentially richest and most competitive state units were sold off at below-market/fair valuation prices (one estimate places the asset value to purchase price at 10%). Opportunistic foreign investors combining with inexperienced, compliant bureaucrats, and consulting groups, including accounting firms, often representing multiple interests, to create this situation.

The transformation process was not altogether a failure. Most, if not all, of the more economically viable state-owned enterprises have been transformed, and most of the marginal ones are out-of-existence. Many of the now defunct enterprises had 10 times (or more) the number of employees that could have been justified by profitability, productivity, or, even, revenue measures.

On the other hand, the transformation appears to have accomplished far less than its architects had envisioned, particularly with respect to employment gains; in fact, the total effect of employment, actual and marginal, is telling. To apply the analogy with which I opened this commentary, for many Polish citizens, transformation represents a very long and quite harsh winter. For example, I passed through whole communities that were decimated by transformation, and where unemployment hovers around 50%.

In this context it seems useful to call attention to the recent publication by Warsaw Innowacja Foundation on Polish Systemic Transformation (1).

Well-know expert on employment Dr. M. Kabaj pointed out in 1989 the rate of employment in Poland was 80,2% and at the end of 2002 – 54,2%(the rates of unemployment were 1,5% and 20,6% respectively) (2).

Phase 2 of the development of the Polish economy began about five years ago and can be characterized as both a consolidation and an assessment period.

The consolidation comes in form of some (not all) foreign interests attempting to maintain and expand their share of the overall market within an industry or sector. Some of the com-

petitive practices being used are grossly unfair. For example, there appears to be attempts to discredit competition from small and medium-sized Polish-owned enterprises by creating the impression that Polish enterprises lack quality standards.

In my opinion, the small and medium-sized enterprise sector was near death as a result of the quick removal of tariff and other protections. These protections should have been phased out gradually in order to allow domestic competition to form a market base. At the same time, funding for small and medium-sized enterprises incubation has been virtually non-existent owing to the transformation of the central banking system, and the attendant consolidation of local banking units through private acquisition activities.

In-depth analysis of the situation of the small and medium-sized enterprises has been carried out by Dr. Wiesław M. Grudzewski and Dr. Irena Hejduk in their study of the competitiveness of Polish companies. (3)

The mixed results of the Polish transformation could be easily exemplified by privatizations.

Assessments of the privatization experience are everywhere one chooses to look. Assessment represents the first real general awareness that something must be done to restore the local economic base, and to eliminate abuse and corruption.

Phase 2 is a crucial phase for Poland politically and economically. If substantial progress is not forthcoming in terms of the perceived fairness of capitalism, either in this or the next presidential election, the Polish people, may, indeed reject American-style capitalism for a more Scandinavian-style mix of socialism and capitalism.

One must understand and appreciate that for many Poles, the “new reality” in terms of quality of life has been worse than the old reality. It would be misguided to blame the American-style capitalism for the situation, but one should not be surprised by such a political development.

Interesting and highly relevant are Dr. Penbera’s remarks and suggestions on the current developments in Poland.

Given the number of college-educated young persons being produced by Polish universities and other educational institutions (both public and private), a serious structural unemployment problem is looming on the horizon and this will not be avoided by entry into the EU.

Some people would say that this problem already exists given the number of new university graduates taking jobs in other countries. To help turn this situation around, one must examine the roots of this problem. In my opinion, government has all been absent in its support of building a middle class strata of business owners. There is no evidence of leadership provided by government during the transformation and privatization process with respect to the incubation of small and medium-sized enterprises. Neither the existing banking system or government policies provide for incentives to grow these types of enterprises. As a result, the expected innovations and commitments that come from the work of young entrepreneurs are being lost.

Typically, I offer advice to a particular corporation or industry; I hesitate recommending broad-based legal or policy changes. However, in my opinion, Poland is in dire need of community reinvestment legislation and funding to provide capital investment at the local level. This can be accomplished in a variety of ways, including providing guarantees to banks to assure repayment of portions of loans that cannot be, otherwise, collateralized by business

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owners. Although certain tenets of the U.S.'s Community Reinvestment Act are instructive, cultural differences need to be considered in making certain that such a policy mechanism will work well in Poland. For example, given the extensive university system in Poland, and the number of senior professors who hold multiple positions in business and government, these new funding and incentive mechanisms may be best coordinated within enterprise groups formed within universities. Such specialized institutes which have demonstrated expertise in areas (accounting, finance, production, risk management, marketing, etc.) are important to guiding the success of business and would have an immediate and visible impact on young people.

In my view, growing this middle business strata of the Polish economy should be the **number 1** economic policy strategy and priority of the new President.

Some Polish scholars, business analysts and journalists – particularly during last five years–focused their attention on relationships between politicians and the big business. In these close relationships some researches see characteristics of traditional Latin American model.

In spite of election promises consecutive Polish governments were unable to reduce unemployment and to modernize and expand infrastructure which would make Poland more attractive to serious foreign investors.

The long term unemployment has led to highly undesirable social phenomena: marginalization, exclusion, increased juvenile delinquency and others. The side–effect of the situation has been disillusionment with democracy and growing propensity to tolerate or even to support nationalistic and authoritarian concepts. So far it does not imply a threat of “the escape from freedom”. (5) Nevertheless in some social groups it does imply diminished interest and trust in democratic institutions and procedures.

These serious issues call for in-depth discussion. The Dr. Penbera's reflections and suggestions represent a valuable contribution to the discussion from a knowledgeable and friendly outsider.

References

1. *Polska transformacja ustrojowa. Próba dyskursu-zarys perspektyw*, Wyd. Fundacja Innowacja, Warszawa 2004
2. M. Kabaj *Syndrom polskiej transformacji* In: see above p.242
3. I. K. Hejduk, W. M. Grudzewski *Konkurencyjność polskich przedsiębiorstw wobec wyzwań europejskich* In: see above
4. I. K. Hejduk, M. Grudzewski, see above p.114
5. E. Fromm *Escape from Freedom*, N. Y. 1969