

Kozarzewski, Piotr; Bałtowski, Maciej

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## Change in economic policy paradigm: Privatization and state capture in Poland

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CASE Working Papers

# Change in Economic Policy Paradigm: Privatization and State Capture in Poland

Piotr Kozarzewski, Maciej Bałtowski

No 3 (127)



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CASE – Center for Social and Economic Research  
al. Jana Pawła II 61, lokal 212, 01-031 Warsaw, Poland  
tel.: (48 22) 206 29 00, 828 61 33, fax: (48 22) 206 29 01  
e-mail: [case@case-research.eu](mailto:case@case-research.eu)  
[www.case-research.eu](http://www.case-research.eu)

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## **Abbreviations**

**CEE** – Central and East European countries

**EU** – European Union

**GDP** – gross domestic product

**MEBO** – managementemployee buyout

**PiS** – Prawo i Sprawiedliwość (Law and Justice) – a Polish political party

**PLN** – Polish złoty

**PO** – Platforma Obywatelska (Civic Platform) – a Polish political party

**PPP** – publicprivate partnership

**PSL** – Polskie Stronnictwo Ludowe (Polish People’s Party) – a Polish political party

**SOE** – stateowned enterprise

**USA** – United States of America

**USD** – US dollar

# The authors

**Piotr Kozarzewski** – political scientist and sociologist, is a member of the CASE Supervisory Council and a professor at the University of Computer Sciences and Economics in Olsztyn. He has participated in numerous research and advisory projects in Poland and abroad devoted to post-communist transition, especially privatization. His research interests concentrate, among others, on the political economy of transition, institutional economy, corporate governance, and private sector development. He is an author or co-author of about 150 publications and reports, including:

- “Formal and Real Ownership Structure of the Polish Economy. State-Owned versus State-Controlled Enterprises”, *Post-Communist Economies*, 2016 (forthcoming; together with Maciej Bałtowski).
- *Zmiana własnościowa polskiej gospodarki 1989-2013* [Ownership change of the Polish economy 1989-2013], Warsaw: PWE, 2014 (together with Maciej Bałtowski).
- “The Reform Process in Post-Communist Transition: Understanding Reform in Eastern and Central Europe and the Commonwealth of Independent States”, in: J. M. Fanelli, G. McMahon (eds.), *Understanding Market Reforms*, Vol. II, Houndmills and New York: Palgrave Macmillan, 2006 (together with Richard Woodward).
- “International Transfer of Knowledge: An Opportunity to Even Out Disparities in Development”, in: M. Jarosz (ed.), *Poland and Its People in United Europe. Economic and Social Imbalances*, Warsaw: ISP PAN, 2011.

**Maciej Bałtowski** – professor of economy, is Head of the Theory and History of Economics Department of the Faculty of Economics at the Maria Curie-Skłodowska University in Lublin. He is also a member of the Council of the Supreme Audit Office in Poland. He is an author and co-author of six books and numerous scientific and press articles devoted to economic transition and ownership changes in Poland. His research interests also cover problems of economic policy as well as the role of the state and state ownership in contemporary economies. Apart from the two publications written together with Piotr Kozarzewski, his publications include, among others:

- „Własność państwowa jako instrument współczesnej polityki gospodarczej” [„State ownership as an instrument of the modern economic policy”], w: E. Mączyńska (ed.), *Modele ustroju społeczno-gospodarczego. Kontrowersje i dylematy* [Models of socioeconomic systems. Controversies and dilemmas], red. E. Mączyńska, PWE, 2015.
- *Transformacja gospodarcza w Polsce* [Economic transformation in Poland], Warsaw: PWN, 2006 (together with Maciej Miszewski).
- “Politicians or Administrators? State Corporate Governance in Poland”, in: T. Mickiewicz (ed.), *Corporate Governance and Finance in Poland & Russia*, Amsterdam-London and Houndmills: Palgrave Macmillan, 2006 (together with Tomasz Mickiewicz).

# Abstract

This paper presents an analysis of the causes and manifestations of Poland's recent shift in economic policy towards a more active role of the state, and uses privatization policy as an example. This change coincided with a shift in "fashion" in economic policy, away from the idea of "state failure" and more towards the idea of "market failure." Our paper begins with a brief presentation of the recent changes in the theoretical approach towards the role of the state in the market economy and of studies devoted to privatization policies in post-communist countries, the latter having, in our view, critical gaps, which we attempt to fill in this paper. To meet this goal, we first discuss the Poland's privatization policy and its place in economic policy during the transition period, as well as its evolution from promoting systemic change towards focusing on predominantly fiscal goals. Analyzing the effects of this privatization policy, we point to a large unfinished agenda in ownership transformation that has had an adverse impact on the institutional setup of the Polish state, creating grounds for rent seeking and cronyism, which, in turn, impede the pace of privatization. We conclude that it is the increasing capture of the state by rent-seeking groups, and not, contrary to popular opinion, the global financial crisis, that most contributes to the growing statist trends of Poland's economic policy.



# Introduction

Since the beginning of the global financial crisis, we have witnessed a shift in national economic policies towards a more active role of the state, far beyond its previous role as a regulator, acquiring more active and interventionist functions. This shift seems to be of a dominant nature and involves countries with different patterns of economic policy: from “neoliberal” USA, through to “pragmatic” Germany, to “statist” (*toutes proportions gardées*) France. This shift enjoys support from many of the most renowned economists, including Nobel Prize winners Joseph Stiglitz (2009) and Paul Krugman (2009), and is contributing to the “resurrection” of Keynesian ideas.

A wide discussion began that was devoted to searching for an efficient model of state corporate governance that would ensure an effective impact of the state of the economy, on the one hand, and would avoid the dysfunctions of an economically active state, on the other (Musacchio & Lazzarini, 2012). Post-communist economies did not remain on the sidelines, and Poland can certainly be found among those that are looking for remedies for their current problems related to a more active role of the state. Thus far, Poland has avoided the implementation of wide-scale direct anti-crisis interventionist measures, such as direct support to failing industries and companies or financial institutions. However, it has not avoided a substantial paradigm shift away from the idea of “state failure” and more towards the idea of “market failure.”

In examining this paradigm shift, we focus our analysis on privatization policy because of its special role in transition economies. Compared to the most developed market economies, in post-communist countries, questions of ownership and the role of the state in economic processes were – and still are – much more important issues. This stems from the specific set of economic policy tasks in this group of countries that not only must meet the challenges of changing economic and social conditions, but also must ensure the implementation of the transition from a planned to a market economy. Among others, such a policy must lead to the appropriate change of the role of the state in the economy as well as to structural change in the distribution of property rights.

In this context, it is important to analyze the initial assumptions and goals of a privatization policy, as well as its place in the overall economic policy of a government, and then to fol-



low the changes in the privatization policy, attempting to understand the reasons for these changes.

The existing literature seems to have significant gaps in this respect. The vast majority of publications devoted to privatization concentrate on best policy issues (in the framework of the various aspects of the state failure versus market failure dispute, deliberations on the best type of owner, and assumptions that the government should act in good faith) or on the practical outcomes of the privatization of state property (in terms of revenues and its impact on restructuring and microeconomic efficiency, among others). There are many valuable publications in both areas. It is also important to mention the “classical” articles by Frydman and Rapaczynski (1994) and Boycko, Shleifer, and Vishny (1996) in the former area. Literature in the latter area is especially broad and varied in conclusions; however, it is important to note a recent publication that summarizes the efficiency of privatization processes (Estrin et al., 2009). At the same time, deep analyses of the real mechanisms that yield a specific privatization policy or comprehensive examinations of the true goals of privatization, why these goals were set and subsequently changed, and the degree to which these goals were realized are often overlooked or marginalized by researchers.

Since the early 2000s, researchers have shown a lessening interest in privatization in Central and Eastern European (CEE) countries, and especially after the European Union (EU) accession of these countries. Perhaps researchers consider this issue outdated now that these states are part of the club of the most developed European economies, and their economies are now predominantly private sector driven. Regarding Poland, there is also limited research on this topic. This explains the steep drop in privatization dynamics in regards to political and ideological factors (Błaszczyk, 2004).

There are only a few articles devoted to recent privatization trends in post-communist countries. Two articles deserve attention: the first is a study of the Russian economy, where changes in government policy are analyzed using the evolution of contemporary theoretic approaches to the choice of an optimal form of ownership (Radygin & Entov, 2013); the second is a study of the changing role of the state and ownership and privatization in Hungary and Poland as a contribution to the development of the theory of Central and Eastern European capitalism models (Szanyi, 2014).

The aim of our article is to contribute to the discussion on the factors that impact privatization policy as a part of economic policy design and implementation in post-communist countries. Taking Poland as an example, this article presents the findings of the most recent stage of research on ownership changes in transition economies – a process we have studied since the early 1990s. We have summarized the previous stages of our research in two books: the first examines privatization in post-communist countries



(Kozarzewski, 2006) and the second examines ownership changes in Poland during the transition (Bałtowski & Kozarzewski, 2014).

In this paper, using privatization policy as an example, we attempt to show that the economic downturn is only partially responsible for this shift in Polish economic policy. Contrary to popular opinion, we believe that it is the increasing capture of the state by rent-seeking groups, and not the financial crisis, that is the main cause of these statistical trends. In fact, the growing imbalance in public finances may even stimulate cautious privatization as a source of revenue for the state budget.

# 1. Privatization and the Changing Role of the State: Initial Conditions and Assumptions

To understand the specificities and mechanisms of the recent pro-statist shift in Poland, we must look at the history of ownership policy in Poland throughout its transition period, and not simply focus on the global crisis period, because the roots of this policy shift took hold much earlier.

As in all other Central European transition countries, the privatization of the Poland's economy was regarded as a pillar of its market reforms. At the end of the communist era, the Polish economy was primarily state property-based, with over 70% of the country's GDP produced by the state sector (with the private sector contributing mostly via agriculture and small businesses). However, from the very beginning of the transition, there was a general understanding among the authors of the economic reform that a market economy must be based on the inviolability of private property.

The economic program of the first post-communist government (the *Balcerowicz Plan*) addressed privatization issues in the context of the creation of market institutions that had stood the test of time in Western economies. Following that simple course of thought, the main privatization goal was of a systemic character: to contribute to the change of the economic system through the creation of private entities. Within the framework of this goal, a number of sub-goals existed, of which the most important was the creation of well-functioning markets, including a securities market, and a change in the role of the state, which would not have to perform ownership functions for the majority of enterprises. Apart from this purely systemic role, privatization would solve the problem of the micro-economic inefficiency of state-owned enterprises; this would, in turn, contribute to the increase in productivity of the whole enterprise sector.

Other privatization goals also existed-political (the creation of a powerful pro-reform lobby that would be involved in the privatization process and utilize its results), social (in terms of social justice, as well as in terms of resolving social problems at an enterprise level), and fiscal. On the one hand, the value of the state-owned stock designated for privatization was large; therefore, the potential privatization revenues for the budget were also significant and able to contribute, for example, to reducing the budget deficit. On the other hand,



privatization would eliminate the need for the state to support enterprises in distress; thus saving budgetary expenditures.

It should be noted, however, that detailed descriptions of the main goals of the privatization were not developed. Only a few goals were officially announced, and most had to be deduced from decisions made by the parliament or other governmental agencies. There was general understanding among decision makers that a large-scale, deep, and comprehensive privatization was needed, but the set of goals and their hierarchy remained, to a large extent, ill-defined. In general, during the first years of transition, systemic and microeconomic goals seemed to be the most important, while fiscal goals were given a much lesser importance.

Another important feature of the Polish privatization was its gradualist and highly consensual character. Its authors were aware of the trade-off between the speed and quality of the transformation processes. They believed that a slower transition speed as a result of the careful preparation of privatization deals (both in technical and social dimensions) was much more important than a massive and rapid formal change of owners because the reformed market environment would exert strong pressure on state-owned enterprises, forcing them to adapt and restructure, thus making their privatization less urgent, albeit still necessary. The gradual nature of the Polish privatization also reflected Poland's decision on what should occur first: privatization (which would create demand for further reforms) (Frydman & Rapaczynski, 1994; Boycko, Shleifer, & Vishny, 1995) or regulation and institutional constraints (in order to create a framework for actors' behavior and prevent tunneling) (Murrell & Wang, 1993). This gradualism reflected a choice in favor of the latter solution.

The main features of the Polish privatization (multiplicity of goals, slow pace, and consensual character) were reflected in the privatization law, which envisaged a wide range of paths to ownership transformation: sales to both strategic investors and via the stock market, management-employee buyouts, and even a unique kind of mass privatization, which was designed not only to transfer a significant (albeit limited in comparison with other post-communist countries) part of the state sector's assets to Polish citizens, but also to create a mechanism for actively restructuring the companies participating in the mass privatization. All paths to privatization were essentially equivalent (buyers paid market price or a price based on valuation), except in the case of the National Investment Fund (NIF) program, where certificates of ownership were distributed among the population for a nominal fee.

## 2. Change over Time

### 2.1. Shift in Goals

The goals and scope of the privatization (and the corresponding concept of the role of the state in the enterprise sector) changed over time.

In mid-1990s, the government began explicitly setting privatization goals, although the goals were primarily of a limited and short- to medium-term nature (such as support for the creation of financial markets or financing social sector reforms). At the same time, the systemic goal was never explicitly set, such as what the ultimate ownership structure of the Polish economy should look like, or what were the criteria for retaining some sectors or companies under the state control. Furthermore, rather quickly and primarily due to pressure from interest groups that were afraid of losing the privileges and rents derived from state-owned companies (directors, trade-unions, among others), the government began excluding enterprises regarded as being of special importance for national interests, thus limiting the scope of the destatization of the Polish economy.

Another important change in goal setting was the growing fiscalization of the process: increasing budget revenues gradually became more important than other expected effects. Eventually, the revenues from privatization became the primary motivation to overcome the growing barriers to selling state property. Increasing resistance came from industrial lobbies not interested in losing support from the state. Political elites also became more skeptical of privatization; through most of the 2000s, the ruling coalition was explicitly opposed to the continuation of the privatization of that which was still controlled by the state. After more liberal-minded political forces re-gained power in 2007, privatization dynamics improved; however, meeting fiscal goals were still the most important issue. Privatization dynamics have again begun to lose momentum since the beginning of 2010s (see below).

It is also important to note the opportunistic behavior of the Ministry of the Treasury, which proved to be, to a large extent, incapable of staying within the boundaries of a task-oriented organization set up to organize the process of transition. It suffered a growing conflict between its owner and seller functions: the fewer assets under control of the ministry, the less its political weight. This attitude was strengthened by the winning political



parties, which began treating state assets as spoils that belonged to the victors. One such example of this behavior was the appointments to the supervisory boards of companies that were controlled by the Ministry of Treasury. Thus, the Ministry contributed to strengthening the elements of crony capitalism.

Other goals, especially long-term goals, lost their importance. First, regarding the systemic goals: in the new century, regardless of whether the ruling coalition was more pro-statist or more liberal-minded, many of the largest privatization deals left control of the company in the state's hands. In other words, the state budget saw revenues from privatization without passing control of the company to private hands, in line with the Polish proverb: *To eat a cake and to have a cake.*

The first method for the state to retain company control was by selling only minority blocks of shares or the "leftovers": small blocks of unsold shares that did not allow for control of the property. According to estimations, in recent years, selling blocks of shares that do not affect ownership control comprise about three-quarters of all privatization revenues (Ministry of Treasury, 2011). The second method for the state to retain company control-non-ownership control-began even earlier, in the late 1990s. This method can be called "reluctant privatization," which refers to the transfer of ownership rights without the appropriate transfer of control rights (Bortolotti & Faccio, 2004). In these cases, the state holds special control rights through "golden shares" (which were withdrawn in 2006 after protests from the European Commission, but "resurrected" in a modified form in 2010) or through special provisions in company charters. Companies that are subject to these special rights of the governments are not numerous, but they are among the largest and most important Polish companies, and are in industries of strategic importance.

The same can be said of the microeconomic goals of finding efficient owners who would bring valuable financial and other resources to privatized enterprises. Passing state property into private hands, especially those of foreign investors, is often regarded as a negative process and is seen as a threat to certain vital Polish national interests. Instead, a campaign devoted to the development of "citizens' shareholdings" has been launched-where large blocks of shares are being sold to a large number of small individual investors, with the Treasury retaining ownership control over the privatized companies.

Now, it seems that almost no one remembers that the government had to create support for privatization and its market reforms. Both the ruling coalition and its political rivals are looking for allies among forces not necessarily interested in a healthy, rent-free market economy where the rules of the game apply equally to everyone. Perhaps this has a practical basis: the pro-reform political base is still too narrow to ensure victory in the next elections or in passing a bill, so the government seeks political support among actors who have real political weight-lobbies, special interest groups, and, last but not least, voters, who, *en masse*, are against privatization and in favor of state paternalism.



## 2.2. Change of Paradigm

Shifts in the hierarchy of goals seem to reflect broader changes in economic policy—specifically, changes in the paradigm of the role of the state in the economy. The state is no longer withdrawing from direct control and intervention in the market, and is instead remaining a powerful player in business and policy—and even has expanded its role, meaning that privatization is falling by the wayside in favor of a new statist ideology. Privatization has ceased to be a pillar of reformist economic policy; rather, its role has become residual. Nowadays, the government will privatize when it has no better solution resolve its problems, namely financial.

This paradigm change manifests itself in many different ways. First, we note the above-mentioned resignation from the complete privatization of companies, especially when these companies can generate financial gains for the state budget. Even economists and decision makers who were regarded as liberal-minded, such as Jacek Rostowski, the former Minister of Finance in Donald Tusk’s government, and Jacek Socha, the former Minister of the Treasury and Head of the Securities and Stock Exchanges Commission, at the beginning of the current decade, declared that profitable companies should not be privatized, at least in the short term, in order to ensure budget revenues from their operations and to possibly sell them at a higher price in the future (Głombicki, 2012; Prusek & Bielecki, 2012). In line with these declarations, the dynamics of privatization (even selling minority blocks of shares) have declined primarily because of the withdrawal of companies from approved privatization plans and the preparation of less ambitious privatization plans for subsequent years. By 2014, privatization had nearly halted (see more below).

Second, despite not declaring any nationalization goals, the state has been gradually increasing its ownership control through the acquisition of previously privatized enterprises by companies controlled by the Treasury (e.g. in the energy sector, among others). Officially, however, the state has not declared this to be a part of its economic policy, but simply “business decisions.”

Third, the state has declared increased investment activity, among others, through the “Polish Investments” program that was launched in 2012. In this program, which is still unwinding rather slowly, the state is expected to invest (e.g. revenues from privatization) in large-scale public-private partnership (PPP) investment projects. However, this program has several pitfalls. There are doubts regarding whether investment projects would be chosen wisely and whether they would create additional investment impulses instead of wasting money on support for impractical but politically attractive projects. There are also doubts regarding the government’s ability to run complicated projects – the state has earned a reputation for being a rather mediocre entrepreneur.





Additionally, a kind of economic xenophobia is developing, and not only among populist politicians and pro-static economists. Thus far, unlike, for example, in Hungary, this xenophobia is still mostly used as a slogan rather than as a concrete course of action. No specific actions have been made, and this refers only to the situation of the banking sector, which is 80% private and where 70% of capital is now controlled by foreign investors. In recent years, however, and in view of the second wave of the global financial crisis, ideas regarding the restructuring of the banking sector as it relates to ownership structure have emerged and have become popular even among some pro-market reform economists and politicians, not speaking about populist-minded opposition. These ideas are referred to as the “domification” or the “re-polonization” of banks: domestic investors should purchase foreign-owned banks to protect the Polish banking sector from the effects of financial turmoil abroad (Kawalec, 2011). It should be noted, however, that previously, there were no signs of such threats: the Polish banking sector has proved itself to be very sound, politically independent, and well functioning, with its only threats coming from a shifting external environment. Poland was the only post-communist country that avoided a financial crisis during the entire 25 years of transition. Furthermore, there were no signs of dysfunctional behavior in the Polish banking sector during the first wave of the global financial crisis. Besides, mechanisms of such a transfer remain unclear: there is neither the appropriate legislation, nor the domestic capital willing to take part in this project. Opponents of this idea also note political risks – domestic investors are less immune to political pressure from the government (Piotrowski, 2012). Quite possibly, at least some proponents of the “domification” count exactly on this: the possibility to exert influence on domestically-owned banks in order to force them to support the governmental policy of providing assistance to Polish companies (i.e. relaxed conditions), or even to become another source of rent for special interest groups.

There are other signs of increasing support for domestic entities, such as the acquisition of shares of a company that was “too important to fail” and the de facto protectionist measures in favor of Polish coal mines that limit competition from Russian coal.

Recently, the government has begun to force changes in legislation that would give the Treasury special rights and privileges in the market, as compared to other owners. In July 2015, the parliament adopted a law that allows the government to block the acquisition of shares by a new controlling investor for a number of companies that have a “strategic importance,” even if the company is fully private. Currently, the government is adopting a law that would remove from the treasury its disclosure requirements related to operations in the securities market, including removing the obligation to make an offer to buy out shareholders when acquiring shares in a company above a certain threshold.



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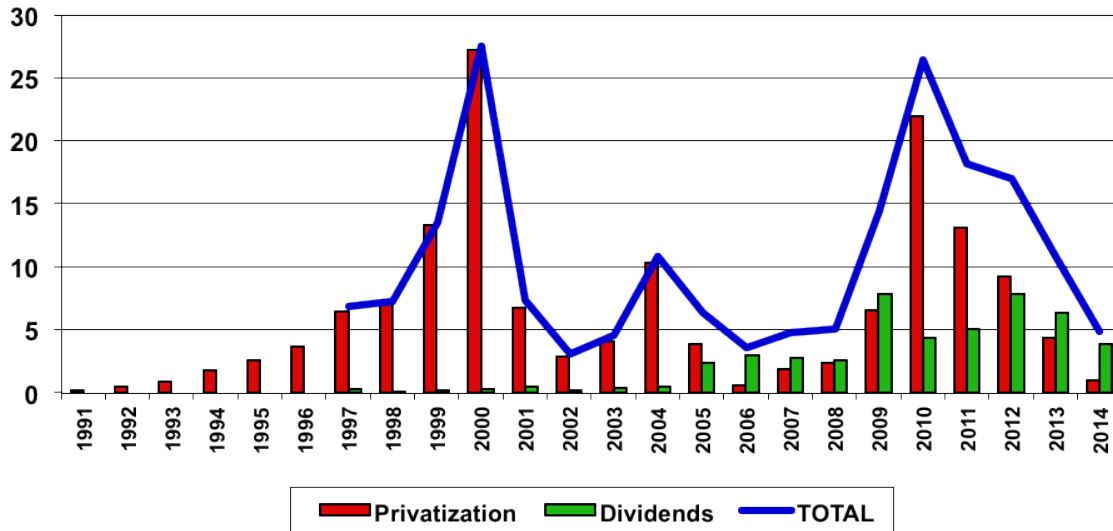
### 2.3. Paradigm Shift versus Income Dilemma

This very cautious attitude towards privatization, which became part of the government's policy at the beginning of the new century, has prevented it from meeting many of its fiscal goals. During 2001–2006, revenues from privatization fell steeply, with even modest revenue plans not being fulfilled (except in 2004, which can be explained by the personality of then-Minister of the Treasury, the aforementioned liberal Jacek Socha, who occupied this position from May 2004–October 2005). A grim “record” was set in 2006, when the lowest privatization revenues in the whole of Poland's transition history were recorded: instead of the planned 5.5 billion PLN, the real revenues were only 600 million PLN (just 11% of the planned amount). Low privatization revenues jeopardized the implementation of policies that were to be financed using these revenues. This situation also contributed to the financial failure of the pension system reform.

However, a partial solution was found: to use the right of the Treasury to receive dividend payments from its shareholdings and direct payments from non-commercialized state-owned enterprises. Since 2005, dividends have become more substantial and, in 2006–2009 and 2013–2014, this source of income provided the state with higher revenues than from privatization. Since 2006, the government began to plan dividend revenues. After the anti-reform coalition led by Kaczyński's PiS party lost the elections in 2007, and the moderately liberal PO-PSL coalition formed the new government, the Treasury re-started a quite ambitious privatization program. However, it did not resign from receiving dividend payments. In Figure 1, we see how, at the turn of the last decade, the “dividend instead of privatization” policy thus changed into a “dividend and privatization” policy. It should be also noted that two consecutive ruling PO-PSL coalitions, which are considered rather liberal (especially when compared to the previous PiS-led coalitions), implemented an even more active policy of draining companies' financial resources through dividend payments. Such a policy raises concerns about the threats to the development prospects of these companies.



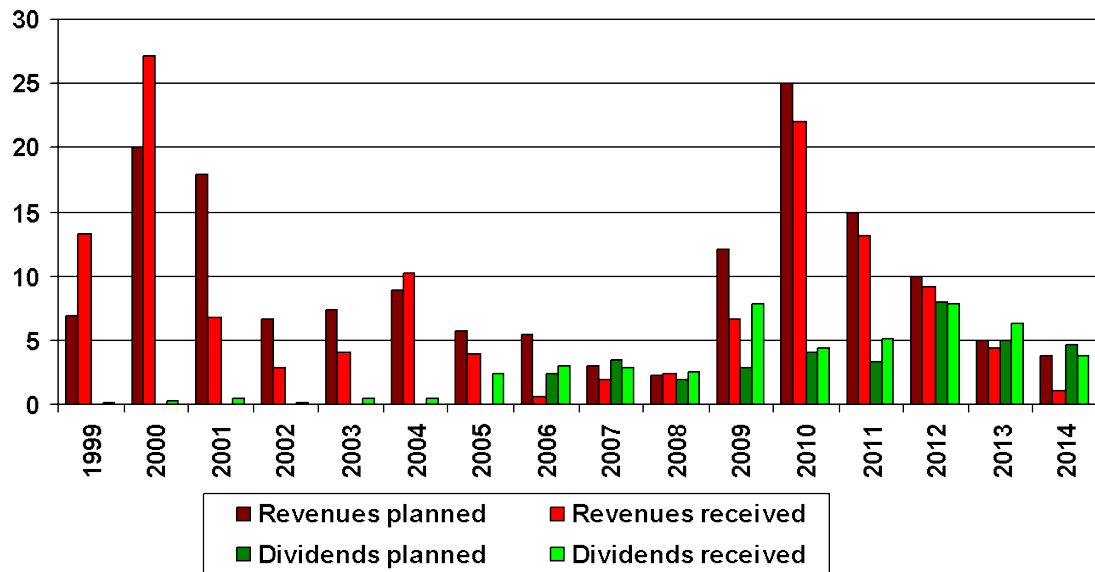
Figure 1. Revenues from privatization and dividend payments (in bln PLN, current prices).



Source: Ministry of Treasury.

If we look at the level of fulfillment of the planned privatization revenues and dividends in Figure 2, we notice that the latter is rather easier to use, being more politically acceptable in the course of solving the above-mentioned *cake dilemma*: dividend plans were usually over-fulfilled, unlike the privatization revenue plans, which, in the new century, often remained unfulfilled.

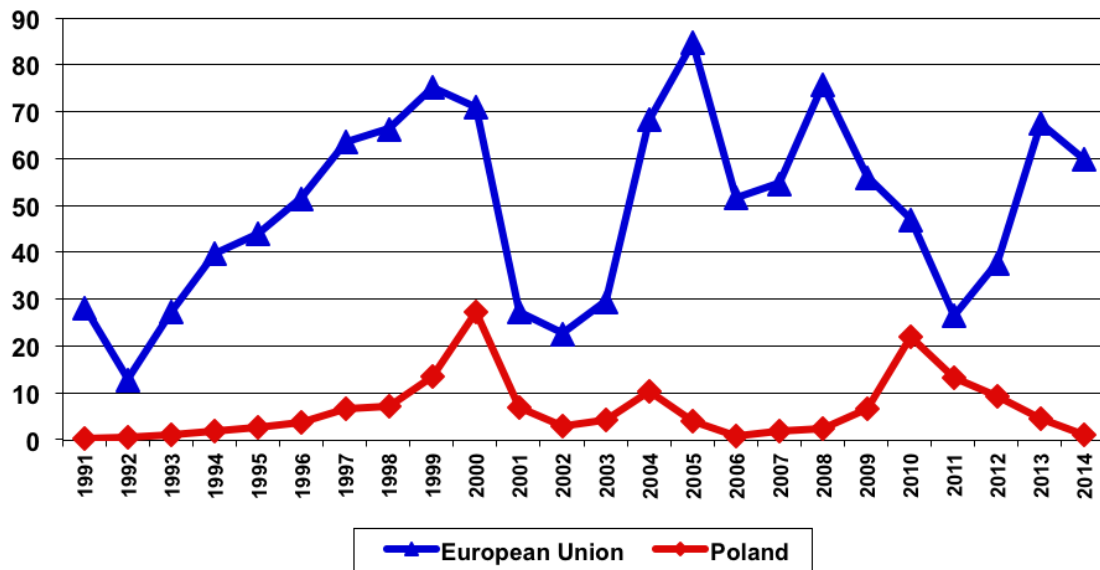
Figure 2. Planned and received revenues from privatization and dividend payments (in bln PLN, current prices).



Source: Ministry of Treasury.

If we compare the dynamics of privatization in Poland (measured by revenues from privatization) with the EU, we will see similar trends until the early 2000s (Figure 3). There was steady growth until the turn of the new century and a steep decline afterwards. Notwithstanding the different place of privatization in the economic policies of CEE post-communist countries and the many developed economies of “Old Europe,” there was some mutual ground in appreciating the role of privatization in the economy – both as a means for improving the functioning of enterprises and as a source of income for state budgets. The beginning of these declining dynamics also had some common ground: the global economic recession. However, after the world economy began to recover, privatization accelerated in the EU, but continued to decline and stagnate in Poland. A few years later, we see how the global financial crisis contributed to the declining dynamics of privatization proceeds in the EU; however, Poland again followed its own path, which was mostly opposite from the rest of the region. The first year of the crisis, 2009, was marked by growing proceeds from privatization in Poland; however, when EU economy began its recovery and privatization proceeds started to increase, a decreasing trend began in Poland.

Figure 3. Revenues from privatization in Poland (in bln PLN) and European Union (in bln USD).



Source: Ministry of Treasury; The PB Report (2015, p. 8).

In attempting to explain this discrepancy in recent dynamics, we may consider the purely fiscal goals of the Polish privatization. The period with the highest proceeds from privatization in recent years coincides with the highest general government deficit (up to 7.6% of the country's GDP in 2010) and desperate attempts by the Polish government to improve the state of public finances and, among others, to have the excessive deficit procedure lifted (which was imposed on Poland by the Council of the EU in 2009). The gradual improvement of the budgetary situation (which, indeed, is taking place since 2011) may mean decreasing incentives to use privatization as a source of revenues.

### 3. Privatization Policy Outcomes

As we have shown above, the winding road of the Polish privatization policy contributed to changes in privatization dynamics and outcomes. Thus far, five stages of Poland's privatization process have been identified (Bałtowski & Kozarzewski 2014):

Creating privatization foundations (September 1989–December 1990): developing the concept and adopting the law.

“Heroic” privatization (January 1991–December 1996): detailed solutions were developed and the government learned how to privatize. At the same time, there was strong grassroots privatization activity using the management and employee buyout (MEBO) technique.

“Mature” privatization (January 1997–August 2000): this was the period of the most intense privatization, where the highest privatization revenues were recorded.

Regress in privatization (September 2000–November 2007): political elites with a negative attitude towards privatization came to power, prompting a policy of support for the state-controlled sector. Privatization essentially stopped, causing severe problems for the state budget.

Privatization in the shadow of statism (December 2007–present): the change in the ruling elites and the more liberal Donald Tusk governments resumed privatization, but usually only for fiscal reasons and without losing state control. This period is also marked by growing support for the public sector and domestic investors.

Weak privatization outcomes in 2014 were followed with even weaker ones in 2015, when a new grim “record” was set with privatization revenues amounting to mere 43.6 million PLN (about 10 million Euro, 3.7% of the planned amount). The new government which was formed after the populist PiS won the parliamentary elections at the end of October 2015, conducts openly statist policy and at the beginning of 2016 declared that it was going to slow down privatization even more, selling only small blocks of shares and “leftovers.” It means that Polish privatization policy has entered the next, and probably the least favorable phase in the whole history of ownership change in this country.

Notwithstanding these obstacles, after 25 years of privatization, the state-controlled sector shrunk significantly. While in 1989, the public sector accounted for 70% of sales, 66% of employment, and about 70% of the country's GDP, by the end of 2013, according to



estimations based on official statistical data (Central Statistical Office, 2014a, 2014b, 2014c), it fell in the non-financial enterprise sector to 9.8% of sales, 12.5% of employment, and, according to our estimations, to about 10% of GDP. This is still somewhat more than in most developed economies; however, it makes the public sector appear marginal, and may mean that Polish economy has become almost fully private sector-driven.

Nevertheless, a quarter century of privatization has left some important items on the agenda unfinished.

The first item is that of the companies that remain under state control. These companies are more numerous than as presented by official statistics. According to our estimations, which will be published in a separate paper and considers all companies that were under effective state control (ownership control plus non-ownership control as a result of “reluctant privatization”), the real public sector share in the non-financial enterprise sector was significantly larger and amounted to 16.1% in sales and 15.1% in employment by end-2013. In our earlier research, we estimated the real share of the public sector’s GDP at about 15-20% for end-2012 (Bałtowski & Kozarzewski, 2014). State control has different forms, such as simply keeping the majority of shares in the hand of the Treasury, or as indirect control by means of holding structures, special provisions in company charters, or special rights of the government towards selected companies. Some of these forms have been discussed earlier.

The second item is that of uneven privatization results across companies of different size. An analysis of the list of the 1,500 largest Polish non-financial enterprises, compiled by the authors of this paper on the basis of the list of the 2,000 largest Polish companies by *Rzeczpospolita* (“Lista 2000,” 2014), verified and supplemented with data from other sources, shows that the bigger the enterprises are, the more likely they are to be controlled by the state (in an ownership or non-ownership way). Among the 100 largest companies in Poland, only 20 are state-controlled; however, their share in sales in this group is 42.5%, and in employment – 50.5%. Among the 25 largest companies, nearly half (12) are under state control, and their share in sales and employment in the group are 64.4% and 62.3%, respectively. Of the 10 largest enterprises, six are controlled by the state.

The third item is that of uneven results across the various sectors of the economy: while in manufacturing industries, the state sector share in sales by the end of 2012 was 5.6%, but in extractive industries and infrastructure, it was almost half: 46.2% and 45.8%, respectively (Bałtowski & Kozarzewski, 2014).

A question arises: Why may an unfinished privatization agenda be a problem for Poland and, generally, transition economies? In the most developed economies, state-controlled companies are generally not less efficient than private companies – both in economic and financial terms, as well as in terms of meeting their purpose: exercising some very important social



and/or economic public functions. Therefore, it can be expected that state-controlled enterprises may play the same role in transition economies. Unfortunately, this is very hard to achieve.

First, the role of the state-owned sector in communist economies differed radically from that of market economies. State-owned enterprises in communist countries were the foundation of the planned economy system, whereas in market economies, they occupy specific niches: public utilities which cannot be provided by the private sector at a desired scale, quality, or price, and the realization of the developmental functions of the state (Szanyi, 2014). The structure of the state-owned sector in Poland (and many other post-communist economies) is still far from that of the most developed economies, and many state-owned enterprises operate in industries where there is no reason (from the point of view of efficient economic and social policy) for the state to be involved.

Second, in developed economies, a state-controlled enterprise sector functions in a much more developed and sound institutional environment: it is efficiently controlled by the market and legal system. However, mechanisms of external corporate control are still weak in post-communist countries, the quality of the law is not always at the highest level, and there are widespread enforcement problems. In this situation, the internal control of private owners gains importance.

This leads to the inferior performance of the vast majority of state-controlled companies, and generally shows that, in given institutional conditions, the state is a less effective owner than a private one, especially in regards to strategic industrial investors. Research conducted by the authors (Bałtowski & Kozarzewski, 2014) shows that, in Poland, from performance point of view, state-owned companies, to a much higher degree than enterprises with non-state owners, were vulnerable to the conditions of the market, showing enormous ups and downs when conditions changed. The relatively favorable financial results of the state-controlled sector hide the high degree of differentiation between a few very profitable companies and the majority of the companies that were unprofitable. From an institutional point of view, these companies were one of the most important sources of rent in the economy. Corporate governance in these companies was often dysfunctional; specifically, the disproportionate authority of executives and trade unions, excessive employment, and a high degree of politically motivated decisions – both in regards to production and their high-rank personnel policies, which are directed by the both companies themselves and by the supervising state body. Thus, the state-controlled sector contributes to the dysfunction of the state, creating grounds for the politicization of economic policy, cronyism, and even outright corruption. Institutions that could help to overcome these dysfunctions are still too weak, and we have yet to see any political will to strengthen them. On the contrary, one may be under the impression that the political elites are trying to widen the scope for arbitrary decision making in the economy.



## 4. Concluding Remarks and Discussion

It can be argued that there are both endogenous and exogenous factors that have contributed to the increasing role of the state in Poland in recent years.

The first endogenous factor is inadequate institutions: the Polish state is still institutionally weak and is often not capable of performing its functions in an optimal way. These institutions are not inclusive enough, to use the terms coined by Daron Acemoglu and James A. Robinson (2012), in the sense of securing a level ground for all economic players with their rights efficiently protected. Still strong (and even showing some growth tendencies) are extractive institutions that “are designed to extract incomes and wealth from one subset of society to benefit a different subset” (Acemoglu & Robinson, 2012, p. 76). It should be stressed, however, that in Poland, privatization processes themselves were infrequently used as sources of rent. The main source of rent lays in the state-controlled sector. It is still characterized by very influential special interest groups that created a kind of political capitalism *à rebours*. While in a “straight” political capitalism, rent seekers abuse the public sector, in a political capitalism *à rebours*, the state sector is, itself, a rent seeker who abuses other sectors and populations not connected with public sector (Bałtowski & Mickiewicz, 2009). Polish extractive institutions originate both from the communist past (e.g. the predominance of state ownership) and the period of systemic reforms. Influential special interests groups of the so-called early winners have emerged who received rent from the transition process itself (Hellman, 1998; Kozarzewski & Woodward, 2006). For example, one group uses the dual role of the Ministry of the Treasury (seller and owner of public property) and extracts a rent from its political weight and possibility to distribute rents for political winners.

The second endogenous factor is the financial challenges of economic policy. The financial problems of the government, such as a high public debt and a budget deficit, should be mentioned. These financial problems force the government to look for additional sources of revenues. This is one of the causes of the fiscalization of the government’s ownership policy as well as the budding hope that support for the state sector and new public investments will help to overcome these financial problems. However, this cause seems to be of secondary importance, which may be indirectly corroborated by recent studies on state



capture in Poland that has shown that periods of slower economic growth (which may mean an aggravation of fiscal problems) did not lead to an increase in state capture. On the contrary, the likelihood of state capture was positively correlated with periods of higher economic growth, while the start of the global financial crisis had a “wake-up effect,” significantly decreasing the likelihood of state capture in that period (Alwasiak et al., 2013). Besides, the fiscal needs of the government may have an adverse effect on privatization trends, stimulating the cautious selling of the elements of state property; however, preferably, without losing control of it.

The state-controlled sector is also used to solve social problems, for example, through the creation of jobs and the protection of certain enterprises and industries that are politically “too important to fail.”

Exogenous factors seem to be relatively less important in Poland: the impact of the global financial crisis, which was followed by a worldwide change in policy paradigm concerning the role of the state (i.e. a shift from “state failure” to “market failure” approaches). From what is seen in current economic policy trends, the state should play a more active role not only in regulation and enforcement, but should also be more interventionist as an active supporter of market players and increase its role as a business player itself. It should be noted that during the first wave of the crisis, during 2008–2009, the Polish government, unlike many other governments in more developed economies, did not conduct a broad interventionist policy. Rather, it focused on protecting the liquidity of financial markets and the stability of the country’s financial system. This was a much less expensive policy that brought about positive results and contributed to the situation where, in 2009, Poland was the only European country that achieved economic growth, albeit very modest. The recent pro-interventionist shift in the role of the state in Poland occurred mainly after the first wave of the global crisis had peaked. Therefore, both the change in the style of economic policy and the direct impact of the global crisis seem to be of secondary importance. In addition, the lack of a correlation between privatization trends in the EU and Poland may corroborate the thesis that the economic policy of the Polish government, at least in its ownership segment, has predominantly endogenous roots.

We treat these conclusions and remarks as small steps towards understanding the subject in question. Further study is needed, such as, among others, a deep analysis of the factors identified in this paper from the perspective of their relative strengths, mutual dependencies, and the specific mechanisms exerting an impact on privatization policy (and, more broadly, on the level of statism in the economic policy of the Polish government).

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