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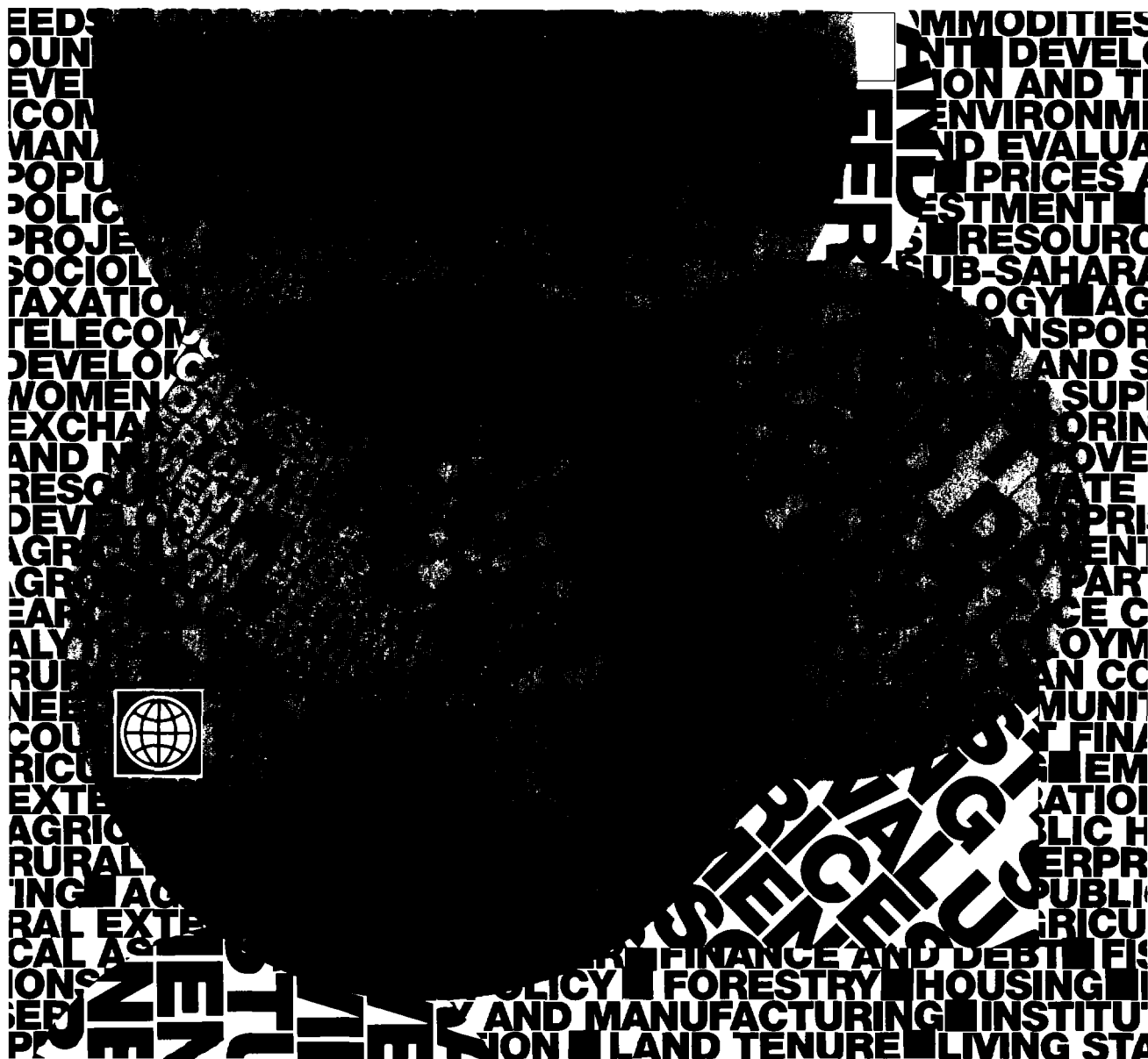
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The Emergence of Private Sector Manufacturing in Poland

A Survey of Firms

Leila M. Webster



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Leila M. Webster

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Washington, D.C.

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FOREWORD

When Communist governments fell in Eastern Europe in 1989 and the new governments embraced capitalism, it was immediately clear that the key to renewed growth would be the transfer of capital from the state to private agents and the transfer of economic planning from bureaucracies to individuals. Questions arose quickly about the speed and the means by which private sectors could be built. Privatization of state enterprises was correctly judged to be a complex and lengthy affair, and many observers doubted that the spirit of entrepreneurship needed to spark large-scale private entry could have survived 40 years of suppression. How quickly could individuals who had grown up in socialist economies adopt the values and behaviors of capitalism and amass the capital needed to invest in private businesses? Many asserted that it would take a generation.

This research confirmed that, contrary to expectations, a great spirit of entrepreneurship sprang forth in Eastern Europe within 18 months of liberalization of entry regulations. By mid-1991 when this survey work was completed, Polish business rosters already contained tens of thousands of newly-registered, private firms, hundreds of thousands of sole proprietorships, and thousands of joint ventures--and the numbers have continued to grow. In addition, this study confirms that many of the new Polish entrepreneurs are, in fact, well-qualified to meet the challenges of private enterprise, particularly in terms of general educational levels and technical, production knowhow. And experience is quickly teaching them the basics of business management.

At the same time, it was clear that the entrepreneurs included in this survey were in trouble due to the very difficult macroeconomic setting that prevailed in Poland in May 1991. The post-reform recession was in full swing at the time of this survey, and this report documents in detail the nature of the difficulties faced by small manufacturers when a former socialist country plunges into recession. Since May 1991, the Polish economy has reversed its steep decline and begun the ascent to sustained, positive growth. And the private sector contribution to this recovery is large and growing. This study, therefore, becomes an important record of the valley through which private Polish manufacturers had to pass in the first years of the economic and political transformation in Poland.

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ABSTRACT

The central objective of the research that is summarized in this report was to document the characteristics and problems of private sector manufacturers in Poland eighteen months into the reform program. Specifically, this project had four objectives: (i) to develop a profile of entrepreneurs and their firms; (ii) to evaluate the impact of the reform program at the firm level; (iii) to identify constraints to growth; and (iv) to formulate recommendations for action, including policy and regulatory changes and initiation of business support programs.

The heart of the research was a firm-level survey of 93 businesses carried out in Poland in May 1991 by teams of researchers. Firms were drawn randomly from the population of registered, majority privately- and domestically-owned manufacturers with seven or more employees. Excluded were the large self-employed sector, firms engaged in trade or services and joint ventures. Interviews lasting 3-4 hours were held with each entrepreneur.

Chapter I contains the project objectives, analytical framework, research issues and the research methodology. Chapter II describes the macroeconomic setting in May 1991 and presents an historical and current picture of the Polish private sector. Chapters III and IV summarize the characteristics of sample entrepreneurs and their firms. Chapter V analyzes firm-level constraints to growth and presents a profile of successful firms. Chapter VI presents entrepreneurs' requests for assistance, and makes a number of recommendations for action, and Chapter VII returns to the research questions raised in Chapter I and sums up research findings.

This survey is part of a comparative study of private sector manufacturing in Eastern Europe financed by the Research Committee of the World Bank in December 1990. The project included comparable surveys implemented in Hungary in September 1991, and in the former Czech and Slovak Federal Republic in January 1992. An additional survey, financed jointly by the former Industry Development Division of the World Bank and the Chief Economist's Office of the EBRD, was carried out in St. Petersburg, Russia in November 1992. A final project document synthesizing findings from all four surveys will be completed in late 1993 or early 1994.

EXECUTIVE SUMMARY

The Project

The central objective of this research was to document the characteristics and problems of private sector manufacturers in Poland so that they can be supported as effectively as possible. In doing so, this project also produced an historical record of the status of private sector manufacturers eighteen months into Poland's reform program. The research had three specific objectives. The first was to develop a profile of entrepreneurs and their firms. The second was to evaluate the impact of the Polish reform program on firm-level operations and to identify constraints to further growth. The third objective was to formulate recommendations for actions to strengthen the Polish private manufacturing sector.

The heart of the research was a firm-level survey of 93 firms carried out in Poland in May 1991 by teams of researchers. Firms were randomly drawn from the population of registered, majority privately- and domestically-owned manufacturers with seven or more employees. Excluded were the large self-employed sector, firms engaged in trade or services, and joint ventures. In-depth interviews lasting 3-4 hours were held with each entrepreneur.

Background

The Polish government's strategies for economic stabilization, liberalization and transformation focussed on rapid, comprehensive reform. The results of the stabilization program in 1990 were promising, but problems with maintaining positive trends became obvious in 1991 as surpluses turned to deficits. Recession set in with falling production in the state sector and increasing unemployment. The difficulties associated with privatization of large numbers of state-owned enterprises became apparent. On the positive side, liberalization policies ended shortages, jump-started markets and opened up the economy to international trade.

Polish reformers stated their intention to remove discriminatory laws and regulations that historically favored state-owned enterprises and to place private firms on an equal footing with other enterprise forms. Passed in January 1989, the "Law on Economic Activity" set the stage for large-scale entry of private entrepreneurs by removing restrictions on the activities and numbers of employees permitted in private firms, and by minimizing licensing and registration requirements. The pre-existing Company Law of 1934 was resurrected to provide corporate forms--limited liability and joint stock companies--for those who wanted to move beyond sole proprietorships.

The response was immediate. By the end of 1989, over 800,000 people had established sole proprietorships and more than 16,000 new companies were registered. The upward trend in the numbers of new entrants continued throughout 1990 and 1991. Estimates were that private enterprises (excluding agriculture and cooperatives) contributed about 19 percent of GDP and 18-20 percent of total employment by end-1990. By end-1991, the private sector share of employment (excluding agriculture and cooperatives) had reached about 26 percent and by end-1992, about 34 percent. Including cooperatives but excluding agriculture, private sector employment reached 44 percent of total employment by end-1992. Private sector share of GDP (excluding agriculture and cooperatives) was about 24 percent for 1990 and 35 percent by end-1992.

Consistent with the rest of the economy, however, the 1990 boom in private sector industry slowed down substantially in 1991. The numbers of private industrial units continued to grow but at a slower pace, and the capacity to absorb additional labor appeared to have stagnated. Most new growth

in the private sector took place in trading, particularly in importing. However, the Polish economy rebounded in 1992, and private sector industrial production expanded to account for about a third of total industrial output.

Survey findings should be understood within the macroeconomic setting prevailing in May 1991 to both clarify and qualify results. At the time of this survey, the favorable conditions of 1990 had disappeared and the costs of the transition were negatively impacting sample firms. The state sector was collapsing; CMEA trade had closed down; the zloty had appreciated; private traders had brought competing imports into the smallest towns; and unemployment had risen to 10 percent of the labor force. In sum, this research was conducted at a low point in the Polish recovery--a fact confirmed by the much-improved performance of the economy in 1992.

The Entrepreneurs

The majority of sample entrepreneurs were middle-aged and well-educated men with strong technical skills, usually in engineering. Most previously were managers in state enterprises. As expected, they were highly inexperienced in operating private businesses: the current business was the first business for 88 percent of those interviewed, and 60 percent were manufacturing products that were unrelated to those produced previously. They were motivated to enter private business first by the desire to work on their own, second by the desire to exploit fully their skills, and third by financial remuneration. Their personality traits were similar to entrepreneurs everywhere: they were practical people who liked to be in control and were willing to take some risks.

The skills required to succeed in May 1991 differed from those needed by the first wave of post-reform entrepreneurs who started up in 1989 and 1990. The first group were opportunists who started by filling shortages in their local economies. As shortages eased with massive "gap-filling" by Polish importers and large numbers of new domestic producers, profitable opportunities for those with sharp eyes and a willingness to risk diminished. The second wave of successful entrepreneurs--captured in this survey--was composed mostly of engineers who were able to combine strong technical skills with abilities to manage small businesses.

The Firms

Almost all firms surveyed were limited liability companies owned by groups of three to six individuals. Just under half were located in rural areas. Firms were small. Sixty percent had fewer than 20 workers, and almost 75 percent reported monthly sales of less than US\$50,000. Ninety percent originated as private firms. Firms were engaged predominantly in the five sectors that were pre-selected through stratifying the sample: knitting, clothing, plastics, metal working and machinery.

Sample firms traced their origins to three main sources. Three-quarters were new start-ups. Twelve percent were former private sector craftsmen who had taken corporate form, and 10 percent traced their origins to the state enterprise and cooperative sectors. Of note is the minimal contribution of the state enterprise sector to the formation of the private industrial sector in Poland. A comparison with comparable samples of firms in the former CSFR and Hungary shows that approximately half of firms in these countries originated in the state and cooperative sectors.

Almost all entrepreneurs relied on cast-off equipment from state enterprises, much of it purchased at cut-rate prices based on personal connections. Production equipment averaged 10.4 years in value-weighted terms, but appeared far older in vintage. Many entrepreneurs were anxious to replace their

equipment, but they were unwilling to borrow funds for investment until interest rates fell. A surprising 65 percent of entrepreneurs had received short-term loans from banks since 1988, and there was general agreement that it was relatively easy to get a loan from a bank if one were willing to pay going interest rates. Loans were distributed equally across weak and strong firms and rising and falling sectors, indicating some weakness in Polish banks' abilities to appraise loan applications.

The average monthly cost per worker was US\$297, and monthly wages averaged US\$155. Entrepreneurs offered fewer benefits to their workers than provided by state employers. Entrepreneurs reported few problems recruiting unskilled workers, the bulk of workers in most firms. Rather, the difficulty was in luring skilled workers away from state firms. Most firms appeared to have little if any capacity to absorb more workers and indeed, many needed to shed some of those they had hired when sales were higher in the final months of 1990.

Problems in labor markets were substantial, including: (i) immobility of workers due to housing shortages; (ii) lack of information systems that would link employer with potential employee; (iii) an incentive structure that appeared to favor continued employment in the state sector for some workers; (iv) a strong social ethic among private employers against laying off workers even when they were redundant; (v) a narrow skill base among workers; and (vi) apparent low labor productivity and a dearth of mechanisms with which to improve it.

Counter to researchers' expectations, almost all entrepreneurs had secured factory space with relative ease, even in cases where ownership questions were unresolved. Most had long-term leases on their factory buildings--a practice that guaranteed entrepreneurs stable rent and access to their buildings for periods long enough to justify the often substantial renovations required. Entrepreneurs had invested heavily in extensive renovation of factory buildings at their own expense. Of note is the fact that only 12 percent of Polish entrepreneurs owned their buildings compared with 28 percent of Hungarian entrepreneurs interviewed and 45 percent of Czech and Slovaks.

With few exceptions, entrepreneurs were able to obtain a full range of imported and domestic raw materials and intermediate inputs, a powerful testimony to the efficacy of "big bang" reform. The extent to which private firms were simply serving as conduits for imported inputs is shown by the fact that over 80 percent of the value of domestic inputs used by entrepreneurs was produced by state enterprises. Half of sample firms sold mainly to state firms and half to private firms. Entrepreneurs reported no problems with distribution.

Constraints and Prospects

Three issues dominated when entrepreneurs were asked to name their three main problems in order of importance. Lack of demand was cited first by 30 percent of entrepreneurs; financial problems by 28 percent; and constantly changing government regulations by 10 percent.

Demand problems were of two kinds: a loss of markets due to the introduction of competition--considered a necessary loss in the adjustment process--and a loss of markets due mainly to economic recession--a loss to be minimized. Based on analysis of the sources and intensity of competition faced by firms, researchers estimated that about 60 percent of entrepreneurs who cited inadequate demand as their principal problem were, in fact, having trouble competing with imports. Most knitting, clothing, and plastics firms fit into this category.

Two important questions follow. The first asks why many entrepreneurs were unable to compete with imports. Possible explanations included: overvaluation of the zloty, pent-up demand for Western goods among Polish consumers, and inferior quality and higher prices of Polish goods. This survey produced no data that could answer this question definitively, but anecdotal evidence was that the latter two factors were more critical than the first. The second question asks how entrepreneurs were responding to falling orders for their products. Some entrepreneurs were jumping from product to product as niches opened and closed; a few were developing new products; some were watching their inventories grow and were hoping for miracles; and many were folding.

The remaining 40 percent of entrepreneurs with demand problems were in trouble for other reasons. Some entrepreneurs were producing competitive products, but had lost sales due to the recession. Some were suppliers for state firms that were declining. Others had lost sales due to unexpected government cutbacks or sudden shifts in government regulations.

The 28 percent of entrepreneurs who cited financial problems as their primary problem were concerned about exorbitant interest rates, slow payment by state firms for goods delivered, and lack of working capital. Entrepreneurs were uninterested in distinguishing between nominal and real interest rates. In their view, rates charged by banks were far too high and they held the government responsible for allowing rates to climb. Shortages of working capital often were inter-linked with slow payment or lack of payment by state firms. Many private entrepreneurs had taken working capital loans to cover the financing gaps created by non-payment, thus involuntarily extending credit to the state sector.

Identification of the additional costs of doing business involves analysis of the impact of government regulations, the state of physical infrastructure, the dominant state enterprise sector, and prevailing social attitudes toward private enterprise. The success of the Polish government in formulating a new regulatory framework that would support private sector entry was verified by entrepreneurs who obtained start-up licenses and permits painlessly and quickly. At issue was the stability of government regulations, particularly tax regulations. Entrepreneurs complained that they were not able to plan when regulations change frequently and with no warning. The result was a cynicism and distrust of government that was plainly visible to interviewers.

Substandard infrastructure did not prevent entrepreneurs from doing business, but it clearly lowered their efficiency. Transacting business in person instead of by telephone and installing their own power lines raised entrepreneurs' costs and chipped away at their ability to compete in world markets.

The dominant state industrial sector had contributed virtually nothing to the formation of the private productive sector beyond used equipment. Researchers observed no evidence of the kind of wholesale transfer of assets from state to private hands envisioned by the government's privatization program. Where state firms were in rapid decline, supplies of raw materials and inputs for private buyers had become unreliable. State enterprises were the largest customers in the economy, but they imposed hardship on private firms when they did not pay their bills. Sample entrepreneurs who competed with state enterprises were convinced that the scales remained tipped in favor of their state-owned competitors through access to credits, subsidies, and "inside deals" not available to them.

A deep and observable ambivalence toward private enterprise and accumulation of personal wealth appeared to remain in both public and private spheres. Forty-five percent of entrepreneurs said that the attitudes of public officials toward them were negative; 26 percent said they were neutral. When asked about the attitudes of the average citizen toward them, 52 percent said they were negative and 22 percent said they were neutral.

Firm's prospects were assessed through combining production and profitability data with rankings assigned each firm by survey teams. About half of firms were contracting, a high percentage especially when compared to private Hungarian and Czechoslovak firms in comparable samples, most of which were on the upswing. The winners and losers in this transition economy were clear. Most knitting and clothing companies and the lower-tech plastic and metal products were declining, primarily due to competition from lower-cost imports. Firms producing machinery and more complex plastic and metal products were stable and some were expanding. Well over half of sample entrepreneurs had added retail trade to their activities to bolster revenues.

A comparison of strong and weak firms shows that the key to success among sample manufacturers was locating niche markets protected from the intense competition of imports and state enterprises. Successful firms identified specific needs in given markets and responded with specialized products, usually sticking with single products and upgrading equipment to improve efficiency and product quality. Finished goods from strong firms usually were of higher quality than the imported equivalent or were unique and specialized. Most intermediate goods were custom products for which demand was fairly inelastic and imported substitutes were hard to find. Successful firms' products tended to be technically more complex than those in failing firms: they were building machines rather than cutting sheets of metal. While most of the technical expertise embodied in these products stemmed from owners' previous job experience as engineers and designers, upgrading of technology and knowhow in a few firms was facilitated by a foreign partner or a formative experience abroad.

The key to failure among sample firms was production of mass-produced, cheaper goods that could not undersell competing imports. If they were finished goods, they were subject to diminished consumer demand and to a flood of low-priced imports. Some intermediate goods were subject to dropping demand as state firms reduced output. Goods produced by these firms tended to be simple mass-produced items such as plastic containers, blue jeans, knitted shirts and metal braces.

Needs for Assistance and Recommendations

When asked to describe the types of training courses that would be most useful to them, most entrepreneurs asked for training in management and marketing and for information of all kinds. Management referred generally to the ability to organize production in more efficient ways, motivate workers to be more productive, and manage company finances more effectively. The lack of marketing knowhow was an outstanding weakness in entrepreneurs' skills. Entrepreneurs also clearly suffered from a dearth of product-specific information needed for strategic planning. Most had had little experience with available technical assistance programs, but the few who had participated were disappointed with them.

The central focus of policies and programs to encourage industrial growth should be to enhance the competitiveness of Polish products in domestic and foreign markets. First-order recommendations to move toward this objective include: (i) adoption of a pro-active initiative to move beyond getting incentives right to building capabilities of entrepreneurs and developing institutions to facilitate their success; (ii) inclusion of private sector issues in the national political and economic debate; (iii) broadening and deepening of labor and financial markets; and (iv) increasing the flow of several types of information critically needed by entrepreneurs. Second-order recommendations focus on lowering the costs exacted from private producers by the business environment through: (i) privatizing state sector as quickly as possible; (ii) stabilizing official regulations affecting private producers; and (iii) improving infrastructure, with particular emphasis on telecommunications and local infrastructure. Third-order recommendations involve delivery of a variety of technical services to entrepreneurs.

Conclusions

The reform program adopted by the Polish government had both helped and hindered private firms included in this survey. On the one hand, legal and regulatory reforms cleared the way for massive private sector entry. Liberalization policies successfully jump-started markets to the extent that, in May 1991, manufacturers were able to locate factory space, buy used equipment, employ workers, obtain domestic and imported intermediate inputs, secure working capital loans, and distribute their products internally and abroad--all without prohibitive difficulties. On the other hand, many entrepreneurs in this study were in trouble, unable to sell their products in an economy characterized by recession and fierce competition. Rapid trade liberalization forced domestic producers to compete on world markets almost immediately, without time to learn business basics and without institutional support--a situation avoided in Hungary and CSFR where exposure to world markets proceeded more slowly.

With hindsight, are there ways in which the reform program adopted by the Poles could have been improved upon? Analysis shows that, in at least four respects, the sequencing of the reforms was somewhat unfortunate. First, the Law on Economic Activity which precipitated massive private sector entry was passed in January 1989, a full year before adoption of the reform program which liberalized prices and the trade regime. Therefore, the 800,000 self-employed persons and the almost 12,000 registered companies that started up in 1989--as well as the tens of thousands who began in the first months of 1990--did so in response to signals in the pre-reform environment--most notably shortages and limited import penetration--only to find they had invested their limited resources in products that were no longer profitable in the post-reform economy. Their losses and subsequent disillusionment could have been avoided had the legalization of private business and liberalization of the economy proceeded in tandem--a problem that perhaps could not have been foreseen in the Polish context but could possibly be avoided in other countries.

Second, rapid trade liberalization--designed to introduce competition generally and to force efficiency gains in the state sector specifically--may have been more effective in undercutting the fledgling private manufacturing sector than in prompting the state sector to restructure. A major instrument of trade liberalization was full currency convertibility, a measure which allowed hundreds of thousands of self-employed traders to bring in a flood of higher quality and lower cost imports. Consumers benefitted, but private producers were overwhelmed. To the extent that firms had little potential to compete with imports, necessary losses were incurred. But to the extent that entrepreneurs could have competed with imports had they been afforded more time and resources, unnecessary losses were sustained and irreplaceable good will was lost.

Third, the failure to privatize the large state industrial sector maintained a playing field tilted in favor of the state sector, and diluted the effectiveness of the reform effort. Industrial assets that could have been used productively by the private sector remained in state hands, and the dominance of the state sector crowded out private sector investment. Privatization issues dominated government time, and diminished the time available for work on private sector development.

Fourth, interviews with entrepreneurs indicated that the Polish government did a poor job of communicating with its citizenry about the reform process and enlisting broad-based participation. Most entrepreneurs demonstrated little understanding of capitalism or of the government's reform program. They did not see themselves as key actors or even participants in the transformation process, but rather as marginal players who more often than not were victimized by the process. Unrealistic expectations probably were unavoidable, but the disillusionment and cynicism observed among entrepreneurs might have been lessened had they been given more information and somehow included more in the process.

The final question posed in the report asks whether the trouble observed in at least half of sample firms was part of a necessary and healthy adjustment process or whether it was a harbinger of stagnation in the private industrial sector? Two compelling and apparently conflicting explanations are examined. In the first argument, the downturn observed is interpreted as temporary adjustment shock--a necessary cost of reorientation of the economy and a positive sign that the reform program was in fact achieving its objectives of producing a competitive private sector. A second, conflicting interpretation is that the downturn observed in large numbers of firms was an indication that the 1989-1990 boom for private producers was over, and that much of the private industrial sector was headed down--unable to surmount the effects of the recession, the failure to privatize the state sector, and the flood of competing imports. The report lays out the evidence on both sides of this critical question and then concludes that, in fact, both forces were at work in the Polish economy in May 1991 and time would tell which will prevail.

Addendum

Additional information and insights are available as this report goes for publication. The Polish recession lifted over the course of 1992, and the growth of industrial output, led by private sector growth, became positive by a slight percentage. Despite some scrambling of aggregate statistics, it is clear that the private sector share in GNP and employment is large and growing. With hindsight, it has become obvious that this survey was conducted in a particularly difficult period for private Polish manufacturers who were faced with the triple challenges of adjusting to new price signals in the domestic economy, coping with a severe recession, and confronting the reality of competition in world markets. Few had profit margins sufficient to blunt the impact of these three enormous forces, and many were in deep trouble. This report documents the precise nature of that trouble. Current positive trends in private sector growth are heartening because they indicate that substantial numbers of private producers have come through the valley of 1991 to a higher level of success in 1992 and 1993. Especially encouraging is the strong growth of private sector exports, an indication that Polish producers are finding avenues by which they can compete in world markets.

INTRODUCTION

This report contains the findings of a survey of private manufacturing firms carried out in Poland in May 1991. This survey is part of an 18-month comparative study of private sector manufacturing in Eastern Europe financed by the Research Committee of The World Bank. The project also includes comparable surveys implemented in Hungary (September 1991) and in the Czech and Slovak Federal Republic (January 1992).

The report is organized as follows. Chapter I contains the project objectives, analytical framework, research issues, and the research methodology. Chapter II describes the macroeconomic setting in May 1991 and presents an historical and current picture of the Polish private sector. Chapters III and IV lay out the basic characteristics of sample entrepreneurs and their firms. Chapter V analyzes firm-level constraints to growth and presents a profile of successful firms. Chapter VI presents entrepreneurs' requests for assistance, and makes a number of recommendations for action. Chapter VII returns to the research questions raised in Chapter I and sums up survey findings.

Of note is the presentation of survey data. Firm characteristics were cross-tabulated with firm size, sector, age and location. It was quickly observed that firms' characteristics varied a great deal by sector and location, and almost none by size or age of firm. Therefore, data are presented throughout the text in terms of firm sector and location, with references to firm size and age only when relevant.

The nature of this project should be kept in mind. Survey findings are based on in-depth, three-to four-hour interviews with a carefully selected group of private Polish manufacturers in May 1991. The results are, in effect, a series of detailed quantitative and qualitative photographs of firms operating in the setting prevailing at that time. In retrospect, it has become clear that the Polish business environment documented here has improved greatly since the survey was concluded. In this sense, this survey report becomes valuable mainly as an historical document that spells out the problems faced by private firms during post-reform recession.

I. THE PROJECT

Project Objectives

The central objective of this research was to document the characteristics and problems of private sector manufacturers in Poland so that they can be supported as effectively as possible. In doing so, this project also produces an historical record of the status of private sector manufacturing eighteen months into Poland's reform program.

The research had three specific objectives. The first was to develop a *profile* of entrepreneurs and their firms. The second was to assess sample firms' *prospects*, an analysis that included an evaluation of the impact of the Polish reform program on firm-level operations and identification of constraints to further growth. Key factors for success were identified by comparing high performance firms with those that were failing. The third objective was to formulate recommendations for *actions* to strengthen the Polish private manufacturing sector.

The Analytical Framework

The theoretical literature provides no single framework to analyze the development of private, productive enterprises in formerly centrally-planned economies. The most closely related area of research is empirical work on firm-level response to structural adjustment programs. The sources of economic problems in pre-reform Poland and the magnitude of the transformation involved differ from those in typical adjusting countries, but the macroeconomic imbalances and the measures taken to stabilize and liberalize the economy are similar. A pilot survey conducted in Poland prior to this study indicated that constraints faced by Polish entrepreneurs were indeed similar to those reported in adjusting countries. Without underestimating the unique set of circumstances in Poland, the empirical evidence on firm-level response to adjustment programs is used here as a starting point from which to formulate research issues.

Firm-level Response to Adjustment: What We Know

At the aggregate level, the *Report on Adjustment Lending II*^{1/} confirms that private investment response in many adjusting countries has been disappointing, and offers some possible explanations, as follows:

- (i) Tight monetary and credit policies discourage investment by raising the cost of credit and the opportunity cost of retained earnings.
- (ii) Real devaluation discourages investment by raising the price of imported capital goods and intermediate inputs as well as reducing aggregate demand.
- (iii) With trade liberalization comes a reduction of investment in import-substituting industries.
- (iv) Potential investors are unwilling to risk their capital when they are uncertain about the continuity of new policies, regulations, prices and incentive schemes.

^{1/} "The Report on Adjustment Lending II: Policies for the Recovery of Growth," The World Bank. March 26, 1990 pp. 84-93.

- (v) Cuts in government investment in complementary public projects, such as roads, ports, and telecommunications, have a negative impact on private investment.

Dornbusch offers a further discussion of the lack of investment response in adjusting countries in "From Stabilization to Growth".^{2/} He views stabilization and adjustment as necessary but insufficient conditions for resumption of growth, and criticizes official institutions for offering "unjustifiably rosy scenarios ...based on assumptions that do not hold in practice." His explanations for low levels of private investment include: (i) budget corrections that reduce real wages and hence internal demand, without which firms will not invest; (ii) diversion of scarce available resources away from exports and import substitution; (iii) short-run contractionary effects of real depreciation on demand; (iv) cutting back of credit and an inability to finance government support measures; and (v) entrepreneurs' lack of confidence in the stability of the policy environment.

Firm-level studies include those carried out in Africa^{3/}--Ghana, Malawi, Senegal, and Tanzania--and in Latin America^{4/}--Chile, Argentina, and Uruguay. Researchers in Africa found no shortage of entrepreneurs but rather a host of constraints to growth, mostly traceable back to the macroeconomic setting. Sample entrepreneurs were squeezed by higher input costs and an inability to raise prices due to eroded domestic demand and competing low-cost imports. Even the strongest firms lacked access to institutional credit for working capital and investment, despite an apparent willingness to pay going interest rates. Entrepreneurs were isolated from larger, growing markets and information sources, and they had few linkages with large enterprises. The regulatory environments were neutral in principle, but in practice government officials had failed to facilitate private sector growth by processing required paperwork in a timely fashion, cutting through bureaucracy, and supplying needed information.

An analysis of the prospects for Ghanaian firms in 1989 revealed that the process of adjustment envisioned by policy-makers for the state enterprise sector was in full swing in the private sector. Firms that could not compete in the post-reform environment were failing, and those that had located niche markets were expanding. Weaker firms manufactured mass-produced, undifferentiated goods--typically textiles, clothing, and simple metal products--that competed, or rather failed to compete, with imports. Stronger firms exploited niche markets, producing custom goods that faced little competition from imports. Where they did compete with imports, successful producers aimed for the top end of the market. Successful Ghanaian entrepreneurs were young and well-educated, often with engineering backgrounds.

^{2/} "From Stabilization to Growth" by Rudger Dornbusch, Massachusetts Institute of Technology. Presented at the World Bank Annual Conference on Development Economics, 1990 pp. 30-34.

^{3/} See "Ghana's Small Enterprise Sector: Survey of Adjustment Response and Constraints" by William Steel and Leila Webster (June 1990), Industry and Energy Department Working Paper, Industry Series Paper No. 33 and "Adjustment and Constrained Response: Malawi at the Threshold of Sustained Growth" by Claudio Frischtak (October 1990), Industry and Energy Department Working Paper, Industry Series Paper No. 41. Survey data for Tanzania and Senegal have been analyzed and papers are forthcoming.

^{4/} See "Scrambling For Survival, How Firms Adjusted to the Recent Reforms in Argentina, Chile, and Uruguay" edited by Vittorio Corbo and Jaime de Melo. World Bank Staff Working Paper, Number 764. 1985.

Researchers in Latin America looked at how managers of firms were adapting to import competition. They found that four strategies for improving efficiency dominated. First, firms met import competition by greater product specialization and improvements in product quality. Second, they consolidated production and reduced their labor force. Third, they increased investment in new machinery and plant modification. And fourth, they purchased foreign blueprints and negotiated profit-sharing and licensing agreements with foreign firms.

In addition, researchers in Latin America found that appreciated exchange rates resulted in "misplaced" investment to produce exports that never materialized. A shift from production to importing was common in all three countries when the trade regimes were liberalized. Of particular relevance to Poland was the finding that policy reversals delayed adjustments in efficiency. Adjustments were most comprehensive and quickly implemented when there was little doubt about the irreversibility of policies.

Research Issues

Combining the above empirical work on firms in adjusting economies with knowledge of conditions in Poland, the following appear to be the key questions for research:

- (i) How have the components and sequencing of the Polish reform program affected the prospects of private producers? Which elements of the program have been most beneficial to private manufacturers' growth and which have been most detrimental?
- (ii) What are the major constraints reported by entrepreneurs? What are the sources of these problems, and how do they differ from firm-level constraints reported in adjusting countries?
- (iii) What factors enable some entrepreneurs to overcome constraints and operate profitably? What measures will entrepreneurs take to maintain profitability in their changing, increasingly competitive environment? Are their strategies to maintain competitiveness similar to those found in Argentina, Chile, and Uruguay?
- (iv) What is the impact of the dominant state sector on private producers? How has the government's privatization program affected the formation and development of private sector manufacturing?
- (v) What kinds of assistance could most effectively support the development of Polish private manufacturing?

Research Methodology

The Approach

Changes were underway in data collection practices of the Central Statistical Office in Poland, particularly concerning private sector statistics. However sound, aggregate data reveal little about entrepreneurs' perceptions and behavior, and almost nothing about their prospects. In-depth interviews with owners and managers provided researchers with detailed information about firm-level responses to macro-level changes.

Selection of a nationally representative sample was fundamental to formulating valid conclusions about the Polish manufacturing sector as a whole. A nation-wide approach also produced key data about the distribution of opportunities across regions, and between urban and rural areas.

The Population

To be eligible for inclusion in the population from which the sample was drawn, firms had to be:

- (i) registered companies;
- (ii) at least 51 percent privately and 51 percent domestically owned;
- (iii) engaged primarily in manufacturing;
- (iv) employers of seven or more workers.

The population was restricted to registered firms--limited liability and joint stock companies--because these incorporated enterprises tend to be larger and more formally organized than other types of private domestic units. As well, fairly complete rosters of registered firms exist in all three sample countries, a key factor in obtaining comparable cross-country samples. Under the assumption that larger firms have stronger prospects than smaller ones, an employment criteria was applied to exclude microenterprises.

Several large and important groups of private enterprises were excluded from this population. First, self-employed persons (sole proprietorships) who numbered over one million in Poland were excluded. Anecdotal evidence is that some large enterprises operated as sole proprietorships but the vast majority appeared to be quite small, averaging 1.7 workers including the owner. Inclusion of this group would have precluded selection of a representative sample as the population of self-employed persons was unknown. Rapid turnover would have limited the possibility of tracking firms over time. Second, joint ventures and foreign firms were excluded because their constraints and prospects are likely to differ substantially from those of domestic firms. Third, firms whose primary activities are trade and services were excluded because these entrepreneurs operate their businesses under a different set of parameters than those affecting manufacturers.

Sample Selection

The sample was randomly selected on January 9, 1991 from the roster of 6,646 registered, manufacturing firms in the Central Statistical Office in Warsaw. With the longer term objective of cross-country comparisons, a random sample drawn from the whole population was supplemented by five stratified random samples representing industrial activities common to Poland, Hungary and CSFR. The activities were plastics, clothing, knitting, metal working and manufacture of machinery.

The sample was selected in two segments. The initial sample of 440 firms was reduced through a subsequent step in which letters were sent to the selected entrepreneurs, asking them to verify their activities, ownership structure, and number of workers, and inviting them to join the survey.^{5/} The final sample of 93 firms was selected randomly from the 270 responses, and it represents 1.4 percent of the

^{5/} A potential source of bias arises from non-respondents to the letter. To the extent that letters were not returned because businesses had failed, survey results are overly positive. To the extent that entrepreneurs did not respond because they were indifferent to a World Bank survey or were doing well and had few complaints, survey results are overly negative.

population.^{6/} Sample firms in each of the five targeted groups represent about 2.5 percent of the population of each activity, except for knitting where the sample is 8 percent of the population. Firms were located throughout the country, and two-person survey teams spent about three hours with each entrepreneur (see map of company locations in Annex 3). The survey was completed in three weeks, ending the middle of May 1991.

^{6/} Of the ineligible respondents, about 25 percent each had fewer than 7 workers, had closed down, had switched into trade or services, or had moved to unknown addresses. The final sample originally contained 120 firms. Fourteen firms withdrew in the week before the survey began. A total of 106 companies were interviewed, but 13 firms were disqualified in the field.

II. BACKGROUND

Section A of this chapter reviews the main components of the Polish stabilization and liberalization program and outlines the macroeconomic setting that prevailed in May 1991. Section B briefly summarizes the post-war history of the Polish private sector, identifying key characteristics that were discernable at the time of the survey. Section C describes aggregate trends in private sector development from 1989 through 1991.

Stabilization and Liberalization

The comprehensive economic reform program adopted in January 1990 followed the overthrow of the Communist government and the decision to transform Poland's economy from a centrally-planned to a market-based system.^{7/} Policymakers were faced with the tasks of stabilizing an economy that was reeling from hyperinflation and severe external payments problems, and liberalizing policies such that positive growth could replace the downward trends of the late 1980s. The government tightened the money supply and devalued the zloty, pegging it to near-market rates and making it freely convertible. Most price controls were lifted, and wage increases in the state sector were limited to a fraction of price increases. Trade barriers were lowered to minimum levels. Laws and regulations were re-written to support a market economy, and the financial sector was restructured and commercialized. A privatization program was launched to shift the assets of thousands of state-owned enterprises into private hands, beginning with sales of small retail shops and moving on to large enterprises.

The results of the ambitious reform program were mixed in 1990. Initial hyperinflation subsided, but prices were 250 percent higher in December 1990 than official levels in December 1989. Measured gross domestic product declined by almost 12 percent; real wages fell by 31 percent; and private consumption fell by 15 percent. Owing to the initial deep devaluation, exporting state enterprises enjoyed an unexpected profitability as exports to the West rose and offset falling ruble exports. Increased revenues in the state enterprise sector translated into unexpected revenues for the state.^{8/} The devaluation of the zloty also decreased imports especially from the West, strengthening Poland's balance of payments position which ended the year at a surplus of 6.3 percent of GDP.

1991 brought a pronounced downturn in the Polish economy. Budget surpluses became budget deficits as revenues from the state enterprise sector collapsed with appreciation of the zloty in real terms and the collapse of CMEA trade in January 1991. Estimates place the decline in GDP at an additional 8 percent for 1991 for a total drop of about 20 percent since January 1990. Real sales of industrial enterprises fell by over 20 percent from January to September 1991, bringing industrial production in mid-1991 to 56 percent of mid-1989 levels. Inflation is estimated to have dropped to about 77 percent for the year, and deflated wages fell by over 40 percent since 1990. Unemployment, less than 2 percent of the total work force in early 1990, reached about 12 percent by end-1991. The strengthened position

^{7/} This summary of the macroeconomic situation in Poland and most of the aggregate statistics in Section C were taken from "Poland: Economic Transformation at a Crossroads" by Gerardo Corrochano and Luca Barbone. The World Bank, November 27, 1991, and from *International Financial Statistics*, February 1992.

^{8/} Unexpectedly high revenues in the state sector in 1990 also were due to exceptional, one-time conditions, namely: a sharp fall in real wages in early 1990, liquidation of inventories and of foreign exchange deposits, lack of external competition due to overshooting of the nominal exchange rate in the beginning of the program, and questionable accounting.

of the zloty stimulated imports with a resulting negative balance in the current account of the balance of payments.

The impressive achievements of the Polish reform program are not captured by the above macroeconomic indicators. Liberalization measures laid the groundwork for a market economy, and market formation was well underway in May 1991. Domestic prices operated freely, and the shortages of the past were gone. The zloty was devalued to near market rates, and foreign exchange was freely available. Abolishment of regulations limiting private economic activity resulted in a boom of private trading and investment, mostly in domestic firms but also in joint ventures. Thousands of small, mostly retail establishments were transferred from the state to the private sector, and government subsidies for remaining large state enterprises were mostly eliminated. Privatization of larger state-owned enterprises has gone slowly in Poland. The level of competition in the economy rose dramatically in 1990 and 1991 due to a fast-growing private sector and a tremendous influx of imports.

Survey findings must be placed in the macroeconomic setting prevailing in May 1991 to both clarify and qualify results. At the time of this survey, the favorable conditions of 1990 had disappeared. Macroeconomic problems had become evident and were negatively impacting sample firms. The state sector was collapsing; CMEA trade had closed down; the zloty had appreciated; imports had penetrated even the smallest towns; and unemployment had risen to 10 percent of the labor force.

The Private Sector in Post-war Poland

Three characteristics of the historical Polish private sector are important in understanding current private sector development. The first is that Poland's private sector has been an active if cyclical participant in the economy since the war.^{9/} Second, private entrepreneurs were only tolerated to the extent that they filled gaps in the state sector, e.g., small workshops that manufactured spare parts or built custom machines. In this role, many private enterprises held monopoly positions and worked for a single state client. Third, private enterprise and the accumulation of profit were ideologically illicit.

Treatment of the private sector has been cyclical since World War II characterized by long periods of repression involving exorbitant taxes, tight restrictions on the types of activities and the numbers of workers allowed, and the threat and actuality of retaliation for minor infractions broken by brief periods of liberalization.^{10/} Medium and large enterprises were nationalized by 1947, and restrictions were placed on the remaining small-scale private sector. The government created a national wholesaler through which all trade was to pass, and the share of employment in private sector trade was reduced to a negligible percentage of the work force.^{11/} In the period of "uncompromising Stalinism" (1949-1953), the private sector was all but dismantled by the forced socialization of all industry and trade and the introduction of repressive policies regarding taxation, licensing, labor, pricing, and access to foreign exchange and intermediate inputs.

9/ For participation rates, see Lulek and Paga, in *The International Journal of Social Economics*, vol.16, no.1, 1989.

10/ See *Private Enterprise in Eastern Europe: The Non-agricultural Private Sector in Poland and the GDR, 1945-1983* by Anders Aslund. Macmillian Press, London, 1985.

11/ The classic ideological arguments against private trade, namely that traders were reaping high profits based on the labor of others, were voiced by some entrepreneurs interviewed in this survey.

Following Stalin's death in 1953, policies governing private business were liberalized and the private sector reached a peak of 10,000 enterprises employing 30,500 people. Private sector activities were again restricted heavily from 1958-1964 followed by a brief liberal period from 1965-1968 which was reversed again in 1968. In 1972, private industry was banned: all small-scale activities were classified as handicrafts, and enterprises were limited to 6 employees. After the workers' uprising in June 1976, the Gierek administration was forced to liberalize the private sector to redress severe market shortages. Martial law, imposed in 1981, once again tightened restrictions on private entrepreneurs.

In sum, brief periods of liberalization took place in times of economic crisis when the reserve capacity of the private sector was needed. Private enterprises quickly expanded to meet the shortages but when private incomes rose and competition became a possibility, the government cracked down again on the grounds of unacceptable inequities in income. Economic necessity demanded private enterprise at critical times, but ideology legitimized its repression once the crisis was over.

The Current Status of the Polish Private Sector

In adopting measures to promote private sector development, Polish reformers stated their intention to remove discriminatory laws and regulations that historically favored state-owned enterprises and to place private firms on an equal footing with other enterprise forms. Passed in January 1989, the "Law on Economic Activity" set the stage for large-scale entry of private entrepreneurs by removing restrictions on the activities and numbers of employees permitted in private firms, and by minimizing licensing and registration requirements. The Company Law of 1934 was resurrected to provide corporate forms--limited liability and joint stock companies--for those who wanted to move beyond sole proprietorships.^{12/}

The response was immediate. By the end of 1989, over 800,000 people had established sole proprietorships and more than 16,000 new companies were registered. The numbers of new entrants continued to grow, and current estimates are that the share of GDP contributed by new private firms (excluding agriculture and cooperatives) rose from 11 percent of GDP in 1989 to 19 percent in 1990.^{13/} The private sector share of total employment (excluding agriculture and cooperatives) rose from 13 percent in 1989 to about 26 percent in 1991.

^{12/} For details on the legal foundation of private sector firms, see "The Legal Framework for Private Sector Development on a Transitional Economy: The Case of Poland" by Cheryl Gray, Rebecca Hanson, Michael Heller, Peter Ianachkov, Danial Ostas and Youssef Djehane, PRE Working Paper 800, The World Bank, November 1991.

^{13/} New difficulties have arisen in measuring the growth of the new private sector in Poland. The Central Statistical Office in Poland has recently redefined the private sector to include cooperatives, social organizations and other establishments which number almost 20,000 mostly large units that employ something like 400,000 people. The percentage of these units that is truly private is unknown. Newly-privatized state enterprises have been added to the private sector roster as is appropriate, but the Polish authorities apparently also have amended former private sector data to include these same state firms. These additions have inflated all basic private sector characteristics--to an unknown extent in some cases--and have obscured trends in the new private sector. Therefore, all current statistics on the private sector must be qualified as to whether they include the cooperative sector and newly privatized state enterprises.

Numbers of Units and Sectoral Distribution

Private domestic firms--joint stock and limited liability companies--totaled 45,077 units by end-1991 (Table 2.1). Sole proprietorships--the self-employed sector--numbered 1.4 million units. Joint ventures almost tripled during 1991 to total 4,796 enterprises.

Table 2.1: Total Economic Units
(Number of units)

				Rate of Growth		
		1989	1990	1991	90/89(%)	91/90(%)
I.	State enterprises	7,337	8,453	8,228	15.2	-2.7
II.	Commercial law partnerships <u>a/</u>	16,906	36,267	53,771	114.5	48.3
	1. Treasury-owned	208	248	376	19.2	51.6
	2. Joint ventures	429	1,645	4,796	283.4	191.6
	3. Private firms (Incorporated)	11,693	29,650	45,077	153.6	52.0
	4. Other law partnerships	4,576	4,724	3,522	3.2	-25.4
III.	Sole proprietorships (Unincorporated)	813,500	1,135,500	1,420,000	39.6	25.1
IV.	Cooperatives	15,024	16,650	17,374	10.8	4.3
V.	Small foreign enterprises	841	862	787	2.5	-8.7
VI.	Other establishments	-	1,956	1,650	-	-16.0

^{a/} Commercial law partnerships are limited liability and joint stock companies, the population from which this sample was drawn.

Source: EC2CO, The World Bank from the Central Statistical Office.

A sectoral breakdown shows that much of the 1991 growth in private sector start-ups occurred in wholesale and retail trade with some slowdown in industry (Annex Table 1.1). The number of incorporated companies increased by 52 percent during 1991, industrial firms by 35 percent and trading firms by 92 percent. Sole proprietorships were dominated by industry in 1989; almost evenly divided between trade and industry in 1990; and by the first half of 1991, the self-employed sector contained four traders for every three industrialists. Joint ventures in industry increased sharply from 853 firms in 1990 to 2,697 in 1991.

Official figures show an increase of about 50 percent in private industrial production from end-1990 to end-1991. This sizeable increase was due to overall positive annual growth of private firms, but also to a new classification scheme introduced in 1991 which re-classified the large industrial cooperative sector as "private"--a change which increased the private sector contribution in all areas substantially. Industrial production in the private sector was uneven with a drop of 17 percent in the first quarter of 1991, followed by increases of 31 percent in the second quarter, 23 percent in the third, and 10 percent in the last quarter of 1991. While it is unclear whether production in new firms picked up in the latter half of 1991 or whether newly-added privatized state firms boosted production figures, it is important to note that the first quarter drop in production closely preceded the survey carried out in May 1991.

Employment in the Private Sector

Re-classifications of private sector statistics in 1991 has obscured employment trends among new firms, but some patterns are clear (Annex Tables 1.2, 1.3 and 1.4). Between end-1990 and third quarter 1991, total employment in Poland, excluding private agriculture, dropped by 2.8 percent--a fall of 7.4 percent in the state sector and an increase of 6.5 percent in the private sector (including cooperatives). The increase in private sector employment was accounted for mainly by construction and trade, with a growth rate of only 0.1 percent in industry. By end-1991, excluding agriculture and the cooperative sector, the private sector share in employment was 26 percent, up from 19 percent in 1990 and rising to 34 percent in 1992. Excluding private agriculture and including the large, re-classified cooperative sector, the private sector share of employment was 44 percent at end-1992. Including agriculture, private sector employment accounted for about two thirds of total employment by end-1992. The most important facts about employment in Poland in May 1991 were that more than two and one half million people were working in sole proprietorships with an average labor force of 1.8 persons including the owner; limited liability companies employed just over 200,000 people in 1990 and averaged 7.3 workers per firm in 1990; and joint ventures employed about 85,000 people in 1990 and were much larger with an average of 51.8 workers in 1990.

Investment and Trade

Investment data indicate that the share of private sector investment in total investment was 41 percent in 1990. Private investment dominated in agriculture, trade and other material and non-material services in 1990; private sector investment was 15 percent of industrial investment. Private sector participation in foreign trade exploded from 1990 to 1991 (Annex Table 1.5). The share of private sector exports grew from 5 percent in the first quarter of 1990 to 31 percent in the fourth quarter of 1991. Agriculture and food products led export growth in 1991, followed by light manufacturing. The share of private sector imports grew from 16 percent in the first quarter of 1990 to 52 percent in the fourth quarter of 1991. Primary private sector imports in 1991 were agricultural products followed closely by light manufacturing and processed foods.

III. THE ENTREPRENEURS

Section A of this chapter provides general characteristics of sample entrepreneurs: their ages, education, and employment histories. Section B describes their motivations for starting private businesses and the personal qualities they have brought to the task. Section C briefly characterizes the shifting profile of the successful private sector producer.

General Characteristics ^{14/}

The youngest entrepreneur interviewed was 27 years old and the oldest was 63. The average was 42, somewhat older than expected. Eighty-two were men and 11 were women. They were well-educated: 68 percent were university graduates and 18 percent had completed technical college. More entrepreneurs in urban areas were university graduates than in rural areas, but more rural entrepreneurs had completed technical schools. Only 15 percent had any training abroad, and most was elementary and brief.

Over 60 percent of the new manufacturers worked either for a state enterprise or for the government prior to starting their current businesses. About 10 percent worked previously in another private business they owned, and 7 percent worked for a foreign company in or out of Poland. Two-thirds of those who came from the state sector previously were managers. Just over half of this group were general managers, usually of departments of state enterprises or in government, and just under half were production or technical managers. Fourteen percent previously were technicians--most commonly design engineers--and 14 percent were skilled or semi-skilled workers. Eight percent previously were educators, usually heads of departments or professors in universities.

Researchers noted that entrepreneurs' backgrounds often were mirrored in the skills and perspectives they brought to their businesses. Former managers in state firms tended to exhibit more awareness of the big picture--they were knowledgeable about the market share held by their products, the identity and resources of their competitors, and the most effective means of dealing with official requirements. Technical experts were well-informed about available technologies in Poland and abroad, and commonly were involved in developing new products. Former skilled workers typically made use of prior skills, e.g., a seamstress set up her own clothing business. Others made scant use of their backgrounds, jumping from product to product to take advantage of opportunities as they arose, e.g., two former auto mechanics who were producing men's suits with great success in a small town where there was a shortage of tailors.

Most sample entrepreneurs were highly inexperienced--much more so than their Hungarian and Czechoslovak counterparts in comparable samples. Eighty-eight percent of Polish entrepreneurs reported that their current business was the first business they had owned. Almost 60 percent were manufacturing products that were entirely unrelated or only tangentially related to products made in their former places of employment--a powerful indicator of the uncharted territory occupied by many Polish manufacturers.

Motivation and Personal Qualities

The most powerful testament to the long-suppressed spirit of entrepreneurship in Poland came when entrepreneurs were asked their primary objective in starting up a private business (Table 3.1).

^{14/} In this section and those that follow, the reader can assume that the whole or very close to the whole sample responded to each question. If the response rate was low, it is noted as such.

Fully 86 percent of entrepreneurs responded with one of three answers. Independence--defined as the freedom to work on one's own--was the answer given by 39 percent of respondents. Achievement--the desire to use fully the skills that one has--was the primary objective of 24 percent of entrepreneurs. Profits were the goal for 23 percent of respondents.

Table 3.1: Primary Personal Objectives In Starting a Bbusiness ^{a/}
(percentage of responses)

Independence	Achieve- ment	Profits	Status/ Prestige	Other	Economic Necessity	Power	Career/ Security	No. of Respondents
39	24	23	4	4	3	1	1	92

^{a/} Entrepreneurs were asked for their primary objective in starting a private business. They were not shown responses.

When asked for the factor that precipitated their entry into private businesses, half indicated that they were pulled to the private sector by perceived opportunities, and half said they were pushed by unacceptable circumstances in their previous employment. On the "pull" side, most entrepreneurs reported that they started private businesses when they saw a profitable opportunity and decided to take it. Many people interviewed fit this description, including one company that started by making T-shirts which soon lost out to imports, then moved to production of import-imitation bed linens, and then shifted to sell bulk Korean athletic shoes when the linens business went under. These individuals fit easily into the common definition of an entrepreneur as an "opportunist", especially alert to profit possibilities that arise from markets in disequilibrium.

On the "push" side, entrepreneurs said that frustration with work in state-owned enterprises led them to private business. Entrepreneurs with advanced degrees told painful stories of years of frustration in state enterprises, describing their inability to obtain serious consideration of new ideas for bettering production, professional humiliation in acquiescing to inefficient production practices and poor-quality products, and dismay with the extent to which economic decisions were politicized. Many of those interviewed took obvious pleasure in simply working to their technical capacity. This group resembles McClelland's entrepreneurs who are motivated chiefly by the need to achieve through making use of their skills.

In a rough attempt to test some of the literature concerning the personal qualities of entrepreneurs, respondents were read a list of personality traits traditionally associated with entrepreneurs and asked to choose the three that best described themselves. Business partners or family members present at the interviews often assisted. Entrepreneurs were quick to identify these traits as their own, thereby placing themselves squarely in the camp of entrepreneurial personalities in most cultures (Table 3.2).

Table 3.2: Personal Qualities of Polish Entrepreneurs ^{a/}

Personal Qualities	No. of Responses	Percentage of Respondents
A practical person with practical skills	48	18
Like to feel in control of what is going on	45	17
Highly disciplined, committed to hard work	43	16
A risk-taker, willing to live with uncertainty	37	14
A high achiever, easily bored with routine, restless	35	13
Self-confident, fairly sure of success	32	12
Independent, a loner, somewhat separate from others	11	4
Grew up in a difficult, troubled family	11	4
Other	4	2
Total	266	100

^{a/} Entrepreneurs were shown the list of personal qualities and asked to choose the three that describe them best.

Entrepreneurship Development

The numbers of new entrants demonstrate that there is no shortage of entrepreneurs in Poland. However, the prerequisites for success in private manufacturing appeared to be shifting in May 1991. Manufacturers who started in 1989 and the first months of 1990 produced basic consumer goods needed in Poland's shortage economy. Shortages began disappearing as trade liberalization and convertibility of the zloty resulted in massive "gap-filling" by new domestic entrants and a flood of imports. By May 1991, sharp eyes and a willingness to risk were no longer sufficient to maintain profitable businesses, especially in simple consumer goods where competition had grown particularly fierce. Indeed, many of this first wave of producers were moving into trading activities as they found themselves unable to compete with imports. As discussed in Chapter V, the strongest firms in the sample were headed by technically-proficient entrepreneurs, usually design engineers who manufactured relatively sophisticated plastics, machines and metal products. These entrepreneurs had located niche markets or they were able to undersell competing imports. In sum, it appeared to researchers that the opportunists of 1989 and 1990 were being displaced in 1991 by the technically-proficient with better potential to compete in world markets.

IV. THE FIRMS

Section A of this chapter summarizes sample firms' characteristics: their ownership structure, age, location, sectoral distribution, size, and origins. Section B discusses entrepreneurs' use of physical capital and finance. Section C describes firms' labor force: its size, gender breakdown, compensation, skills and training, and representation. Section D focuses on the use of land and buildings; Section E on raw materials and intermediate inputs; Section F on product markets and distribution; and Section G on the characteristics of firms that had closed down.

General Characteristics

Nearly all firms were limited liability companies. Well over half had multiple owners, most commonly three or four former co-workers or school-mates who had pooled their resources and started a business. Most clearly needed the start-up resources available from more than one owner, but they also appeared to enjoy working in groups. Only 20 percent of firms had single owners, and few were family businesses.

Firms were young, and almost all were new companies. Over 75 percent were started between 1988 and the present. Only 12 percent were operating prior to 1980 and could be classified as traditional craftsmen. Ninety percent were independent since start-up and were never associated with the state sector. The fact that most Polish firms were started "from scratch" contrasts sharply with sample firms in Hungary and CSFR, large numbers of which came directly from the state sector. In sum, most Polish entrepreneurs--unlike their Hungarian and Czech counterparts--had to create their businesses from the ground up, without benefit of already established networks.

Surprising to researchers, firms were almost evenly split between urban and rural locations (54% and 46% respectively). They also were evenly distributed in all regions of the country except for the eastern region, where there were only 7 firms. Obvious implications are that: the private business constituency in Poland is far-flung and varied; assistance programs will have to reach deeper into Poland to contact private producers, and national entrepreneurship associations will find it difficult to assemble a representative constituency.

Seventy-five percent of firms were engaged in five industries pre-selected through sample stratification: knitting (17%); clothing (18%); plastics (8%); metal working (16%); and machine production (15%) (Table 4.1). Of the 20 plastics firms selected originally, only 8 were still in business at the time of the survey. Firms were evenly distributed by sector in rural and urban areas except for machinery manufacturers, most of whom were located in urban areas.

Firms were small as measured by numbers of workers and by average monthly sales. The average number of workers was 32. Almost 60 percent had fewer than 20 workers, and almost 90 percent had fewer than 50 (Table 4.2). Only four had more than 100 workers. Over 50 percent had monthly sales of less than US\$20,000, and over 75 percent had less than US\$50,000. Four firms had sales of more than US\$200,000. Average monthly sales were US\$47,098.

Table 4.1: Distribution of Sample Firms by Sector a/
(Number of firms)

	Total	Knitting	Clothing	Plastic Products	Metal Products	Machinery	Others <u>b/</u>
Number of Firms	93	16	17	8	15	17	20

a/ The sectoral distribution of sample firms is not necessarily representative of the entire private manufacturing sector because five stratified samples make up the bulk of firms. However, the sample is roughly representative in that the sectors targeted are the major ones in the population.

b/ Other sectors include Food Manufacturing (311, 312), Beverage (313), Leather Products (323), Wood Products (331), Furniture (332), Industrial chemicals (351), Other Chemical Products (352), Pottery, China, Earthenware (361), Glass Products (362), Non-metallic Mineral Products (369), Transport Equipment (384), Scientific Equipment (385), Other Manufacturing (390).

Table 4.2: Distribution of Sample Firms by Size
Number of workers a/

	Total No. of Workers	1-10	11-20	21-50	> 50
Number of Firms	93	19	35	27	12

a/ Employment figures are full-time worker equivalent, calculated by adding the number of 8 hour days worked by part-time workers and the number of full-time workers.

b/ The size distribution of sample firms is not representative of the entire private manufacturing sector because firms with fewer than 7 workers were excluded from the sample.

Firms typically had one of three origins. Three-quarters were new companies started by groups of friends or former classmates who had quit their jobs in state enterprises, pooled their resources, registered limited liability companies, set up small factories using cast-off equipment from state firms, and started producing something--usually a cheaper or somewhat improved replica of a manufactured, relatively low-tech good produced in the state sector.^{15/} The choice of at least the initial product was based on previous job experience of one or more of the partners. These firms typically could undersell state competitors through cost-cutting, but low-cost imports were burying many of them. Some were quitting in defeat but many were struggling on by lowering production costs still further, casting about for new products, and shifting into retail trade. Many clothing firms were in this position, able to compete with state firms but undercut by higher quality imports.

About a third of these new companies were started by groups of high-level professionals--invariably engineers or people with strong technical skills--who had left state enterprises often as a group to set up their own companies. Most competed with their former employers by producing the same or a related product, and several were producing intermediate inputs needed by the state firm they had left. Included in this group were university professors who were trying to apply their technical expertise in a business setting. Most had conducted some kind of market research, and almost all were developing new products. Having most of the necessary production skills and knowledge of markets, many of these firms were competing successfully with state enterprises and, in some cases showed promise of competing

^{15/} Due to the exclusion of joint ventures, the role of foreign partners in business formation was unimportant in the sample. Three firms had minority foreign partners.

with imports and exporting. Examples include a firm that made electronic resistors and another that produced measuring devices used in processing sugar beets, both competing directly and successfully with their former employers.

Eleven firms (12%) in the sample traced their origins to family businesses, operating since the 1960s and 1970s and now transformed into limited liability companies. Some evolved from part-time work at home, and others were started by individuals who disdained work for the state on ideological grounds. Initial motivations may have differed, but almost all were small workshops that historically relied on a few steady contracts from state clients, usually for metal spare parts or simple plastic items. Prospects appeared poor for most of these family businesses as the shortages they once filled had diminished; demand from their state customers had declined; and imports had rendered some of their products non-competitive. Common examples of these family business were home-based metal and woodworking shops.

Represented by 10 firms (10%), the third route to private business was through the state sector. In the most common situation, entrepreneurs took over divisions or entire state enterprises or cooperatives that were failing or had folded. They invariably leased the buildings and equipment and, more often than not, hired the former workers. Several sample companies were "nomenklatura" firms--set up by former or current high-level managers of state firms as suppliers or competitors of their enterprises. Numerous upfront benefits accrued to these private firms, e.g., cheap credit, subsidized rents, and ready sources of inputs and customers, but their success was far from guaranteed. Indeed, they either faced the same problems which had caused the division to fold originally, or they faced critical and costly needs to restructure. Four firms originally were cooperatives. This route proved profitable in every case as these entrepreneurs were able to obtain low-interest loans, equity participation, and access to free or very low-cost machinery. According to entrepreneurs, the only drawback was that the cooperative labor force with its poor working habits came with the buildings and equipment.

Capital

Physical Capital

Most production equipment was produced in Poland (52%), followed by Western Europe and East Asia (35%--mostly German and Japanese), other Eastern block countries (9%), and self-made (4%). Almost all equipment was used, and almost all was purchased from state-owned enterprises or cooperatives. Purchasing arrangements varied. Most entrepreneurs indicated that someone in a state enterprise let them know when surplus equipment was to be sold, and they took advantage of the tip to purchase what they needed, much of it apparently at below market prices.^{16/} In contrast to sample manufacturers in Hungary who made extensive use of leasing arrangements, only eight Polish firms were leasing their equipment--in all cases from cooperatives that had stopped production.

^{16/} While the practice of purchasing used equipment from state enterprises and cooperatives at below-market prices using seemingly unregulated procedures raises legitimate questions about losses of potential state revenues and equity of access, acquisition of this equipment was the key factor that allowed many to start up their businesses.

Much of the equipment in use appeared quite old in vintage, but was less dated in years than expected.^{17/} The average age of equipment (in value terms) was 10.4 years, with negligible differences between rural and urban firms. Value-weighted averages show that 25 percent of firms were using a combination of machinery and tools that averaged 3 years or less; 25 percent used equipment that averaged 5-10 years in age; 17 percent had equipment that averaged more than 20 years old; and 15 percent used equipment that was 10-15 years old. Of interest is the fact that the average age of equipment in eastern Poland was 6.7 years, and the average age in western Poland was 11.4 years.

Finance

Like entrepreneurs everywhere, most Polish entrepreneurs started their businesses with personal savings and loans from family. By the second year, most were relying on re-invested profits, and many had turned to financial institutions for short-term loans.

Counter to researchers' expectations that access to credit would be limited, 68 percent of entrepreneurs had received bank loans--almost all short-term credits of 12 months or less--since 1988. Twenty-eight percent chose not to apply for loans, citing concerns that they would be unable to repay them at going interest rates (reportedly 60-70% at the time of the survey). Only four people had applied for loans and were turned down. Almost a third of respondents said that it was very easy to get a loan from a bank if one were willing to pay going interest rates; only 15 percent were of the view that it was very difficult. Anecdotal evidence indicated that nominal requirements for collateral were high but, in practice, banks appeared to have been liberal in the range of assets they accepted as collateral, apparently including broad use of guarantees signed by family and friends.^{18/} There were no differences in the numbers of urban and rural firms that had received loans.

Labor

Size and Gender of the Labor Force

Including part-time workers, the average full-time labor force was 32 workers per firm. The largest firm interviewed had 351 full-time workers. The average number of workers was roughly similar across the five major sectors, with the lowest average number in plastics (17) and the highest in clothing (29). Urban firms were larger, with an average of 41 full-time workers compared an average of with 23 in rural firms.

Women's high level of participation in the labor force was evident in the fact that 53 percent of full-time workers were women. The vast majority of workers in metal-working, machinery and plastics companies were men, while workers in clothing and knitting companies were almost exclusively female. Anecdotal evidence indicated that job discrimination based on gender--a hot issue in the West--was not of concern to most Poles. Rather, there appeared to be societal consensus that in production, women do the finer hand-work and men do the heavier, dirtier work. In management, women keep books and design products; men take responsibility for managing finances, production, and marketing.

^{17/} Entrepreneurs were asked to list all of their machinery and tools, giving the age, manufacturer, and current replacement value for each.

^{18/} Hearsay evidence is that Polish banks have been less liberal in their credit policies since the recent banking scandals.

Labor Compensation

The average cost per worker was US\$297 per month and the average wage was US\$155 per month.^{19/} The lowest wage was US\$55 and the highest was US\$376. Workers in urban firms cost an average US\$321 per month and received US\$159 per month in wages. Workers in rural firms cost an average of US\$267 per month and received an average salary of US\$148 per month. The average non-taxed allowances or benefits per month totaled US\$50 per worker, US\$59 per month for urban workers and US\$22 per month for rural workers. Employers were required to pay two labor taxes which together add 65 percent to the cost of salaries paid: a wage tax of 20 percent and a social security payment of 45 percent.

Of note is the fact that wages in sample firms were not substantially higher than wages in state firms, a fact easily accounted for by high unemployment rates in Poland and by the reality that most jobs in sample firms required unskilled labor. The exception may have been urban, skilled workers who reportedly commanded higher salaries. Entrepreneurs reported that they typically paid unskilled workers 10 percent more than they made in state enterprises and skilled workers what they could afford, up to twice what they were paid by state enterprises.

Workers in private firms were protected under Polish labor laws, but they appeared to receive far fewer additional benefits than workers in state firms. By law, people who have worked anywhere for more than ten years are entitled to three months notice if they are laid off, one month if they have worked for less than ten years. Standard benefits include 26 vacation days per year and 6 months' maternity leave. Additional benefits provided by sample firms included special work clothing, transportation supplements where workers live far from work, and Christmas bonuses. Several firms also had instituted profit-sharing schemes and escalating production incentives.

Although the enterprise was not in the sample, an interview with a large joint venture between a British company and five state enterprises provided an opportunity to inquire about the benefits provided to state employees. The 6,000 workers in this company reportedly received the following benefits: (i) 30 days leave plus a special vacation allowance; (ii) long-term loans at subsidized rates; (iii) transportation to work or allowances if personal cars were used; (iv) use of resort facilities; (v) support payments for children of poorer workers; (vi) year-end bonuses of 1-5 months salary; and (vii) special funds for managers to pay for flats, cars or overseas training courses. Some of these benefits may have been mechanisms to avoid excess wage taxes levied on state firms and benefits may have been reduced since May 1991, but it was clear that in no case were the benefits received by workers in sample firms even close to those enjoyed by these state workers.

Labor Skills and Training

Three out of four entrepreneurs reported that their workers were as highly skilled as needed. This response matched researchers' impressions that most employment in the private sector consisted of unskilled or semi-skilled jobs for which workers generally could be found, e.g., operating traditional knitting and injection-molded plastics machines. Some entrepreneurs who were producing more sophisticated products expressed concern that their workers' skills were not sufficient to upgrade product

^{19/} The average cost per worker was obtained by dividing the total monthly labor bill of the firm by the number of full-time equivalent workers in the firm (full-time plus part-time workers). The total labor bill includes salaries, employment taxes, cash bonuses, and special allowances. The exchange rate used was 9,310 zloty = US\$1.

quality to competitive levels or to operate newly-purchased equipment. Job training appeared to be brief, casual, and practical.

About half of those interviewed reported that they had difficulty recruiting highly skilled workers when they were needed. The most sought-after professionals appeared to be engineers with specialized skills and people with expertise in quality control, marketing and sales. Two-thirds of urban firms--as opposed to one third of rural firms--reported problems in recruiting skilled workers. Many people with strong technical skills reportedly had left their jobs in state enterprises to start up their own businesses, while those still employed in state enterprises apparently were commanding higher and higher salaries in exchange for staying.

Labor Representation

Researchers asked entrepreneurs if workers in their companies were represented by a union or workers' council. Without exception, the answer was no and the response was incredulity at the question. Solidarity apparently has functioned more as a political party than as a standard labor union, and labor organizations in Poland appeared to be poorly regarded. Employers agreed that workers in their firms would never join one. The consensus was "there is no need for them here."

Land and Buildings

Counter to researchers' expectations, almost all entrepreneurs had secured factory space with relative ease, even in cases where ownership questions were unresolved. Over 70 percent of entrepreneurs were leasing their buildings and land, half from private persons and half from state firms and cooperatives. The fact that only 12 percent of those interviewed owned their factory buildings is an important indicator of the thin capital base of most Polish entrepreneurs, a base that appears even smaller when compared with Hungarian and Czechoslovak counterparts about half of whom owned their factory buildings. Leases were multi-year agreements, an arrangement preferred by most entrepreneurs who wanted guaranteed access for a period long enough to justify the often substantial investments needed to render the building suitable for their purposes. To the outsider's eye, arrangements heavily favored the interests of lessors. Entrepreneurs had replaced walls, plumbing, and wiring as well as built roads and power lines at their own expense. They complained about the costs of renovations, but none challenged the system that put the burden on the tenant.

Eighty-two percent of entrepreneurs confirmed that factory space was available to those who could pay rising real estate prices.^{20/} Private businesses were operating in a wide variety of settings. Many had leased standard, small factory buildings. Some factories were set up in one owner's basement with a room in another owner's flat serving as an office. Others had rented buildings from a family member or located in garages behind private houses. Production premises often were in the midst of residential neighborhoods.

^{20/} Entrepreneurs in some rural areas reported shortages where the supply of factory buildings was limited and ownership issues had not yet been clarified.

Intermediate Inputs and Raw Materials

The state continued to be the major source of inputs for entrepreneurs. The value-weighted share of inputs purchased from state suppliers was 71 percent with 29 percent supplied by the private sector.^{21/} Also in terms of value, 72 percent of inputs were produced domestically and 28 percent were imported. The potentially worrisome fact that most private suppliers were functioning primarily as conduits for imported inputs rather than producing substitutes was seen in the finding that state firms produced over 80 percent of the value of domestic raw materials and inputs used by entrepreneurs. Entrepreneurs' suppliers and sources of inputs depended in large part on their activities. Metal workers, machine manufacturers, and plastics producers bought their primary inputs--metals and plastics--from state enterprises that produced them; clothing and textile producers relied mainly on state enterprises for domestic yarns and fabrics, and on private suppliers for imported ones.

Product Markets and Distribution

Growing private sector participation in the economy was shown by the fact that just under half of sample entrepreneurs sold their products primarily to state enterprises, and just over half sold mostly to private retailers (Table 4.3). Finished goods were sold mostly to private retailers, and intermediate inputs were sold mostly to state enterprises. A similar pattern to that of input markets emerged on the output side, namely that metal, plastics and machinery manufacturers relied largely on state firms to purchase their products, and clothing and textile manufacturers relied mostly on the private retail sector. As discussed in the next chapter, machinery manufacturers, and producers of high-tech plastic and metal products --firms with the closest links to the state enterprise sector--had the best prospects among the sample surveyed. An interesting question asks to what extent these stronger firms had access to below-market prices or other special deals from state firms and to what extent their strength derives from having chosen activities in which they could compete. Entrepreneurs had no complaints about the availability or costs of distribution in existing channels. They delivered their products to their customers themselves or they paid a freight charge to trucking companies.

Twenty-one firms (23%) were exporting, all to the West and many in subcontracting arrangements. Exports as a percentage of total sales were 17 percent, far lower than export percentages in Hungary and CSFR. Sixty-four percent were exporting less than half of their output, and only two firms were exporting 100 percent of their production. Analysis of their characteristics shows that the majority of exporters were relatively large, urban firms that were assembling clothing from pre-cut components. Over half of exporting firms were located in the northern region of Poland. Their principal problem was obtaining sufficient financing. A surprising finding was that analysis of strong and weak firms (see Chapter V) shows that more exporters were among the weak firms than among the strong ones. This is consistent with evidence from Hungary and CSFR that subcontracting arrangements often are only marginally profitable for the subcontractor.

^{21/} Entrepreneurs were asked to list their intermediate inputs and raw materials, unit prices, suppliers (private or state sector), and sources (imported or domestic).

Table 4.3: Product Markets--by Sector
(Percentage of Responses in Each Category)

	Total Responses	Knitting	Clothing	Plastic Products	Metal Products	Machinery	Others
Primary Markets:							
Sell directly from shop	10	6	0	0	12	15	22
SOEs (as inputs)	22	6	0	38	50	21	22
Other private firms (as inputs)	15	17	0	31	6	21	17
SOEs (as finished goods)	17	6	32	15	19	15	13
Private retailers (as finished goods)	32	53	63	8	12	21	22
Government (as finished goods)	2	0	0	8	0	0	4
Private exporters	2	6	5	0	0	0	0
Other	2	6	0	0	0	7	0
Total Percentage		100	100	100	100	100	100
Total Responses	102	(17)	(19)	(13)	(16)	(14)	(23)

Note: Some firms cited two or more channels; hence the total number of responses exceeds the number of firms in the sample.

Firms that Had Stopped Production

Thirteen of the 106 entrepreneurs who were interviewed had recently stopped production. Their characteristics were similar to those of the weakest firms in the sample. All were started since 1988, and 11 of the 13 had closed between the last few months of 1990 and the first few of 1991--the period when the Polish economy took a sharp turn downwards. The weakest sectors in the larger sample dominated among closed firms: three firms each in clothing, low-tech metal working, and simple plastics; and two in knitting. The most binding problems cited by these entrepreneurs were the same as for the larger sample: lack of consumer demand, competition from imports, and delinquent payment of bills by state-owned customers. Almost three-quarters of firms that had closed were highly dependent on sales to state firms that were declining. Of note are the facts that none of these firms had declared bankruptcy and all but two entrepreneurs were moving on to new activities, almost all in trade and services.

V. THE BUSINESS ENVIRONMENT: CONSTRAINTS AND PROSPECTS

Section A of this chapter first presents the constraints cited most often by entrepreneurs and then traces them back to their sources. Demand problems are disaggregated into those associated with increased competition and those stemming from adjustment-related factors including recession, downturn of the state sector, and closure of CMEA markets. Explication of supply problems involves analysis of markets, identifying those that appeared to be functioning well and those that did not. Section B looks into the costs of operating a private manufacturing business in Poland, focussing on laws and regulations, infrastructure, linkages with the state enterprise sector, and private and public attitudes toward private enterprise. In Section C, a group of strong firms is compared with a group of weak firms to identify those variables that were associated with success.

Constraints Cited by Entrepreneurs

Three issues dominated when entrepreneurs were asked to name their three main problems in order of importance. Lack of demand for their products was cited first by 30 percent of respondents; financial problems were the chief concern for 28 percent; and 10 percent complained first of government regulations.^{22/} Demand problems were presented as "people do not have enough money" (25%) and "too much competition" (5%). Financial problems included high interest rates (15%), late payment by state enterprises (7%), and lack of working capital (6%). The first-cited problem with government regulations was that "the rules change too often" (10%).^{23/}

Issues of Demand

Demand problems cited by entrepreneurs in mid-1991 appeared to result mostly from a combination of diminished aggregate demand and a rapid expansion in the number of suppliers, i.e., a shrinking pie cut into more and therefore, smaller pieces. Analysis of the sources of demand problems shows that they stemmed from one or more of three factors:

- (i) a decline in consumer demand due to diminished real wages and rising unemployment;
- (ii) a decrease in demand for private sector inputs into state enterprises that were cutting back on production due to reduced government subsidies, closure of markets in the USSR, and shrinking domestic markets; and
- (iii) a tremendous expansion in the supply of goods due to large numbers of new domestic firms and a surge of competing imports.

Some distinction can be made between firm downturns due to lack of competitiveness with newly-admitted, often higher quality or lower cost imports--considered necessary costs of adjustment--and those due mainly to other adjustment-related factors including economic recession, the collapse of the state sector, and regulatory fluctuations--considered transitional costs to be minimized. In the first case,

^{22/} Other complaints involved high tax rates, a shortage of skilled workers, and high prices for local materials.

^{23/} Aggregation of all three problems yields similar results: insufficient demand and high interest rates dominated entrepreneurs' concerns followed far behind by changing government regulations, too much competition, and lack of working capital.

remedies would include enhancement of producers' abilities to compete and facilitation of their move into different sectors. In the second case, remedies presumably lie in the policy arena.

Analysis of the sources and intensity of entrepreneurs' competition sheds some light on the issue. When entrepreneurs were asked to identify their main competitors, responses from all sample firms were almost equally divided among imports, other small firms, and state enterprises (Table 5.1). The sectoral distribution tells the story. Knitting and clothing firms were competing--or rather failing to compete--with imports. Many of these firms had lost state customers that previously sold to the former USSR, and they reported that they were unable to sell in the private sector due to competing lower-cost imports from the Middle East and East and Southeast Asia. Injected-molded plastics producers, competing mainly with other small private firms, suffered from indirect import competition. State firms no longer needed to purchase plastic containers to fill with soaps and cleansers because Poles were buying already-bottled, imported substitutes. Metal and machinery manufacturers competed, successfully for the most part, with other small firms and with state enterprises.

Table 5.1: Sources of Competition--Distributed by Sector ^{a/}
(Percentage of Firms Responding)

	Total	Knitting	Clothing	Plastic Products	Metal Products	Machinery	Others
Small private firms	23	6	23	62	14	38	18
Large private firms	5	13	6	0	0	8	4
State enterprises	24	6	6	12	54	31	32
Cooperatives	3	0	6	0	9	0	0
Foreign-owned firms	5	0	12	0	0	8	9
Imports	24	75	47	0	0	0	14
None	14	0	0	25	23	14	23
Total Percentage	100	100	100	100	100	100	100
Total Responses	(98)	(16)	(17)	(8)	(22)	(13)	(22)

^{a/} Entrepreneurs were asked to identify their chief competitors. The number of responses exceeds the sample size because in several cases, firms listed two major competitors.

The intensity of competition was indicated by the numbers of other firms producing in entrepreneurs' main markets. Thirty-seven percent of firms were competing with less than 10 other firms; 21 percent with 10 to 50 other firms; and 26 percent with more than 100 firms (Table 5.2). A sectoral breakdown reveals large difference among sectors in the level of competition they faced. As expected, knitting and clothing firms faced intense competition from imports; plastics and metal firms reported a moderate level of competition; and machinery manufacturers competed with few other firms.

A more detailed analysis of those entrepreneurs who specifically cited weak demand as their main constraint showed a similar breakdown, namely: about 60 percent competed mainly with 10 or more other small firms and imports--both of which reportedly offered strong competition in most cases--and 40 percent of these entrepreneurs reported that they had no competition or that they competed mainly with relatively few cooperatives and state enterprises--reported easily outsold. Therefore, a reasonable estimate would be that about 60 percent of firms with demand problems had difficulty outperforming and underselling other private firms and imports. The remaining 40 percent of entrepreneurs with demand problems were in trouble for other reasons. Some entrepreneurs were producing competitive products, but had lost sales due to the recession. Some were suppliers for state firms that had come into hard

times. Others had lost sales due to unexpected government cutbacks or sudden shifts in government regulations.

Table 5.2: Intensity of Competition--Distribution by Sector ^{a/}
(Percentage of Firms Responding)

Numbers of Competing Firms	Total	Knitting	Clothing	Plastic Products	Metal Products	Machinery	Others
None	9	0	0	0	13	14	18
1-10	37	7	18	57	40	71	41
11-50	21	20	18	29	27	7	27
51-100	8	0	6	0	20	7	9
More than 100	26	73	59	14	0	0	5
	100	100	100	100	100	100	100
Total Responses	(90)	(15)	(17)	(7)	(15)	(14)	(22)

^{a/} Entrepreneurs were asked the number of other firms competing in their main markets.

Two questions follow from this analysis. The first asks why at least 60 percent of firms were having trouble competing with imports. Possible explanations include: (i) appreciation of the zloty by more than 10 percent at the time of the survey with ongoing domestic inflation, a situation where prices of competing imported goods were dropping as Polish production costs presumably were rising; (ii) a pent-up preference among Polish consumers for Western imports regardless of their price or quality; and (iii) inferior quality and higher prices of Polish goods relative to imports. This survey collected no quantitative data with which to answer this important question, but observation and discussions with entrepreneurs indicated that the latter two explanations accounted for most of the problems with import competition.

For example, clothing and knitted goods from Asia were overwhelming local producers more because of their superior quality, current styling and status than a price advantage conferred by the exchange rate. Manufacturers of import lookalikes and those who inserted fake labels in their clothing were able to sell them at current import prices simply because consumers thought they were imported. Similarly, the numerous plastic container producers in the sample told researchers that they were losing their markets to pre-packaged, imported processed foods and cleansers not because of the prices of these goods, but because Polish consumers believed they were higher quality products. Some admitted that their extruding machines lacked the capacity to produce plastic goods of a quality comparable to imported plastics. The only cases where researchers felt that the exchange rate was the key factor in import sales was in low-cost, poor-quality goods, i.e., cheap clothes from Syria and inferior chemical products from southern Europe. In these cases, entrepreneurs indicated that low import prices were the key factor in the sales of their competitors.^{24/}

The second question asks how entrepreneurs were responding to falling demand for their products and the threat of imminent failure. A small number--mostly design engineers--were busily developing new products. A few firms were actively pursuing export markets. Some were closing, and at least a

^{24/} A cross-country comparison of Polish production costs with costs in other countries, e.g., Thailand or Indonesia is a much-needed piece of research that would clarify Poland's true cost advantage.

third of those with severe demand problems were moving into retail trade, either supplementing their manufacturing businesses or abandoning them. Others were passively watching their inventories grow, regretting investment of their savings in capital equipment with little flexibility, and wondering what to do next. Others were switching from product to product, trying to find a profitable niche. The common attitude was one of defeat, anger and disappointment.

Of perhaps more interest was what troubled firms were not doing. Few demonstrated an understanding of the basic function of prices in an economy. When asked questions about whether they had lowered prices when demand was weak or raised them when demand was strong, responses invariably were negative, usually accompanied by comments to the effect that demand and price were unrelated. It is not surprising, therefore, that few entrepreneurs indicated that lowering costs was a strategy to increase their competitiveness. The more common strategy was to produce greater volume. Entrepreneurs in trouble were not getting on buses and going West to assess their competitors. Most were not exploring export possibilities, but rather were operating with the assumption that their products could not reach export quality. Many said they needed help with management and marketing, but few had found means of upgrading their skills--training courses were too expensive--or to acquiring more up to date equipment--interest rates were too high. In sum, the entrepreneurial spirit was everywhere in evidence, but the confidence and assertiveness to pursue opportunities--as well as the opportunities themselves--appeared to be in short supply, particularly among more isolated entrepreneurs in small towns.

Issues of Supply

The reform program adopted by the Polish government appears to have had remarkable success in stimulating the supply of factors needed by private producers to manufacture and distribute their goods. An analysis of the constraints involved in the production and delivery of products necessarily focusses on how well capital, labor, input, and foreign exchange markets were functioning.

Capital Markets. Twenty-nine percent of entrepreneurs cited financial problems as their primary constraint: exorbitant interest rates (15%); slow payment or non-payment by state firms for goods delivered (8%); and lack of working capital (6%). Analysis of these firms showed that 81 percent had received short-term bank loans, and only two of these entrepreneurs had applied for loans and been turned down.

As noted above, entrepreneurs showed little awareness of the connection between interest rates and other macroeconomic indicators and were uninterested in discriminating between nominal and real interest rates. Entrepreneurs believed that interest rates were excessively high, a perception that was reinforced by the fact that many were competing with foreign producers with fixed exchange rates--a circumstance which prevented them from raising their prices in tandem with the rest of the economy. Those who had received loans in 1990 had witnessed a sharp rise in nominal interest rates from 30-40 percent when they took the loan to 80-90 percent when interviewed. Many were fearful that they would be unable to repay their loans and angry that the government had allowed interest rates to rise to such high levels.

As reported in Chapter IV, the Polish banking sector had made mostly short-term loans to sixty-eight percent of entrepreneurs since 1988. Almost all sample entrepreneurs said that they were unwilling to commit themselves to long-term loans so long as interest rates were high and unstable. They indicated that banks likewise were uninterested in extending term credits. Lack of investment credits obviously

was limiting entrepreneurs' abilities to purchase needed new equipment--a critical problem in the medium to long-term.

Several survey findings pointed toward weaknesses in the Polish banking system. An analysis of the firms that received loans showed no correlation between sector and extension of credit. Knitting and clothing firms, many of which were failing, had received as many loans as firms that produced machinery, a sector mostly on the upswing. Similarly, 56 percent of firms classified as the weakest ones in the sample had received loans along with 50 percent of firms classified as high performers. Financial services appeared minimal and of poor quality. Entrepreneurs reported that routine financial transactions with banks were needlessly inefficient. Exporters complained bitterly about the time taken by banks to transfer funds abroad. Researchers encountered no instances of banks' offering more sophisticated services such as leasing or equity financing.

The second and third most commonly noted problems with finance--slow payments by state firms and lack of working capital--often were related. In some cases, an inability to pass through increased production costs to consumers due to competing lower-priced imports was presented as a shortage of working capital. In others, working capital was eroded by state enterprises that required cash payment for raw materials and inputs but demanded credit for goods delivered. As a result of this practice, many private firms were forced to take working capital loans, thus subsidizing their state customers. Extracting payment from state firms obviously was time-consuming for all, but particularly troublesome for entrepreneurs who were forced to plan their production schedules around payments from state firms. Legal procedures were reported useless--extremely slow and expensive, with little or no mechanisms to enforce judgements particularly in cases where the state customer was bankrupt.

Labor Markets. The beginnings of a labor market in Poland were discernible in the movement by workers from employment in the state sector to the private, in a widening gap in salaries between skilled and unskilled workers, and in differential salary scales between rural and urban areas. Many problems remained, however, and researchers were able to identify the following specific instances where poorly functioning labor markets were impeding growth and efficiency in the private firms interviewed.

First, labor mobility appeared critically limited by non-functioning housing and information markets. Wide-spread lack of housing meant that employers were forced to hire workers who lived nearby or to pay commuting costs. This problem was particularly evident in small towns and rural areas where half of sample firms were located. Labor mobility was further hampered by the lack of formal information networks that would link prospective employers and workers. Workers seeking jobs and employers needing workers found each other by word of mouth, an inefficient grapevine.

Second, continued provision of critical benefits by state enterprises and the low wages and fragile positions of many private firms appeared as powerful disincentives for many workers to move to the private sector. The choice to move to the private sector apparently was less difficult if the state employer was bankrupt or if one had strong technical skills and an entrepreneurial spirit, but more difficult if one had a family and depended on the housing and family benefits that come with state employment. The most common situation appeared to be one in which workers had to choose between their state employer who was limping along and private entrepreneurs who were unable to afford high salaries or many benefits. One can hypothesize that so long as workers believe that the government will bail out their employers, the incentive is to remain with the state enterprise as long as possible.

Third, most sample firms appeared to have a negligible capacity to absorb more workers and indeed needed to shed some of the workers they had. The fact that the labor force in sample firms tripled

since firms started up reflected their fast growth and the positive conditions for many private firms that existed in the Polish economy in 1989 and 1990. But in May 1991, many sample entrepreneurs were in the uncharted positions of having hired additional workers when their firms were expanding in 1990, only to find that they could not afford them when sales and profits dropped in 1991.

Fourth, the formal education system and years of working in state enterprises have produced workers with a narrow skill base. Entrepreneurs reported that unskilled workers commonly come to private firms able only to sew pockets in clothing or to operate one metal working machine. Several entrepreneurs who had purchased new equipment faced problems in upgrading workers' skills to exploit the new technologies.

Fifth, researchers concluded that the communist regime in Poland may have done more to reshape the culture of work than the culture of entrepreneurship. On the one hand, many employers exhibited binding loyalty toward their employees, avoiding lay-offs when they clearly were needed because times were hard and unemployment rates were climbing. On the other hand, the same entrepreneurs complained consistently and loudly that labor productivity was exceedingly low and highly resistant to improvement. Entrepreneurs complained that workers brought their work habits from state enterprises: absenteeism, long work breaks, poor quality control, drinking on the job, and of perhaps most interest, no response to pay incentives. Reports of poor work performance in Poland contrast sharply with reports of hard-working Poles abroad, leading to the speculation that incentives for productive work in Poland have remained highly distorted.^{25/} A number of firm owners were cynical about reported high unemployment rates in Poland. In their minds, unemployment was equated with an unwillingness to work honestly and hard.

Raw Material and Input Markets. A powerful testimony to the efficacy of "big bang" reform was found in the fact that, with few exceptions, entrepreneurs reported that they were able to obtain a full range of raw materials and inputs. The legacy of shortages and the history of blocking private producers' access to material inputs makes this achievement of the Polish reform program particularly noteworthy. Entrepreneurs who were using mainly imported inputs reported no difficulty in obtaining the quantity and quality of inputs needed in the time frame required. But 20 percent of those who relied on domestically-produced inputs said that they sometimes had problems getting production materials from state enterprises. Previous shortages had given way to surpluses and lower prices as state managers actively tried to sell their products. Private producers who formerly waited at the end of lines to purchase what was left over now had no problems with access. Current problems were more that some state suppliers were closing down or producing irregularly, forcing their customers to look more extensively for new suppliers.

The fully functional goods markets in Poland contrasted sharply with goods markets in Czechoslovakia and, to a lesser degree, in Hungary where a host of factors functioned to restrict the flow of imported and domestic inputs to private entrepreneurs. The wide-spread, largely private retail sector selling imported and domestic goods that developed in post-reform Poland was not found in Czechoslovakia and Hungary. In these countries, restrictions on access to foreign exchange for self-employed persons have limited the inflow of imports and maintained state trading companies that handle both domestic and imported goods. In addition, "small privatization" has proceeded more slowly in Hungary and CSFR with resulting slower growth in retail markets. In Czechoslovakia, access to

^{25/} An intriguing and much needed piece of micro-level research would answer the empirical question of how productive Polish workers actually are, as well as identifying the key variables that would increase their willingness and ability to work more productively.

domestic inputs was restricted by managers of state firms who resisted selling to private producers, preferring to maintain the status quo until the "large privatization" decides their fate.

Foreign Exchange Markets. Entrepreneurs reported that they could purchase foreign exchange with no difficulties. The few individuals who said they had problems were located in small towns, and their branch banks were not yet selling foreign exchange. Further testament to the ease with which sample entrepreneurs were using foreign exchange was found in their trouble-free procurement of imported equipment and inputs.

The Cost of Doing Business

This section focusses on the costs imposed upon private producers by various aspects of the business environment, specifically the legal and regulatory framework, physical infrastructure, the dominant state sector, and prevailing public and private attitudes toward private profit-making.

The Legal and Regulatory Framework ^{26/}

The success of the Polish government in formulating a new regulatory framework that would support private sector entry was verified by entrepreneurs who obtained the proper start-up licenses and permits painlessly and quickly, usually in less than a month. Entrepreneurs operated with few restrictions, producing almost any product they chose, purchasing domestic and imported inputs from whomever they chose, and selling their products wherever they found buyers in domestic or foreign markets.

Entrepreneurs consistently voiced two complaints about the legal and regulatory environment. The first, cited by 10 percent of entrepreneurs as the principal problem affecting their businesses, was lack of clarity and instability of government policies and regulations. Entrepreneurs described a number of examples where politicians in Warsaw had shifted regulations or budget allocations rapidly and, most damaging of all, without warning. Constantly shifting import duties and tax regulations were the objects of many complaints. Sudden cutbacks in government spending meant that some firms producing goods or services for the government lost their markets immediately and with no notice. For example, one firm was producing cotton sheets for use in government-owned student and worker hostels. Another was producing replacement window and door frames for hospital renovations, and a third was producing the components for plastic educational aids for schools. In all three cases, the government cut its expenditures for these items with no notice and the businesses producing them immediately folded.

The second complaint involved tax regulations, specifically the rates at which entrepreneurs were taxed, the frequency with which taxes were changed, and the lack of clarity concerning the content of the regulations. Polish producers were paying high tax bills. They were exempted from the excess wage tax levied on state firms in 1991, but they were liable for corporate income tax of 40 percent; turnover tax of 20 percent for most products, special turnover taxes at varying rates for imported goods; personal income tax that exceeded 40 percent for incomes greater than about US\$5,000 per year; and wage and social security taxes that total 65 percent. Investment costs of less than about US\$100 could be written off as production costs, a practice that led to importing machinery by its component parts. Apparently, amortization allowances were increased in 1991. There were universal complaints about the numbers of

^{26/} The points of view expressed by entrepreneurs are presented here with no attempt to present an in-depth analysis of the legal/regulatory environment.

changes that were made in tax regulations in the previous 18 months: entrepreneurs showed interviewers four-inch stacks of tax regulations to illustrate their point.

Infrastructure

Entrepreneurs were asked to list and describe their main problems with public services. Of the 78 firms that responded, 58 listed telephone services as their main problem, 10 cited electricity, and 10 described a variety of other problems. Problems with telephones included an inability to obtain a listed telephone number even when lines had been installed, frequent interruption of services, and delays in calling outside of the immediate area. Entrepreneurs were operating their businesses with a minimum of communication by telephone, relying instead on personal contact and wasting a great deal of time in the process.

There were also reports of problems with electrical service. In some cases, current systems apparently could not handle the power demands of entrepreneurs' equipment. A number of people were installing their own transformers and primary lines to increase capacity. Some had put in their own roads, power lines and even water systems. The policy of local governments in provision of public services was unclear, but entrepreneurs appeared to accept that provision of services above what already existed was their responsibility.

Linkages with the State Sector

State-owned enterprises (SOEs) contributed little to the formation of sample firms, but most entrepreneurs depended heavily on SOEs as suppliers of their raw materials and inputs and as customers for their products. In some cases, state enterprises were primary competitors.

Origins in the State Sector. The state sector in Poland contributed almost nothing to the formation of sample firms beyond former workers and cast-off equipment. The ineffectiveness of the Polish privatization program was clearly seen by the fact that not one firm in the sample was established as a result of official privatization efforts, and very few were initiated through informal privatization efforts. The state owned a minority share in three firms. Only 10 sample firms could trace their origins even indirectly to the state sector. Connections included: three cases where private individuals, including workers, had bought divisions of or entire state firms or cooperatives after they stopped production; three cases where private entrepreneurs had leased idle space and equipment from a state enterprise that had closed down; and four firms that previously were cooperatives.

The failure of the Polish government to develop a mechanism by which assets in the state sector could be passed to the private sector takes on greater significance when compared with Hungary and CSFR. Preliminary analysis of data from comparable surveys in Hungary and CSFR showed that approximately half of firms in each of these samples were former state enterprises that have been transformed into private companies. In Hungary, many companies came into private hands through spontaneous privatization and transformation of quasi-private enterprises operating within state enterprises. In CSFR, many sample firms took private form through the "small privatization" auctions and through the restitution program. As a result, the asset base among sample firms in Hungary and CSFR was far larger than in Poland, where the state sector apparently had successfully resisted yielding its industrial assets to the private sector at the time of the Polish survey.

State Enterprises as Suppliers. As noted in Chapter IV, half of all inputs and raw materials used by sample firms were produced domestically, almost all by state enterprises. Three points are noteworthy concerning the state sector as supplier for the private sector. First, the strongest firms in the sample--

machine manufacturers and high-tech metal and plastics producers--relied almost exclusively on the state sector for their raw materials. Second, about 20 percent of those who used mainly domestic inputs said that they were experiencing increasing problems in obtaining their inputs due to instability in the state sector. When production stopped in the state firm, production also stopped in the dependent private firm until an alternative source of the input was located or the state firm resumed production. Third, state firms reportedly demanded cash for products sold to private producers but delayed payment for goods received as long as possible. This practice forced private firms to extend involuntary credit to state enterprises.

State Enterprises as Customers. Most entrepreneurs agreed that, despite payment problems, state enterprises were the most desirable customers because their orders typically were much larger than orders from the private sector. Many entrepreneurs were caught between declines in orders from SOEs that were cutting back and an inability to secure private buyers who preferred to sell imports. In some cases, products were specialized to the needs of the state firm and were not particularly adaptable to other uses. In others, selling to state clients allowed private producers to maintain product quality below that dictated by the open market, particularly for finished goods. Rural areas appeared hardest hit because the local state enterprise was often the only customer within miles of the private producer. Examples of this dependency included a company that produced cleaning fluid for the Polish railroads which was privatizing its cleaning service, and a chemical company that once produced 100 tons of a leather processing compound and now produces 2-5 tons because its state-owned customers have closed.

State Enterprises as Competitors . Twenty percent of entrepreneurs--mostly manufacturers of machinery and high-tech metal products--said that their chief competitors were state-owned enterprises. Many of this group were in excellent positions to underprice competing state firms, and a number were quietly waiting for the competing state firm to fail so that they could take over the market. Many entrepreneurs believed that biases remained that favored the state sector to the disadvantage of competing private firms, including access to cheap credit that do not require repayment and monopolization of MFA quotas.

Private and Official Attitudes

Private sector development has been touted by the Polish government as a major cornerstone in the emerging market economy, but a deep and observable ambivalence toward private enterprise and personal wealth appeared to remain in both public and private spheres. Forty-five percent of entrepreneurs said that the attitudes of public officials toward them were negative; 26 percent said they were neutral (Table 5.3). A similar pattern emerged when asked about the attitudes of average citizens toward them: 52 percent said negative and 22 percent said neutral. Negative opinion among public officials reportedly dominated the tax offices where entrepreneurs said they were treated as "subhumans". Negative attitudes among private citizens toward private entrepreneurs were ascribed mostly to workers in state firms who believed that those in private business were amassing fortunes. Jealous neighbors apparently see a new car or other purchase and alert the tax office to "wrongdoings".

Table 5.3: Attitudes of Public Officials and Private Citizens Toward Private Business ^{a/}
(Percentage of Firms Responding)

	Number of Firms	Very Negative	Negative	Neutral	Positive	Very Positive	Total
Attitudes of:							
Public Officials	91	12	45	26	15	1	100
Private Citizens	92	1	52	21	22	2	100

Note: Figures may not sum to total due to rounding.

^{a/} Entrepreneurs were asked "How would you rate the attitude of government, public officials, managers of state enterprises, and the average citizen toward private business and profit making?"

Entrepreneurs were not indifferent to public attitudes toward them as shown by the ways in which many chose to set up their businesses, particularly in small cities and towns. Companies often were hard to locate even when armed with correct addresses. They were located, almost hidden sometimes, in obscure alleys and ordinary apartment buildings. Many had no signs pointing the way to their offices or even the name of the company on the front door. Rents were probably cheaper in such locations, but one suspected strongly that the desire for anonymity also played a major role in the choice of location. The impression was that at least some private entrepreneurs were not entirely comfortable in their role as capitalists and may, in fact, have harbored some self-doubts.

Prospects: Strong Firms Versus Weak Firms

Groups of strong and weak firms were identified and compared with one another to help clarify factors associated with success. The strength of operating firms was judged using three criteria:

- (i) whether production had increased in the past 12 months,
- (ii) whether profits were increasing,
- (iii) rankings given each firm by interview teams.

Fifty-two percent of firms reported that production had increased since start up; 30 percent said that it had decreased; and 17 percent said that there was no change.^{27/} Researchers noted that about half of entrepreneurs raising production volume were doing so in the face of falling demand, most notably in clothing and knitting firms. When asked whether their businesses were more or less profitable than in the first few months after starting up, 58 percent said less profitable; 36 percent said more profitable; and 6 percent said profits were unchanged. Forty percent of urban entrepreneurs said their businesses were more profitable versus 33 percent of rural firms.

^{27/} Trends in production were unclear, due in part to the timing of the survey and to less-than-optimal phrasing of several survey questions. May 1991 is somewhat of a midpoint between the last six months of 1990 in which sample firms apparently were expanding, and the first six months of 1991 in which many were contracting and actually switching out of production and into trading. This discontinuity rendered questions based on 12-month trends less useful than they might have been. Estimating production trends over the previous 12 months also was problematic in that the baseline for many sample firms was zero because they were started in the past year.

Survey teams ranked firms as to their prospects based on having listened to their owners and/or managers, viewed their facilities, examined the trends in their businesses, and applied knowledge from other firms in the same activities. Prospects were considered poor for 42 percent of firms, unclear for 24 percent and positive for 34 percent. Poor meant that survey teams predicted that these firms would soon be closed or bankrupt unless new products were found. Unclear meant that the entrepreneur was competent and his/her prospects depended on conditions in the general economy, the appearance of competing imports, and events in the state sector. A positive ranking was given to firms managed by competent entrepreneurs who were manufacturing products for which demand was growing or relatively inelastic, and for which imports were unlikely to offer serious competition.

Firms were classified as strong if all parameters were positive: production was increasing, profits were rising, and the rating from the interview team was positive. Weak firms were those for which all parameters were negative: production had decreased, profits were falling, and the interviewers rated the firm's prospects as poor. There were 18 firms in each group. The remaining 57 firms in the sample fell in between, ranking positively on some criteria and negatively on others.

Strong and weak firms diverged sharply along several dimensions. First, strong and weak firms were producing in different sectors and at different levels within the same sectors. A third of the strong firms were machine manufacturers (Table 5.4). Examples of successful machine manufacturers included firms producing scientific measuring devices and custom machines used as free-standing units or as components in production lines. Other strong firms included several clothing manufacturers who were producing unique, high quality clothing, e.g., expensive knitted sweaters and baby clothes and women's tights in large sizes. Several niche metal producers were among the strong firms and were manufacturing such items as traditional Polish metal picture frames, metal signs printed in Polish, and decorative metal gates for houses and factories.

Table 5.4: Distribution of Strong and Weak firms by Sector ^{a/}
(Number of Firms)

	Total	Knitting	Clothing	Plastic Products	Metal Products	Machinery	Others
Strong Firms	18	2	3	1	3	6	3
Weak Firms	18	4	6	1	4	1	2
Total in Sector	93	16	17	8	15	17	23

^{a/} Firms classified as strong reported that production and profits were increasing and they were judged as having positive prospects by the interview teams. Firms classified as weak reported that production and profits were decreasing, and they were judged as having poor prospects by the interview teams.

Weak firms were clustered mainly in three sectors: plastics, clothing, and knitting. Over half of plastics firms in the initial sample had closed before survey teams arrived, and only one plastics firm of the eight interviewed was among those classified as strong. Virtually all clothing firms producing everyday clothing, i.e., low and medium quality men's and women's pants, shirts and dresses, were in trouble. With a few notable exceptions, knitting factories were on the brink of collapse having lost their state customers when the USSR market closed, and found themselves unable to compete with imports. Mass-produced simple metal products made by cutting and grinding machines--often materials used by the construction industry--suffered from lack of demand.

Second, there were striking differences between strong and weak firms in the source and intensity of competition each were facing (Table 5.5). Forty-five percent of successful firms reported that their chief competitors were other large and small private firms; over 20 percent had no competition; and only 17 percent cited imports as their primary competitors. For example, machinery manufacturers--the strongest firms in the sample--had almost no competition because their buyers typically could not import substitutes due to unique specifications and therefore had to rely on custom orders. In contrast, 56 percent of failing firms reported that imports were their main competitors followed by state firms at 31 percent.

Table 5.5: Sources of Competition in Primary Markets ^{a/}
(Percentage of firms responding)

Major Competitors	None	Small Private Firms	Large Private Firms	State Enterprises	Coop.	Foreign-Owned Firms	Imports	No. of Firms
Strong Firms	22	39	6	11	0	6	17	18
Weak Firms	0	6	0	25	6	6	56	16

^{a/} Entrepreneurs were asked to identify their primary competitors.

Similarly, strong firms contended with far fewer competitors than did weak firms (Table 5.6). Sixty-seven percent of strong firms--compared with 24 percent of failing firms--reported that fewer than 10 other firms were selling in their main markets. Just under 90 percent of successful firms--compared with 53 percent of failing firms--were competing with 50 or fewer other firms. Almost half of weak firms reported that they were competing with more than 100 other firms. As expected, a larger number of failing firms (63% vs. 33%) reported that competition in their main product had become greater since they started up. Differences in the intensity of competition also were reflected in firms' principal constraints: entrepreneurs from strong firms complained first of financial problems while entrepreneurs from weak firms cited lack of demand as their biggest problem.

Table 5.6: Intensity of competition ^{a/}
(Percentage of firms responding)

Number of Competing Firms	None	1-10	11-50	51-100	> 100	No. of Firms
Strong Firms	11	56	22	0	11	18
Weak Firms	0	24	28	6	41	17

^{a/} Entrepreneurs were asked how many other firms produce in the main markets.

Third, strong and weak firms were in different locations, an indication that private sector manufacturing was emerging unevenly in Poland. Two-thirds of strong firms were in urban areas, and two-thirds of weak firms were in rural areas. Specifically, strong firms tended to be clustered in the environs of Warsaw and the central region of the country, and weak firms were mostly from the western and northern regions. The relative strength of firms in the central region is shown by the fact that there were no weak firms located there.

Other differences between strong and weak firms include the following. Equipment in strong firms was far newer than equipment in failing firms--almost 50 percent of machines used in strong firms was less than 3 years old versus 6 percent in the failing group. Owners of strong firms were more likely to report that their workers were not as highly skilled as needed and that they had problems recruiting skilled workers. Successful firms were more likely than failing firms to have stayed with a single product since start up rather than shifted to new ones (65% vs. 41%) and were more likely to have upgraded their method of production (67% vs. 47%). Two-thirds of strong firms relied primarily on domestic inputs purchased from state firms whereas two-thirds of weak firms used mostly imported inputs purchased from private firms. A comparison of output markets shows a slight reverse trend, namely that almost two-thirds of strong firms sold primarily to other private firms while weak firms were evenly divided between state and private customers.

In sum, most of the strongest firms in the sample were urban producers from Poland's central region that were manufacturing high quality products for niche markets protected from imports. Two-thirds of the weakest firms were in rural areas and most were producing low-quality, mass-produced goods unable to compete with imports that were flooding the market. An implicit conclusion from this analysis is that the growth edge in private sector manufacturing was in urban areas. At the same time, the fact that almost half of sample manufacturers were located in rural areas dictates that care be taken to include rural enterprises in analytical work and in assistance programs.

VI. NEEDS FOR ASSISTANCE AND RECOMMENDATIONS FOR ACTION

Section A of this chapter summarizes the types of assistance requested by entrepreneurs and their views of programs that were in place. Section B contains a series of recommendations for action, based on the constraints cited in Chapter V and specific requests for assistance described here.

Requests for Assistance

Entrepreneurs were asked to describe the types of short-term training that would be most useful to them. The responses given most often were management (29%) and marketing (25%), followed by assistance in obtaining credit (9%), import/export information (8%), and accounting (7%). In addition, entrepreneurs expressed needs for numerous types of information in the context of other questions.

"**Management**" was used as a general term to refer to a broad range of skills including the ability to organize production in more efficient ways, motivate workers to be more productive, and manage company finances. In fact, most entrepreneurs appeared to be managing fairly well. Almost all knew their local markets and had a good grasp of their competitors. Most were maximizing the utility of their outdated equipment, and many were struggling with how to raise the productivity of their workers. They knew where to find raw materials and inputs, and most had made price comparisons between domestic and imported products. All kept careful and detailed records of costs and revenues, and most knew quite well how prices had changed and the implications for their businesses.

Entrepreneurs were functioning well in their present conditions, but most had little sense of where their businesses were headed in the future. Obvious explanations for this lack of planning were: lack of exposure to basic business practices that teach one how to plan, a dearth of product-specific information needed to plan, and the volatility of the marketplace that, according to one entrepreneur, turns business planning into gambling. All sample entrepreneurs were self-taught. Almost none had training or experience in free-market business when they started, and virtually none in the sample had received any technical assistance since they began. Their starting point was the status quo of production in state enterprises, opportunities in their local markets, and technologies embodied in used equipment from the state sector.

Those who said that they needed assistance with *marketing* knew that they needed to sell more products in a larger number of markets. The lack of marketing knowhow was an outstanding weakness in entrepreneurs' skills, and the most mystifying to survey teams who encountered entrepreneurs with rising inventories and absolute bewilderment as to what to do.

Entrepreneurs' explanations of this problem provided useful insights into its sources and possible remedies. First, it must be understood that the need to market is new. Many entrepreneurs were accustomed to selling as wholesalers to state enterprises often within ongoing, sizeable contracts. Falling demand in the state sector and a rising supply of goods from new entrants has forced private producers to scramble to secure buyers.

Second, interviewers detected a passivity, bordering on an aversion, to marketing. Sample firms employed no marketing or sales personnel, and entrepreneurs expressed little awareness that products need to be distinguished or that markets can be created. As in the past, orders were coming mostly from personal contacts with none of the anonymity of the modern marketplace. Even as orders fell in the first months of 1991, most entrepreneurs had taken few steps to penetrate new markets though they clearly

knew they needed to do so. Researchers hypothesized that aggressive marketing may symbolize "going public", breaching the historical dictate that private entrepreneurs operate unobtrusively.

Third, a number of sample entrepreneurs demonstrated little understanding of the roles played by middlemen--distributors and retailers--in market economies and, true to their ideological past, characterized them as "sponges" who produce nothing but earn much by reaping profits that rightfully belong to producers. Several expressed the conviction that they were being swindled by retailers selling their products at more than twice the wholesale price, a practice they thought prevented sales of their products. Some who used imported inputs charged that traders from whom they bought were commanding extortionists' prices.

Fourth, some entrepreneurs blamed the poor reputation of Polish products for their inability to market their products. Many complained that Polish consumers preferred imported products even when theirs was superior. Several were manufacturing import lookalikes, e.g., T-shirts embroidered with "Chanel, France". Few clothing products bore Polish labels. One enterprising manufacturer was producing, using and selling labels saying "Made in Thailand". The poor reputation of Polish products apparently was the first obstacle in selling abroad. Sample exporters said they commonly could sell only to customers who knew them or who were referred to them through personal contacts.

A few entrepreneurs were trying to market their products. The typical approach was to take photographs of their products to retailers in their area and try to persuade them to buy. Several had printed simple brochures. When queried about public advertising, the response was either a blank look or a contention that it does not work because newspapers do not allow pictures needed to draw the Polish buyer, and the public ignores newspaper ads where state enterprises historically have advertised.

Lack of product-specific *information* impaired seriously entrepreneurs' abilities to anticipate the types of shifts needed to maintain competitiveness. Many had little or no idea of the structure of national or world markets for their products. They only learned of more advanced or cheaper production when competing imports arrived in their area, too late for them to respond. In this sense, isolation had rendered many entrepreneurs reactors rather than actors in the marketplace, unable to assess the competition in advance and plan accordingly. One example of this isolation was a man who patented a small plastic cover to prevent rusting of roofing nails only to be eclipsed by imported galvanized roofing nails.

Types of information specifically requested by entrepreneurs included the following:

- (i) manuals on the basics of starting and operating a business;
- (ii) national and international product-specific information about technologies and markets;
- (iii) information about banking practices including international financial transactions;
- (iv) information about Western accounting systems;
- (v) information about stock markets and how they operate;
- (vi) English and German language training.

Entrepreneurs' Views About Assistance Programs

Existing Assistance Programs

Sixty percent of entrepreneurs had heard about assistance programs designed to help owners and managers of private firms, but only 10 individuals had participated in a training program or had applied for a loan from a directed credit program. Without exception, the experience was a negative one. Those

who had attended training programs complained that trainers were foreigners with little knowledge of Polish conditions and that training materials were drawn from other countries and not relevant to Poland. For example, one man and his wife attended a seminar on the mechanics of the forthcoming value-added tax and were disappointed to come away with only a three-page handout detailing how the tax is applied differently across a dozen countries, with virtually no information on how the change in tax system would affect their business. Another claimed that an accounting course offered by a British agency taught participants British accounting practices unrelated to practices in Poland.

The second most common complaint was that training programs were too expensive. Several entrepreneurs noted that one would have to take out a loan to afford a training course on how to prepare business plans needed to qualify for a loan. One person cited an ad on television for a two-week business course offered by an international business school that cost 40 million zloty (US\$4000).

The only credit program designed specifically for private business with which entrepreneurs were familiar was the Polish-American Foundation. About five firms had applied for loans from this Foundation and their experiences were uniformly negative. Several had applied for loans six or more months previously and had heard nothing about their applications. One person complained of being treated rudely and indirectly solicited for bribes. Another complained of a US\$20,000 ceiling on loan size which was too low to purchase the machinery that he needed.

Entrepreneurship Associations

A surprisingly high 76 percent of entrepreneurs were not members of any trade or business association. Those who were members generally belonged to a trade-specific organization, e.g., a textile association. When queried about membership benefits, most laughed and said that thus far they had received no benefits. Many were cynical about entrepreneurship associations, saying that private consultants and lawyers running such organizations have little actual connection to private entrepreneurs. None saw industry-specific, membership associations as a potential source of technical assistance or political power. The lack of interest in membership associations in Poland contrasted with the situation in Hungary, where the national entrepreneurship association has a strong constituency that receives technical services and effective representation in the government.

The Government as a Source of Assistance

Entrepreneurs were asked for their views as to what the government should do to assist private sector entrepreneurs in starting and operating their businesses. The four most common answers in order of frequency were: lower interest rates, raise import barriers, stabilize government policies and regulations, and create information networks for private producers. Many entrepreneurs believed that the government should simply lower interest rates so they can purchase much-needed new equipment. Entrepreneurs, particularly clothing manufacturers, railed against the government for failing to protect them against competing, lower-cost imports. Many felt that the most important thing the government could do for private business was to keep their policies, particularly import duties, consistent so that producers could make reasonable business plans. A number of entrepreneurs felt that the government should take an active role in providing information, especially on its own regulations (particularly tax regulations) and industry-specific market opportunities and new technologies.

Additional ways that entrepreneurs thought that government could assist private sector entrepreneurs included: (i) provision of incentives for new firms in the form of tax holidays or cheap loans; (ii) introduction of more competition into the banking sector so that banks would deliver better

services; (iii) updating of vocational education so that students are trained with modern equipment; (iv) provision of greater access for private manufacturers to MFA quotas for the EC and the US; (v) tightening up the wording and implementation of Polish patent laws to better protect inventors; and (vi) offering tax incentives to those who hire additional workers.

Recommendations for Action

Given the number of compelling needs in Poland, and the scarcity of resources with which to respond to those needs, recommendations for action must be prioritized. The following recommendations were formulated and prioritized based on entrepreneurs' accounts of the constraints hindering their growth, researchers' judgements after hundreds of hours observing Polish entrepreneurs and their firms, and a preliminary assessment of the strengths and weaknesses of Polish firms relative to their counterparts in Hungary and Czechoslovakia where comparable surveys have been completed.

The central focus of policies and programs to encourage industrial growth should be to enhance the competitiveness of Polish products in domestic and foreign markets. First-order recommendations to move toward this objective include: (i) adoption of a pro-active initiative to develop Polish private manufacturing, moving beyond getting incentives right to building capabilities and developing support institutions; (ii) inclusion of private sector issues in the national political and economic debate; (iii) broadening and deepening of labor and financial markets; and (iv) increasing the flow of several types of information critically needed by entrepreneurs. Second-order recommendations focus on lowering the costs exacted from private producers by the business environment through: (i) privatizing state sector as quickly as possible; (ii) stabilizing official regulations affecting private producers; and (iii) improving infrastructure, with particular emphasis on telecommunications and local infrastructure. Third-order recommendations involve delivery of technical services to entrepreneurs.

First-order Recommendations

The *first* priority is to take a pro-active approach to strengthening the position of Polish products in world markets. As shown by the survey data presented in this report, the adjustment process that weeds out non-competitive firms through import competition was well underway in May 1991. The issue was not how to eliminate those who could not compete but rather, it was how to support and build those who could. Despite the enormous progress made in the past 24 months, ongoing recession, pervasive market imperfections, the distortionary effects of the large state sector, and the lack of institutional support for private producers combined to produce substantial barriers to the growth of competitive private industry.

What can be done? A recent OED review of the Bank's support of industrialization in selected countries lays out a useful framework for approaching this question.^{28/} The OED report posits that industrial success depends on the interplay of three factors: incentives that guide allocation of resources, and capabilities and institutions that determine the response to incentives. Two types of interventions are available when markets fail in any of these three areas: functional interventions that address generic market failures without favoring one activity over another, and selective interventions that redress market failures for selected activities.

^{28/} "OED Study of Bank Support of Industrialization in Newly Industrializing Countries: Case Studies of Korea, India and Indonesia," Operations Evaluation Department Report No. 9899, Vol. I, The World Bank, September 1991.

The initial thrust of the reform program in Poland focussed on getting the incentives right through stabilization and liberalization measures. Without question, private manufacturers' abilities to compete in world markets were critically hampered by the difficult macroeconomic setting prevailing in May 1991. But firm-level observations indicated that entrepreneurs' abilities to compete were also critically affected by the capabilities they brought to the task and by the presence or absence of institutions that facilitated their success. A pro-active approach to private sector development in Poland would move beyond the view that getting incentives right is sufficient and would actively seek effective means of enhancing entrepreneurs' capabilities and developing the institutions that are needed.

The *second* priority is to include the private sector in national policy debates as key participants in the transition. Discussions of industrial policy have centered almost entirely on debates over the most expeditious and equitable approaches to dismantling the state sector, with little focus on fostering private sector growth. Failure to include the private sector in policy and programmatic considerations has kept the focus on the dying sector instead of the emerging one, and it has contributed to the growing alienation observed among private entrepreneurs. Entrepreneurs clearly felt like marginal figures in the reform process underway. Periodic statements by government officials that equivocated about the desirability of private enterprise endorsed public sentiment against private entrepreneurs and delivered an official message that private activity was not yet fully legitimate.

The *third* priority is to commit resources to broadening and deepening markets. Serious problems appeared to be brewing just below the surface: the labor force reportedly was immobile and unproductive; banks offered virtually no financial services beyond short-term loans; and obsolete technologies diminished entrepreneurs' abilities to compete.

Labor mobility would increase if people could shift their residences to take advantage of employment opportunities. Efficient information networks that link potential employers and employees would address problems with unemployment and facilitate more productive matches between employers and employees. Research is badly needed to clarify the labor productivity of Polish workers and the barriers to improving current levels. If such research should confirm this study's finding that relations between employers and workers are poor, interventions engineered by human resource personnel could be useful. Further clarification as to the incentives or disincentives for movement on the part of workers from the state to the private sector could be useful as state enterprises are privatized and workers are laid off.

Banks need to develop financial services for private business consistent with those in the West. Analysis of loan recipients indicates that loan officers may not be appraising loan applications as carefully as they might. There were no examples of banks providing firms with investment loans, lease or lease/purchase arrangements, venture capital or equity. International financial transactions appeared entirely inadequate. Training courses for loan officers could improve the quality of project appraisal and supervision. Training courses for bank managers could result in the introduction of extended and more sophisticated financial services.

Updating technology in private manufacturing companies is likely one of the most difficult problems to address. When queried about the possibilities of export production, most entrepreneurs were enthusiastic but aware that their products were of too poor quality to compete in world markets. Some portion of this gap was due to outdated equipment, and some to lack of production knowhow. Unlike Hungary and CSFR where lease/purchase arrangements were available and where foreign partners or buyers have assisted with equipment and knowhow provision, Polish entrepreneurs appeared to have few alternatives for acquiring updated equipment. There were few foreign partners generally, and even fewer

willing to shoulder at least part of the cost of upgrading equipment; banks did not offer alternative financing arrangements such as leasing facilities; and venture capitalists were nowhere in evidence.

The *fourth* priority is provision of information needed by entrepreneurs to plan and operate their businesses effectively. Three problems need to be addressed. First, researchers were struck by how little most entrepreneurs understood about market economics, the basics of demand and supply. Many were confused about where government responsibilities end and individual ones begin. Second, all knew that the Polish government had instituted a reform program, but few understood its objectives and methodologies and none appeared to perceive themselves as participants. The common attitude was to blame the reform program for falling orders and the devastating influx of competing imports. Third, producers needed better access to the kinds of domestic and international product-specific information that are critical for planning, e.g., markets, prices, technology information.

An information campaign on four fronts could address these problems. The first should consist of basic courses on how market economies operate including the role of prices, how markets function, and the rights and obligations of private business. The second should be a campaign to educate the Polish citizenry about the design and the objectives of the government's reform program, progress to date, future objectives, and means of achieving them. The third should be a massive effort on the part of government to gather and disperse as much information as possible about the basics of operating private businesses. The fourth should be a concerted effort to make national and international, product-specific information available to private producers on a regular basis.

Regardless of whether these campaigns are led by government or by private initiative, all four should aim for maximum national coverage, making use of all media available including newspapers, magazines, journals, radio, televisions, schools, and public meetings. They could involve one-time events and publications, or regular series could run in newspapers and on television. The content should be as factual as possible, resisting the temptation to politicize the facts. All should be free of charge and available to a broad audience throughout the country.

Second-order Recommendations

The second order of recommendation addresses problems found in the general business environment, and three stand out. For all the reasons cited throughout this report, the first priority is privatization of the state enterprise sector. Private entrepreneurs faced a large shock in 1990 when trade liberalization brought a flood of competing imports, and they will face a second shock when privatization actually occurs. Delays in privatization have maintained distortions and prevented final adjustment to a market economy. The solution is to privatize the state industrial sector as quickly as possible and in the meantime, streamline legal procedures for collecting payments from delinquent state firms.

Second, survey findings indicated that sample entrepreneurs were not burdened unnecessarily by official registration or licensing requirements, but they were incensed by the instability of regulations that critically affected their businesses, e.g., tax codes and import duty schedules. The government should resist the temptation to continually change regulations that affect private business. The cost in good will may well be higher than the expected benefits of the change. When changes must be made, advance notification would boost entrepreneurs' confidence in government.

Third, problems with infrastructure ranged from non-existent or poorly-functioning telephone systems to inattention of local governments to basic services such as road, water, and power. The faster telephone service is improved, the more efficient private business will be. If credit facilities were

available to finance such projects, municipal governments or private individuals conceivably could take responsibility for much of the basic infrastructure that entrepreneurs currently finance themselves. Clarification and development of municipal governments' roles and responsibilities is an issue of time and education.

Third-order Recommendations

The third order of problems involves direct delivery of technical assistance services to entrepreneurs. Without prescribing programmatic content of technical assistance programs or pointing toward executing agencies, some obvious conclusions about the basic shape of assistance for private sector manufacturers follow naturally from the survey. *First*, a primary objective of technical assistance programs should be to help new and aspiring entrepreneurs perform market studies and write preliminary business plans *before* they invest their personal savings or take loans from banks. Entrants in 1989 and 1990 could not have anticipated the enormous changes they would face with the reform program, but entrepreneurs starting today should be able to analyze the market and make sound choices. Short courses that focus on basic business skills should be offered as frequently and in as many locations as possible, and the fee should be minimal.

One idea suggested by a consultant for this project is utilization of mobile training units, reminiscent of the American book-mobile that for years extended the reach of libraries into neighborhoods. Such vehicles would contain user-friendly, interactive software appropriate for formulating business plans. With the help of instructors who are aboard, fledgling and operating entrepreneurs could enter various cost combinations and compare rates of return. Several hours of developing and comparing individuals' options could have enormous benefits in maximizing use of their resources, avoiding unnecessary losses, and learning business fundamentals through planning for their own businesses.

Second, technical assistance programs that go beyond basic business training should be designed along sectoral lines, avoiding past mistakes in other countries where all-purpose government extension services have been constituted with the result that services offered were too general to be of help and cost/benefit ratios were abysmal.^{29/} Industry-specific information about production, technologies, and markets would be of great value to entrepreneurs, and could be dispersed through printed material, television, courses and study tours. Updated technologies specific to given industries could be introduced and taught in classes designed for people engaged in similar activities. Industry-specific studies could be carried out and periodically updated so that entrepreneurs could have a view of the larger picture when they plan for their companies.

Third, maximum efforts should be made to increase Polish entrepreneurs' contacts with Westerners to upgrade skills and increase awareness of best-practice production. Programs could range from study tours, to exchange programs where entrepreneurs work in Western companies, to matchmaking events where potential investors meet Poles interested in forming joint ventures. Of note is the fact that the most often mentioned source of new products and new technology was the centuries-old, annual trade fair held in Poznan in 1990. Entrepreneurs appeared to have benefitted enormously just from the exposure to a broad range of products and production equipment. A recent visit by the author to a highly successful national trade fair in Hungary confirmed the value of this traditional forum.

^{29/} See *World Bank Lending for Small and Medium Enterprises: 15 Years of Experience* by Leila Webster, World Bank Discussion Paper Number 113, 1990.

Fourth, the process and criteria by which entrepreneurs receive loans, whether through the formal banking system or through special directed programs, should be made as transparent and efficient as possible. While many entrepreneurs had received short-term loans from banks, they had little notion of the basis on which such decisions were made. They were poorly informed about the process by which interest rates are set, and many were caught unaware when variable interest rates rose from 30 to more than 80 percent. Donors who introduce specialized credit programs should invest heavily in communication with potential clients to prevent the misunderstanding and disappointment that apparently has ensued from some entrepreneurs' interactions with the Polish-American Foundation.

VII. CONCLUSIONS

This chapter sums up survey findings and addresses the research questions posed in Chapter I. Section A analyzes some of the ways in which components and sequencing of the Polish reform program have helped and hindered private sector manufacturers. Section B looks at how Polish firms were adapting to the new economic environment and compares them with firms in other adjusting countries. Section C concludes the report by presenting two opposing views of present trends.

The Components and Sequencing of the Reform Program

Without question, the manufacturing firms surveyed in this project had benefitted enormously from many aspects of the reform program. Legal and regulatory reforms cleared the way for massive entry into the private sector, and set out the terms under which firms would operate. Stabilization measures ended hyperinflation and set reasonable exchange rates, prerequisites for successful business operations. Liberalization policies successfully jump-started markets to the extent that, in May 1991, manufacturers were able to locate factory space, buy used equipment, employ workers, obtain domestic and imported intermediate inputs, secure working capital loans, and distribute their products internally and abroad--all without prohibitive difficulties. The enormous response of the Polish citizenry to the new incentive structure was powerful testimony to the mileage gained by simply clearing away basic obstacles. Comparisons with Hungary and CSFR, where more gradual approaches were chosen, show that entrepreneurs in these countries still have some problems with access to the basics.

Nevertheless, many entrepreneurs interviewed for this study were in trouble. They were unable to sell their products in an economy characterized by recession and fierce competition, and most had few means of improving the competitiveness of their products. As discussed above, Polish entrepreneurs had had few opportunities to build an asset base--far fewer than their counterparts in Hungary and CSFR. Rapid trade liberalization had forced domestic producers to compete on world markets almost immediately, without time to learn business basics and without institutional support--a situation avoided in Hungary and CSFR where exposure to world markets proceeded more slowly. Entrepreneurs in this study were almost entirely inexperienced in business, and most had no exposure to the technologies embodied in competing imports. They had no access to affordable training programs, financial institutions with experience in extending services to small firms, testing and standards facilities, or established information channels. Investment capital was unavailable, and the failure to privatize the state sector kept industrial assets in state hands instead of passing them through to private entrepreneurs who desperately needed them. In sum, Polish private producers were thrust upon the world stage but given few resources with which to improve their performance.

With hindsight, are there ways in which the reform program adopted by the Poles could have been improved upon? Analysis shows that, in at least four respects, the sequencing of the reforms may have been unfortunate. First, the Law on Economic Activity which precipitated massive private sector entry was passed in January 1989, a full year before adoption of the reform program which liberalized prices and the trade regime. Therefore, the 800,000 self-employed persons and the almost 12,000 registered companies that started up in 1989--as well as the tens of thousands who began in the first months of 1990--did so in response to signals in the pre-reform environment--most notably shortages and limited import penetration--only to find they had invested their limited resources in products that were no longer profitable in the post-reform economy.

The timing of these reforms benefitted some groups over others. Apparently, many traders exploited shortages and made enormous legal and illegal profits. As gaps were filled, retailers could shift

easily to different products. To a large extent, manufacturers were in a different position. Some reported high profits in 1990 when shortages prevailed. But the shortages that dictated their initial product choice in 1989 and early 1990 were filled by imports brought in by Polish retailers in 1990 and 1991. Many could not shift products easily as they had invested in long-term leases on factory buildings, production equipment and new employees. Their losses and subsequent disillusionment could have been avoided had the legalization of private business and liberalization of the economy proceeded in tandem--a problem that perhaps could not have been foreseen in the Polish context but could possibly be avoided in other countries.

Second, in the short run, full trade liberalization--designed to integrate Poland into world markets in one giant step and specifically to force efficiency gains in the state sector--may have been more effective in undercutting the fledgling private manufacturing sector than in prompting the state sector to restructure. A major instrument of trade liberalization was full internal currency convertibility, a measure which allowed hundreds of thousands of self-employed traders to bring in a flood of higher quality and lower cost imports. Consumers benefitted as did those private producers who utilized imported capital goods and inputs. The state sector, the primary target of rapid exposure to world markets, reportedly found ways to avoid hoped-for restructuring. But private producers were overwhelmed, and many lost their businesses in short order. To the extent that firms had little potential to compete with imports, necessary losses were incurred. But to the extent that entrepreneurs could have competed with imports had they been afforded more time and resources, unnecessary losses were sustained and irreplaceable good will was lost.

Third, the failure to privatize the large state industrial sector maintained a playing field tilted in favor of the state sector, and diluted the effectiveness of the reform effort. Industrial assets that could have been used productively by the private sector remained in state hands, and the dominance of the state sector maintained market distortions and crowded out private sector investment. Privatization issues have dominated government time, and diminished the time available for work on private sector development.

Fourth, interviews with entrepreneurs made clear that the Polish government had done a poor job of communicating with its citizenry about the reform process and enlisting its participation. Most entrepreneurs demonstrated little understanding of capitalism or of the government's reform program. They did not see themselves as key actors or even participants in the transformation process, but rather as marginal players who were more often than not victimized by the process. For many, results were far below expectations, and they commonly held the reform program and the government responsible. Unrealistic expectations probably were unavoidable, but the level of disillusionment and cynicism among sample entrepreneurs might have been lower had they been given more information and somehow included more in the process. An example of a country where the populace was brought into the reform process effectively and on a large scale is Czechoslovakia. Sample entrepreneurs in CSFR clearly felt that they were an integral part of the reform process, perhaps because the government did a good job in communicating its objectives and methods, fostering national debate, and directly involving ordinary citizens in the reform process through the privatization and restitution programs.

Comparisons with Firms in Other Adjusting Countries

Similarities and differences between Polish companies and firms in other adjusting countries were striking. The constraints faced by Polish firms were indeed similar to those of firms in adjusting African countries as outlined in Chapter I. As found in the African surveys, Polish entrepreneurs were caught between rising input prices and an inability to pass on increased costs to consumers due to eroded domestic demand and competition from low-cost imports. As was also the case in Africa, firms that

could not compete were being weeded out and remaining firms were occupying niche markets where they could avoid the full impact of import competition. Similarly, the weakest firms in Poland were manufacturing low-cost, undifferentiated products, particularly ordinary clothing and textiles and simple metal and plastic products. Poles set up businesses quickly in response to liberalization but, at the time of the survey, interviewers perceived a growing wariness of making long term investments in the uncertain Polish economy. As seen in the African surveys, many entrepreneurs were moving out of manufacturing and into trading activities where risks were lower and returns faster and higher. As in Africa, entrepreneurs at the helm of the strongest firms invariably were engineers with strong technical skills.

There were also important differences. On the one hand, the elusive "supply response" sought in Africa for the past ten years took place in Poland overnight--perhaps the difference between latent and pent-up entrepreneurship. The question in mid-1991 was less one of inducing private investment than of exploiting this burst of entrepreneurial energy. On the other hand, the extent of personal and professional change required of Polish producers appeared far greater than that required of private entrepreneurs operating in other adjusting countries. Entrepreneurs in the African context were confronted with falling domestic demand and increased import competition, but the essential business rules were unchanged by adjustment programs. In Poland, entrepreneurs were being asked to function according to an entirely new system of principles. Their confusion was obvious as they stumbled over questions about the impact of price on demand for their products, their strategies for undercutting the competition, and their plans to rationalize their labor force. Basic assumptions about market functioning that underlie business planning and operations in the West often were absent. The historical isolation of Poles from the West meant that producers had had little exposure to Western products and technologies, and time will be required to catch up. In short, the transformation underway in Poland was far more comprehensive than seen in most countries that are adjusting.

It is interesting to compare the response of Polish entrepreneurs to competition with that of Latin American entrepreneurs who were described in Chapter I. Like the Latin Americans, many Polish entrepreneurs were struggling to improve product quality. But unlike the Latin Americans, the Poles had few resources to enable them to do so. Few had received the many potential benefits of interchanges with foreign partners, producers or buyers. Also unlike the Latin Americans, the Poles who were interviewed had not shed redundant labor, and had almost no capital to invest in new machinery and plant modification. The only obvious similarity with Latin American firms was that some firms appeared to be moving toward greater product specialization, cutting back on the numbers of products and focussing on those with the greatest potential. In essence, most Polish firms had not yet found means of competing with imports as shown by the fact that the strongest firms in the sample essentially had located niches where they could avoid import competition.

The Transition: On or Off Track?

Well over half of sample firms were encountering serious difficulties. The degree of difficulty ranged from firms that were moving furniture out as interviewers were walking in, to those whose unsold products were filling available factory space and whose workers were sitting smoking cigarettes, to those who were watching anxiously as their profits shrank with falling orders. Was the trouble at these firms part of a necessary and healthy adjustment process or was it a harbinger of stagnation in the private industrial sector?

The Arguments

Two compelling and apparently conflicting explanations need examination. The first argument says that the transformation is on-track, and the second says that it has been de-railed. In the *first* point of view, the downturn observed is interpreted as temporary adjustment shock--a necessary reorientation of the private sector to post-reform conditions and a positive sign that the reform program was in fact achieving its objectives of restructuring the economy. Central to this point of view is the fact that large numbers of private firms were set up in 1989 and the first months of 1990, before the reform program was put in place and its effects were felt. A *second*, conflicting interpretation is that the downturn observed in large numbers of sample firms was an indication that the 1989-1990 boom for private producers was over, and that the private industrial sector was headed down--unable to surmount the effects of recession, the failure to privatize the state sector, and the flood of competing imports. The paragraphs that follow lay out the evidence on both sides of this critical debate.

"On-Track" Arguments. Arguments in favor of the view that the difficulties observed in sample firms were growing pains en route to a more competitive private industrial sector are the following:

(i) Though fewer in number than those entering trading activities, large numbers of new industrial entrants offer convincing evidence that the basic conditions needed for entry were present and that opportunities for profits existed;

(ii) A third of firms reported that their primary problem was inadequate demand for their products. Entrepreneurs in the declining sectors--knitting, clothing, and simple metal and plastic consumer goods--indicated unequivocally that the loss of markets to competing imports superseded the loss of sales due to reductions in consumer purchasing power. Losing out to low-cost consumer goods from East and Southeast Asia clearly was painful and demoralizing to the individuals involved, but appeared as necessary losses in the process of adjustment;

(iii) Most entrepreneurs reported that operating conditions worsened in late 1990 and early 1991. One argument is that the depreciated zloty and the surprisingly positive performance of the state sector during most of 1990 protected the fledgling private sector, protection that had eroded by May 1991 with appreciation of the zloty and collapse of the state sector. The downturn in the private sector can thus be seen as an adjustment to the tougher conditions pertaining in 1991;

(iv) One indication that a positive adjustment process was underway was that the early opportunists and "gap-fillers" were giving way to those with strong technical skills. The most successful sample firms were headed by Poland's highly-trained engineers who, in the view of researchers, form the basis of Poland's potential comparative advantage in world markets. Movement to the foreground by these individuals is a positive sign;

(v) The fact that since start-up, fully 50 percent of those interviewed had changed their primary product in response to changing conditions and 50 percent reported that they had altered their method of production indicates that a critical seasoning process was underway. Developing the ability to respond flexibly to new opportunities is the hallmark of successful small businesses everywhere. To the extent that Polish entrepreneurs were forced to learn how to interpret changes in their environment accurately and to respond quickly, an essential learning process took place and the narrow skill base of Polish private business was widened;

(vi) The timing and the methodology of this survey may have skewed findings downward. Rising private industrial sales in the second half of 1991 might indicate that May 1991 was an atypically difficult period for private producers. The zloty had appreciated by May 1991 and, in fact, it was devaluated by about 15 percent on the final day of this survey. The fact that the sample interviewed for this survey was national in scope meant that poorer-performing rural firms, comprising 50 percent of the sample, pulled performance indicators down for the sample as a whole.

"Off-track Arguments". Arguments that favor the view that sample firms were failing because the transition process has been de-railed are as follows.

(i) Close examination of aggregate data shows that growth in private sector trading activities far outstripped growth in private sector industry 1990 and 1991. About a third of sample entrepreneurs had either switched into trading activities because they were more profitable or had added a commercial division to their company to subsidize their manufacturing activities. While it is common to see individuals starting with trading activities to generate capital needed to invest in production, Polish producers were moving into trade because they could not make profits in manufacturing. The danger of this trend is that the investment needed to upgrade manufacturing could be abandoned, and Poland could become a nation of traders.

(ii) The failure rate among sample firms was high. Fifty percent of letters returned by potential survey participants had postal stamps saying they were out of business or no longer located at the address listed in official records; over 10 percent of eligible companies stopped production in the two months between contacting them about the survey and the arrival of survey teams; and survey teams judged that 40 percent of sample firms were headed toward bankruptcy. Arguments that high closure rates are normal in industrial economies fail to assess the political costs of high failure rates among the first generation of post-reform, private producers, the small size of the Polish private manufacturing sector, and the key role it must play in the transformation.

(iii) Many firms were failing because they could not compete with imports, but the size of the total pie to be sliced had shrunk due to recession which was exerting a discernible, negative influence on almost all sample firms. Even the strongest firms reported that orders had fallen for both intermediate and final goods due to depressed demand.

(iv) It is hard to conceive of short-term strategies that would raise the very low technological base observed in most sample firms. Production know-how must be upgraded and equipment must be replaced if entrepreneurs are to compete. Raising capabilities requires substantial time and investment, and modernizing equipment takes capital investment currently not available.

(v) Only 21 entrepreneurs of the 106 who were interviewed were exporting, and most were exporting a small percentage of their production. Breaking into world markets was proving difficult for entrepreneurs who, in most cases, had no contacts in Western markets and lacked the skills or the equipment needed to compete in export markets. Without an effective campaign to stimulate export production among private producers, this situation appeared unlikely to change in the near future.

(vi) The state sector contributed little to the formation of the private sector beyond excess workers and used equipment. To the contrary, the state sector continued to control the bulk of Poland's industrial assets. As a result, most sample firms necessarily were tightly linked to state enterprises which were increasingly unreliable as suppliers, verging on reprehensible as customers, and reportedly in possession of unfair advantages as competitors. To the extent that privatization is prolonged and state

firms are allowed to descend into chaos, the majority of private producers who depend on the state sector will be negatively affected.

In reality, both of these conflicting interpretations describe forces at work in the Polish economy in May 1991. Competition was forcing private firms to adjust, and this survey verified that weak firms were closing and those who could compete or avoid competition were on the rise. At the same time, macroeconomic recession, pervasive market imperfections, and distortions generated by the state enterprise sector were negatively affecting even the strongest private producers. Which forces will prevail is not yet clear, and the outcome is far from pre-ordained. As described in Chapter VI, there are a number of actions that could positively impact the development of private sector development in Poland. Active promotion and support could make the difference.

ADDENDUM

Additional information and insights are available as this report goes for publication. The Polish recession lifted over the course of 1992, and the growth of industrial output became positive. Despite some scrambling of aggregate statistics, it is clear that the private sector share in GNP and employment is large and growing. With hindsight, it is clear that this survey was conducted in a particularly difficult period for private producers who were faced with the triple challenges of adjusting to new price signals in the domestic economy, coping with a severe recession, and confronting the reality of competition in world markets. Few had profit margins sufficient to blunt the impact of these three enormous forces, and many were in deep trouble. This report documents the precise nature of that trouble. Positive trends in private sector growth in 1992 are heartening because they indicate that substantial numbers of private producers have come through the valley of 1991 to a higher level of success in 1992 and 1993. Especially encouraging is the strong growth of private sector exports, an indication that Polish producers are finding avenues by which they can compete in world markets.

ANNEX I: TABLES

Annex Table 1.1: Economic Units in the Private Sector
(Number of Units)

	1989	1990	1991	90/89 (%)	91/90 (%)
1. Private Firms (Incorporated) <u>a/</u>	11,693	29,650	45,077	153.6	52.0
Of which:					
Industry	2,769	6,416	8,676	131.7	35.2
Construction	2,640	5,171	8,749	95.9	69.2
Trade	1,759	8,326	15,942	373.3	91.5
Transport	86	319	-	270.9	-
Communication	18	50	-	177.8	-
Other	4,421	9,368	11,710	111.9	25.0
2. Joint Ventures	429	1,645	4,796	283.4	191.5
Of which:					
Industry	240	853	2,099	255.4	146.1
Construction	12	71	319	491.7	349.3
Trade	32	198	1,158	518.8	484.8
Transport	14	67	207	378.6	209.0
Communication	-	5	-	-	-
Other	131	451	1,013	244.3	124.5
3. Sole Proprietorships (Unincorporated)	813,500	1,135,500	1,420,000	39.6	25.1
Of which:					
Industry	288,200	334,600	348,900	16.1	4.3
Construction	-	165,500	171,700	-	3.7
Transport	-	61,400	62,081	-	1.1
Trade	71,800	346,300	550,300	382.3	58.9
Other	-	105,601	159,585	-	51.1
Services	-	122,099	127,434	-	4.4
4. Cooperatives	15,024	16,650	17,374	10.8	4.3
Of which:					
Industry	2,233	2,411	2,535	8.0	5.1
Agriculture	4,200	4,244	4,141	1.0	-2.4
Trade	3,150	3,650	3,766	15.9	3.2
Other	5,441	6,345	6,932	16.6	9.3
5. Small Foreign Enterprises	841	862	787	2.5	-8.7
Of which:					
Industry	731	739	656	1.1	-11.2
Other	110	123	131	11.8	6.5
6. Other Establishments					
Of which:					
Social Organ.	1,629	1,722	1,294	0.6	-24.9
Foundations	85	175	158	105.9	-9.7
Religious	-	59	198	-	-

Source: EC2CO from the Polish Central Statistics Office (GUS).

a/ Includes limited liability and joint stock companies.

Annex Table 1.2: Distribution of Total Employment in the Private Sector in 1990 a/
(1000s of persons)

	Total	Distrib.	Sole Proprietor- ship <u>b/</u>	Incorp. Firms <u>c/</u>	Joint Ventures	Foreign Enterp.	Other Private
Total	2,335,931	100.0	1,923,456	215,672	85,249	81,924	29,360
Distribution	100.0		82.3	9.2	3.7	3.5	1.3
Average Employment of which:			1.7	7.3	51.8	95.0	
Material Production	2,172,445	93.0	1,813,605	199,780	76,262	81,833	965
Industry	902,205	38.6	721,336	51,903	58,653	69,545	768
Construction	425,111	18.2	350,859	61,210	2,856	10,153	33
Agriculture	6,511	0.3	2,515	1,420	2,576		0
Forestry	195	0.0	0	107	74		14
Transport	74,186	3.2	70,992	2,134	845	70	145
Communications	459	0.0	0	407	52		0
Trade	573,837	24.6	535,261	35,667	2,873	31	5
Other material production	118,810	3.0	14,628	46,269	8,208	2,026	0
Community Services	71,131	5.1	118,014	663	125	8	0
Non-Material Production	163,486	7.0	109,851	15,892	8,987	91	28,665

Source: EC2CO from the Polish Central Statistics Office (GUS).

a/ Excludes private agriculture. Excludes cooperatives and other establishments now classified as part of the private sector. These enterprises were semi-private and subject to government direction. Now most are privatized and operating relatively autonomously.

b/ Sole Proprietorships refer to the large self-employed sector.

c/ Incorporated Firms are limited liability and joint stock companies.

Annex Table 1.3: Total Employment Public and Private Sector 1990-1991
(1000s of persons)

	Total employment <u>a/</u>			Public sector			Private sector <u>b/</u>		
	1990	3Q 1991	% change	1990	3Q 1991	% change	1990	3Q 1991	% change
Total	12,405.5	1,2061.4	-2.8	8,243.4	7,630.3	-7.4	4,162.1	4,431.1	6.5
of which:									
Material production	9,312.7	8,957.9	-3.8	5,682.6	5,003.3	-12.0	3,630.1	3,954.6	8.9
Industry	4,404.0	4,093.6	-7.0	3,030.0	2,718.0	-10.3	1,374.0	1,375.6	0.1
Construction	1,091.1	1,112.1	1.9	631.3	539.2	-14.6	459.8	572.9	24.6
Agriculture	775.5	662.4	-14.5	510.9	432.1	-15.4	264.6	230.3	-13.0
Forestry	114.0	104.1	-8.7	113.8	102.3	-10.1	0.2	1.8	-
Transport	725.0	649.0	-10.5	614.8	529.9	-13.8	110.2	119.1	8.1
Communications	170.7	171.6	0.5	170.2	171.5	0.8	0.5	0.1	-
Trade	1,458.7	1,628.5	11.5	259.9	186.1	-28.4	1,198.8	1,442.4	20.3
Community services	424.9	420.7	-1.0	297.4	273.4	-8.1	127.5	147.3	15.5
Other material									
Production	148.8	115.9	-22.1	54.3	50.8	-6.4	94.5	65.1	-31.1
Non-material production	3,092.8	3,103.5	0.3	2,560.8	2,627.0	2.6	532.0	476.5	-10.4

Source: EC2CO from the Polish Central Statistics Office (GUS).

a/ Excludes private agriculture. The total number of individual farmers for 1990 was 4.1 m.

b/ Excludes foundations. Figures based on new classification of the private sector, which includes cooperatives and other establishments.

Annex Table 1.4: Sectoral Distribution of Sole Proprietorships

		Number of firms (000)	Employment (000) <u>a/</u>	Average employment (000)
Total	1989	813.5	1,475.5	1.8
	1990	1,135.5	1,915.5	1.7
	1991	1,420.0	2,591.1	1.8
of which:				
Industry	1989	288.2 (35.4%)	1,086.1 (73.6%)	3.8
	1990	334.6 (29.5%)	716.1 (37.4%)	2.1
	1991	348.9 (24.6%)	835.2 (32.2%)	2.4
Construction	1989	-	-	-
	1990	165.5 (14.6%)	349.2 (18.2%)	2.1
	1991	171.7 (12.0%)	399.0 (15.4%)	2.3
Trade	1989	71.8 (8.8%)	-	-
	1990	346.3 (30.5%)	485.4 (25.3%)	1.4
	1991	550.3 (38.8%)	871.5 (33.6%)	1.6
Other	1989	-	-	-
	1990	289.1 (25.5%)	364.8 (19.0%)	1.3
	1991	349.1 (24.6%)	485.4 (18.7%)	1.4

Source: EC2CO from the Polish Central Statistics Office (GUS).

a/ The percentage of establishments employing 5 or fewer workers was 96.8 percent in 1991.

Annex Table 1.5: Foreign Trade
Public and Private Sector Shares

	1 Q 90	2 Q 90	3 Q 90	4 Q 90	1990	1 Q 91	2 Q 91	3 Q 91	4 Q 91	1991
Total export (bln zlotys) <u>a/</u>	25,978	32,094	10,209	67,774		27,076	36,421	36,056	53,486	
Public sector share	95.3	95.3	98.4	94.5	95.1	80.2	84.0	87.4	68.9	80.2
Private sector share <u>b/</u>	4.7	4.7	1.6	5.5	4.9	12.4	16.0	12.6	31.1	19.8
Total imports (bln zlotys) <u>a/</u>	17,098	16,868	6,299	50,248		30,250	34,294	34,249	52,124	
Public sector share	83.6	88.9	93.1	84.3	85.6	63.6	52.6	54.8	48.5	53.9
Private sector share <u>b/</u>	16.4	11.1	6.9	15.7	14.4	36.4	47.4	45.2	51.5	46.1

Source: EM2CO.

a/ Totals are in current zloty.

b/ Private sector shares based on new classification of the private sector which includes cooperatives and other establishments.

ANNEX II: QUESTIONNAIRE

April 12, 1991
The World Bank
Industry Development Division

Interviewer: _____
Date of Interview: _____
1. Firm ID #: _____
2. City/Town: _____

INTERVIEWING GUIDE FOR POLISH PRIVATE FIRMS

I. BASIC INFORMATION

- /3. Name of Person Interviewed: _____
4. Position of Person Interviewed: 0. Owner 1. Manager
8. Other (Specify) _____
5. Gender: 1. Male 2. Female
6. Age: _____ years
- /7. Name of firm: _____
- /8. Address or location: (Be specific) _____
9. Month/year of registration: _____
10. Month/year of start-up: _____
11. Who owns this company?

- | | | | |
|----|----------------------------------|-------|---------|
| 0. | The Government | _____ | percent |
| 1. | The owner being interviewed | _____ | percent |
| 2. | Other private partners | _____ | percent |
| 3. | Private investors outside Poland | _____ | percent |
| 4. | Workers | _____ | percent |
| 8. | Other (Specify) _____ | _____ | percent |

Total 100 percent

(note: if 0 or 4 are > 50 percent, the firm is ineligible)

12. What is the ownership history of this company?
0. Fully independent since start-up
1. Fully independent now but previously owned by or legally connected to the State
2. Owned by or legally connected to a larger private company
3. Owned by or legally connected to a state-owned enterprise
4. Associated with a cooperative
8. Other (Specify) _____
9. N/A
13. What is the legal form of this company?
0. Limited liability company
1. Joint stock company
8. Other (Specify) _____
9. N/A

14. Principal product/activity/service: _____
15. Polish code _____ 16. ISIC Code _____
17. Secondary product/activity: _____
18. Polish code _____ 19. ISIC Code: _____

II. THE ENTREPRENEUR

A. Background

20. What was/is your father's occupation? _____
21. Who is/was your father's employer?
- 0. The government
 - 1. A state-owned enterprise
 - 2. A private company
 - 3. He is/was self-employed
 - 8. Other (specify) _____
 - 9. N/A
22. What was/is your mother's occupation? _____
23. Who is/was your mother's employer?
- 0. The government
 - 1. A state-owned enterprise
 - 2. A private company
 - 3. He is/was self-employed
 - 8. Other (specify) _____
 - 9. N/A
24. Has anyone in your family worked in the private sector?
- 0. No
 - 1. Yes
- Who, and what did they do? _____
25. What is the highest level of school you completed?
- 0. None
 - 1. Primary
 - 2. Secondary
 - 3. Commercial
 - 4. Technical
 - 5. Apprenticeship
 - 6. College or university
 - 7. Post-graduate
 - 8. Other (Specify) _____
 - 9. N/A
26. Have you received any training abroad?
- 0. No
 - 1. Yes
- What kind, when, and where? _____

27. What do you think is the major source of the primary skills/knowledge you use to operate this business?
0. University/technical education
 1. Experience in previous jobs
 2. Manufacturer of equipment
 3. Purchaser of final product
 4. Trade/technical journals
 5. Learning on your own
 6. Training programs outside of the education system
 8. Other (Specify) _____
 9. N/A
28. What kind of short term training course would be most useful to you today? (circle only the most important one)
0. None
 1. Accounting or bookkeeping skills
 2. Marketing
 3. Skills to obtain financial services from a bank
 4. More familiarity with different technologies
 5. Legal
 6. Management (What kind of management?) _____
 7. Import/export
 8. Other (specify) _____
 9. N/A
29. Who did you work for before you started this business?
0. Worked for a government institution. Which one? _____
 1. Worked for a state-owned enterprise. Which one? _____
 2. Worked for another private company. Which one? _____
 3. Worked in another business I owned. What kind? _____
 4. How many businesses have you owned? _____
 5. Worked for a foreign company in Poland. Which one? _____
 6. Worked for a foreign company outside of Poland. Which one and where? _____
 8. Other (Specify) _____
 9. N/A
30. How many people were employed where you last worked?
- | | |
|-------------------|----------------|
| 0. 25 or fewer | 1. 25 to 50 |
| 2. 50 to 100 | 3. 100 to 200 |
| 4. 200 to 500 | 5. 500 to 1000 |
| 6. More than 1000 | |
31. What was your occupation in your last job? _____
32. Are you producing the same product in your current business that was produced in your last several jobs?
0. The same
 1. Very similar
 2. Related but different
 3. Completely different
 9. N/A

B. Start-up

- /33. Origin of firm. Why it was started, when, by whom, with what products? Major differences now vs. when it was started. (let the owner tell his/her own story here.)
-
-
-

34. Who started this business?

- 0. Started business alone
- 1. Started business with my spouse
- 2. Started with another family member
- 3. Started with a non-family member
- 4. Started with a combination of the above
- 5. Bought the business from a family member
- 6. Bought the business from a non-family member
- 7. Inherited the business from a family member
- 8. Other (Specify) _____
- 9. N/A

35. What is the primary reason why you started up this business? (pulled to opportunity or pushed to it by problems elsewhere)

- 0. Lost job, was laid off, or expected to be laid off
- 1. Frustrated with work in state-owned enterprises
- 2. Few job opportunities elsewhere, private sector was only option
- 3. Previous salary was too low, thought could make more in private sector
- 4. Wanted to put training to use
- 5. Saw a profitable opportunity and took it
- 6. Laws on private enterprise were changed
- 7. Parents/relatives were in private business
- 8. Other (Specify) _____
- 9. N/A

36. What were your primary personal goals in starting up this business? (interviewers, choose one that best matches the person's answer. Let them tell you in their words)

- 0. Achievement--wanted to use the skills you have
- 2. Status/prestige--wanted to move up in the world
- 3. Independence--wanted to work on your own
- 4. Power--wanted to be in charge
- 5. Money--wanted to earn more money than was before
- 6. Economic necessity--had few other choices
- 7. Career/security--this route offered the best future
- 8. Other (Specify) _____
- 9. N/A

37. Which of the following descriptions best fits you? (Interviewers, read them the list. They can choose 3)

- 0. A high achiever, easily bored with routine, restless
- 1. A practical person with practical skills
- 2. Highly disciplined, committed to hard work
- 3. A risk-taker, willing to live with uncertainty
- 4. Like to feel in control of what is going on
- 5. Self-confident, fairly sure of success
- 6. Independent, a loner, somewhat separate from others
- 7. Grew up in a difficult, troubled family
- 8. Other (Specify) _____
- 9. N/A

38. What are the three biggest problems affecting your business today?
[Coder] Explanation (Write down the responses)
39. []#1 _____
40. []#2 _____
41. []#3 _____

(Interviewer: After respondent gives own answers, follow up if necessary to discover the root problem; write in their answers in the blanks above. Later, find the closest answer in the list at the back of the questionnaire and enter its number beside of 30, 31, 32. Most important problem comes first, etc.)

42. If you had the opportunity to start over, would you choose this business again?
0. Would not start this business again if I could choose again
1. Would start another business in a different industry. Which industry? _____
2. Would start again in the same industry _____
8. Other (Specify) _____
9. N/A
43. Are you a member of a trade association or other business association?
0. No 1. Yes 9. N/A
If so, name of association: _____
- /44. What benefits do you receive as a member? (For example: information on markets, technology, laws and regulations, political representation, education, insurance)
- _____

III. FIRM PROFILE

A. LABOR AND LABOR COSTS (enter 0 for none; leave blank if no answer)

1. Profile of Labor Force
45. _____ Owners and other family members who work full-time
46. _____ Full-time wage workers
47. _____ Full-time Apprentices
48. _____ Total, all full-time workers including owners and family members
49. _____ Part-time owners and family members
50. _____ Part-time wage workers and contract employees
51. _____ Total, all part-time workers

Gender Profile

52. _____ Male full-time workers
53. _____ Female full time workers

Skills Profile

54. _____ Workers directly operating production machinery

55. _____ Workers providing ancillary support e.g., moving materials within the plant, packaging the product.
56. _____ Administrative workers, e.g., bookkeepers, sales persons, etc.
57. _____ Technical/engineering support workers
58. _____ Other (Specify) _____
59. Are your current workers as highly skilled as you need/want them to be?
0. No Comment: _____
1. Yes Comment: _____
8. Other (Specify) _____
9. N/A
60. Do you have problems recruiting workers who have the specific skills and are as highly trained as you need for the growth of your company?
0. No
1. Yes What problems? _____
8. Other (Specify) _____
9. N/A
61. Do you provide any training to your workers?
0. No. Why not? _____
1. Yes. Please describe. (What kind, to whom, how often for what duration?) _____
8. Other (Specify) _____
9. N/A
62. Where have most of your workers learned the skills they use in your company?
0. In the school system
1. In training courses outside the formal education system
2. From on-the-job training in previous jobs
3. From on-the-job training in your company
8. Other (Specify) _____
9. N/A
- /63. What do you think would be the best approach to training and upgrading the skills of workers in Poland?
- _____
64. Are your workers represented by a union or a worker's council?
0. No Why not? _____
1. Yes What kind? _____
8. Other (Specify) _____
9. N/A
65. Are your workers protected against losing their jobs, i.e., are you prohibited from firing a worker if you want to?
0. No, workers have no protection against losing their jobs
1. Yes, workers are protected by job security laws in Poland
If so, what are the laws? _____
2. Yes, workers are protected by other measures. What measures? _____
8. Other (Specify) _____
9. N/A

2. Labor Costs

What is the total cost of labor of your business? (including wages, bonuses, allowances, taxes and social security)

66. _____ zloty per week/month (specify time unit)
67. _____ the total wage bill in US\$ per month (figure later)
68. Of the total wage bill, how much do you pay directly to workers? (including salaries, bonuses and allowance)
_____ zloty per week/ month (specify time period)
69. Of the total wage bill, what percent do you pay for taxes on wages?
_____ percent
70. Of the total wage bill, what percent do you pay for benefits?
_____ percent
71. How do you decide wages for your workers?
0. You decide yourself
 1. The State sets the wages that you must pay
 2. You have to bargain with workers unions or councils
 3. The market--demand and supply for workers--sets the wage
 4. The amount that you pay is determined by the amount the state-owned enterprises pay
 8. Other (Specify) _____
 9. N/A
72. What kinds of compensation/benefits do all workers receive?
- | | |
|--------------------------------|--|
| 0. None | 6. Maternity |
| 1. Retirement/pension benefits | 7. Vacation with pay, # of days? _____ |
| 2. Health insurance | 8. Other (Specify) _____ |
| 3. Housing allowance/allotment | 9. N/A |
| 5. Transportation allowance | |

B. PHYSICAL CAPITAL

1. Land and Buildings

73. How many square meters of floor space does your firm occupy?

74. How did you obtain the factory space (building) you now occupy?
0. Bought it. What year? _____ From whom? _____
 2. Inherited it.
 3. It belongs to a family member
 4. Lease it on a multi-year basis. From whom? _____
 5. Lease it on annual basis. From whom? _____
 6. Lease it on a monthly basis. From whom? _____
 8. Other (Specify) _____

75. How did you obtain the land your business sits on?

- 0. Bought it. What year? _____ From whom? _____
- 2. Inherited it.
- 3. It belongs to a family member
- 4. Lease it on annual basis. From whom? _____
- 5. Lease it on a multi-year basis. From whom? _____
- 6. Lease it on a monthly basis. From whom? _____
- 8. Other (Specify) _____

76. Are the land and building space you now have sufficient for your needs?

- 0. Too small
- 1. Just right
- 2. Too big
- 3. Poorly located
- 8. Other (Specify) _____
- 9. N/A

77. Is it possible to rent or purchase a larger building or more land for your business needs?

- 0. No. Why not? _____
- 1. Yes
- 8. Other (Specify) _____
- 9. N/A

2. Equipment

/78. What are the main production machines in your business? Name, manufacturer, date of manufacturer, rated capacity (of throughput or output per hour).

<u>Machine</u>	<u>Manufacturer</u>	<u>Year Made</u>	<u>Capacity (Machine Manufacture)</u>	<u>Replacement Cost Today (New Machine)</u>	<u>In which Hard Currency (if not local)</u>
1. _____	_____	_____	_____	_____	_____
2. _____	_____	_____	_____	_____	_____
3. _____	_____	_____	_____	_____	_____
4. _____	_____	_____	_____	_____	_____
5. _____	_____	_____	_____	_____	_____

79. What is the average age of your equipment?

- 0. Less than one year old
- 1. 1 - 3 years old
- 2. 3 - 5 years old
- 3. 5 - 10 years old
- 4. 10 - 20 years old
- 5. More than 20 years old
- 8. Other (Specify) _____
- 9. N/A

80. Have you purchased equipment (new or used) since start-up?
(Other than initial investment)

- 0. No
- 1. Yes
- 9. N/A

81. Who are the main suppliers of equipment for your enterprise?
- 0. Domestic producers
 - 1. Producers in ruble areas
 - 2. Producers in non-ruble areas
 - 8. Other (Specify) _____
 - 9. N/A
82. Are there problems in procuring imported equipment?
- 0. No
 - 1. Yes. If so, what are they? _____
 - 8. Other (Specify) _____
 - 9. N/A
83. Is domestic equipment available that meets your needs?
- 0. No
 - 1. Yes
 - 8. Other (Specify) _____
 - 9. N/A
84. What problems, if any, are there with domestically-made equipment?
- 0. It's of poor quality
 - 1. It's more expensive than the imported ones
 - 2. The specifications are wrong for what you need
 - 3. The equipment you need is not manufactured in Poland
 - 8. Other (Specify) _____
 - 9. N/A
85. Are the spare parts that you need easy to get?
0. Very difficult 1. Difficult 2. Easy 3. Very easy
9. N/A
- If difficult, why? _____
86. From whom do you buy spare parts?
- 0. Import directly from the manufacturer who makes the machine
 - 1. Buy them directly from producers of domestic machines
 - 2. Buy them from domestic retailers of spare parts
 - 3. Buy them second-hand or take them from discarded machines
 - 4. Make them myself
 - 8. Other (Specify) _____
 - 9. N/A
87. How do you account for depreciation of capital equipment?
- 0. Written off as current expense
 - 1. Amortized at an annual rate of _____
 - 8. Other (Specify) _____
 - 9. N/A

C. FINANCE AND THE COST OF CAPITAL

Please check the following items to describe how you obtained and maintained the funding and financing required to initiate and maintain the ownership of your business. Check as many boxes as are appropriate.

Source of funding	Time Period			
	88. Initially or during the first six months of operations	89. Between the first six months and first year operations	90. Between the first and third years of operations	91. After three years in business.
0. Own savings				
1. Family borrowing				
2. Borrowing from friends				
3. Government program				
4. Commercial or investment bank loan				
5. Profits from the business				
6. Supplier credits				
8. Other (Please specify)				
9. N/A				

/92. What is your biggest problem with financing your business?

93. Since start-up, have you tried to get a loan from a bank or promotion agency?

0. No
1. Yes, but not successful. Why not? _____
2. Yes, short term loan received
Terms of loan: interest rate _____ term _____
name of bank _____
3. Yes, long term loan received.
Terms of loan: interest rate _____ term _____
8. Other (Specify) _____
9. N/A

94. If a long-term loan were available from a bank or government agency at current interest rates of _____ percent, would you apply for one?

0. No Why not? _____
 1. Yes _____
 8. Other (Specify) _____
 9. N/A

95. Assuming you are willing to pay current interest rates, how difficult is it currently to get a long term loan from a bank?

0. Very easy
 1. Fairly easy
 2. Fairly difficult
 3. Very difficult
 8. Other (Specify) _____
 9. N/A

96. The main difficulty in getting a loan is:

0. Paperwork
 1. Not enough money to be loaned
 2. Size of loans available is not large enough
 3. Bankers prefer to make larger loans
 4. Lenders prefer favored clients, those who have large deposits or are long-term clients
 5. Lenders do not like my kind of business
 6. Lenders require more collateral than I have
 Details on collateral: _____
 8. Other (Specify): _____
 9. N/A

97. Do you have problems in getting foreign exchange?

0. No 1. Yes 9. N/A

If so, what problems? _____

D. RAW MATERIALS, INTERMEDIATE INPUTS AND ENERGY CONSUMPTION

/98. What are the principle raw materials and intermediate inputs used in your product? (list in physical units per year, month or week)
 (Imported means imported directly or by a retailer)

<u>Raw Materials and Inputs</u>	<u>Quantity # of units</u>	<u>Time Period (week/month/year)</u>	<u>Price per Unit</u>	<u>Supplier (private, state)</u>	<u>Source (Domestic, imported)</u>
-------------------------------------	--------------------------------	--	-----------------------	--	--

1.
2.
3.
4.

99. What proportion of your raw materials or intermediate inputs are imported, either by you or an importer? _____ percent

100. Do you have problems obtaining the imported raw materials and intermediate inputs you need?

0. No 1. Yes 9. N/A
 If so, what problems? _____

101. Since start-up, is the proportion of your raw materials and inputs that is imported:
0. about the same 1. greater 2. less 9. N/A
If it has changed, why? _____
102. Do you have problems obtaining local raw materials and intermediate inputs?
0. No 1. Yes 9. N/A
If yes, what problems? _____
103. What is the amount of energy consumed by your factory? (electricity, coal, gas, oil in physical units) (Specify time units: per year, month or week)

What are the main problems with public services (transportation roads, railway, water and sewage, electricity, communications-phone, telegraph, etc.) your business faces?

- | | |
|--|---|
| 104. Service: _____ | 105. Service: _____ |
| 0. none | 0. none |
| 1. occasional interruption | 1. occasional interruption |
| 2. frequent, longer or serious interruptions | 2. frequent, longer or serious interruption |
| 3. too expensive | 3. too expensive |
| 4. delay in obtaining | 4. delay in obtaining |
| 8. other (Specify) _____ | 8. other (Specify) _____ |
| 9. N/A | 9. N/A |

E. PRODUCTION AND CAPACITY UTILIZATION

1. Production

- /106. What is the actual, current output of your plant? (Major products, in physical units for each product, per day or shift). [Specify time unit]

107. How many hours per week does your company operate? _____ hours
108. How many hours per week could your company operate if it were at full capacity?
_____ hours
109. For the most important product, what is the number of units produced per month? _____ per month.
110. The current selling price per unit is: _____ (specify the unit)
111. How has the retail price of this product changed in the past 12 months?
0. It has not changed
1. It has increased. By what percent? _____ %
2. It has decreased. By what percent? _____ %
If it has changed, why has it changed? _____
8. Other (Specify) _____
9. N/A
112. For your second most important product, what is the number of units produced per month? _____ per month

113. The selling price per unit is: _____ (specify the unit)
114. How has the retail price of this product changed in the past 12 months?
- 0. It has not changed
 - 1. It has increased. By what percent? _____ %
 - 2. It has decreased. By what percent? _____ %
If it has changed, why has it changed? _____
 - 8. Other (Specify) _____
 - 9. N/A
115. At present, is the firm selling everything that it produces?
- 0. No, [demand constraint, accumulating stock involuntarily]
 - 1. Yes, and could sell more [supply constraint]
 - 2. Yes, but couldn't sell much more [demand constraint]
 - 8. Other (Specify): _____
 - 9. N/A
116. If you cannot sell all that you can make, have you lowered your prices?
- 0. No
 - 1. Yes
 - 9. N/A
- If not, why not? _____
- If so, what was the result? _____
117. If you could sell more, have you raised your prices?
- 0. No
 - 1. Yes
 - 9. N/A
- If not, why not? _____
- If so, what was the result? _____
- /118. If you could sell more than you are producing, what is the main reason you are not producing more?
- _____

2 Changes in Production

119. In the past 12 months, how has your production volume changed? For what single most important reason? (*circle only one*)
- 0. No significant change
 - 1. Increased, because foreign exchange (inputs) more available
 - 2. Increased, because local raw materials are more available
 - 3. Increased, because demand has increased
 - 4. Increased, because of entering new markets
 - 5. Increased, because imported goods now are more expensive
 - 6. Increased, because production in state-owned enterprises has declined
 - 7. Increased, other reason (specify) _____
 - 8. Decreased, because demand is weak
 - 9. Decreased, because of competition from imports
 - 10. Decreased, because of increased domestic competition
 - 11. Decreased, because of high costs of imported inputs (lack of working capital)
 - 12. Decreased, because of high costs of local inputs (lack of working capital)
 - 13. Decreased, because of labor problems
 - 14. Decreased, other reason (specify) _____
 - 99. N/A

120. Have you changed your mix of products since start-up?

0. No 1. Yes 9. N/A

New products (Describe them, why did you choose this product? Source of design?)

Producing more of _____
Producing less of _____
Stopped production of _____

121. Have you changed, in any way, your methods of production since start-up?

0. No
1. Yes How? _____
8. Other (Specify) _____
9. N/A

122. In comparison with other companies that make the same product, what is unique or special about your method of production on your product?

0. Nothing. You produce the same product using the same techniques as other companies.
1. My production technique is different.
How? _____
2. My product is different.
How? _____
8. Other (Specify) _____
9. N/A

123. What are your plans for the business in the future (i.e., actually expect to do)? (*Circle only one*)

0. Maintain production at the same level and composition
1. Maintain production level but switch to a new product
2. Substantially expand production and capacity (increase size of the firm)
3. Expand production without substantially changing capacity (keep firm about same size)
4. Reduce production
8. Other (Specify) _____
9. N/A

124. If your plan is to stay at the same level or reduce production, why? Main reason (*circle only one*)

1. It meets my needs at the present level
2. I couldn't sell more if I produced more
3. Demand is seasonal
4. No funds to finance an expansion
5. Afraid to risk a new investment
8. Other (Specify) _____
9. N/A

F. **SALES AND MARKETING**

1. **Profits**

125. Approximately what is the total sales revenue of your factory in an average month? _____ zloty

126. Is the business currently making profits?
(i.e., is owner getting any income out of it?)
0. No 1. Yes 9. N/A
127. Is the business more or less profitable now than in the first few months after start-up?
0. About the same 1. More profitable
2. Less profitable 8. O t h e r (S p e c i f y)
9. N/A
- Why? _____
128. Are you satisfied with the profits of this business?
0. Unsatisfactory and unreasonable
1. Reasonable
2. Below the potential of this business
3. Unpredictable
4. Better than I expected
8. Other (Specify) _____
9. N/A
2. Distribution and Markets
129. Through which channels do you sell your products?
1. Sell directly from your own shop
2. State-owned enterprises (as inputs)
3. Other private industries (as inputs)
4. State-owned enterprises (as finished goods)
5. Private shops, retailers (as finished goods)
6. Government (as finished goods)
7. Private exporters
8. Other (Specify) _____
9. N/A
130. Where are most of your products sold?
(circle one only)
1. Locally
2. In surrounding towns
3. Nationally
4. Other countries in Central Europe
5. Western Europe
6. CMEA countries
8. Other (Specify) _____
9. N/A
131. Describe the typical person who buys your products?
1. Rural people/farmers
2. Low-income urban people
3. Middle-income urban people
4. Upper-income urban people
8. Other (Specify) _____
9. N/A

132. Do you have problems distributing your product?

0. No 1. Yes

8. Other (Specify) _____

9. N/A

If yes, what are they? _____

133. Are there regulations regarding distribution channels you have to use for your products?

0. No 1. Yes

8. Other (Specify) _____

9. N/A

If yes, what are they? _____

3. Exports

134. Do you export your product (directly or through traders)?

0. No

1. Yes, export directly

2. Yes, export through others

8. Other (specify): _____

9. N/A

135. If yes, about what proportion of your production is exported:
_____ percent

[coder: leave blank if not answered]

136. If yes, what kind of changes in your products have you made to ensure that they are competitive in world markets?

0. No changes, my products are competitive without changes

1. I have switched product lines

2. I have upgraded the quality of my products

3. I have switched export markets to stay competitive

From which countries to which countries? _____

4. I have lowered my prices to undersell the competition

8. Other (Specify) _____

9. N/A

/137. How do you decide which products to export, what quality they should be and what prices to charge?

/138. If you are exporting, what are the main obstacles that you face? (For example: taxes, paperwork, knowledge, costs)

139. If you are not exporting, have you considered it?

0. No 1. Yes

8. Other (Specify) _____

9. N/A

If no, why not? _____

4. Competition

140. Who are your firm's main competitors? (*circle one*)

- 0. None
- 1. Other small private firms
- 2. Large private firms
- 3. State enterprises
- 4. Cooperatives
- 5. Foreign-owned firms
- 6. Foreign-local joint ventures
- 7. Imports
- 8. Other (Specify) _____
- 9. N/A

141. Has the number of firms producing in your main product become greater since you started-up?

- 0. No 1. Yes
- 8. Others (Specify) _____
- 9. N/A

142. How many other firms now produce in your main market?

- 0. None 2. 1-10 3. 10-50 4. 50-100
- 5. More than 100
- 8. Others (Specify) _____
- 9. N/A

143. Why do you think your customers buy your product instead of your competitors'? (Circle the one most important reason)

- 1. My price is lower than my competitors'
- 2. My product is better designed, of higher quality and is more reliable
- 3. My product is the only one of its type on the market
- 4. I deliver my product on time
- 5. I offer customer support/services
- 6. My business is conveniently located
- 7. My reputation, people know me
- 8. Other (Specify) _____
- 9. N/A

IV. GOVERNMENT POLICIES AND REGULATIONS

A. Registration Information

144. What kinds of registration, licenses, permits does this firm have?

145. Did you have problems obtaining any of the licenses and permits that you have?

- 0. No 1. Yes
- 8. Other (Specify) _____
- 9. N/A

If so, what kinds of problems with which licenses or permits? (Be specific) _____

146. How long did it take you to get all of the licenses and permits that you needed?

0. Same day 1. Less than a month; 2. 1-3 months
3. 3-6 months 4. more than 6 months
8. Other (Specify) _____
9. N/A

B. Taxes

(Interviewers, once you are sure that you know the answers for the next six questions, you can skip them but write them out for the first five interviews)

/147. What types of taxes do you pay, other than those connected with payroll and workers? (For example: VAT, sales, income, inventory, import or export taxes...)

148. How have these changed since early 1989?

0. Not at all
1. Minor changes
2. Significant changes, explain _____

/149. What are the main regulations regarding taxes on profits from your enterprise?

/150. How is the base for the income taxes you pay calculated:

/151. What is the tax treatment for profits reinvested in the company?

152. Are there any special incentives for investment in new machinery and equipment?

0. No
1. Yes, explain _____
9. N/A

153. Have you used any of these incentives?

0. No 1. Yes 9. N/A

If so, which ones? _____

V. CONCLUSIONS

/154. What are the major problems facing someone trying to start a new business today in your country?

155. How would you rate the attitude of government, public officials, and managers of state enterprises toward private business and profit-making?

- 0. very negative
- 2. neutral
- 4. very positive

- 1. negative
- 3. positive

Explain: _____

156. How would you rate the average citizen's attitude toward private business and profit-making?

- 0. very negative
- 2. neutral
- 4. very positive

- 1. negative
- 3. positive

Explain: _____

/157. In your view, what should the government do to make it easier for you or someone who is starting a new business? (includes policies and special programs)

/158. Have you heard about any special programs to help private business with credit or with training?

- 0. No 1. Yes
- 8. Other (specify) _____
- 9. N/A

If so, which program and what is your opinion of it?

159. In your view, what is the future of the private sector in Poland?

Interviewer's notes on the Entrepreneur and/or the Business:

Coding List For Question on Problems

Demand

1. People don't have enough money (generally)
2. People aren't buying because it is the off season
3. Too many other firms in the same business
4. Too many imports
9. Other demand problems (specify) _____

Raw Materials and Inputs

11. Can't get enough local raw materials and inputs
12. Quality of raw materials and inputs is poor
13. Price of local raw materials and inputs is too high
14. Can't get enough imported raw materials and inputs
15. Price of imported raw materials and inputs is too high
16. Tariffs on imported raw materials are too high
19. Other; (specify) _____

Technology, Equipment

21. Equipment is old and needs replacing or updating
22. Replacement costs are too high
23. Can't get spare parts
24. Local equipment is inferior, can't afford imports
25. Repairs are difficult to do or get done
29. Other; (specify) _____

Finance

31. Have to give too much credit to customers
32. Can't get credit for raw materials or working capital
33. Can't get credit for equipment
34. Banks are too difficult to deal with (guarantees are too high, too much collateral, other)
35. Interest rates are too high
36. Cash flow problems due to delayed clearing of payments to threat the bank
37. State enterprises are not paying on time
39. Other; (specify) _____

Labor, Management

40. Lack of skilled workers; workers don't have the right skills
41. Lack of unskilled workers
42. High wages and benefits for skilled workers
43. High wages and benefits for unskilled workers
44. Not allowed to lay workers off
45. Inadequate management skills. In which area? _____
46. Not permitted to increase wages sufficiently to attract appropriate labor
47. Workers unmotivated or lazy
49. Other; (specify) _____

Infrastructure

50. Lack of or frequently interrupted electricity
51. Inadequate telecommunications, specifically _____
52. Inadequate roads for transport
53. Transportation costs are too high
54. Shipping by land, sea and air is very difficult to arrange
55. Shipping by land, sea and air is very expensive

- 56. Factory space is inadequate and getting a larger space is too expensive
- 57. Factory space is inadequate and a larger space is not available
- 58. Warehouse space is not available
- 59. Other; (specify) _____

Business Environment

- 60. Taxes
- 61. Regulations, licensing, permits
- 62. Obtaining foreign exchange
- 63. Rules and policies change too often
- 64. Standards and quality requirements are unreasonable (e.g., for gov't. procurement)
- 65. Government rules and regulations are too costly to comply with
- 69. Other; business environment (specify) _____

Marketing and Distribution

- 70. Too few distributors
- 71. Distributors won't handle the firm's product
- 72. Distributors will pay too little for the firm's products
- 73. Difficult to gain access to retail market directly
- 79. Other; (specify) _____
- 80. Other problems; (specify) _____
- 99. N/A = not asked, not applicable, no answer

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