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**Social Aspects of International Trade in Central and Eastern Europe within the European Integration Process – Case of Poland**

**Abstract**

*The aim of this article is to assess the activities of international business from the point of view of its effects on the labour markets of those accession countries which are undergoing systemic transformation. This analysis covers two spheres, i.e. foreign trade and the activities of transnational corporations in the Central and Eastern European Countries (CEECs) in light of their accession to the European Union.*

*Many of the countries undergoing economic transformation from centrally-planned to free-market economies experienced high trade deficits in the initial period of ownership transformation, in part owing to the predominance of import in the economic activities associated with foreign investment, which in turn exercised a negative effect on their labour markets. Subsequently the trade deficit was incrementally reduced as the share of firms with foreign capital in overall export began to increase and the overall national economies increased their capacities to bring in and handle foreign investment. This increase in exports and reduced trade balance had the effect of creating new jobs.*

**Introduction**

The aim of this article is to assess the activities of international business from the point of view of its effects on the labour markets of those accession

countries which are undergoing systemic transformation. An attempt will be made to answer the following research questions:

- What is the theoretical relation between international trade and the situation on the labour markets of the economies undergoing transformation?
- What were the social consequences of international business activities for those countries which have gained EU membership with special reference to Poland?

### 1. Foreign Trade and the Labour Market-theoretical aspects

The results of the Uruguay Round of GATT/WTO have also had a significant effect on the liberalization of trade, as has the creation of a number new regional integrated trading networks such as NAFTA and MERCOSUR in America, the intensified integration in Europe within the context of the UE, CEFTA i EEA, APEC in Asia, and others.

Based on observations from the period of the last twenty years one may assert that **there is a relationship between the reduction in the aggregated demand for labour and the increase in international trade**. While the average unemployment rate has risen in all countries, its increase has been most significant in the most highly developed countries, in particular in those of Europe (for example in the OECD countries the average unemployment rate between 1980-1997 increased 2 percentage points more than in the countries outside the OECD, where the increase did not exceed 0.5 percentage points) while the largest unemployment rate in the developing countries was noted in South America and Sub-Saharan Africa. The proportionate share of labour income in overall national income also fell, and this decline was greatest in the highly developed countries<sup>1</sup>.

Based on income research conducted by A. K. Ghose<sup>2</sup> into 96 highly developed and weakly developed countries (excluding those countries undergoing systemic transformations), it can be concluded that within the context of the growing inequalities in income and the rise in income gaps

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<sup>1</sup> *International trade and labour market performance: major findings and open questions - Policy issues in international trade and commodities*, Study Series No 20, p. 1.

<sup>2</sup> A. K. Ghose, *Global economic inequality and international trade*, International Labour Office, Employment Paper 2001/2, Geneva, p. 20, Compare also R. C. Shelburne, *Trade and Inequality: The Role of Vertical Specialization and Outsourcing*, Paper presented at IT&FA Congress, San Antonio, May, 19-22, 2004.

between the rich and poor which can be observed over the past 20 years in the world economy, two other related processes are also visible:

- an increase in income inequality within countries,
- a decrease in income inequality between countries.

In accordance with the theory of international trade, those countries with the lowest income levels will profit more from the development of international trade than countries with high income levels, owing to the inflow of foreign investment which will naturally flow more to countries with low capital resources than to countries with a large supply of capital. Trade between countries will also bring about a reduction in barriers to the inflow of investment capital to developing countries and will aid the transfer and diffusion of technology, which will in turn accelerate development in poorly developed countries. Large countries which are poorly developed can gain an even greater advantage from international trade if it is focused, for example, on goods whose comparative advantage is based on scale of production. In such a case their large internal markets can be used to encourage both production and sale of such goods<sup>3</sup>. In addition countries with large domestic markets are more able to attract foreign capital than countries with small domestic markets. Owing to the trade liberalization in industrial markets which has occurred within the GATT/WTO framework, this factor/process has been more visible in the last twenty years with regard to industrial goods than with regard to trade in services or agricultural and food products<sup>4</sup>. Thus large countries with low income levels have generally benefited more from the development of international trade than small countries with low income levels.

Nevertheless it should be noted that countries with low income levels – both large and small – can also lose more as a result of international trade than highly developed countries, inasmuch as the development of international trade brings with it increased competition. Enterprises in countries with low income levels face stiff competition in their domestic markets as a result of the liberalization of trade, which can have a negative effect on the future economic growth of such countries. In order to trade competitively such countries may wind up specializing in the production of goods which are neither associated

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<sup>3</sup> Cf. P. Krugman, *Scale economies, product differentiation and the pattern of trade*, "American Economic Review" 1981, vol. 70, No 1, pp. 950-959, and P. Krugman, *Increasing returns, imperfect competition and the positive theory of international trade*, [in:] G. M. Grossman and K. Rogoff, eds., *Handbook of International Economics* 1995, vol. 3, Amsterdam: Elsevier Science.

<sup>4</sup> Z. Wysokińska, *Konkurencyjność w międzynarodowym i globalnym handlu technologiami* (Competitiveness in International and Global Trade in Technology), PWN, Warszawa 2001, pp. 36-40.

with the positive phenomenon of „*learning by doing*” nor aide in the improvement of their technological capabilities, which would enable them to „*catch up*” with the more advanced economies. Thus under certain conditions the long-term prospects for economic development may be more hampered than aided by liberalized trade.

## **2. Foreign trade and the labour market in Poland**

In the 1990's the Polish economy underwent a process of liberalizing its trade markets within the framework of three free-trade zones: the European Community, EFTA, and CEFTA – as well as significantly liberalizing its trade market within the framework of WTO (whereby it reduced its customs duties by 39% for industrial goods and 36% for agricultural and food products since the beginning of the application of WTO provisions until the turn of the new century).

Liberalization of the trade market for industrial goods within the above-mentioned integrated groups was completed by the end of the 1990s, with the exception of the automobile market, liquid fuels, and steel, where liberalization was delayed by a year. Thus there is no reason to expect a further penetration of imports in upcoming years as a result of the liberalization of customs duties. Nevertheless the significant penetration of imports which has already occurred has influenced the Polish labour market by eliminating enterprises and industrial branches with low competitive capacity indicators, which either did not possess or lost their comparative advantage in terms of costs. As a result there has been an increase in structural unemployment.

With regard to Polish exports to the EU, up until 1998 a number of labour-intensive industries managed to maintain their comparative advantage (based on price competitiveness, as measured by the RCA indicator). These included, among others, furniture, appliances, construction equipment, sanitary and plumbing devices, clothing, wood and cork products, artificial fertilizers, metal, iron and steel production and products as well as non-ferrous metals, road and transportation equipment, leather and enhanced leather products, and rubber products. While among the aforementioned groups of products those with a relatively low level of processing were dominant in the export structure, such as furniture, clothing, and artificial fertilizer, nevertheless a positive trend was observable in the value-added index for some goods requiring a high level of processing (and thus employing highly qualified workers), including

automobiles, transportation equipment, construction appliances and equipment, and sanitary and plumbing devices<sup>5</sup>.

A new, although significantly lesser, impulse towards restructurization will be supplied by Poland's acceptance of the EU external customs tariff, which following its liberalization, within the framework of the WTO, for industrial goods should reduce Poland's current external (non-EU) tariff rate from 6,2% to 3,2%<sup>6</sup>. This may mean the bankruptcy of some inefficient enterprises in industrial sectors which will be subject to and threatened by imports from third countries, in particular those from the non-EU Eastern Europe and Asia. The effect this phenomenon will have on the labour market will depend on the ability to adapt manifested by those industries threatened by the increased competition arising from import from third countries, as well as on their ability to make use of the new protective mechanisms which will be available. Following accession and full integration with the EU the Polish market may be better protected against unfair foreign competition (so-called excessive import, subsidized industrial import, as well as dumping prices).

It should be noted that if firms which adapt to EU norms and technical standards, including veterinary and sanitary standards, are able to increase their marketing activities and compete in the European and world markets, their increased export will have a positive and stabilizing effect on the Polish labour market.

### **3. The effect of the trade deficit on the Polish labour market**

As a result of the near total liberalization of trade in all areas, Poland's foreign trade balance in the 1990's was characterized by a large - and growing - foreign trade deficit, the effects of which were keenly felt in the Polish labour market.

Poland's current foreign trade deficit, which in 1995 reached 6,035.8 million USD, increased to 20,185.3 million USD in 1999. In subsequent years it began to decline, dropping to 18,977.2 million USD in 2000, and to 15,177.2 million USD in 2001. As can be seen from the calculations contained in Table 2, it is estimated that Poland's foreign trade deficit in goods and services resulted in a loss of approximately 2,573,000 jobs in 1999, 2,300,000 in 2000, and

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<sup>5</sup> Z. Wysokińska, J. Witkowska, *Integracja europejska. Rozwój rynków* (European Integration. The Development of Markets), PWN, 2002, p. 320.

<sup>6</sup> Cf. Z. Wysokińska, J. Witkowska, *Integracja europejska. Rozwój rynków* (European Integration. Development of Markets), PWN, Warszawa-Łódź 1999.

declined to approximately 1,632,000 in 2002. (See Table 1). An analysis of the same data on the basis of Poland's balance of payments (data supplied by the Polish central bank, NBP) reduces the scale of this effect to 1,257,000 jobs lost in 1999, 1,315,000 jobs lost in 2000, and 734,000 jobs lost in 2001. (See Part II, Table 1 – calculations based on Balance of Payments).

The explanation for the relationship between the trade deficit and unemployment level in Poland may be found in the systematic decrease in Polish exports of goods based on natural resources and/or labour-intensive processing methods during the period of economic transformation. While the increase in the production and export of goods based on capital investment (primarily from firms with foreign capital investment) as well as the small but growing increase in technological goods must be seen as positive signs, these processes have not sufficiently engaged the resources of the Polish labour market. Given the increasingly sharp competition on the Polish domestic market arising from imports, as well as the same increasing competition Polish export faces in the European markets ( i.e. the UE, CEFTA, and EFTA – to which 80% of Polish export is directed), a large number of Polish workers have been eliminated from the job market and correspondingly the level of unemployment in Poland has risen. Although the above presented effects of restructurization must be considered as positive, nevertheless the effects they have had on the labour market demonstrate that the restructurization of the labour market, looked at from the point of view of the education and qualifications of workers, has not kept pace with the restructurization of the processes of production and trade, i.e. export. On the other hand the partial reversal of the negative trend which can be seen in 2001 and 2002 must be noted and attributed to the fact that for the first time in a decade growth in exports is exceeding growth in imports.

The negative effects on the labour market have been exacerbated by Poland's negative trade balance in services in the years 1999-2000.

**Table 1. The relationship between unemployment in Poland and its trade deficit in goods and services**

CALCULATIONS BASED ON THE BALANCE OF TRADE									
Lp.			1995	1996	1997	1998	1999	2000	2001
1.	Gross value added for the whole economy	mln. zł.	268289,1	336853,5	412870,4	485177	535829	622840,3	656047,7
2.	Import of goods	mln. zł.	70502,3	100231,3	138897,8	162963	182400	213071,8	206252,8
3.	Export of goods	mln. zł.	55515,1	65819,4	84479,6	98647,9	108757,9	137908,7	148114,5
4.	Import of services	mln. zł.	7384,7	9696,6	11217,1	14624,6	19575,6	22601,3	20322,1
5.	Export of services	mln. zł.	7738,7	9122,2	12217,7	12849,8	13132,4	15281,9	16326,5
6.	Trade balance (positions.3+5-2-4)	mln. zł.	-14633,2	-34986,3	-53417,6	-66089,9	-80085,3	-82482,5	-62133,9
7.	Trade balance (positions.3+5-2-4)	mln. USD	-6035,8	-12974,7	-16281,9	-18916,9	-20185,3	-18977,2	-15177,2
8.	Approximate share of trade with the UE in the trade balance	%	44,8	59,49	63,41	61,58	56,76	45,74	41,45
9.	Relationship between the trade balance and the gross added value for the entire economy (positions 6:1)	%	5,45	10,39	12,94	13,62	14,95	13,24	9,47
10.	Actively employed persons	in thousands	17004	17064	17052	17162	17214	17300	17229
11.	Approximate number of jobs lost due to the negative trade balance	in thousands.	926,7	1772,9	2206,5	2337,5	2573,5	2290,5	1631,6
12.	Approximate number of jobs lost due to the negative trade balance with the UE	in thousands	415,2	1054,7	1399,2	1439,4	1460,7	1047,7	676,3
13.	Registered unemployment	in thousands	2628,8	2359,5	1826,4	1831,4	2349,8	2702,6	3115,1
14.	Unemployment rate	%	13,1	11,5	10,2	10,4	13,1	16	18,5
15.	Share of unemployment caused by the negative trade balance to overall registered unemployment	%	35,3	75,1	120,8	127,7	109,5	84,8	52,4

**Table 1. The relationship between unemployment in Poland and its trade deficit in goods and services – continuation**

CALCULATIONS BASED ON THE BALANCE OF PAYMENTS									
1.	Gross value added for the whole economy	mln. zł.	268289,1	336853,5	412870,4	485177	535829	622840,3	656047,7
2.	Import of goods and services	mln. zł.	70935	100223,6	140782,2	184878,8	199903,6	248867	238562
3.	Export of goods and services	mln. zł.	78171,7	94191,6	120408,1	155873,8	160768,8	201548	210585
4.	Trade balance (position 3-2)	mln. zł.	7236,7	-6032	-20374,1	-29005	-39134,8	-47319	-27977
5.	Trade balance (position 3-2)	mln. USD	2984,9	-2237	-6210,1	-8302,1	-9863,8	-10886,9	-6833,8
6.	Approximate share of trade with the UE in the trade balance	%	44,8	59,49	63,41	61,58	56,76	45,74	41,45
7.	Relationship between the trade balance and the gross added value for the entire economy (positions 6:1)	%	2,7	-1,79	-4,93	-5,98	-7,3	-7,6	-4,26
8.	Actively employed persons	in thousands	17004	17064	17052	17162	17214	17300	17229
9.	Approximate number of jobs lost due to the negative trade balance	in thousands	-459,1	305,4	840,7	1026,3	1256,6	1314,8	734
10.	Approximate number of jobs lost due to the negative trade balance with the UE	in thousands	-205,7	181,7	533,1	632	713,2	601,4	304,2
11.	Registered unemployment	in thousands	2628,8	2359,5	1826,4	1831,4	2349,8	2702,6	3115,1
12.	Unemployment rate	%	13,1	11,5	10,2	10,4	13,1	16	18,5
13.	Share of unemployment caused by the negative trade balance to overall registered unemployment		-17,5	12,9	46	56	53,5	48,6	23,6

**Table 1. The relationship between unemployment in Poland and its trade deficit in goods and services – continuation**

TOTAL CALCULATIONS									
I.	Approximate number of unemployed caused by the negative trade balance (based on an average of two different methods of calculation used by the Polish National Statistics Office, GUS)	in thousands	233,8	1039,15	1523,6	1681,9	1915,05	1802,65	1182,8
II.	Approximate number of unemployed caused by the negative trade balance with the EU (based on an average of two different methods of calculation used by the Polish National Statistics Office, GUS)	in thousands	104,75	618,2	966,15	1035,7	1086,95	824,55	490,25
III.	Share of unemployment caused by the negative trade balance to overall registered unemployment	%	...	26,2	52,9	56,6	46,1	30,5	15,7

**Conclusion**

- Many of the countries undergoing economic transformation from centrally-planned to free-market economies experienced high trade deficits in the initial period of ownership transformation, in part owing to the predominance of import in the economic activities associated with foreign investment, which in turn exercised a negative effect on their labour markets. Subsequently the trade deficit was incrementally reduced as the share of firms with foreign capital in overall export began to increase and the overall national economies increased their capacities to bring in and handle foreign investment. This increase in exports and reduced trade balance had the effect of creating new jobs.
- The above-described trends were evident in the Polish economy as well throughout the period of economic transformation and EU integration. In the 1990's one could observe an increase in the trade deficit with the EU, which brought with it the loss of approximately 1,500,000 jobs in Poland. Beginning with the turn of the new century this situation began to improve as a result of the growth in exports, particularly by firms with foreign capital, and the situation in the Polish labour market improved accordingly.