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# GEMINI

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# Study of Informal Cross-border Trade Poland

by

SMG/KRC Poland

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## **PREFACE**

The Poland Small Business Project of the Growth and Equity Through Microenterprise Investments and Institutions (GEMINI) Project commissioned this study as a component of its national assessment of the role and impact of the small business sector on the economic restructuring process of Poland. This report describes the role of informal sector trade between Poland and the former Soviet Republics. The impact of cross-border trade on new market development and employment generation is examined to determine opportunities for policy reform and promotional support by the government.

Unique marketing, economic, legal, and regulatory problems impact on informal sector cross-border trade. The major problems identified are the absence of trade accords between Poland and the new Commonwealth of Independent States (CIS), and the sharp decline of trading opportunities due to the devaluation of the ruble and economic and political instability in CIS states. The collapse of CIS markets is a serious problem for Poland generally and informal and small business traders in particular.

This draft report was prepared by the Warsaw consultancy firm, SMG/KRC Poland. Findings and conclusions presented are based on an analysis of data and information derived from 45 interviews with informal sector traders and six officials in three eastern boarder regions of Poland.

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## EXECUTIVE SUMMARY

This report presents the findings and conclusions derived from a field study of the informal cross-border trading sector in the eastern part of Poland. The method used was an unstructured in-depth interview with 45 traders and six local officials and a questionnaire. The aim of the study was to collect information on informal trade and to test hypotheses on its role in reducing unemployment, expanding markets for Polish goods, and providing a way to enter a more serious and formal business. The report attempts to answer the question: What actions could be undertaken by governments to promote and regulate this kind of economic activity.

The data reveal that a substantial majority of the people engaged in cross-border trade are small-time operators who can be divided into three groups, based on the nature of the trade, the scale of operations, and the long-term expectations of the group members. The first group consists of unregistered people who export small amounts of merchandise and import goods from the former Soviet Union as well as those who export considerable amounts of merchandise and bring only rubles into the country. The second group is "oriented toward growth." They export larger quantities of merchandise and carry only rubles back to Poland. They are ready to adapt to a new situation and to start a new business on their own. The third group consists of people who take rubles out of Poland. They are clients of the previous group. They are importers of Soviet products (often manufactured on a Western license) like washing powders, tools, and vodka. Many of them do not resell the goods but use them in their household. In addition to these groups in the informal cross-border trading sector, there is a fourth group that consists of professionals who try to buy and sell — legally or illegally — large quantities of merchandise.

The results of the study show that today the cross-border trade has declined because of the decreased profitability in the last year. This decrease results from the mounting political, economic, and financial instability in the former Soviet republics. Although Polish economic reform and the opening of the country have provided new opportunities for informal trade, merchandise on the Eastern side is in short supply and the new currencies are rapidly losing value due to hyperinflation; thus, Polish goods are too expensive for their Eastern neighbors.

Even one year ago, informal border trade constituted a viable alternative for those who lost their jobs. However, taking recent economic and political events into consideration, the majority of traders today are limiting their activity, reducing turnover and even planning to discontinue their operations. They have no plans for expansion. The end result is that the previous important role of cross-border trade in reducing unemployment is diminishing.

Similarly, the potential importance of this trade as a way of expanding into a more serious business also has declined. The possibility of accumulating capital for investment in one's own business is almost nil today. Because of the decrease in turnover, cross-border trade today has little effect on expanding the market for Polish goods. Some of the goods exported to the former Soviet republics are manufactured in Poland, but many other are imported from Thailand, Turkey, and other countries. In fact, the outflow of foreign currency seems to be a negative trend.

It is difficult to design a government policy to promote and regulate informal cross-border trade because many factors determining its development are beyond the control of any authorities. The most important factor is the extremely unstable economic and political situations in the former Soviet republics whose government institutions are in a state of crisis and transformation. The subsequent breakdown of legal order makes transactions risky, even when dealing directly with state-owned enterprises and officials.

Promotion and regulation of cross-border trade should begin by negotiating intergovernmental agreements that could regulate the rules of cross-border trade and define the principles of exchange. At the same time, cooperation ought to be encouraged between local governments to provide conditions for developing trade. However, it appears that such actions will not bring the desired effects as long as the former Soviet republics remain in a deep political and economic crisis.

## INTRODUCTION

The purpose of the study was to test hypotheses put forward by the client, to pose new ones, and to collect basic information about the people involved in street trade. It was assumed that the informal cross-border trade might be an important field of economic activity. It might be particularly important in the eastern regions of Poland, which are historically underdeveloped as compared to the rest of the country. The eastern part of Poland, with its traditional agriculture and lack of modern industry, is suffering from recession and unemployment. On the other hand, the official system of Polish-Soviet trade has collapsed in the last two years due to a several reasons:

- The financial system of trade has changed — clearing has been liquidated, as has been the institution of "transfer rouble," the conventional currency used for Polish-Soviet trade accountancy;
- The Soviet Union entered a deep political and economic crisis; and
- The Polish economic reform was totally incompatible with the Soviet and later ex-Soviet economic system.

It was reasonable to test the hypothesis that this situation could open new opportunities for trade in the eastern regions of Poland. The land borders the Commonwealth of Independent States. The people are linked through heredity and culture, as many Polish people have families in these Eastern countries. The Polish reforms give more opportunities to develop trade. To illustrate how the existing system for informal cross-border trade works, the people involved, the apparent obstacles, and how the government (local or national) could help or promote this activity, the following questions were posed:

- What is the role of the informal cross-border trade in providing employment for Polish citizens?
- What is the role of the informal cross-border trading sector in expanding the market for Polish products?
- What is the role of the informal cross-border trading sector in generating a basis for formal commercial activities?
- What actions and steps should be taken by governments to improve the efficiency, impact and societal value of the informal cross-border trade sector?

To answer these questions and describe the system of informal cross-border trade, field research was conducted in the eastern part of Poland.

## **FINDINGS ON INFORMAL CROSS-BORDER TRADE**

The study shows that the people involved in informal cross-border trade between Poland and ex-Soviet republics can be divided into three different groups, based on the nature of the trade, the scale of operations, and the long-term expectations of the group members.

### **Traders With a Short-term Outlook**

There is a large group of traders who, for many reasons, choose not to register their activities. These people import a small amount of merchandise (for example, 15 pairs of jeans) from the Soviet Union as well as export considerable amounts of merchandise (over 50 pairs of trousers, for example) and bring rubles into the country. The distinguishing characteristic of this group is a common reaction to the changing situation: in view of the worsening price relations reducing profits to a minimum, they anticipate that it will be necessary to eventually discontinue their business activities.

These traders might have begun trading as a reaction to a depressed labor market or a fear of losing their job in a state-owned enterprise. Surprisingly, they openly express a desire to find a regular, secure job. It is common for one member of their family to have a steady job, almost always in the state sector; unfortunately, those state jobs are being constantly reduced. The vendors themselves are considered legally unemployed, for the most part collecting unemployment benefits.

This group of traders represents a particular age group of people between 30 and early 40 years of age; there are no representatives here of the youngest generation of smugglers. Most likely, they have families to provide for and perhaps also parents, so the inherent risks of this profession would usually be unacceptable to them.

The composition of this group reflects changes taking place in the structure of the petty smugglers' community in the last several months. There is a trend away from importing large quantities of merchandise. Rubles are usually bought and sold for cheaper purchases for oneself and one's immediate family. Hence, represented in this group is the category that until recently was the largest -- simultaneously exporting and importing. The group gradually replacing it is the exporters bringing rubles into the country.

The assortment of goods exported is very narrow. Until recently it consisted primarily of cosmetics, mainly manufactured in Poland. There are also some inexpensive, domestically produced synthetic skirts. The most popular items continue to be jeans, especially skirts. Their origin is not entirely clear. Most of the respondents mentioned imports from Thailand and Turkey, but it is very possible that these are Polish fakes. There really are no problems with the availability of these goods; they are acquired from local wholesale firms (one can already purchase wholesale five pairs or more). It is profitable for the larger exporters to travel to the center of the country (for example, to Lodz), where wholesale prices are somewhat lower.

Selling merchandise abroad is a problem, however. The situation where jeans could be sold easily for a relatively high price, yielding a profit on one pair of up to 30 thousand zloties, is gone forever. The Lithuanian market is already considerably saturated. There are two ways of exporting this merchandise. First, the merchandise can be sold on one's own, selling it in Lithuanian bazaars or distributing it among family or friends residing abroad; this is time-consuming (due to decreasing demand) and often costly (for example, the local mafia collects marketplace fees of 2,000 rubles). Second, one can sell the entire lot of merchandise to local distributors; the price is lower but time is saved, allowing for more runs across the border.

In the opinion of all of the respondents, the problems lie almost exclusively on the Eastern side. Objective factors cause most of the problems, among which the most important are decline of prices for exported products and uncertainty about the developing economic situation, especially the inflation rate and the eventual introduction by Lithuania and other post-Soviet republics of their own currencies. Even with the two-week trading cycle, the decline of the exchange rate of the ruble in Poland exposes the exporter to considerable losses. The ruble is declining in value not only because of price rises but also because of the anticipation of the Lithuanian government changing currencies from the ruble to the lit.

Another problem is created by the fact that the Eastern market is no longer able to offer the same amount of cheap goods suitable for import to Poland. Though most of the goods available in bazaars for free-market prices are still lower in price than in Poland, Russians who have access to cheaper products sell them in Poland at competitive prices.

These uncertainties combined with the vast corruption taking place in these newly formed countries further harms trade. The regional and national mafias excise payments for conducting business in their area. Crossing the border in a business capacity can be nearly impossible without bribing the local customs officials. The difficulties created by Polish customs officers appeared in several interviews. Until July, people with larger amounts of merchandise were turned back to Poland. Despite the discontinuance of such practices, many of the respondents did not know this had changed.

The reaction to the increasing problems is a wait-and-see policy and the often declared intention to discontinue business. No one could envision legalizing his activity, though even this would not make business more profitable. These people treat their present occupation rather as a way of supplementing unemployment benefit or saving up some money for consumption expenditures. According to their own declarations, they were unable to accumulate any money for starting up their own, legal business. Even if there is interest in this question among "exporters," the evaluation of the needs of the local market (Sejny) is not encouraging — "everything needed is already in the city, and the people are not rich."

### **Traders Oriented Toward Growth**

The criterion used to distinguish this group is its orientation toward growth. This feature is connected not so much with estimation of the chances for successfully continuing the present

activity but rather with the readiness to adapt to a new situation and continue "business on one's own."

All of the representatives of this group export merchandise in larger amounts (minimum 100 pairs of trousers) and bring large amounts of rubles into the country. This group is made up of people who already had something to do with private business: former owners of shops that went bankrupt, people who were dismissed from neighboring state plants, and — an especially interesting category — young people who often are high school students. All of them either collect unemployment benefits or are candidates for unemployment. Their activity is unregistered, so they pay no taxes. Young people regard it as the main source of income and a way of achieving financial independence.

The assortment of goods exported from Poland is practically the same as in the case of the smaller exporters in the first group. Thus they are first and foremost jeans (especially skirts) from Thailand or Turkey, cosmetics, and skirts of synthetic fabric. These goods are purchased in local wholesale firms, but on rare occasions it pays to travel into the heartland of the country. Connections with local wholesalers make it possible to sell goods on consignment. The popularity of this form of financing purchases is evidence that the representatives of this group do not deal in large sums of money.

In the cases of these informal traders, the trips are more frequent. Although members of the first group travelled once every few weeks, high school students go once a week and the others even more often. The most convenient means of transportation, in this instance, is by bus.

The income of this group is largely dependent on a consistent exchange rate for the ruble. Every decline in the ruble's value means losses for them because profits from the conversion of rubles are spread out over time. The permanent and considerable devaluation of the ruble over the last several months due to inflation in Russia and the flight from the Soviet currency in Lithuania has greatly reduced the profits of Polish exporters.

There is also a feeling of uncertainty connected with continually decreasing demand and, thus, with the prices of goods exported from Poland. The former Soviet Union is a potentially huge market, but access to it is ever more difficult. For the representatives of this group, the business risk is great and it is connected with the efficiency of the Eastern customs officials. One of the interlocutors told stories of "busts" — the confiscation of merchandise or currency in which as much as 50 million zloties has been lost in a single instance. The introduction of customs controls between the republics also increases the risk, which discourages trips into the "heart of Russia." Also, the Soviet economic mafia is a major deterrent; it attempts to keep Polish exporters out of the most "starved" markets by appearing in the role of compulsory middleman or collecting tribute for the possibility of trading in local bazaars. In the opinion of one of the interlocutors, "you don't come back from there with money."

The main problem is the form of payment for the exported merchandise. The commercial offer of Lithuania, as one could gather during the promotional exposition organized by the mayor of Pusk, is exceptionally meager. Being a middleman in the export of Lithuanian

goods to the West also does not seem to have much of a future. The Lithuanians themselves are already appearing here in the role of middlemen buying merchandise in the heart of Russia. It is rumored that the prices asked by the Lithuanians often exceed world prices.

This group will probably attempt to adapt itself to the changing situation in an active way. The younger tradesmen declare that they will certainly "attempt trade with the Germans or Hungarians, as once before." Some of the former smugglers also now are trying legal trade with the East. So far, however, the results have not been impressive.

### **Domestic Focus Group**

The third group identified in the study are nonexporters who do not fit neatly into the categories suggested in the project. However, there are certain arguments in support of including them. They are one of the basic elements of the system that has grown up around informal trade with the East. It seems worth examining other forms of entrepreneurship arising from petty trade across the border, because it seems that local production has not been stimulated by cross-border trade.

This group uses rubles acquired in Poland to purchase their supplies. In this way group members are the most important customers of the exporters, because they constitute the sales market for the exporters' rubles. Encompassed in this group are representatives of two different categories. The first are people importing goods in commercial quantities for profit. The second are those who make cheaper purchases for themselves and their families. As one can gather from the responses, the second category is growing larger and larger. The factors causing changes within this group are the situation in the Soviet market, where for all intents and purposes goods are available only for bazaar prices, and the competition of Soviet tradesmen selling their wares in Poland.

The most frequently imported products are washing powders produced on Western licenses, toothpaste, household articles, small tools, and clothing. The goods whose import are especially profitable and can be sold quickly at home are gasoline and vodka.

Among the importers who want to sell the goods they bring into Poland are many residents of the countryside. Since the purchase of such goods as alcohol and gasoline require a certain elementary confidence in the seller, they become the main suppliers of these goods in their circle. There is always a considerable demand for these goods at low prices. Such importers tend to repeat trips across the border several times because of their chosen means of transportation across the border — the motor bike. People crossing the border on motor bike have to purchase a "Warta" insurance policy (minimum period two weeks) and a voucher giving the right to cross the border for a period of three days. Motorcyclists can avoid the several-day's wait in line on the Lithuanian side, allowing them several trips. The interlocutors said that laid off worker-peasants often appear in the role of such providers; however, they do not treat such activity as their only source of support — owning their own farm gives them a greater sense of security.

In this group are also those importers who subsequently attempt to sell their wares in the local marketplaces in Suwalki or Augustow. Their profits are greatly reduced by the Russian-Lithuanian competition. In view of shrinking profits they do not see any prospects for the future in their present occupation. They spend their earnings maintaining their present standard of living.

Buyers also constitute a segment of this group. They regard the Eastern border markets as places to make inexpensive purchases. They acquire rubles (from one to two thousand) from street money changers and set out on one of the four express buses traveling the route Elk-Suwalki-Sejny-Lozdzije (on the Lithuanian side). These buses bypass the lines at the border crossing. The cost of the round-trip ticket is 50 thousand zloties and an additional 10 thousand for a voucher that one buys together with the ticket. The return takes place a few hours later, because the purchases are made in the bazaar in Lozdzije. Those who engage in this form of trade are housewives and older people providing their families with both manufactured goods and foodstuffs. One can surmise that the savings made thanks to this way of making purchases are a big help to family budgets.

### **Formal Traders**

In addition to the informal cross-border traders, the study also looked at formal or legal trade. From a quantitative point of view (number of people engaged in it), legal trade with the East is much smaller in scale than informal trade. This group differed considerably from the informal traders in its approach to the problem of trade with the former USSR: other motivations, other forms of trade, and different aspirations and plans for the future.

These respondents have higher occupational and financial positions. They own their own firm or are employees of trading companies. Professional preparation and practice, they emphasized, are very important in opening one's own business. Work in a trading company or a store gives them the opportunity to become familiar with tax regulations, the credit system, commercial codes, and customs regulations.

The motivation that inclines the subjects to go into "serious trade" is similar: the desire "to make a lot of money" (to get rich quick). It is generally accepted that the Eastern market provided an exceptional opportunity for industrious people: "The future belongs to firms producing for the Eastern market (no competition at all)."

The respondents spoke rather unwillingly, and only generally, about their business. Export to the former USSR is almost impossible because Polish goods are too expensive. Food products in demand are hard to export in the present situation (the time of waiting on the border is too long). However, it was discovered that firms exporting potatoes to the Ukrainian market are making healthy profits.

The products most frequently exported from Poland are fabrics, clothes from Thailand, electronic equipment, and automobiles. The merchandise is purchased most frequently from

wholesalers, who are rapidly developing in the frontier area. The vendors go to Lodz for synthetic fabric.

The respondents most often use their own funds to purchase merchandise. The wish to take out bank loans in the future was often stated (a lowering of the interest rate would encourage this). The subjects also described the exceptionally profitable procedure of semilegal and illegal trade with the East. For some time now in the border area new firms have been purchasing non-ferrous metals. (In the former USSR the sale of raw materials is forbidden.) After crossing the border, however, the merchandise is sold in metal purchasing centers. Upon being transported across the Western border the profits become enormous.

The Polish side does not create any formal or technical obstacles to commercial activity. From the Polish authorities the respondents anticipate only actions that would help the businessmen to increase their sales (for example, lowering the interest rate on loans for businesses trading with the East and the charge per square meter for store area).

The Eastern — Ukrainian or Lithuanian — side is in such disarray that many more difficulties are anticipated. Crossing the border presents a host of problems. The Soviet customs officials are "corrupt, insolent, and aggressive." There is no law (or rather none is observed). For people doing business legally, operating quickly, the frustrations and bureaucratic ignorance are great impediments to conducting business.

Perhaps the most serious obstacle is the lack of credibility of the Eastern partners. The commercial code there is not enforced, so commercial activity is based on "connections." To purchase merchandise or sell it one has to know "somebody". There are still many regulations standing in the way of the most simple financial operations. Hyperinflation and the nonconvertibility of the ruble constitute big problems. Hence barter will overtake this form of trade in the future.

## **ROLES OF CROSS-BORDER TRADE**

### **Providing Employment for Polish Citizens**

The eastern provinces have high unemployment rates. At the same time the closeness of the border and the specific characteristics of the Soviet market have created a rather simple mechanism for channeling unemployment — namely, informal cross-border trade. Interlocutors in the regional employment office did not even have any approximate data on the percentage of those who collect unemployment benefits while, simultaneously, making money as small-time smugglers, buying and selling rubles as middlemen, and importing goods from the East as unregistered vendors. Based on the everyday experience of the respondents, until recently there had been no fear of unemployment in these regions. "At the worst I'll take up trade" was the common reaction. The obvious exception were people who for personal or prestige reasons saw no chances for themselves in trade. As late as half a year ago the profits from small-time

smuggling were so great that "people could afford to leave work in the fields and travel to Russia."

The picture one gets of the present situation from talks with the vendors themselves differs almost completely from that situation. All of the respondents agreed that the profitability of cross-border trade has diminished considerably. The source of the problems lies exclusively on the Eastern side of the border. It turned out, for example, that the relatively shallow Lithuanian market has already been saturated with Poland's stronger exports. Expansion of the assortment of goods exported to the East is practically impossible due to the unfavorable relative price. At the same time, small-scale import by Poles from the Eastern market has been considerably hampered by difficulties in acquiring attractive goods and by the Russian competition in Polish bazaars.

The result of the above difficulties has been a gradual change in the structure of the smuggling community. There has been a clear decline in the group of those who exported small lots of goods (5-10 pairs of jeans) and brought back articles for sale. Given present prices, the profit on one pair of jeans, for example, comes to 5-6 thousand zloties in comparison with 30 thousand only half a year ago. A significant profit comes only from the export of at least 50 pairs of jeans.

### **Expanding the Market for Polish Products**

The products that make up the core of Polish exports come either from imports or are brought from the heart of the country. Because most of the exporters buy their merchandise from local jobbers, the local wholesale firms are the first official economic unit deriving profits from the entire operation. The surpluses appearing in subsequent transactions still remain in the unregistered area. The question of the legality of the unregistered sector — money changing, selling in the bazaar without the proper documents — is not an arena of conflict; the police "shut their eyes" to this activity, and threats from the police were not among the problems mentioned by the smugglers.

One should be able to judge the effect of income earned from informal trade on a community. Although a considerable part of the imports from the former USSR satisfy immediate consumption needs, they also draw many customers away from the local stores. In Suwalki, for example, retail stores are experiencing decline in revenues. The shops are frequently changing the products they carry to find a place for themselves in the market. This is a good sign of their adaptability and recognition of market conditions, but it also signifies the negative effect of cross-border trade on domestically produced products.

A more serious problem seems to be the outflow of foreign currency. Its most unfavorable form is described in the following sequence of events: an Eastern "tourist" brings into Poland a product that is cheaper than a local one and sells it, thereby taking away customers from the Polish merchant, and then takes illegally purchased foreign currency out of the country. In the worst-case scenario, the Eastern tourist pushes Poland into an even deeper recession, reduces the tax revenues from trade flowing into the local budgets, and worsens Poland's balance

of payments. The conclusions from almost all of the interviews indicate that other scenarios (the tourist brings in merchandise that Poland has to import anyway, the tourist takes from the country goods purchased in a Polish store) are much rarer.

Certain signs of an economic upswing can be seen in the appearance of small businesses engaged in making fake jeans that are subsequently sold in wholesale lots as Thai or Turkish. Most firms of this type have sprung up near the big textile centers: Lodz, Poznan, and Warsaw. For example, in Bialystok province there are companies making the above products more attractive by sewing on labels and trademarks of well-known Western firms. For the most part though, this remains a cottage industry (small and employing family members).

In the Bialystok region today there are about 40 registered enterprises, including 22 wholesalers (six state ones). The assortment of goods produced for the Eastern market is an attempt to fill in the gaps that appeared after the breach of government commercial agreements with the former USSR. Until now the private businessmen have exported chiefly textiles and small amounts of food articles. The present food situation in the new republics has created new hopes for an increase in the export of Polish food products. Some of the firms are expanding the scope of their activity by offering the Lithuanian side, in addition to clothes, Polish food (which in turn stimulates local agricultural production) and also specialized agricultural and gardening tools. Unfortunately, the unstable situation across the Eastern border and the lack of binding international commercial agreements effectively block many of these initiatives.

The implications of this import/export trade extends into the infrastructures of the local communities. Around this trade informal hotels and restaurants have cropped up to accommodate both Poles and foreigners. There is also a relatively large group of commercial jobbers — people purchasing goods from arriving Russians and selling them in other regions of Poland.

The export of goods to the former USSR is on the decline. In several months it could die out completely. Small traders now are carrying only small amounts of Thai jeans (jackets, trousers) and Polish materials (synthetic fabric). Polish goods do not find customers because they are too expensive.

### **Creating a Basis for Formal Activities**

Today cross-border trade has diminished considerably because of the decline in profitability. For this reason, the potential for this trade to provide a way of expanding into a more serious business also has declined. The possibility of accumulating capital for investment in one's own business is almost nil today. For most of the vendors, trade is an occupation that provides a primary or secondary source of income; it usually does not allow for accumulation of investment funds.

Owing to the specific features of the activity, traders do not require infrastructure investments — a store, means of transport, or even a booth — and do not need much working capital. The vendors make most of their trips by public transport — regular buses or train —

or motorcycle. Travel by car is less convenient because of the lines at the border crossings. Lorries are not used for the same reasons and also because of the small-scale of the enterprise.

The economic situation in these Eastern countries cause great uncertainty for Polish businessmen. The instability of the economic, political, and monetary situation across the border precipitates unpredictable events and makes planning future activities difficult. Therefore, most of them regard trade as something temporary, to be pursued as long as it remains possible and profitable; they foresee no future in this business.

Customs regulations hamper the development of trade. Although there are no export tariffs, one can take out of the country only limited, "non-commercial quantities." Such a legal situation rewards trade in small amounts of various goods and does not promote business on a larger scale or specialization. The transport of larger amounts of merchandise requires registration, payment of taxes, and meeting other formal requirements; the small vendors fear this process. They are discouraged from legalizing their activity by the instability of the situation and the disinclination to incur additional costs. As a rule the small traders also do not have the skills, such as knowledge of the market and familiarity with the regulations, that are required to conduct business on a wider scale.

As the data from the study show, a substantial majority of people engaged in cross-border trade are small-time operators. They spend their profits on consumption, though one can surmise that farmers may also reinvest part of the profits from trade in their farms. From elsewhere we know that farmers nowadays are not very willing to make investments, and so one can assume that cross-border trade helps them to survive the recession in agriculture.

In addition to the development of cross-border trade, there are other possibilities of commercial activity that this trade stimulates to some extent. Among them are tourist services for people traveling in to and from the East. These services are developing very slowly, but they have certain prospects for the future.

Generally speaking, the situation in cross-border trade is as follows. The majority of traders are limiting their activity, reducing turnover, and even intending to drop this activity; they have no plans for development. Also a very narrow group of traders have developed their informal trade and are working to formalize and expand their activities with the East. They have a chance to develop, but many factors lie beyond their control — first and foremost on the developing situation in the East. And this situation is largely unpredictable. One can guess that the development of commercial activity by this group will encounter competition from the larger trading companies that will be able to operate professionally.

## **FACTORS AFFECTING FUTURE TRADE**

The most important factors determining the development of cross-border trade are beyond the control of the Polish authorities. The main factor is the economic and political situation of the former Soviet republics. The present economic situation is unfavorable. Uneven price

relations greatly limit trade. The ruble is officially not convertible, but even its black market rate is much lower than the zloty; Polish goods are ordinarily too expensive for Eastern customers. The breakdown of the commodity market on the Eastern side, exemplified by the shortages, makes it impossible to purchase goods in exchange for what has been exported. This study has shown, however, that this last obstacle can easily be overcome by foresight, although as a rule this requires bribery. Besides this, Poland has a hard currency, which promotes imports rather than exports.

The macroeconomic situation is exceptionally unstable. The introduction of national currencies in the Ukraine and Lithuania could entirely change the conditions of trade. There are no indications yet of whether and when such a thing might happen. It is likewise with prices, which are changing very rapidly due to hyperinflation combined with freeing of prices incrementally.

Irrespective of the currency factors, partners on the Eastern side have been found to be unreliable and unpredictable, which makes it hard to do business. As a rule only one-time transactions are possible.

All of these factors, which have the greatest bearing on the conditions of trade with the East, are beyond the control of the Polish authorities. A step toward rectifying some inconsistencies on the Polish side could provide for a better, healthier business environment. Taking into account the lack of incentives for Polish traders to conduct formalized business, the government could pursue a more favorable enterprise development policy representing the needs of these entrepreneurs. More consistent, binding international agreements regulating cross-border trade and legal questions concerning payment would be a "good faith" step in the right direction.

It is true that the Polish authorities cannot change another country's laws or policies or make another government less corrupt. There is currently a breakdown of the legal order in the East that makes business transactions very risky. Business is often conducted illegally and, more often, on the borderline of legality. The institutions protecting the interests of the partners, and even their life and health, do not function. From the accounts of interlocutors, a picture emerges of the Eastern republics as lands where law does not function. One is not protected by government institutions and, in fact, these institutions may even be a source of danger. The customs officials and the police on the Eastern side act quite arbitrarily; they are corrupt and entirely exempt from punishment. The average Pole is completely defenseless against their actions. Here the biggest problem is the lack of agreements between Poland and the new republics (or the ineffectiveness of such agreements) that could guarantee the safety of merchants.

Defects in the infrastructure servicing cross-border traffic on both sides could be improved. This is more true for the Eastern side. On the Polish side the roads and border crossings are well kept in contrast to the Eastern side.

All of these difficulties are characteristic of relations between countries in a deep economic and political crisis, beginning to build or transform their structures. Promotion of

cross-border trade must start with fundamental matters — for example, entering into intergovernmental agreements that could regulate the principles of traffic across the border, define the principles of exchange, and give the travelers legal guarantees of safety. At the same time, cooperation ought to be encouraged at the local level, between the authorities of provinces or cities. Such cooperation would put in place certain technical conditions facilitating traffic across the border. However, it seems that such actions will not bring the desired effects as long as the Eastern republics remain in deep political crisis.

**APPENDIX A**  
**METHODOLOGY**

Field work for this study took place during November-December 1991, with the initial data analysis undertaken between January-March 1992. The basic tool used was the unstructured, in-depth interview. Following guidelines, the interviewers collected information that could help to understand and describe how the informal cross-border trade system works, the people involved, how they operate, the nature of business conducted, how much money is earned, and what the main obstacles are. After conducting the interview, additional information was collected from the respondents by using a questionnaire concerned with problems formulated by Development Alternatives, Inc., which the respondents could reply to in depth.

### THE SAMPLE

The study was conducted in the region of Suwałki, Białystok, and Przemysł on a sample of 45 respondents engaged in trade across the Polish eastern frontier. The questionnaire contained nine open questions and a demographic section (sex, age, education, occupation, place of residence). The sample was not representative in a statistical sense, which means that the quantitative characteristics of the sample (for example, breakdown by age, sex, occupation) cannot be treated as characteristics of the whole population of informal traders. The nonrandomness was caused by the following:

- The sample (45 individuals) is too small to make statistical generalizations; and
- Randomness implies application of rigid statistical procedures of selection. In this case, where we dealt with unstructured population, the application of these procedures was not possible unless we make a large survey on a big sample of inhabitants of eastern regions.

The methodology applied does not allow making statistical description of the target group. It was a qualitative study whose aim was to give insight into a system of economic activity that was completely unknown.

### THE RESPONDENTS

Among the 45 respondents, the vast majority (73 percent) were men. Approximately 11 percent had elementary education, 25 percent - vocational, 49 percent - secondary and postsecondary, and 16 percent - incomplete or complete higher. More than one-fourth of the respondents were students and pupils. Aside from students, the most widely represented occupational groups were skilled manual workers and service workers. One must expect that the considerable over-representation of people with higher education and pupils is artificial and results from the nonrandom selection of the sample. It is well-known that interviewers never

select their respondents at random even if they try to do so. There also exists a social bias -- the interviewers, being university graduates, always select more people with social status close to their own. Only the rigid selection procedure can help to avoid that and in this case the application of this procedure was impossible. Only 15 percent of the respondents were residents of the countryside. Among the respondents, half of them were people aged from 30 to 50, and about one-third of them were young people below 30. The respondents of six interviews were representatives of the local authorities: custom officers, policemen, and local governments officials.

The amount of time in trade across the Eastern border ranged from one month to 20 years. Only in the last two years has there been a visible increase of activity in this area. Eighteen percent of the respondents have been engaged in this activity for two years, and more than one-third for about a year. In the last half year somewhat fewer people (20 percent) decided to go into trade.

The information obtained in in-depth interviews proves that the informal cross-border trade was the most profitable in 1990-1991, because of the new opportunities that opened in the course of the market economy reforms and opening of the country. For the last six months profitability has been gradually decreasing. It was the result of changes in the former Soviet Union -- the economic crisis and growing political instability.

Most of the respondents (88 percent) citing the main reason for taking up this activity gave a financial motive, i.e. the desire to "make a buck," "support a family," as well as a "wish to work for myself" or "lack of prospects in my present job." Most of the respondents (69 percent) did not give up their previous job, however. Three people combine trade with work on their own farm. For nearly 30 percent of the respondents trade is the sole occupation. Four among them are unemployed, the rest (23 percent of the whole sample) are people who have left state jobs, but are not registered as unemployed. Nearly all of the subjects conducted this activity illegally. Only six people (13 percent) answered that they have a firm and pay taxes.

Many respondents believed that trade across the border is not very profitable. Seventeen people (46 percent among those who answered explicitly) stated that they earned just enough to make a living. Eight people declared that they also supported someone else from this income. On the average 1.8 people had to live off the profits from trade.

The respondents traded goods both domestically and of foreign production. Among the foreign products they most often exported jeans from Thailand and Turkey (20 people) and other clothes from these countries (6 people). Individual respondents also said that they traded in Western store clothes and cosmetics as well as Soviet food and gold.

The most often-mentioned Polish goods were cosmetics and fabrics -- chiefly synthetics (5 people each, 11 percent) and food, clothing, and furniture. Several respondents also mentioned electronics and raw materials without stating the place of their origin. Twelve people also traded in dollars, four in rubles.

The merchandise came from various sources. Half of the tradesmen supplied themselves in warehouses, 29 percent in stores, 10 percent in bazaars; several people purchased from the producer or from smugglers.

The vast majority (84 percent) relied on their own funds, 26 percent borrowed from their family or friends, 8 percent took merchandise on consignment. Seventy percent of the respondents got their working capital from one source.

The difficulties the respondents complained about are first and foremost diminishing profitability, vexatious customs controls by the former Soviet side (10 people) and the lack of stability in the former USSR (9 people). Lack of familiarity with the customs regulations, lack of working capital, and bottlenecks at the border crossings (2 people each) were also listed as problems. Nine people stated that they have no problems with their work.

Fourteen of the respondents admitted that they have no plans for the future. Most of the others responses concerned work. Seventeen people intended to develop commercial activity, most often in some legal form; five people wanted to give up their present activity (smuggling) and go into something else. For three people the main goal was to become well-off. Individual respondents spoke about private plans such as getting married and going abroad.

### **THE INTERVIEWERS**

The interviewers were Sociology students of the University of Warsaw collaborating with SMG/KRC Poland. In addition to training for this particular study, all of the interviewers in the past had completed poll-taking courses given by SMG/KRC Poland.

### **THE COORDINATORS**

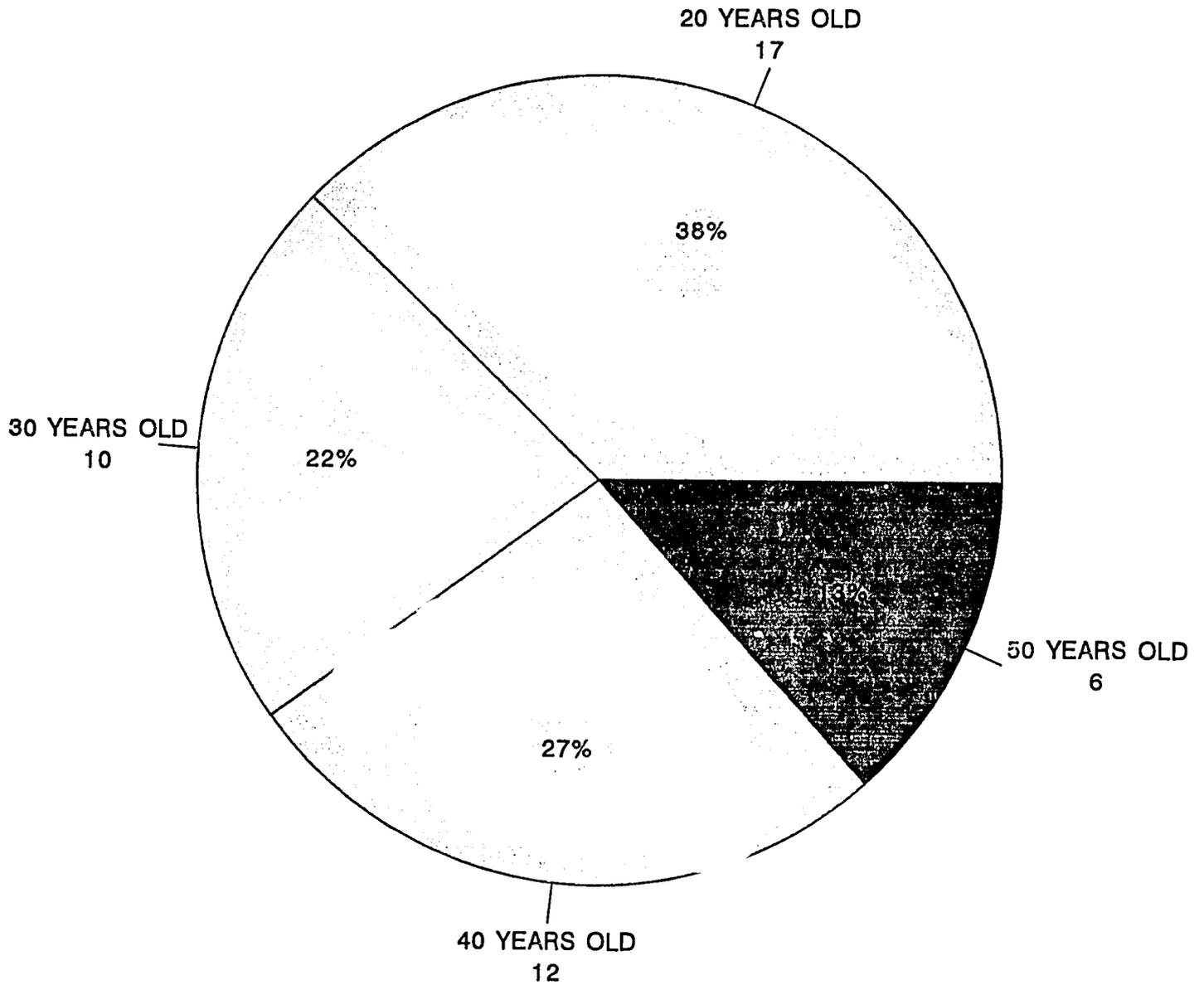
The study was coordinated by Dr. Krzysztof Nowak and Michal Oklot, M.A.

**APPENDIX B**  
**GRAPHIC PRESENTATION**

# GENERAL DISTRIBUTION OF RESPONDENTS BY AGE

NUMBER OF OBSERVERS

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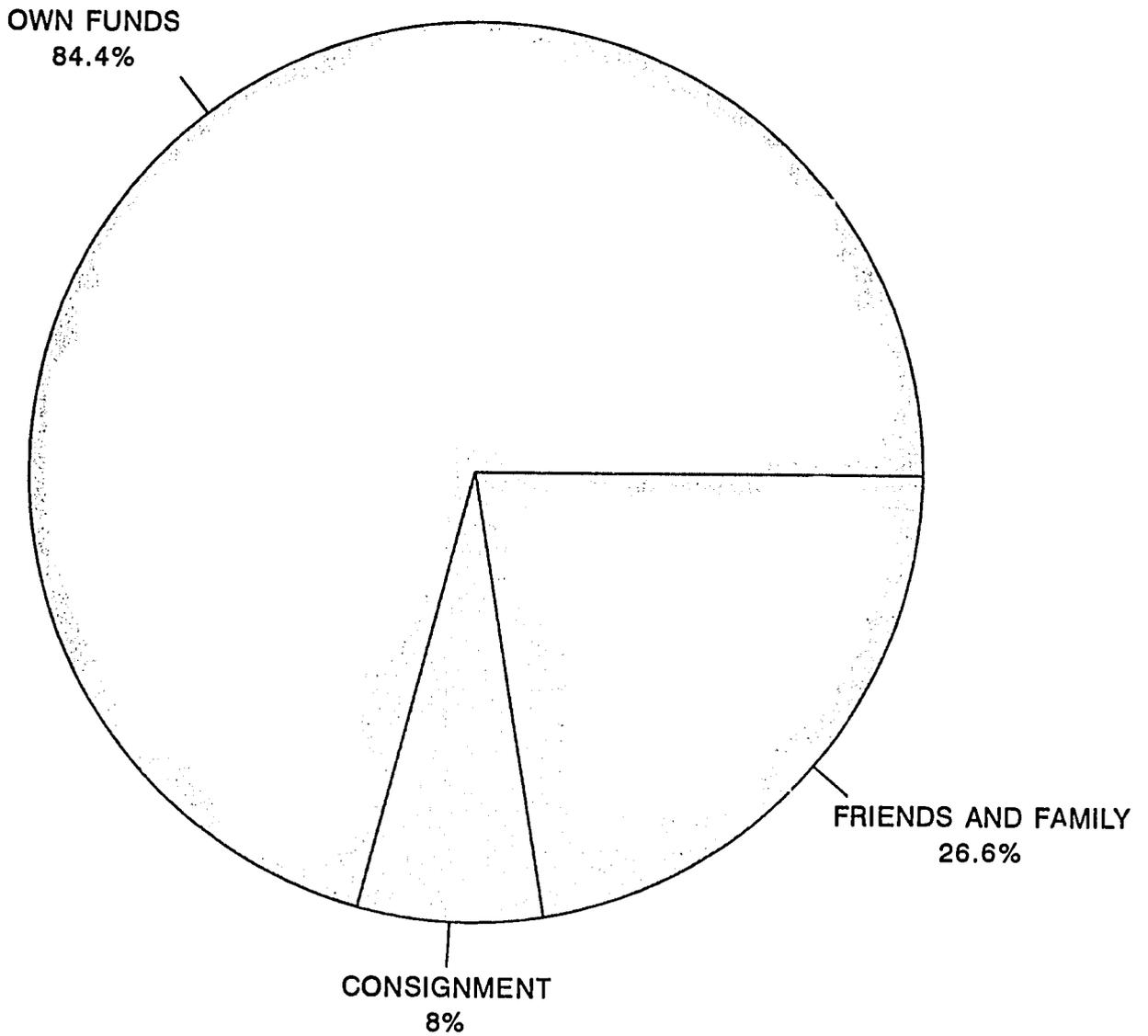


RESPONDENTS AGE

# SOURCES OF WORKING CAPITAL

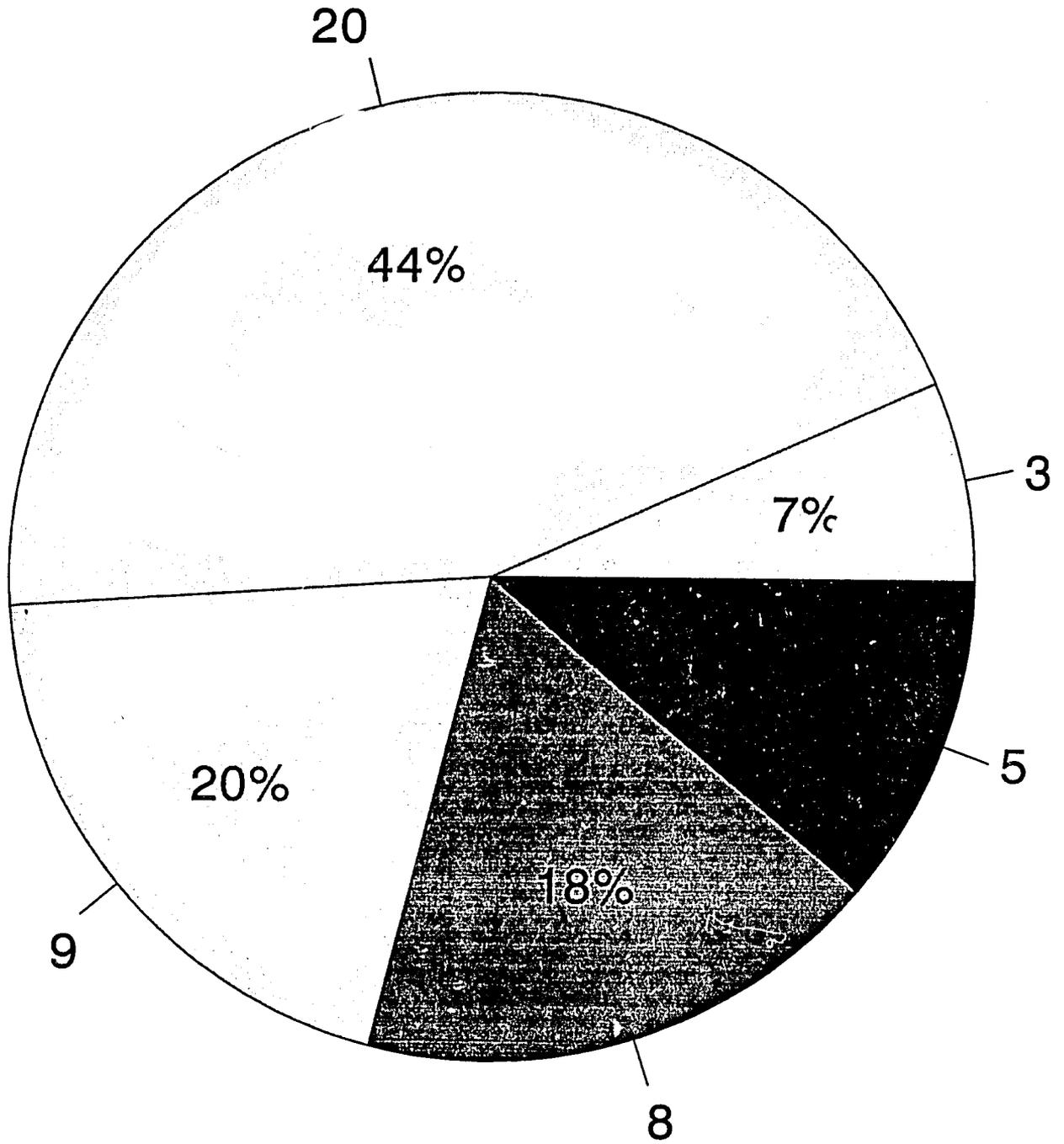
## PERCENT OF OBSERVERS

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B-5  
NUMBER OF PERSONS MAINTAINED BY A RESPONDENT (SMUGGLER)  
NUMBER OF OBSERVERS

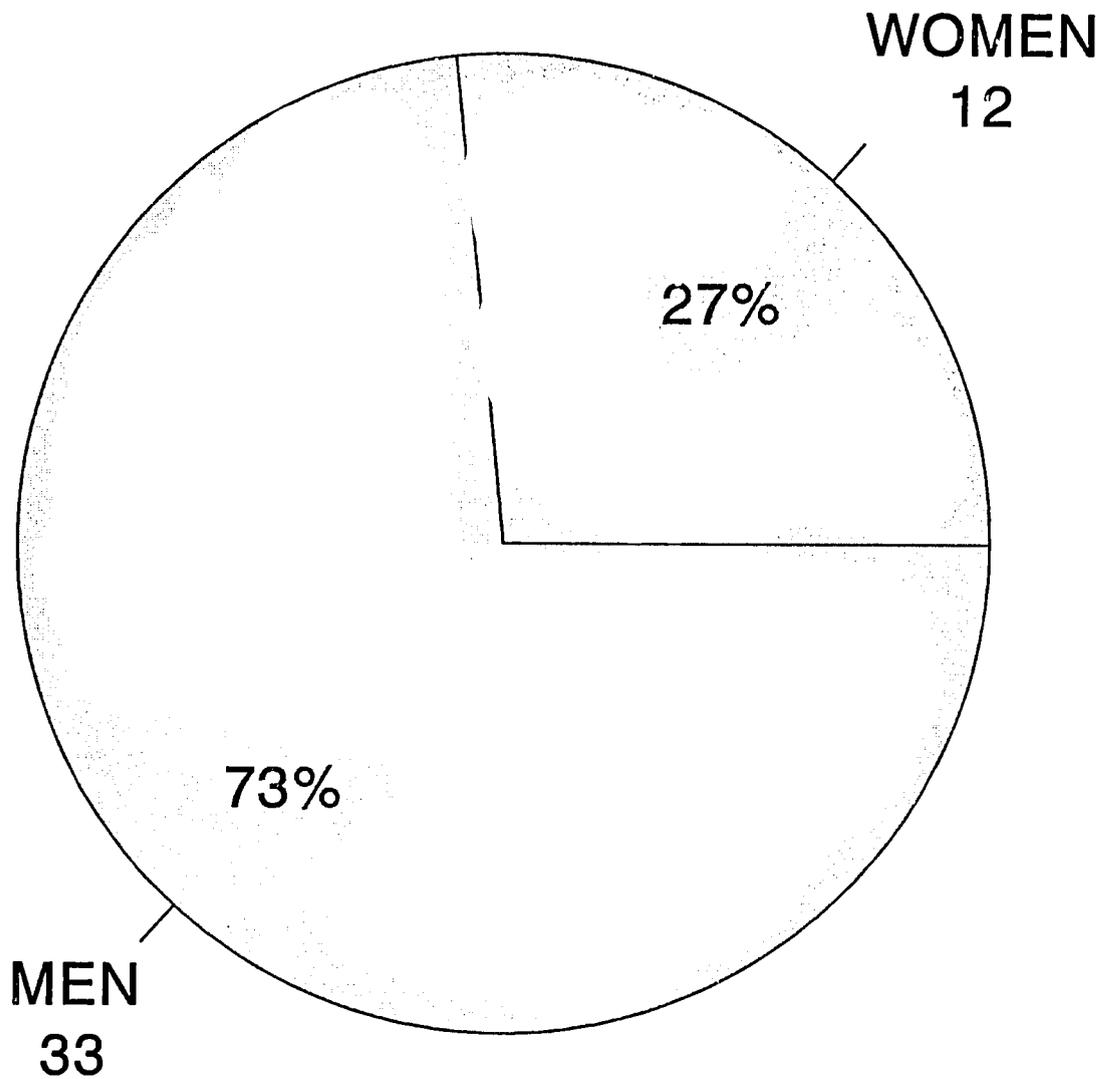
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# DISTRIBUTION OF SMUGGLERS BY SEX

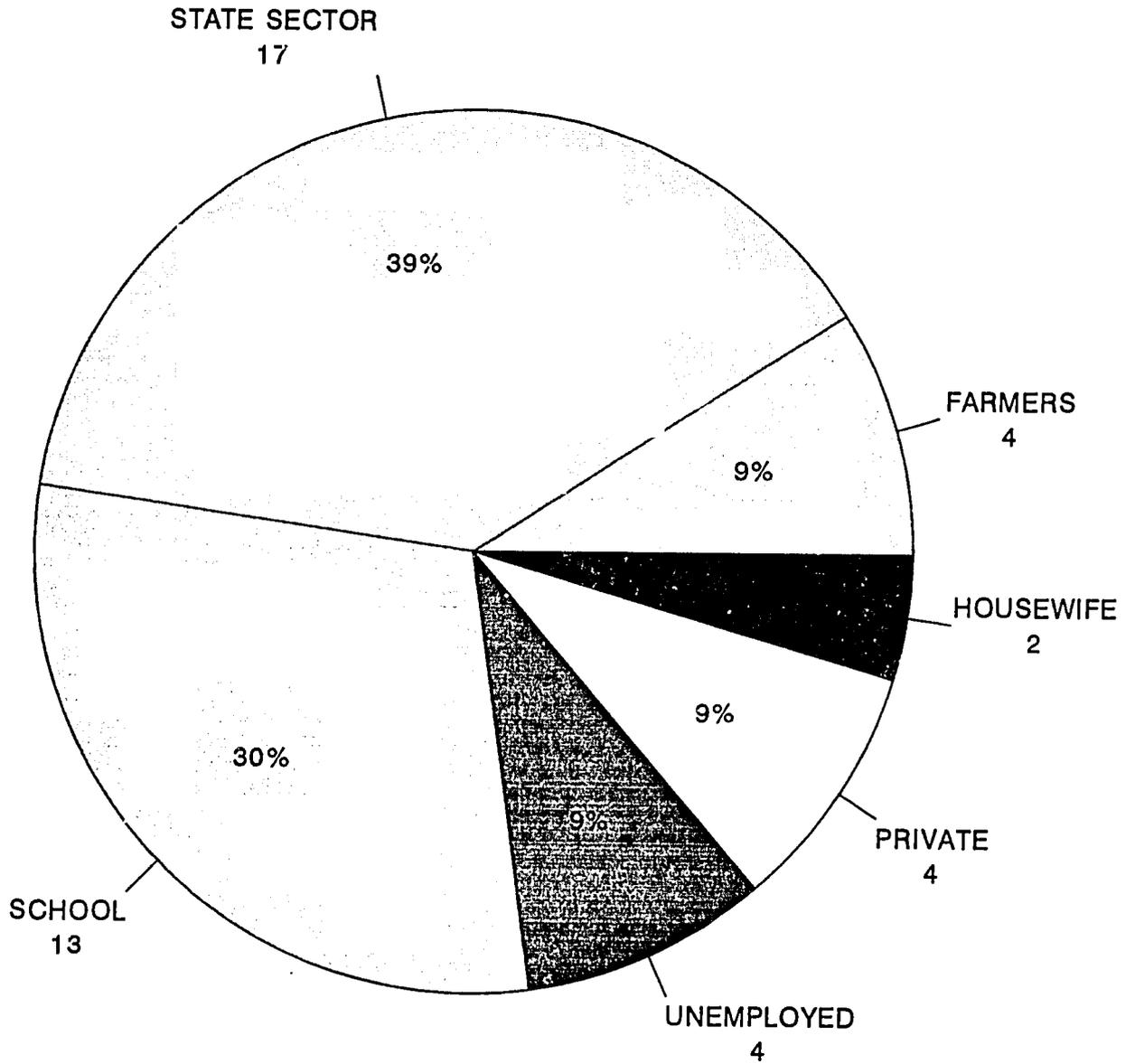
NUMBER OF OBSERVERS

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B-7  
RESPONDENTS OCCUPATION BEFORE UNDERTAKING SMUGGLING  
NUMBER OF OBSERVERS

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