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SHIFRINSON

14

ID	Doc Type	Document Description	No of Pages	Doc Date	Restrictions
150716	MEMO	TO NORMAN BAILEY RE. ROMANIA R 11/28/2017 M452/1	1	1/27/1982	B1
150717	MEMO	RE. ROMANIA [ATTACHED TO DOC. 150716] PAR 11/28/2017 M452/1	2	1/27/1982	B1
150714	MEMO	NORMAN BAILEY TO WILLIAM CLARK RE. CCC CREDIT FOR ROMANIA R 11/28/2017 M452/1	1	1/27/1982	B1
150715	MEMO	CLARK TO SECRETARY OF STATE, TREASURY, DEFENSE, ET AL, RE. CCC CREDIT FOR ROMANIA R 11/28/2017 M452/1	1	ND	B1
150719	LETTER	POPE JOHN PAUL II TO RR R 12/7/2016 M452/1	6	1/4/1982	B1

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NATIONAL SECURITY COUNCIL

January 22, 1982

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MEMORANDUM FOR WILLIAM P. CLARK

FROM: NORMAN A. BAILEY *NAB*
SUBJECT: Poland; the Carrot Part of the Carrot
and Stick

The President several times has expressed interest in offering Poland some kind of "Marshall Plan" for Poland if martial law were lifted, the political prisoners released and dialogue reopened with the Church and Solidarity. Interest in such an approach waned quickly when it was realized what the cost would be.

The attached paper (Tab I), developed jointly by John McClaughry of the OPD and myself, suggests a positive approach which would:

- (1) Have great propaganda value;
- (2) Cost the government very little (perhaps \$1-2 million); and
- (3) In the unlikely event of being accepted, would mean the beginning of the end of Marxism in Poland.

RECOMMENDATION:

That you place this plan or something similar on the NSC or NSPG agenda for discussion.

Approve _____ Disapprove _____

cc: Richard Pipes
Paula Dobriansky
William Stearman
Carnes Lord
Henry Nau

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January 22, 1981

A POSITIVE U.S. INITIATIVE FOR A FREE POLAND

"... a democratic-capitalist revolution in the communist world, perhaps of a gradualist kind, would do more than anything else to eliminate the threat of nuclear war."

- John Lenczowski, "A Foreign Policy for Reaganauts", Policy Review #18, Fall 1981.

I. Present Situation

Since December 13, 1981 Poland has been under martial law, which has precluded continuation of the activities of Solidarity and Rural Solidarity. The Polish economy is rapidly sinking due to non-cooperation of the workers and the general disruption.

The United States, in protest of the stifling of free association and reform in Poland, has announced sanctions against the Jaruzelski regime, including suspension of fishing and aviation rights, food shipments to the government, and further credit. NATO allies have been urged - without conspicuous success - to join in imposing sanctions against the Government of Poland. The President has expressed his strong personal support for the movement toward free association and political freedoms. He has called upon the regime to lift martial law, release the detained leadership of Solidarity, and initiate talks with Solidarity and the Church to develop a politically acceptable future for Poland.

The Polish foreign debt situation remains perilous. The Government of Poland owes some \$26 billion to the West, and it seems unlikely that scheduled - or even rescheduled - payments will be met, at least in the absence of Soviet subventions.

Poland's food situation remains critical. Government policies for many years have operated to depress agricultural energy and productivity, despite the regime's reluctant acquiescence in private ownership of 80% of the nation's farmland. State-controlled agricultural inputs have been lavished upon state collective farms, which habitually fail to produce. The state has fixed farm prices at low levels to win the support of urban consumers. Receipt of farm pensions has been made contingent upon deeding private plots to the State instead of to heirs.

Nonetheless, despite martial law the Government seems willing to recognize the necessity for adopting widespread economic reforms. Wladyslaw Baka, the chief economic reform official, stated in Trybunu Ludu in early January that a reform program built around modest progress toward worker self-management of independent enterprises is being developed. Stefan Olszowski, the PCP propaganda chief, has been promising the same thing, despite maintaining a hard line against political dissent.

While it is obviously necessary to pursue a strong diplomatic course aimed at focusing world opinion on the stifling of incipient liberties in Poland, and in making such acts as difficult and painful as possible for the governments of Poland and the USSR, the present situation also affords the United States and its allies a significant opportunity to take actions which, while overtly non-threatening to the respective governments, nonetheless promise both to improve the lot of the Polish people and undermine the strength of communism throughout the Eastern Bloc.

II. Recommended Policy

It will obviously be difficult to attempt any significant policy initiatives so long as martial law is in effect. However, it is recommended that a well-conceived strategy be developed, which can be implemented once martial law is relaxed or terminated.

The policy recommendation can be stated as follows:

In addition to implementing the present policy of the Administration from political, diplomatic, and national security perspectives, the Administration should develop a sound plan, consistent with the President's philosophical principles, aimed at subtly strengthening free market forces, private ownership of land, worker ownership and self-management of industry, decentralized economic (and ultimately political) decision-making, agricultural productivity, and ultimate integration of Poland into the relatively free market economies of the OECD.

The implementation of such a policy should proceed essentially independent of diplomatic and political pressure on the Jaruzelski regime. It should be made to appear dedicated to improving the well-being and standard of living of the Polish people, reducing their dependency upon both Western and Soviet credit.

It must also be made eloquently clear, through our International Communications Agency and through the many Western networks that reach the Polish people, that cooperation with this Reagan initiative holds promise for increased well-being (particularly in food) and increased opportunity for Polish

unions, associations, parishes and other mediating structures to shape the future of their country.

III. Supporting Arguments

a) The program is intended to be non-threatening to the Polish government, and indeed in large measure is compatible with many of the reform proposals now under discussion within the government itself. Such a program would move Poland closer to the Hungarian "New Economic Mechanism" than to an American model, but that is still a major step in the right direction.

b) The program is also intended to be non-threatening to the USSR, although Politburo theoreticians may well recognize in it the seeds of radical divergence from the Marxist command economy.

c) The program is based on President Reagan's oft-enunciated beliefs favoring the free marketplace, decentralized political and economic power, and strengthened private property ownership as the path to abundance and liberty.

d) The program is strongly rooted in Catholic social thought, notably the principles of personalism, subsidiarity and pluralism set forth in Quadregesimo Anno (1941) and Laborem Exercens (1981). The 1981 Encyclical, for example, states "A way toward that goal (of helping workers to share in ownership) could be found by associating labor with the ownership of capital, as far as possible, and by producing a wide range of intermediate bodies with economic, social and cultural purposes; they would be bodies enjoying real autonomy with regard to the public powers, pursuing their specific aims in honest collaboration with each other and in subordination to the demands of the common good, and they would be living communities both in form and in substance in the sense that the members of each body would be looked upon and treated as persons and encouraged to take an active part in the life of the body." (paragraph 14.)

e) The program is based on the fundamental human right of private property ownership set forth in the Universal Declaration of Human Rights (Article 17).

f) The program can be designed to maximize the use of private sector initiatives from the West, such as Sister Cities, the American Farm Bureau Federation, CARE, AT International, Catholic Relief Services, the Cooperative League of the USA, the AFL-CIO, the land grant colleges, small farm research centers, direct farm marketing networks, the Polish American Congress, etc., all of which could be coordinated as a special project of the President's Commission on Private Sector Initiatives.

g) The program could make effective use of surplus agricultural commodities to generate zloty balances, which can in turn be used (with Government approval) for numerous purposes in support of the program. Such use of zloty balances was strongly

encouraged by Congress in section 709 of the International Security and Development Cooperation Act of 1981.

h) To the extent that it assists the Polish people in increasing their productivity, and hence their capacity to earn hard currency through export sales, the program will cause the Polish debt problem to recede.

IV. Possible Program Items

Possible inclusions in the program are:

a) Technical assistance for the reprivatization of nationalized Polish industries, drawing upon the experience in British Columbia and Chile, and making use of innovative US financing techniques such as Employee Stock Ownership Plans (ESOPs).

b) Technical assistance for moving toward worker self-management, built upon American and British experience extensively studied by Cornell University and other US institutions.

c) Technical assistance in installing profit sharing plans, provided by the Council of Profit Sharing Industries and the Profit Sharing Research Foundation.

d) Technical assistance in teaching Polish bankers how to extend self-financing credit to decentralized independent enterprises, which as a result of a January 1981 decree will now be allowed to exist.

e) Technical assistance in the formation of genuine cooperatives - farmer, consumer, producer, and housing - drawing on the experience of the Cooperative League of the USA and affiliated organizations. (The present extensive system of cooperatives in Poland is now under state domination, but there are possibilities for moving it in the direction of the Basque Mondragon model.)

f) Technical assistance in improving the productivity of small farms, delivered through the USDA extension service, the land grant colleges, and US (and other) small farm centers and organizations (such as VIISA, Rodale Research Center, Graham Center, New Alchemy Institute, Land institute, etc.)

g) Technical assistance in direct farm marketing and community bartering, provided by the National Association of State Departments of Agriculture, the National Center for Citizen Involvement, etc.

h) Technical assistance in creating grassroots urban and rural credit unions, provided by the National Credit Union

Administration, USAID, the Japanese Hotokusha societies, etc.

i) Technical assistance in redesigning Poland's pension system, especially with respect to farm pension plans, provided by the US insurance industry, the Chilean Ministry of Finance, etc.

j) Provision of PL 480 food in a "food for development" program, already tested by AID in South Asia.

k) US support for the channeling of all future hard currency loans from such institutions as the UN Capital Development Fund to farmer- and worker-owned enterprises with responsible business plans, which enable productive workers to earn individual ownership shares and profits of their enterprises.

l) Mobilization and coordination of private sector humanitarian relief for the Polish people, working closely with Catholic Relief Services, the Polish American Congress, Friends of Solidarity, CARE, and other US organizations.

m) Communication of the humanitarian, non-threatening nature of this US program to the people of Poland through aggressive ICA broadcasting and through networks which extend into Poland, such as the Catholic church and organized labor.

V. Organization for Policy Development

It is proposed that the development of this program for presentation to the National Security Council and the President be undertaken by a relatively inconspicuous working group including:

National Security Council (Bailey, Dobriansky)
Office of Policy Development (McClaughry)
Treasury (Leland)
Labor (Stepp)
Agriculture (Perry, Bertrand)
State (Scanlon)
Private Sector Initiatives (Moorhead)
Office of Public Liaison (Burgess)
AID (Greenleaf)
ICA



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BAILEY

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(U) WORKERS IN COMMUNIST COUNTRIES:
CHALLENGE TO THE SYSTEM

Key Findings

A major study of worker-regime relations in communist states provides perspective on 1980-81 events in Poland by examining the changing role of labor there as well as in Czechoslovakia, Hungary, and the Soviet Union.^{1/} The study, completed before the imposition of martial law in Poland, notes that worker dissatisfaction in other East European communist countries likely would not follow the Polish course. More specifically, it makes these findings:

- Socioeconomic conditions are less important than differences of political history and expectations as determinants of the relative assertiveness of workers in Eastern Europe.
- Nevertheless, certain patterns affecting socioeconomic conditions evidently have influenced the perceptions of workers in all these states over the last two decades. Their experience under tightening economic

^{1/} This paper draws on the work of a group of University of Michigan sociologists and area experts headed by Zvi Gitelman. Their findings were summarized by Alex Pravda in a monograph, "Industrial Workers and Political Development in the Soviet Union and Eastern Europe." The study was commissioned by the National Council for Soviet and East European Research, which is supported by funds from the Departments of Defense and State, the Arms Control and Disarmament Agency, and the Central Intelligence Agency.

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conditions has sharpened their awareness of threats to their standard of living, and this has contributed to the rise of a more cohesive and assertive working class.

- Communist workers, despite government lip service to their exalted role in society, are experiencing a sense of negative class consciousness caused by decreasing social mobility and increasing feelings of being locked into their position in society. Concurrent with this perception, they have an image of society as sharply dichotomous, in terms of privileges and lifestyles. In the case of Polish workers, this perception has engendered a form of class consciousness replete with sentiments of social inequality and disadvantage.
- Communist workers nonetheless still manifest a degree of commitment to the prevailing system as long as it guarantees certain social and economic benefits.
- This social compact between workers and the regime is being eroded, however, by difficulties in delivering the expected services on the one hand and by rising expectations on the part of workers on the other hand. In fact, the problems associated with workers' demands are almost insoluble in the foreseeable future.
- These problems also may be aggravated by the sort of economic interdependence that has sprung up, in which the West may have played no small role in changing worker-regime relations. The need to export to the West has increased pressures on workers for greater productivity in a number of communist countries, notably Poland; and Western credits have delayed overdue economic reforms. Both developments have helped to change workers' perceptions and expectations concerning their regimes and have put strains on the social compact.

* * * * *

Is It the System or the Locale That Determines Change?

The study includes data dealing with the worker-regime relationship in various settings within each country--in society, the economy, the enterprise, and the national political arena. The findings suggest that variations occurred far more often between states than among any of these settings within a particular state. What set the Poles apart from the others in terms of the scope and frequency of blue-collar protest actions was differences in workers' expectations, previous patterns of assertiveness, and political management rather than social and economic conditions.

The relative quiescence of Hungarian workers in similar conditions derived from a different political experience and a government far more sensitive to workers' rights. Lack of assertiveness among Czech and Slovak workers seems to derive from relative social equality, stable economic development, and a degree of regime responsiveness to workers' needs. The lack of unrest among Soviet workers may be attributable largely to relatively low levels of social tension, ethnic and regional differences cutting across social cleavages, a greater degree of integration of workers within the enterprise, economic stability, and a rather high measure of blue-collar tolerance for repression.

Notwithstanding these country variations, there also have been significant common patterns in the changing role of workers in industrialized communist states over the last two decades. In particular, blue-collar workers' rising expectations have been coupled in the last decade or so with the emergence of a more cohesive, assertive generation of industrial workers intent on higher material rewards and greater control over their immediate environment.

A New Class Consciousness

Although communist dogma places workers at the apex of socialist society, they generally rank below the intelligentsia in consumption, education, power, and prestige. The social distance varies among the various countries--greater in Poland and less in the Soviet Union. But a homogenization of blue-collar ranks has also developed in these countries. Distinctions between skilled and unskilled workers have been blurred by a slowdown in social mobility, narrowing wage differences, and rising education levels.

Data from the study suggest that these developments have engendered in workers a feeling of being walled in and have contributed to status consciousness; that is, a notion of sharing similar material, educational, and power attributes. The question remains whether these perceptions are contributing to a social identity that could support collective protest action under certain circumstances.

Whatever the mix of factors affecting the outlook of workers, it appears that in Eastern Europe skilled workers in particular have a sharply divided picture of society with the privileged elite on one side and the mass of ordinary workers, among whom they include themselves, on the other. It is, however, only in Poland that the collective self-image of workers seems to have developed to any fullness. The repeated clashes of Polish workers with the authorities throughout the 1970s gave rise to a corporate labor consciousness associated with feelings of social inequality and disadvantage. Elsewhere, particularly in the Soviet Union, a much more fatalistic attitude still seems to prevail, although there are signs of an emerging working-class identity even there.

But the Bottom Line Is Economics

Whatever socio-psychological pressures may affect workers in these communist states, economic factors have remained the pivotal element determining their orientation toward the system. Full employment, low income differentials, stable food prices, and a welfare wage are the elements of a sort of social compact between workers and the system. Workers acquiesce in strong state controls as long as the regime's delivery of this security-welfare package is vouchsafed.

This social compact has come under increasing pressure, however, as changing economic conditions and rising workers' expectations have rendered its continued maintenance increasingly costly and precarious. Although events in Poland prior to the onset of martial law are the most vivid reminder of this phenomenon, strains upon the social compact in the other countries have also continued to grow.

For the last two decades all of the countries have experienced a shift in patterns of economic growth wherein once relatively cheap security-welfare benefits have become increasingly costly. Economies faced with a tightening manpower pool have found labor redundancies and high turnover rates associated with job security and full employment increasingly burdensome. Moreover, efforts to raise productivity by improving labor discipline and relating wages more closely to performance have tended to collide with expectations of a leisurely work pace and equal pay. At the same time, a commitment to stable prices of food and other basics has tended to swell budgetary subsidies to enormous proportions.

Strong worker attachment to the values of the social compact suggests no relief from these problems in the near- or mid-term future. Adding to their intractability is the circumstance that young workers seem to be no less attracted to social compact rights than their parents; indeed, they take them for granted. In fact, rather than substituting new values for the old, the younger generation has added expectations that place even more exacting demands on the socialist economy. The interesting jobs they want are not available in sufficient numbers, leading to growing dissatisfaction at the work place. Demands for higher wages and a better standard of living go unfulfilled, contributing to an acquisitive egalitarianism among younger workers that owes much to the officially sponsored consumption "kick" of the early 1970s.

Economic slowdown and recession have therefore only opened up a substantial gap in each of these countries between workers' expectations and economic performance. Although this consumption gap seems to have been widest in Poland and narrowest in the Soviet Union, it continues to place a strain on worker-regime relations throughout the region.

Workers as a Factor in Political Change

As events in Poland suggest, workers' perceptions of the legitimacy and performance of political authority are of fundamental importance in assessing the prospects for domestic tranquillity. For these perceptions, however, those socioeconomic attributes of the worker-regime relationship common to communist countries appear less important than a particular set of national experiences and circumstances. Hence, there is little reason to believe that economic conditions in Hungary, Czechoslovakia, or the Soviet Union similar to those in Poland would have replicated, at least in form and intensity, the Polish worker protest of 1980.

Finally, there is probably more than a kernel of truth in the Soviet belief that Poland's excessive economic dependence on the West was heavily responsible for the events of 1980. While the need for exporting to the West helped to intensify pressures for higher productivity and thereby strained the social compact, imports from the West helped to inflate workers' consumer expectations, and Western credits temporarily reduced the need for instituting the necessary economic reforms. In a more general sense, Western economic involvement may well have contributed throughout the region to the current transition in the role of labor in communist societies from a supporter of continuity to a force for change.

Prepared by Eric Willenz
x22225

Approved by E. Raymond Platig
x21342



Supply-Side Analytics

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CONTAINING POLAND'S GREAT DEPRESSION

By Alan Reynolds

In the late 1920's, Germany was busily repairing the damage of war and hyperinflation, borrowing heavily from the U.S. to build industry. The debts were manageable as long as Germany would sell goods here to acquire the dollars that would service the debt. But in 1929, the U.S. initiated a trade war that collapsed world commerce. In the squeeze, Germany led the spreading retrenchment, instituting an austerity plan that worsened rather than helped the economy, paving the way for Nazism. The contraction of international commerce contributed to the domino-like toppling of financial institutions, and what started out as a recession in the United States became the Great Depression.

In the Sixties and Seventies, Eastern Europe was busily repairing the damage of Stalinist centralization and isolation from the rest of the world. East-West trade was liberalized and Western investors poured resources into Eastern Europe in exchange for Eastern debt. The parallel with the 1920s is precise. For these debts to be managed, Eastern Europe has to be able to send goods West. But the United States, which has blundered into its second recession in two years, is not only squeezing East-West commerce by its slimmed appetite for goods. It also contemplates economic warfare against the Soviet bloc by applying financial pressure on Moscow *indirectly* via Poland. As in the 1920s, economic warfare is a dangerous game. While keeping an eye on M1B and the unending fiscal debate in Washington, the Polish economy is well worth watching too. As in Germany of 1929-33, seemingly localized economic moves in Poland could have domino political effects of the kind that lead to multiple contractions in the intricately integrated world economy.

January 27, 1982

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Supply-Side Analytics CONTAINING POLAND'S GREAT DEPRESSION

In 1970, the new regime of Edward Gierek in Poland, faced with economic stagnation in the nation of 35 million, moved to integrate Poland into the expanding global market. At times described as a capitalist riverboat gambler, Gierek opened up the economy with a series of domestic reforms that troubled Communist theoreticians in Moscow. His initiatives looked so promising that Western bankers, eyeing the disciplined, educated and skilled Polish workforce, seemed to thrust funds on Poland.

Gierek cut tax rates on personal incomes, tried in 1973 to decentralize economic planning, and got bankers rather than planners more involved in allocating capital. A third of Polish employment is private, and in 1976 there were additional initiatives toward small-scale capitalism, as reported by *The Economist* (January 1, 1977):

A new Polish law passed two weeks ago promises tax cuts and higher pensions and family allowances for the self-employed. It may also make it easier for them to get hold of raw materials and suitable office and shop accommodation. The Polish government has even invited outsiders, especially Poles living in the west, to open laundries, motels and other small businesses in Poland, promising that they can take their profits to the West.

At first, the Gierek reforms clearly worked. From 1970 to 1976, real GDP grew by 6.5% a year in Poland — faster than Japan. By the end of that period, according to World Bank data, real GNP per capita in Poland was close to Italy or Spain. Industrial output rose by 10.5% per year from 1971 through 1976, agricultural output also rose substantially before two bad crops in 1975 and 1976. Exports rose by almost 15% a year through 1976.

After the global recession of 1975, as Table 1 shows, industrial production's momentum slackened and by now there have already been three years of decline in real GNP, falling from about \$110 billion in 1978 to \$88 billion last year (in 1978 dollars). The inherent inefficiency of socialism is the usual explanation of this decline. Central planners simply imported too much, it is said, or the wrong industries were built. Or, the Western bankers got too greedy in pushing credit on Poland, expecting Moscow would always be there for a bailout.

On January 25, General Jaruzelski scratched his head over this puzzle in his address to Poland's Parliament:

How did it come about that a country that is potentially so rich as Poland found itself at the bottom of a humiliating and protracted crisis? Why have other countries of real socialism been able over the same years to achieve considerable progress while we were floundering in difficulties? The blunders and wrongdoings of the ruling teams are obvious.

Table 1

Poland's Austerity Program:
Changes in Industrial Production

1974	12.5%
1975	10.9
1976	9.3
1977	6.9
1978	4.9
1979	2.1
1980 ^e	-3.0
1981 ^e	-13.0

It may be obvious to Jaruzelski that "the blunders and wrongdoings" of Gierek were the source of the problem, which is why Gierek is in jail. But what were the blunders? Bureaucratic socialist inefficiency is no answer; Jaruzelski is right in that other Eastern bloc nations have advanced as Poland itself did earlier in the decade. All countries allocate some goods and resources by price, others by the queue or political priorities. Economic analysis applies to socialist as well as market economies, which after all are not polar opposites, but differ in degree. Poland's vast private employment is not much less as a percentage than some Western European nations.

Poland's debt crisis is not simply a matter of an insatiable appetite for Western imports. Imports were restrained after 1977, and the volume of debt did not rise relative to rising exports. The cost of servicing foreign debts instead rose mainly because interest rates went up. That symptom of declining confidence in Western currencies was not Poland's fault.

Investments in energy-gobbling industries eventually turned out to be a bad idea. But the largest increases in Poland's imports of Western machinery and equipment were in 1972-74, before the oil crisis or the later limit on Soviet shipments of cheap oil and gas. Again, an external surprise.

Two projects were started in 1976 and 1977 to expand Poland's vital copper exports. With the collapse of the U.S. housing and auto industries, which are important users of copper, world copper prices plummeted by nearly 50% after early 1980, devastating all copper exporters including Poland and Chile. If we accept the supply-side hypothesis that the United States has been the chief culprit in the shocks the world economy has sustained in the last decade — by its abandonment of the international monetary system — then certainly Poland has felt the shock as well. But there may be a double irony in the possibility that Gierek's gamble on Western credit and Western-style internal reforms — far more so than any other East-bloc economy — is why Poland has been squeezed far more than its neighbors in the latest U.S. monetary-inspired recession.

Not all of Poland's troubles are external, of course. In a confidential document offered to Western creditors last November, Polish officials revealed a misunderstanding of their nation's economic dilemma similar to the view of many American capitalists to the dilemma of the U.S. economy. Among the hypothetical new "reforms" discussed are "imposing taxes on units of the socialized economy," the "introduction of a special stabilization tax on industrial consumers," "imported goods will be taxed," and "a conception of taxation of the higher incomes is also being prepared."

As in the declining U.S. economy, social spending in Poland has also been climbing dramatically in the last two years. In an AFL-CIO type solution to the unemployment problem, Poland has introduced an early-retirement system ("vocational deactivation") for certain groups of workers, with paid leaves for mothers with small children. Social benefits rose to 20.5 percent of the state budget from 13 percent in 1979. From 1975 to 1980, social benefits had risen 113 percent, wages 72 percent and personal income from private sector employment, including agriculture, has risen only 54-55 percent. Obviously, even during the period of Solidarity's successes in expanding democratic freedoms, the Polish private sector has been crushed by economic forces.

Monetary disorder is almost surely the chief culprit. Poland's budget recently slipped into deficit, and the document says "the budget deficit will ultimately be covered by the issue of inflationary money." Yet Table 2 shows that the government has been printing a lot of currency long before the budget imbalance. Again an irony: Of all the Eastern bloc, Poland's farmers are the most free. But by being free they can not escape the zloty inflation, as they would in a commune where production, such as it is, is bartered for real goods.

Table 2

New Money Issue
(billion zlotys)

1970	58.6	1977	182.6
1971	67.3	1978	209.3
1972	78.2	1979	238.9
1973	96.3	1980	296.7
1974	117.2	1981 ^e	260.0
1975	141.2	1982 ^e	500.0
1976	164.0		

Polish officials acknowledge a consumer inflation rate of about 8%, and plan the same in the future, though an honest measure would be closer to 30% and rising. The exchange rate was recently lowered from 35.5 to 80 zlotys to the dollar, and the black market rate was about 500-to-1 in December and falling fast. The government's sanguine attitude toward devaluation further reduces the willingness to accept and hold zlotys, adding to inflation.

The demand for money is also being undermined in other ways. There have been discussions inside Poland about "currency reform," but that raises fears of a replay of 1950, when the Polish government likewise swapped old money for new, but in strictly limited quantities. Anticipation of that kind of "reform" acts like a 100% tax on added holdings of pre-reform currency, causing people to treat extra money like a hot potato. Zlotys are quickly swapped for goods or other currencies, raising inflation and sinking the actual exchange rate. The prospect of confiscatory "reform" also discourages added work or production in exchange for the suspect currency. The net effect is runaway inflation, collapsing production, especially in the private sector where wages can't be indexed, and a reversion to primitive local barter. If price controls are in force, as they are in Poland, these effects are greatly magnified. The country can more easily feed itself, given these circumstances, under communism, martial law, or state capitalism.

Why does Poland continue to pursue policies that destroy the money economy? Polish workers have long been encouraged to put money into low-interest savings accounts or bonds to finance state enterprises. The runaway inflation is a familiar device for defaulting on the Polish government's internal debt to the Polish people, an expropriation of their life savings. The resulting destruction of the monetary system, however, is no longer in anyone's real interest.

The solution to repressed inflation has always been to peg the currency to something acceptable, and to eliminate price controls. In 1921, Lenin alleviated a runaway inflation by simply legalizing the black market. Later, the Soviet ruble was eventually defined as a specific weight of gold. The black market European exchange rate between rubles and dollars has been quite stable for two decades, so Poland could stabilize the zloty by adjusting money creation to maintain a fixed exchange rate with either currency.

When Poland's workers ask for more money, they don't mean speeding-up the printing press. What they want is an increase in real, after-tax wages. The prolonged decline in labor effort reflects diminished incentives due to a rising tax burden and a collapsing currency. Poland's labor unrest is really an inarticulate tax revolt.

A socialized economy extracts disguised taxes largely by keeping prices up and wages down, thus generating profits from the near-monopoly of product and labor markets. The Polish state budget "used to absorb over 70 percent" of the difference between revenues and costs of state enterprises — a very high tax.

Deputy Prime Minister Rakowski says that martial law is "an umbrella for conducting necessary economic and social reforms." Yet genuine reform would, by definition, make things better, and would not have to be imposed by force. The government actually wants to raise prices much more than wages in order to raise profit margins of state enterprises, most of which go to pay for the government budget.

Quadrupling a few more consumer prices is intended to enable the government to finance more transfer payments, subsidies to inefficient enterprises, and the police state. It will not work.

Controlled prices do indeed produce shortages when monetary policy is blatantly inflationary, but arbitrarily raising the margin between consumer and producer prices would just be a further increase in an already destructive tax on labor. Controlled consumer prices have already been rising 8% faster than producer prices for several years. Poland is on the wrong side of the Laffer curve, and has no viable choice but to repair incentives and stabilize the currency.

The orthodox solution to painful economic mismanagement, however, is a larger dose of pain — cut demand. Felix Rohatyn thus writes that “the level of austerity and sacrifice that would have to be imposed on Poland as part of any new credits would be drastic . . . and the life of the Polish people might be very much harsher than in recent years,” (*The New York Times*, January 11, 1982).

When a country is “living beyond its means,” it has to either raise its means (produce more) or lower its living (consume less). In a relatively modern economy, like Poland, the option of retrenchment is severely limited. Cutting critical imports of equipment and raw materials, for example, can have a disproportionate effect in reducing the ability to produce and export. The trade imbalance gets even worse, and the burden of debt rises relative to the smaller economy.

In the first nine months of last year, Poland cut Western imports of cotton by more than a third; Polish production and export of cotton fabrics obviously declined. Imports of hides were slashed, but so were exports of shoes. A television factory operates at 20% of capacity because it lacks some imported components. More of this kind of belt tightening will not help.

* * * *

The role of commercial banks and the function of bankruptcy appear widely misunderstood. First of all, U.S. banks hold only about 15% of the total bank loans to Eastern Europe, about 9% of the loans to Poland. There has been virtually no increase in U.S. bank loans to Poland since 1976. Commercial banks in Western Europe were often under pressure from their governments to expand loans to Eastern Europe, but they too have stopped lending to Poland.

Poland owes twice as much to U.S. taxpayers as it does to U.S. commercial banks. There were \$1.9 billion in guaranteed loans from Eximbank and C.C.C. even before the U.S. guaranteed another \$670 million in food credits last year. A Polish default could cost Americans well over \$2 billion in added debt or taxes. Losses to bank stockholders would likewise reduce the nation's real wealth, though the loans are too spread around to actually close any major bank.

“The United States,” says Felix Rohatyn, “can declare the Polish debt in default and refuse to participate in new refinancing plans.” It should, he says, even use this “weapon of capital” on all other satellites. If the U.S. government does not want to be repaid, that would make it easier for the international banks to get their money. It might even lower Poland's debt service costs enough to enable them to get new credit from some other part of the world. Lenders are rarely in good position to threaten weak borrowers, and insisting on the impossible is not the way that skilled bankers salvage dubious loans.

As in the case of Germany in 1929, Western debts to Eastern Europe could not be repaid if the West closes all means of continuing to receive their goods, including trade financing. In that case, the goods already sent to the Soviet bloc would become gifts. The prohibitive tariffs the U.S. still imposes on most of the Soviet bloc contribute to the problem. Unsuccessful U.S. efforts to keep the Soviets from selling more natural gas to Western Europe would have likewise made it even harder for the West to get anything valuable in exchange for Soviet IOUs.

In 1979, the C.I.A. warned that Western Europe might not get enough oil from the Soviet Union. Now, the worry is that Western Europe might get too much natural gas from the Soviet Union. William Safire explains that "a threat of cutoff of the new Kremlin natural gas pipeline would force Europe to its knees." This risk seems remote. West Europeans could hold extra reserves, set aside spare capacity in Holland and the North Sea, and make sure that industry could easily be switched from gas to oil. The Soviets would stand to lose much more from the temporary loss of hard currency and from the permanent loss of their reliability as energy exporters. More energy from more sources is generally less dangerous than less energy from fewer sources.

It is possible to tighten-up on Western exports of technology that might benefit the Soviet military without greatly shrinking the whole market. U.S. exports of computer technology to Poland, for example, amounted to only \$138,000 in 1977, \$151,000 in 1978 — a little more than one tenth of one percent of total U.S. exports to Poland. U.S. exports to Poland have been mainly grain, oil, seeds, raw textile fibers, hides and fats. Imports from Poland were meat, clothing, metalworking machinery, coal, steel, footwear and organic chemicals.

Conservative intellectuals have expressed dismay at President Reagan's relative mildness in imposing sanctions. The *Wall Street Journal* joined Rohatyn's call for an official U.S. statement of Polish bankruptcy. Columnist George Will denounces those who put "commerce" above the fight against "Communism." The neoconservatives seem ready to launch all-out economic warfare against the Soviet bloc, and there are even those who refuse to engage in hypothetical conversations on how Poland might pull itself together — so intently do they see this as an opportunity to force democratic reforms on Eastern Europe and even Russia via the economic collapse of Poland.

Economic warfare could only damage the East more than the United States, though, if all the West joined together against the Socialist bloc, which of course is not going to happen. As Napoleon discovered in his attempt to starve England into submission, as long as England could trade with one continental power, it wound up trading with them all, even France itself via the middlemen.

A U.S. grain embargo, reimposed, would only reignite the Argentina boom, and is not in the cards as long as President Reagan is in office. It was Reagan who said instantly upon learning that President Carter had imposed the embargo of January 1980: "We're shooting ourselves in the foot."

One common argument is that deeper economic collapse in Poland would force the Soviets to cut back on military spending in order to feed the Poles and repay their debts. Stansfield Turner, for

example, argues that “a greater orientation toward market forces . . . can be achieved only under severe economic pressures.” But the notion that catastrophe promotes improved policy is historically weak. The fact is that the Polish economy will work better even under martial law if some of the so-called Western influences are removed, especially the currency inflation. And as Citibank’s Walter Wriston observed in his *Face the Nation* appearance January 24, the Soviets are closer than ever to something Russia has wanted for centuries — persuading Poland that Russia is its only friend.

Poland could work its way out of the more acute symptoms of social and economic collapse, either through greater regimentation or liberalization. There are signs the Polish government does not yet grasp the nature of its policy failure, though, and is contemplating imposition of even greater disincentives, perhaps a greater inflation. Western reactions could make difficult a constructive solution, in any case, forcing Poland into helpless dependency on the Soviet Union. History suggests that economic warfare is not a substitute for shooting war. It only prepares the way.

* * *

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THE DIRECTOR OF CENTRAL INTELLIGENCE

WASHINGTON, D. C. 20505

27 January 1982

National Intelligence Officers

MEMORANDUM FOR: Dr. Norman A. Bailey
National Security Council

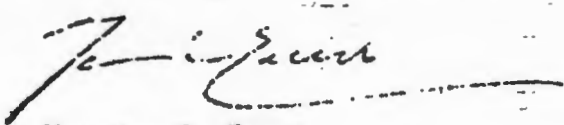
FROM: Maurice C. Ernst
National Intelligence Officer for Economics, CIA

SUBJECT: Romania's Balance of Payments and Debt Problems

As per your request, attached is some material on Romania's balance of payments and debt problems. Romania clearly is unable to meet its financial obligations. To do so would require cuts in imports so severe as to force substantial declines in industrial production, such as occurred in Poland. The Romanians have already squeezed all the consumer goods they can out of the economy, and this has occasioned some sporadic unrest.

The receipt of a \$65 million CCC credit would fill only a small part of the balance of payments gap. They would probably use such a credit to free up foreign exchange with which to pay interest on debt and perhaps repay those creditors they cannot put off.

The prospects of such a credit being repaid would be poor. There is little chance that the Romanian economy will substantially turn around in the next two or three years, and next to no chance it will generate large new sources of foreign exchange earnings. Their oil fields, traditionally a large source of hard currency earnings, are at a late stage of development and declines in production are probably inevitable. Romania hopes to further diversify its hard currency exports, but has had little success to date.


Maurice C. Ernst

Attachment,
As stated

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NLRR M452/1 #150716

BY fu NARA DATE 11/28/16

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~~NO DISSEMINATION~~

150717

26

27 January 1982

MEMORANDUM FOR: National Intelligence Officer for Economics

FROM:



EUR/EE/SE

EO 13526 3.5(c)

SUBJECT:

Romanian Difficulties in Meeting
Debt-Service Obligations

1. Romania will continue to have difficulties in meeting debt service obligations on its estimated hard currency debt of \$10 billion. Bucharest has placed its needs for 1982 at \$4.5 billion, including \$2 billion in principal on medium- and long-term debts, a \$.5 billion current account deficit, \$.5 billion for short-term credits, \$.3 for building up reserves and extending credits, and \$1.2 billion in arrearages from 1981. Projected sources of finance fall far short of needs. Bucharest hopes to secure approximately \$2.45 billion, consisting of \$.75 from the IMF and World Bank, \$1.2 billion in supplier credits, and \$.5 billion from "other sources" (probably a balance of payments loan from Arab financial institutions). The financial gap could prove to be even larger than the \$2.05 billion presented by Bucharest. Holding the current account deficit to just \$.5 billion will be difficult as Bucharest encountered serious domestic problems in slashing the 1980 current account deficit of \$2.4 billion by \$1 billion last year. Furthermore, supplier credits may not be as readily available until the arrearages are cleared up.

2. Rescheduling is currently under way with Western bankers, but reaching an agreement will be difficult. Bankers so far have offered to reschedule only \$1.5 billion of the amounts due this year with the condition that government debts be rescheduled too. Bucharest desires to reschedule everything due this year--including the arrearages--plus debts due through 1984.

3. Romania faces hard times even if rescheduling takes place. Its principal hard currency exports are hindered by the soft world market for petroleum products and by a second consecutive poor performance in the agricultural sector.

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NLR M45211 #150717

BY RW NARA DATE 11/28/17

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~~NO DISSEMINATION~~

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SUBJECT: Romanian Difficulties in Meeting
Debt-Service Obligations

Bucharest continues to push food exports despite the severe shortages at home. Most nonessential imports have been cut and import reductions are now affecting needed raw materials. Further cuts in imports will have negative repercussions for domestic growth and already low living standards.



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MEMORANDUM

324

NATIONAL SECURITY COUNCIL

January 27, 1982

~~CONFIDENTIAL~~

ACTION

MEMORANDUM FOR WILLIAM P. CLARK

FROM: NORMAN A. BAILEY *NB*
SUBJECT: CCC Credit for Romania

In accordance with your instructions, I have prepared a memorandum (Tab I) from you to the appropriate department heads opposing the granting of CCC credits to Romania on grounds that Romania cannot pay (Tab II -- CIA report) and that, in any case, granting the loan at this time would send the wrong signals.

RECOMMENDATION:

That you sign the memorandum to the department heads at Tab I.

Approve _____ Disapprove _____

cc: Richard Pipes
William Stearman
Paula Dobriansky
Henry Nau

Attachments

Tab I Memo to Department Heads for Your Signature
Tab II CIA Report

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Review January 27, 1988

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NLRR M4521 #150714

BY *RW* NARA DATE 11/28/17

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WASHINGTON

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MEMORANDUM FOR THE SECRETARY OF STATE
THE SECRETARY OF THE TREASURY
THE SECRETARY OF DEFENSE
THE SECRETARY OF AGRICULTURE
THE DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET
THE DIRECTOR OF CENTRAL INTELLIGENCE

SUBJECT: CCC Credit for Romania

The Commodity Credit Corporation has under consideration a \$65,000,000 loan to Romania for the purchase of corn and soybean meal.

It is well known that Romania is in serious financial difficulty, primarily because of mismanagement. It is the best judgment of the CIA, Treasury and OMB that Romania is unlikely to be able to repay this loan.

Although it is true that Romania has exhibited some degree of foreign policy independence from the Soviet Union, it is internally one of the most repressive of Soviet Bloc governments. Thus, granting this loan at this time would not only be bad business but would also send the wrong signals to the USSR and to other countries with reference to our current posture vis-a-vis the Soviet Bloc.

FOR THE PRESIDENT:

William P. Clark

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Review January 27, 1988

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NLRR M452/1 #150715
BY RW NARA DATE 11/28/17

RECEIVED 29 JAN 82 14

TO PRES FROM POPE JOHN PAUL II DOCDATE 04 JAN 82
BREMER 28 JAN 82

KEYWORDS: VATICAN
POLAND

HS

SUSPENSE

SUBJECT: RESPONSES TO PRES LTRS TO POPE RE POLAND & US GOVT POLICIES

ACTION: PENDING STATE RECOMMENDATIONS DUE: 06 FEB 82 STATUS D FILES

FOR ACTION

FOR CONCURRENCE

FOR INFO

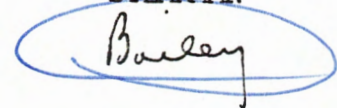
STATE

CLEVELAND

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COMMENTS

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ACTION OFFICER (S) ASSIGNED ACTION REQUIRED DUE COPIES TO

DISPATCH _____ W/ATTCH FILE _____ (C)



DEPARTMENT OF STATE

Washington, D.C. 20520

January 28, 1982

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rw 1/14/82
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*cc: 6715
7378*

MEMORANDUM FOR: Mr. Michael O. Wheeler
NATIONAL SECURITY COUNCIL

SUBJECT: Alerting NSC on Presidential
Correspondence

Enclosed is a copy of a letter to President Reagan from Pope John Paul II, Vatican Office which is transmitted for your information.

This document was received in the Executive Secretariat Information Management Section on January 27, 1982 at 9:56 p.m.

Charles L. Jackson Jr., for
Director, S/S-1
Information Management Section
Executive Secretariat
ext. 23836

UNCLASSIFIED UPON REMOVAL
OF CLASSIFIED ENCLOSURE(S)

DEPARTMENT OF STATE TRANSMITTAL SLIP		CLASSIFICATION <i>rw</i> SECRET /NODIS <i>11/4/13</i>
		DATE Jan. 6, 1982
TO Dept. of State <i>S/S-I</i>		For the Attention of EUR/WE J. Decker
FROM AmEmbassy Rome - Vatican Office		
TO THE FOREIGN SERVICE		TO THE DEPARTMENT
☐ For transmittal to Addressee at the Discretion of Post ☐ Post Information Only ☐ Transmit to Foreign Office ☐ Submit Report ☐ Reply to the Individual		☐ Dept. Information Only ☐ CERP Publications ☐ Enclosure to Previous Airgram ☐ Reply to Department Request
☐ Transmit to: ☐ Inform:		(U. S. Agency)
REFERENCE Letter from Pope John Paul II to President Reagan, dated January 4, 1982		
ITEMS/REMARKS Please transmit enclosed letter to the President at White House. Also it should be handled as SECRET/NODIS . <i>NO</i> <i>Conf. 1/6/86. Exempt</i>		
IN REPLY REFER TO FILE NUMBER AND DRAFTING OFFICE		
FILE NO.	SIGNATURE <i>Ronald Reagan</i>	
CLASSIFICATION SECRET /NODIS	OFFICE VATICAN OFFICE	

~~CONFIDENTIAL~~

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To the Honorable
Ronald Reagan
President of the United States of America

I thank you warmly for the letters of December 17 and 29 that you kindly addressed to me with reference to the latest events in Poland - events sad beyond measure. In your letter of December 17 you emphasized the serious internal developments in the country, and in your letter of December 29 you informed me about the policy of the American Government, with special reference to the responsibility of the Soviet Union and concerning the measures enacted by your Government. Both of these letters testify to the fact that it is a question of extreme importance not only for the good of one country - and that country is my homeland! - but because it calls into question the fundamental principles of the life and coexistence of the nations in the modern world. These principles have reference to the inviolable rights of man and the no less sacred rights of each individual nation as such. The Apostolic See proclaims them constantly and frequently recalls them, from the conviction that the interior tranquility of nations and true peace in the world largely depend upon their being respected. Upon these principles is based the very legitimacy of

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GDS 1/6/88

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NLRR M4521 #150719

BY PW NARA DATE 12/1/16

public authority, as my predecessor John XXIII said in his Encyclical Pacem in Terris (April 11, 1963), and as I too have had occasion to point out, in my address to the United Nations Assembly on October 2, 1979.

Allowing myself to be guided by these principles, on December 18 I addressed a message to the Polish Prime Minister, General Jaruzelski - a message that you are acquainted with and which has been communicated to the Governments which are signatories of the Helsinki Final Act - asking that martial law be lifted and that there be a return to the difficult but not impracticable path of dialogue between the Government and the social groups. I deliberately made my appeal known to the Primate of Poland, Archbishop Glemp, and to Mr. Lech Wałęsa, the leader of Solidarność.

For its part, the Polish Episcopate from the very first days has publicly and repeatedly called for the ending of martial law, the freeing of the prisoners and the resumption of dialogue with the Union. This reflects the mission of the Catholic Church, not only because she is profoundly involved in the history and reality of national life but also because she cannot keep silent and must duly bear witness when human rights and fundamental freedoms are violated, especially in such a radical way.

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This taking up of a moral position will not be merely momentary, and it is an internal and international fact that cannot fail to be significant also for those who intend to limit themselves to examining the facts only, and not feelings. It demonstrates that, in the sad happenings in Poland, it is not political interests that are involved but moral values, and precisely those values which are at the basis of human society worthy of that name.

It is therefore natural, and profoundly just, that in its painful experiences the Polish Nation should find solidarity on the part of all the nations and peoples that are rightly anxious that these fundamental principles should be introduced into and safeguarded in social and international life. And it is equally understandable that those who are most involved and who most directly share in the drama of Poland are in the first place the peoples of Europe, those with a European tradition and special European links - those who are closest in outlook, history and culture. I appreciate all the efforts at concrete assistance, especially at the humanitarian level and in providing food. Initiatives from various sources have been conducted in this regard in order to alleviate the sufferings of the Polish people. The solidarity expressed by individuals, social groups and peoples is certainly the very same that inspires the attitudes assumed by many Governments, like your own, on the international level - attitudes which are not directed against the life and development of Poland, but which intend to support her people's aspiration for freedom.

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.. This common action among all peoples that have moral values at heart is supported by the Holy See in the sphere of its competence and in a manner corresponding to its mission, which does not have a political character. The Holy See has stated this to the Governments that have consulted it, and also to those Governments with which, on this occasion too, it has seen fit to maintain close contacts.

For almost two hundred years my fellow-countrymen have been engaged in a dramatic struggle for the right to their own life in a free and independent homeland, a life in harmony with the fundamental rights of individuals and peoples. These rights are particularly dear to the Polish soul, as is witnessed to by the thousand-year-old history of the national culture. At the end of the eighteenth century, Poland became the prey of the States on her borders, and these latter deprived her of political independence. This deprivation intensified still further the many efforts repeatedly made to recover the sovereign existence of the State, and this was finally obtained only in 1918, at the end of the First World War. The aggression that engulfed the Polish Republic in 1939 caused the outbreak of the Second World War, during which the Polish people endured terrible sacrifices. She fought on almost all the fronts, confident that this blood-soaked struggle (six million of its citizens died, either in action or in the extermination camps!) would morally oblige the civilized world, and in the first place, the Allies, to ensure the independent existence of the Nation.

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In fact, from the very beginning of the War the Western Allies - who were later joined by the United States of America - had committed themselves to restoring the integrity, sovereignty and independence of Poland and the free determination of her people. This commitment preserves its relevance because it corresponds to a profound exigency for freedom.

The events of August 1980 are in a certain sense a continuation of what already took place in Poland in the years 1956, 1968, 1970 and 1976. This process confirms the just aspirations of the workers and, together with them, the whole of Polish society, that the fundamental rights of the individual and of the nation should be respected. The Poles - both the workers and the intellectuals - demand to be responsible subjects in the life of their own homeland. They want to decide upon the forms of social, economic and cultural life, not having hostility to anyone, but equally asking that their own sovereignty be respected.

Mr. President, I thank you once again for your letters, and for everything you are doing in international life for the purpose of ensuring the rights of Poland. I express my hope that such an important cause and ideal will not cease to maintain a lively and effective sentiment of responsibility in all countries, and especially in those countries which are more intimately linked to the Polish Nation for reasons of geographical or ethnic closeness, of historical affinity and experience, or of common spiritual descent.

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I ask you to accept my heartfelt good wishes at this season, and pray the Lord that the New Year will bring peace to the great American Nation and to all the peoples of the world, and serenity and well-being to all humanity.

From the Vatican, January 4, 1982

Joannes Paulus P. II

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