USSR, EASTERN EUROPE, AND CHINA: OUTLOOK FOR GROWTH AND CURRENT ACCOUNT BALANCES

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USSR

At the end of the first year of the Eleventh Five-Year Plan period (1981-85), the Soviet economy was beset with serious problems. Soviet GNP grew approximately 2 percent last year, the third consecutive year with growth at 2 percent or less. Soviet industry experienced its worst performance in the postwar period; industrial output in 1981 grew about 2 percent. At the same time, overall farm output was some 10 percent below that attained in 1978, the last peak year for agricultural output. Most significantly, the Soviets experienced their third consecutive poor grain harvest in 1981. Because record amounts of agricultural commodities had to be imported, Moscow's hard currency position deteriorated. Persistent food shortages, together with increased prices for luxury goods, left many Soviet consumers with less on their tables in 1981 and less in their pockets. 25X1

The response of the Soviet leadership to growing economic difficulties has been cautious and conservative. The Supreme Soviet ratified a revision of the 11th Five-Year Plan last November that made few changes in the original goals approved a year ago. Despite current problems in agriculture and industry, most of the reduced output goals still fall within the range of the original 1981-85 targets--though nearer the lower end. Many of these targets are clearly unattainable. The one action taken in the direction of more realistic planning was the scaling back of planned investment expenditures by some 4 percent, probably to make the 1981-85 plan consistent with available investment resources. Hampered by investment cutbacks and labor supply constraints, Soviet planners are counting on productivity gains, with some assistance from resource conservation efforts, to provide practically all of the growth in agricultural and industrial output in the current five-year plan. Labor productivity growth continues to slide, however, and no new measures likely to be effective have been suggested by the leadership to reverse the trend. 25X1

After building up a substantial foreign exchange cushion in the previous two years, the USSR was hit in 1981 by a soaring agricultural import bill and soft oil prices in its Western markets. As a result, the hard currency trade deficit reached an estimated $6 billion, more than double the 1980 deficit. The current account (excluding arms sales) was in deficit to the tune of $4.2 billion, up from $500 million in 1980. We expect continued large agricultural imports and little or no growth in exports to result in another large trade deficit in 1982. Moreover, the Soviet payments position probably will continue to deteriorate over the next several years as domestic oil requirements run ahead of increments to production and export availability falls. 25X1

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Bulgaria

Bulgarian economic performance rebounded somewhat in 1981, and GNP rose by about 3 percent, in comparison with a small absolute decline in 1980. The key factor was the agricultural sector, as grain output--down sharply in 1980--approached record-setting levels. According to official statistics, industrial production grew at a rate of 6 percent during the first nine months of 1981 with all sectors except construction and mining meeting plan targets. Nevertheless, in the medium term, growth rates are likely to decline because of chronic problems with labor scarcity, sluggish labor productivity, and inefficient central economic planning. Growing Soviet reluctance to supply Sofia's increasing needs for raw materials and energy may further impede growth in the next few years. The 1981-85 plan targets confirm the outlook for slower growth and indicate a continued emphasis on heavy industry, although the consumer sector reportedly will receive more attention than in the past.

In 1981 Bulgaria is expected to register a trade surplus of $400 million--a $700 million deterioration compared with the $1.1 billion surplus in 1980. This primarily results from a deterioration in Sofia's terms of trade with the other socialist countries. Sofia's balance of payments position will become a more critical constraint in the next few years since it will become more difficult to maintain its present trade surplus with the West. Hard currency imports will have to increase to compensate for the expected reduction in future deliveries of raw materials and energy from the USSR.

Czechoslovakia

In 1981, real GNP rose by less than 1 percent as the economy continued to be plagued by lagging labor productivity, energy shortfalls, and transportation bottlenecks. Zero growth is likely in 1982 and prospects are poor for any significant improvement in the domestic economic situtation over the next few years. Recognition of their domestic and external constraints led Prague to adopt sharply reduced economic goals for 1982. The regime hopes that the "Set of Measures," implemented at the beginning of 1981, will increase productivity, but these reforms, so far, appear to be working poorly and will not have much of an impact.

Czechoslovakia ran a small hard currency current account deficit in 1981 and will run another deficit of about $300 million next year. The country needs Western technology to spur productivity, but the regime's conservative borrowing and investment policies have kept trade with the West at a modest level and will keep hard currency trade in rough balance in 1982. Trade with CEMA as a percentage of total trade is expected to rise. Reduction of Soviet exports of energy and possibly of other raw materials could force Prague into heavier reliance on the West. But prospects for a substantial increase in exports of Czech manufactured goods to earn the needed additional hard currency are not good.

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East Germany

While East German growth rates have slowed in recent years, the GDR is still outpacing most other East European economies. In 1981 real GNP grew an estimated 2.6 percent, similar to the previous year, but in 1982 real GNP is expected to grow by only 2 percent. Production was affected by problems with lagging productivity growth and by the loss of key imports from Poland--particularly coal and sulfur. These problems, combined with a worsening balance of payments position and rapidly rising debt, will probably lead to slower growth during the next few years.

Trade with the West--particularly with West Germany--is vital to the East German economy and receives increasing high level attention. But in spite of East Germany's continuing efforts to increase exports, the hard currency trade deficit widened to $1.5 billion in 1981. Hard currency debt grew to over $12 billion in 1981--second only to that of Poland in Eastern Europe. East Germany's hard currency current account could even deteriorate further in 1982, especially if Western demand remains sluggish and if announced limitations on Soviet exports of raw materials to the GDR as well as the Polish crisis force the country to turn more toward world markets. On the bright side, West German Chancellor Schmidt agreed in December to an extension of the "swing credit," essentially an interest-free West German credit. It is unlikely, however, to lead to substantially increased trade with West Germany.

Hungary

A disappointing year in agriculture combined with continued concern over the external accounts held economic growth in 1981 to 1 percent. The growth of real GNP in 1982 should remain about the same, in large measure because of the regime's austerity program aimed at restoring external financial equilibrium. Industrial production should rise only slightly in 1982, while agricultural output may rebound from lower than expected grain production in 1981. Continued emphasis for the next few years on maintaining balance in the external accounts will hold down both economic growth and improvements in living standards. Hungarian efforts to foster efficiency through increased use of profitability criteria and expanded enterprise autonomy will have little impact on economic growth. These measures, however, may enhance international competitiveness. To date, though, implementation of the reforms has been slow, in large part because of bureucratic resistance to change.

Hungary's hard currency current account was in deficit by $0.6 billion in 1981 and is likely to improve only slightly in 1982. Continued economic austerity should enable Budapest to keep its current account under control for the next few years. Admission to the IMF in 1982 will provide a financial safety net against unexpected shocks.

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Poland

Poland's economic crisis deepened in 1981. GNP dropped at least 14 percent in 1981 compared with 1980 and industrial output fell by more than 13 percent--mainly because of shortages of imported and domestic raw materials, shorter working hours, work stoppages, and greater absenteeism. The one bright spot in the Polish economy in 1981 was agriculture, where the grain and most nongrain harvests were favorabe. Nevertheless, Poland will still experience shortages of many basic foods, especially meat, in the state marketing system in 1982, due to continued production shortfalls of some goods, excess demand and hoarding.

Before the imposition of martial low, Warsaw did not expect economic performance to improve in 1982. National income had been scheduled to decrease again, and industrial production was to stagnate. Now, even with the impositon of stricter controls including the return of the six-day workweek, output may fall below plan at least for the next few months if workers decide to slow down production to register their unhappiness over martial law. Beyond 1982, even the most optimistic Polish projections indicate that 1978 levels of economic activity cannot be reached for a number of years. The imposition of martial law, continuing worker resistance and uncertainty about the financial situation make it difficult to forecast trends in output and the external accounts in 1982.

Poland ran an $800 million deficit in 1981, which would have been much larger had Warsaw been allowed to finance its desired level of imports. Before the declaration of martial law, trade was expected to be in balance in 1982, largely for the same reason. Debt relief agreed upon by Western governments and commercial banks for 1981 covered much of Warsaw's 1981 debt-service payments, eventhough a formal agreement on rescheduling non-guaranteed debt has not yet been signed. A substantial amount of new credits also was granted to cover unrescheduled debt service and to finance the trade deficit. Negotiations on rescheduling private and government debt and on new credits for 1982 have not yet started, and martial law has increased uncertainty.

Romania

Romanian GNP in 1980-81 grew at less than half the annual rate recorded in the 1970s. In 1981 the increase was only 2.5 percent. Industrial production remained sluggish, with severe lags behind plan in the extractive industries, chemicals, transportation, and machine building. Agricultural output rebounded little if at all from the sharp decline in 1980, in part because of a late summer drought but also because of pervasive inefficiency, reflecting years of neglect of the farm sector by Bucharest. Consumers bore much of the burden of the economic slowdown, with living standards stagnating--at best. Continued shortages finally forced the regime to institute a rationing program for some foods. Prospects for reversing the slowdown are poor. The recently issued 1982 plan set many growth targets below those in the 1981 plan, but these latest goals are still unrealistically high. Some minor concessions were granted to agriculture but the emphasis still remains on development of the industrial sector.

Romania's current account deficit declined from $2.4 billion in 1980 to $2.0 billion in 1981. Severe hard currency difficulties will remain, however, for the next few years, in part because of the need to import large amounts of oil. Exports will be sluggish due to the poor market for petroleum products in the West and Romania's domestic agricultural problems. Poor quality will probably frustrate Romania's plans to significantly increase machinery exports. Bucharest would like to ease its hard currency problems by increasing the share of its trade with the rest of Eastern Europe. But CEMA countries, notably the USSR, are not likely to provide Romania with significant quantities of energy and raw materials at favorable prices. Thus a sizable reduction in Romania's share of trade with the West is not expected.

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Yugoslavia

While Belgrade's stabilization program has contributed to slow growth in 1981, there has been little progress in providing a lasting solution to major economic problems--high inflation and poor export performance. Increasing shortages of intermediate and raw materials began to take their toll on industrial production in the last quarter of the year, holding the growth rate to 4 percent in 1981 compared with 1980. A 4 percent decline in agricultural output--due to a poor winter crop--kept the GNP growth rate at about 3 percent, about the same as 1980. The 1982 plan, emphasizing austerity, calls for continued slow growth and for a rebound in agricultural production. The plan to hold the inflation rate to 20 percent for the year appears unrealistic, given the 1981 inflation rate of close to 40 percent.

The trend toward buying West and selling East continued in 1981: Yugoslav exports to the developed West declined by 2 percent in the first ten months of the year, while exports to CEMA countries rose by 32 percent. To reverse this trend, Belgrade must try to lower the domestic inflation rate, pursue a more realistic exchange rate policy, and take other measures to improve the competitiveness of its goods in Western markets. Healthy earnings from tourism and workers' remittances in 1981 compensated somewhat for an increased trade deficit, and helped to keep the current account deficit to about $2.3 billion for the year. Highly ambitious export goals, coupled by severe import restrictions, are optimistically aimed at cutting the current account deficit to only $500 million in 1982 but the trade deficit is likely to be at least three times as high.

China

China's real GNP increased by 3 percent in 1981, with agricultural output up 4 percent and light industry up 12 percent. The heavy industrial sector suffered a 5 percent decline in production because of a planned cut in investment, plant closings, and other measures intended to improve efficiency. Stagnating energy production, which contributed to this year's slowdown in economic growth, continues to be a problem. The persistent budget deficit, inflation, and bureaucratic resistance to new economic policies have also created difficulties for planners. Heavy industry has begun to recover from its slump, however, and the Chinese are aiming at 4 percent real GNP growth in 1982.

Beijing has curbed imports and is now boasting a current account surplus, after experiencing financial problems in late 1980 and early this year. Preliminary statistics indicate that exports may exceed imports by more than $1 billion by yearend. Earnings from invisibles in 1981 will probably outpace expenditures by about $500 million. By August 1981 the burgeoning surplus had already boosted China's foreign exchange reserves to a record $4.9 billion, almost double the $2.5 billion held in December last year.

TABLE 1

Communist Countries: Real GNP Growth Rates,
Estimated 1979-81 and Projected 1982

(in percent)

	1979	1980	1981	1982
USSR	0.8	1.3	2.0	5.0
Bulgaria	4.1	-0.2	3.0	2.0
Czechoslovakia	1.1	1.9	0.5	0.0
East Germany	2.9	2.6	2.6	2.0
Hungary	0.2	0.3	1.0	1.0
Poland	-1.9	-2.6	-14.0	NA
Romania	4.3	1.0	2.5	2.0
Yugoslavia	7.0	3.0	3.0	3.0
China	7.0	6.2	3.0	4.0

Note: GNP estimates are based on Western concepts and procedures.

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TABLE 2

Communist Countries: Hard Currency current Account Balances, Estimated 1979-81 and Projected 1982

(billion US dollars)

	1979	1980	1981	1982
USSR				
Current Account	-0.2	-0.5	-4.2	-4.5
Trade Account	-2.0	-2.5	-6.1	-7.0
Non-monetary gold sales	1.5	1.8	2.0	2.5
Invisibles and transfers	0.3	0.2	-0.1	0.0
BULGARIA				
Current Account	0.5	0.8	-0.1	-0.3
Trade Account	0.7	1.1	0.4	0.0
Invisibles and transfers	-0.2	-0.3	-0.5	-0.3
CZECHOSLOVAKIA				
Current Account	-0.9	-0.2	-0.2	-0.2
Trade account	-0.8	0.0	0.1	0.0
Invisibles and transfers	-0.1	-0.2	-0.3	-0.2
EAST GERMANY				
Current Account	-1.5	-0.9	-2.0	-1.5
Trade account	-1.5	-1.0	-1.5	-1.2
Invisibles and transfers	0.0	0.1	-0.5	-0.3
HUNGARY				
Current Account	-1.1	0.2	-0.6	-0.5
Trade account	-.7	0.2	0.0	0.0
Invisibles and transfers	-.4	-0.1	-.6	-0.5

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(Continued)

Communist Countries: Hard Currency Current Account Balances, Estimated 1979-81 and Projected 1982

(Billion US dollars)

POLAND				
Current Account	-2.9	-3.0	-2.4	NA
Trade account	-1.7	-.9	-0.8	NA
Invisibles and transfers	-1.2	-2.1	-1.6	NA
ROMANIA				
Current Account	-1.7	-2.2	-2.0	-1.5
Trade account	-1.2	-1.5	-1.0	-0.5
Invisibles and transfers	-.5	-.7	-1.0	-1.0
YUGOSLAVIA				
Current account	-3.3	-1.9	-2.3	-1.5
Trade account	-6.6	-5.5	-6.3	-5.5
Invisibles and transfers	3.3	3.6	4.0	4.0
CHINA				
Current account	0.2	1.2	1.5	1.5
Trade account	-0.6	0.2	1.0	1.0
Invisibles and transfers	0.8	1.0	0.5	.5