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ECONOMIC REFORM IN EASTERN EUROPE

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ECONOMIC REFORM IN EASTERN EUROPE

Economic pressures and the loosening of Soviet control are undermining the Stalinist economic system in Eastern Europe. The regimes are giving increased weight to economic criteria in planning and are trying to make producers more responsive to the changing needs of customers. They have been unable to obtain much guidance or help from the Soviet Union, and are borrowing techniques and ideas from Yugoslavia and the capitalist West.

Economic reforms are being designed primarily to attack national problems, and so vary considerably from one country to another. The Czechoslovak regime, faced with the greatest economic difficulties and with deep divisions within the party, is contemplating reforms which give considerable scope to the market mechanism. Rumania, with the fastest economic growth in the area and a party unified closely behind the nationalist policies of Gheorghiu-Dej, seems generally satisfied with the existing economic system. The other countries fall in between but clearly are aiming at improving operation of the "command economy" rather than replacing it.

Early Reform

In the late 1950s the Eastern European countries made fairly extensive, but generally unsuccessful, changes in economic planning, management, and incentives. Poland in 1956-58 and Czechoslovakia in 1958-60 experimented with an increase in the authority of enterprises. East Germany and Bulgaria dissolved the industrial ministries in order to eliminate conservative opposition to ambitious growth schemes and to strengthen party control over the economy. Throughout Eastern Europe, new and more complex formulas were introduced as a basis for incentive payments to enterprise managers--in place of the old criteria, based on gross value of production, which tended to encourage the output of poor-quality goods and to delay technological progress.

These reforms caused confusion, however, and had few favorable effects because they barely touched the basic causes of inefficiency--the failure to consider economic criteria in planning, and the disparities between national and individual interests.

Worsening of the Economic Situation, 1961-64

The intensive efforts to increase the rate of economic growth which accompanied the reforms of the late 1950s were successful only for a short time and at a heavy cost. The more industrialized satellites soon exhausted their reserves of labor and productive capacity, and production plans were set too high to permit the increased attention to quality and efficiency that the early reforms were expected to stimulate. Rapid technological change abroad and improving living conditions at home made customers more exacting, and consequently inventories piled up.

Beginning in 1961, signs of strain began to appear; industrial growth slowed down, except in Rumania, and then stopped altogether in Czechoslovakia. Agricultural production, which had reached new postwar highs in the late 1950s, stopped rising or declined in the early 1960s. Investment programs lagged and living conditions stagnated. Pressure built up throughout Eastern Europe, except in Rumania, to undertake more fundamental reforms.

New Wave of Economic Reform

Faced with rapidly disappearing "reserves" and more particular customers, the Eastern European regimes could no longer condone the long-standing inefficiencies of the "Stalinist" system--maintenance of high-cost industries; long delays in the completion of investment projects; sluggishness in the introduction of new techniques; and the inability of producers to adjust quickly to changing demand. In their search for increased economic efficiency, the regimes have looked increasingly to the capitalist West, where they have borrowed both ideas and techniques. The principal changes being considered in Eastern Europe are the following:

(a) To make planning more consistent with rational calculations of economic advantage. This means reducing political interference, and improving the tools of economic planning, especially by use of mathematical planning techniques.

(b) To clarify the line of command in economic administration. This means mainly undoing the reorganizations of the late 1950s and re-establishing a clear hierarchy from the center to the enterprise.

(c) To develop business-like (as opposed to bureaucratic) methods of economic management. A careful study of the management techniques of Western corporations, a willingness to delegate authority, and limitation of party interference with day-to-day management are stressed.

(d) To develop incentives which align personal advantage with national interest. Even the best-laid plans cannot prescribe every action, and yet a basis must be found to make unplanned decisions consistent with the national interest. There is no wholly satisfactory solution to this problem in a command economy, but increased consistency between national and private interests is being sought by basing bonuses on profits while making profits a more meaningful criterion of performance. For the latter purpose, various regimes are bringing prices more into line with relative costs; charging interest for the use of fixed capital; financing more of investments with repayable interest-bearing loans; giving enterprises more authority to negotiate their own contracts, including export contracts; and strengthening the legal position of buyers relative to that of sellers.

There have been few reforms recently in agriculture, except in Hungary, although there is a tendency to pay more attention to farmers' incentives and allow collective farms to manage more of their own affairs.

Sources of Conflict

Despite strong resistance to change from vested interests, there is agreement in principle on the need for extensive reforms. This agreement, however, often obscures differences in emphasis which, at least potentially, involve a fundamental conflict.

The predominant approach of the regimes is to try to make the existing command economy work better. This approach emphasizes reforms of planning and state administration and treats reforms of incentives as a means of promoting the implementation of state plans. It advocates self-restraint by state and party officials, but no basic reduction in their power. Liberal economists and many enterprise managers, however, favor a quite different approach--creation in at least part of the economy of a self-regulating mechanism which would reduce the need for state or party intervention. In its more extreme form, this approach leads to a rejection of the command economy and substitution of some form of market socialism.

Economic reforms are not yet far enough along for these two approaches to have raised important practical issues. Even as reforms progress, it may be possible to combine elements of a market economy in various ways with elements of a command economy. Considerable differences can be expected in the way different economic branches will be managed--for example, management of railroads is certain to be more centralized than that of shoe factories. Sooner or later, however, each country will have to decide whether to rely mainly on a system of commands or mainly on a self-regulating market.

Diversity In Economic Reform

The Soviet regime has been unable to offer much guidance for reforms of the economic system, partly because it does not know how to deal with its own problems. Khrushchev's attacks on dogmatism and his liberties in interpreting "Leninism" helped to break down ideological barriers throughout the bloc and encouraged change, but did not give this change a clear direction.

So the Eastern European countries did not wait for the Soviet Union. They looked instead to the West and also to Yugoslavia, which has had considerable success with a mixed socialist system combining reliance on the market mechanism for current production with state planning and control for key investments and foreign trade. They studied the earlier experience of Poland and Czechoslovakia. And they went ahead with reforms to suit their individual economic and political conditions.

Czechoslovakia

Economic necessity and political instability in Czechoslovakia have spawned the most radical program in the bloc. Economic stagnation since 1962 has convinced the regime that thoroughgoing reforms are necessary. Political divisions have sharpened economic issues and given considerable influence to elements favoring extensive use of the market.

The reform program grew from a long and bitter conflict between the Novotny leadership and liberal elements within and outside the party. After suppressing the agitation for reform which accompanied the "thaw" of 1956, Novotny adopted part of his opponents' program in the decentralization of 1958-60. Beginning in 1962 he was subjected to a new wave of criticism, which grew stronger as economic difficulties multiplied and became associated with an intense political and cultural ferment. Novotny was intransigent at first, but then had to give way, his position greatly weakened. The party gave the liberals an opportunity to develop and publicize their views, and by the beginning of 1964 many economists were advocating a form of market socialism.

The debate then raged within the party, until the outlines of a new system of management were approved by the presidium in September 1964 and by the central committee in January 1965. Parts of the new system have been introduced experimentally in about one fifth of industry. By the end of next year almost all industries will be using it. Considerable authority will pass from bureaucrats to producers, and greater use will be made of the market mechanism. As desired by the liberals, enterprises are to determine their own short-term production plans, deal freely with suppliers and customers, and retain a substantial part of their earnings for bonuses and investments prices are to be set more rationally and some of them are to be flexible; the state is to concentrate on long-term planning and to use mainly indirect financial controls.

Other elements of the program, however, especially the formation of some 100 branch monopolies to manage industry, suggest that the regime intends to retain the means for direct control. Disagreements over the application of these principles are inevitable because of practical difficulties and differences in long-term objectives. The outcome is uncertain, but the severity of the economic and political problems makes the chances for a basic change in the economic system greater in Czechoslovakia than elsewhere in Eastern Europe.

East Germany

East Germany is overhauling its economic system along somewhat similar lines, but because the political leadership is unchallenged, a substantial reduction in the state's authority over the economy is much less likely.

The Ulbricht regime has followed moderate economic policies since being forced in 1961 to abandon the unrealistic Seven-Year Plan (1959-65) and was the first in Eastern Europe to begin introducing a "new economic system," which is to be entirely operative by 1966. The keynote of the "new system" is "scientific" (that is, rational) planning and management, and Ulbricht, once a foremost practitioner of "political" planning and management by exhortation, now can present himself as the principal author of the "scientific" approach. In sharp contrast to the situation in Czechoslovakia, there has been no public criticism of the leadership's policies; public discussion has only elaborated on them.

The new system clarifies the line of command. After Ulbricht had disbanded the industrial ministries in 1958, the responsibilities of the State Planning Commission increased, but effective control over industry was shared with the district party authorities, who already controlled agriculture. The result was confusion. Now there is a clear subordination of enterprises to Branch Associations (VVBs) and of the VVBs to the State Economic Council, the State Planning Commission having been limited mainly to long-range planning.

The key units of industrial management are the VVBs (about 80 in number), which control all enterprises engaged in production of related goods, such as machine tools, cotton goods, and pharmaceuticals. Like enterprises, the VVBs are expected to show profits. Each is to be responsible for making its own detailed plans, purchasing and marketing, specialized research and development, and determination of appropriate methods of production management. "Economic methods" of management, such as profit incentives, are preferred, but directives are to be used where necessary. The regime expects that the revision of wholesale prices which is nearing completion will permit a great expansion in the use of profit incentives.

The reorganization of East German industry is administratively sensible, but its effectiveness depends entirely on the continued support and self-restraint of the leadership. There has been practically no change in the total size of administrative staffs either at intermediate (VVB) levels or at high levels, or in the party's professional apparatus, which numbers some 30,000 people. The Ulbricht regime appears to be convinced that party organs must change their mode of operation, but there are bound to be frequent conflicts between party officials and VVB managers.

The new approach to economic planning and management is probably partly responsible for the improvement in economic performance in the past year or two but continued improvement will tempt the regime to set more difficult production plans. As long as Ulbricht remains in power and the apparatus of control remains intact, therefore, the extent to which planning and management will be rationalized is uncertain.

Poland

In Poland a cautious, centrist regime has continued to rely on the state bureaucracy to make all important economic decisions. Once the most economically unorthodox country in the bloc and still the only Communist country where agriculture is mainly in private hands, Poland has played only a small part in the recent drive for economic reform.

Immediately following the October 1956 revolution, state controls over the economy were reduced, and there was strong agitation for a radical change toward market socialism. As Gomulka consolidated his political position, however, he squelched the liberals, halted the economic reforms, and even reversed some of them. Economic difficulties during the past two years have renewed interest in reform, but the regime seems interested only in making the existing command system more efficient.

Most of the current reforms are weak counterparts of those in East Germany. Poland's Branch Associations recently have been strengthened, but less so than the East German VVBs. The emphasis is on rational planning and on the adaptation of management methods and incentives to the particular conditions of each branch. Poland has introduced a unique system for encouraging exports--in many enterprises, bonuses for export production are related to export earnings in foreign currency. Profit incentives are widely used in combination with other incentives. The chances are that the Polish economy can get by for several more years without drastic reforms, and the present leadership is unlikely to give up any more controls than it considers absolutely necessary.

Hungary

The Hungarian regime has followed a careful and pragmatic approach, ready to introduce unorthodox reforms but avoiding sweeping changes. Reorganization of industrial administration has been limited to some mergers of enterprises and reduction in the number of intermediate administrative units. On the other hand, Hungary in 1959 brought its prices more closely into line with those on the world market than any other bloc country, and it was the first (in January 1964) to charge interest on the use of fixed and working capital. A pragmatic approach also is apparent in the encouragement given to a broad variety of incentive schemes in collective farms. Many collectives couple sharecropping on an assigned plot with a version of the old Soviet work-unit system.

This piecemeal approach has worked reasonably, well and there seems to be no immediate intention to move away from a bureaucratic, command economy. However, Hungary is experiencing a growing shortage of labor and increasing buyer resistance abroad, and the regime has announced that it will consider more fundamental changes in the next two or three years.

Bulgaria

In Bulgaria a reaction to the excesses of the Chinese-like "leap forward" of 1959-60 led to sober economic policies, and recently even to liberal experiments. In 1963 much emphasis was given in official statements to "scientific" planning, and a long-term program was announced for merging industrial enterprises to facilitate specialization and technical progress. In 1964, the emphasis shifted to market-oriented reforms. Fifty-two plants, mainly in light industry, have been permitted to base their production primarily on contracts negotiated directly with trade organs, and central controls over these plants have been greatly reduced.

These experiments are similar to those introduced later in Soviet light industry. Bulgarians plan to extend them to all of industry, but it is not clear how they will be applied in producer goods industries, where demand as well as supply is planned in detail.

Prospects for future reforms are highly uncertain because of the political weakness of the Bulgarian leadership and the absence of a pressing economic need for basic reforms. Because Bulgaria is still at a relatively early stage of industrialization, it has considerable reserves of labor to cover up the inefficiency of its economic system.

Rumania

Rumania in recent years has been the most successful economically and the most conservative institutionally of the countries of Eastern Europe. In essence, Rumania retains the same centralized system of administration it had in the early and mid-1950s--a clearly defined hierarchy headed by economic ministries.

Economic success--especially an average annual rate of industrial growth of about 14 percent a year since 1958--is one of the main reasons for the lack of interest in changing economic institutions. Although the centralized economic system is not in itself mainly responsible for this good performance, at the present stage of Rumanian economic development it has the advantage of facilitating the concentration of resources on projects of high priority. Moreover, the Rumanians have bypassed some of the inefficiency of their system by importing equipment and know-how on a large scale from the West, and have bolstered popular morale by following nationalistic economic policies.

Unresolved Issues

The outlook is for continued experimentation and change, and neither theory nor experience is a reliable guide for judging the outcome. Marxist theory is of no help at all, and is being increasingly ignored in Eastern Europe's search for a more efficient economic system. Western theory has little to say about "mixed" systems. Experience seems to show that partial, poorly integrated steps like the early Polish and Czechoslovak reforms do more harm than good to the economy, but no one knows how far reforms have to go to be really effective. Electronic computers may conceivably turn out to be the salvation of command economies, or it may be necessary to rely as much on the market as Yugoslavia has done.

There is serious doubt that a middle way can work well or that a command system, with or without computers, can cope effectively with the complexities of modern economies. One thing is clear--greater efficiency requires not just a release of producers' initiative, but also good guidance and discipline.

A market is self-regulating, with competition as the policeman. But without a market the problem of guiding and controlling the innumerable decisions that planners cannot make remains unsolved.

Past experience also suggests that economic reforms in Communist countries tend to be ineffective unless accompanied by major institutional changes. As long as the apparatus of state and party control remains strong, there is a tendency to revert to old ways whenever things go wrong. In any case, the fundamental questions are political --how important is it to a regime to increase economic efficiency; and how much deviation from its policies and priorities will a regime tolerate? Each country will have to hunt its own way. [redacted] 25X1

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