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ECONOMIC FACTORS IN THE STABILITY AND COHESION  
OF THE SOVIET SATELLITE STRUCTURE

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S-E-C-R-E-TSummary and Conclusions

Underlying the present general crisis in the European Satellites is an economic crisis which aggravates discontent and which limits the capabilities of the regimes to placate public opinion. Economic conditions alone are not so severe as to create open expression of unrest but would tend to reinforce unrest once it found expression. If the Soviet Union is to introduce economic stability, as well as political stability, to the Satellites, it must revise the assumptions and the economic programs which formed the basis of the 1956-60 plans of the European Satellites.

Since the war, the structure and orientation of the Satellite economies has been profoundly altered by the Soviet-enforced concentration on heavy industry. This reorientation led to chronic economic problems, because the Satellites lack sufficient raw materials, experience, or skills to develop and operate heavy industry except at high cost. At the same time, the neglect of their former export industries, agriculture, and consumer goods, greatly reduced their capabilities to trade with the West on favorable terms. The Satellite economies became dependent upon an insulated Soviet Bloc economic system in which their bargaining position was very weak. By 1954-55, continuation of economic growth at the rate desired by the various countries became dependent upon an extensive program of economic readjustment, of which the New Course was only the first phase. In early 1956, the Soviet Union assumed that the necessary readjustment would be assured the Satellites by a program of Bloc-wide economic coordination which was to become increasingly effective during 1956-60, by a coordinated trade program involving Satellite trade with the underdeveloped countries, and by a series of economic reforms designed to increase the efficiency of operation of the Satellite economies.

Meanwhile, the internal economic crisis within each of the Satellite economies had assumed proportions not fully realized by the Soviet Union. The Satellites required raw materials and advanced equipment which could

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not be supplied by the Soviet Union and which were not assured by their present trading relationships. Inefficiency in the administration of the economic system increased strains and stresses; some plants had unused capacity; others were overworked; the collectivization campaigns had aroused peasant resentment and gains in agricultural production were inadequate; and in Poland and Hungary, the collection system failed to move sufficient food from the farm to the city. Depressed by the economic burdens of Soviet exploitation of the economies, by an increasing defense effort, and by the great investment cost of the development of heavy industry upon an inadequate resource base, improvement in the living standards within the European Satellites was retarded until 1954. The failure of the New Course to introduce the promised improvement in consumption levels permitted consumer resentment to smolder. In Rumania and in East Germany, some food rationing continues; in no Satellite has there been satisfactory improvement in urban housing conditions; and in all Satellites, the cost of living virtually compels each urban family to have at least two wage-earners to maintain adequate family living standards. Even in Poland, which has relatively high food consumption levels, the Poznan riots illustrated that food shortages were sufficiently tangible to reinforce the expression of discontent.

By mid-1956, each Satellite had followed the Soviet pattern in introducing economic reforms meant to increase efficiency in the administration of the economy and to heighten worker satisfaction and incentive. Measures were undertaken to reduce the work week, to raise the wages of selected worker groups, to liberalize the social security system, and to adjust the controls on labor discipline. In addition, measures were undertaken to decentralize the planning responsibility within the economy, to improve the trade system, and to introduce management reforms. In Poland and Hungary, these economic reforms became associated with a larger context of political and social reform labelled "liberalization" and became a movement which went far beyond the Soviet intent.

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Events in Poland and Hungary will have impact, possibly deep, upon the economic plans of the other Satellites. For example, the Hungarian economy will now be unable to fulfill trade commitments with the other Satellites and will have to receive assistance from them if it is to be reconstructed. Changes in the Polish economic program will require Poland to alter the planned pattern of exports and imports with the other Satellites. In addition, it is possible that the Satellites other than Poland and Hungary may have to revise their own domestic plans to prevent overt expression of unrest within their own boundaries. Finally, plans may be revised as the result of possible changes in the general structure and nature of Soviet-Satellite relationships. The general crisis in the European Satellites has erupted at just the moment when CEMA (Council for Economic Mutual Assistance) has begun to effect extensive inter-linking of the trade, production, and investment plans of all of the European Satellites; an extensive change in the economic plans of any Satellite is likely to require some revision in the economic plans of other Satellites.

For the time being, the Soviet Union is accepting a national Communist regime in Poland. Since Gomulka has not clearly transgressed the Soviet policy line, as it has begrudgingly evolved in recent months, he may succeed in establishing a new relation with the Soviet Union which is more acceptable to Polish national interests. To do this, he must carefully manipulate his popular support and Poland's strategic position. The risk element is involved in the fact that he has certainly transgressed the intent of Soviet policy toward Poland and must be viewed with suspicion by the Soviet leadership. Subsequent conclusions are based on the operating assumption that Soviet military action is not undertaken.

It remains to be seen what autonomy Poland will receive in the economic sphere. At any rate, Poland's economic ties to the Bloc are many and Polish planners must attach a high degree of importance to Soviet and Soviet Bloc economic interests. Domestically, economic reforms

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now being proposed show initiative and imagination; their success or failure may have repercussions throughout the Satellite area. Poland is pressing to adopt a modified version of the Worker's Council to provide worker participation in factory management (except for investment and price policy, which remain under centralized control). The control of the State Planning Committee over the economy is being reduced. The Sejm (Parliament) is moving toward greater weight in the formulation of economic policy. The emphasis upon collectivization of agriculture is being reduced in an effort to recruit the productive cooperation of the Polish peasantry. In addition, moves are being taken to redevelop Polish handicraft industries as a means of increasing the availability of consumer goods.

In the realm of economic policy, Poland will continue to press its trade drive in the underdeveloped countries, exchanging Polish manufactures for needed raw materials. Western industrial nations will be approached for advanced equipment and for data on technological advances which will benefit Poland's economic position. Success in this respect will be limited by Poland's difficulty in marketing goods to the industrial West. Coal, which is presenting production difficulties, will continue to be a major earner of Western currencies. In addition, Poland intends to further her shipbuilding program and to earn foreign exchange from shipping services.

If public discontent with living standards so requires, Poland may find it necessary to import consumer goods from the West as the most rapid means of obtaining immediate improvement. On the other hand, public confidence in the new regime may permit the Gomulka government to undertake an economic policy designed to correct the long-term balance of payment difficulties. In either case, Western aid may be required as a short-term measure, or as a longer-term measure if the industrialization program is not modified.

At the present time (December 1956), it appears that stability can be returned to Hungary only through concessions which the Soviet Union

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is not now willing to permit, or through a costly Soviet occupation. For the foreseeable future, Hungary will be a drain upon the Soviet Bloc economy. The Hungarian economy was in parlous condition before the revolution. The present economic crisis, aggravated by revolution, and possibly by future passive resistance, cannot be alleviated without extensive outside aid from the Soviet Bloc, even if the Soviet Union somehow resolves the political crisis.

In the other Satellites, the present regimes are less concerned with obtaining equality of economic relations with the Soviet Union than with stabilizing the domestic situation. On the other hand, economic problems, discontent with the level of living, and interest in the examples established by Poland and by Yugoslavia create the raw materials for general reform, should popular feeling crystallize about a new leadership.

In East Germany, there is latent discontent. Basically, the Socialist Unity Party (SED) has supported Soviet Bloc integration; the more so since Party members feel that reunification of Germany would be to the detriment of the Party and to the economy as presently structured. Despite the presence of Soviet troops, if the Party and the Government maintain too inflexible a line regarding concessions to the workers, the productivity of the workers may not rise as fast as planned. In addition, East Germany is frankly concerned over the economic impact of events in Hungary and Poland. Polish coal and coke are of great importance to East German industry, for example.

Czechoslovakia has quietly conducted a program of extensive reform in its economic life. The regime has taken pains, however, to prevent these reforms from becoming identified with a liberalization program including political and social reform. This, plus the absence of an opposition leadership, has tended to keep domestic affairs under control. In addition, Czechoslovakia has a relatively high standard of living in comparison with the other Satellites. Events in Poland will have

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repercussions upon Czechoslovak economic life, nevertheless, since the two countries had begun extensive bilateral economic collaboration, especially in the development of the Ostrava coal basin. This collaboration has been of mutual benefit and was to some degree stimulated by mutual distrust of Germany.

Rumania and Bulgaria have both made only slight progress in improving living standards. Since both countries are rural in character, however, discontent has not been expressed as dramatically as in industrial centers. The Rumanian government has already approached the Soviet Union for further economic assistance in order that it may maintain internal stability, but has not been given significant assistance. The Bulgarian government may follow suit in asking the Soviet Union for additional aid.

As presently formulated, the 1956-60 Five Year Plans of the European Satellites provide for rates of economic growth below those of the preceding five year period. Prospective plans call for somewhat less disparity between the growth rates of heavy industry and for light industry, including consumer durables and processed foods. Although greater relative gains are scheduled in investments than in real wages for the prospective five year period, the basic downward trend in real wages that began in the middle of the last five year plans (but was partially reversed by the New Course) is to be counteracted. Even if planned growth rates are discounted, it appears that provision exists in the new plans for modest annual gains in real income, albeit more in industrial products than in agricultural commodities and in housing.

If the presently planned prospect for consumers is more favorable than the previous planning period, however, achievement of these gains, together with overall growth, depends more upon increases in labor productivity than additions to overall manpower or transfers from agriculture to industry. A large part of the planned increase in labor productivity is premised on heightened labor efficiency rather than increases in capital equipment available to labor. In order to achieve this increase in labor efficiency, the cooperation of the workers is necessary. In the past, coercive methods have failed to elicit this cooperation.

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On the other hand, the economic reforms necessary to provide effective incentives to the workers, would require a significant adjustment in plans, probably including lower goals for investment and heavy industry. An approach to the problem of augmenting worker incentives through greater individual freedom, decentralization of economic decision making, and other administrative reforms, might initiate a chain of events similar to those in Poland and Hungary.

Since recent Soviet editorials have completely reversed the true roles and have portrayed Hungary as having been the guilty party for attempting to industrialize too rapidly, it is possible that the Soviet Union will accept a downward revision of industrialization plans in other Satellites. After such revisions are made, and the secondary effects of events in Poland and Hungary are reflected in overall Soviet Bloc planning, it is likely that the production targets of the Satellites for 1960 will be more modest than the earlier targets. After the good Soviet harvest of 1956, and poor harvests in such Satellites as Rumania, the Soviet Union may be able to give the Satellites supplementary aid in agricultural products. There is little indication, however, that the Soviet Union will be able to give extensive supplementary assistance in capital goods, consumer goods, or in raw materials, without scaling down its own economic plans. Unless the Soviet Union feels that its political and military objectives in the Satellites are seriously threatened, it is unlikely that it would give economic assistance which would impair its own development. A more likely alternative would be to permit a downward revision of Satellite economic plans.

Despite potential changes in the economic relations among the Satellites and the Soviet Union, it is probable that the Satellites will continue to press their expansion of trade with the underdeveloped countries. This program serves both the political and the economic interests of the Satellites. If left to the determination of the individual Satellites, there is some reason to believe that the countries selected for maximum penetration effort may not be identical with Soviet target preferences. Currently, the Soviet Union has demonstrated prefer-

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ence for penetration of the Near East, whereas Poland, for example, may have greater interest in India, South America, and areas other than the Near East. A high degree of Bloc-wide coordination of the penetration efforts had been achieved in early 1956, judging by the small number of trade conflicts reported to have occurred among the Bloc countries; greater autonomy of economic policy on the part of countries such as Poland would tend to increase the number of minor trade conflicts, yet partnership in the penetration effort would likely be considered economically desirable and possibly would be dependent upon following the Soviet version of the "rules of the game".

The Soviet Union has now admitted that it has abused the principle of equality in its economic relations with the Satellites and has affirmed its desire to develop a new set of working relationships. In addition, the Soviet Union has indicated willingness to reconsider recall of Soviet advisers (although it is probable that the Soviet Union will attempt to retain advisers in high-echelon offices such as State Planning Commissions). In the economic sphere, all the Satellites are still very much dependent upon the economic policy of the Soviet Union, foreign and domestic, as constraining limits to their own policy, but Poland has now obtained greater latitude of action within these limits.

Although the USSR may permit apparent changes in its economic relationships with the European Satellites, there is little evidence that the changes will permit the Satellites significant increase in freedom in the determination of economic policy, except where political necessity may dictate (as in Poland and, possibly, in Hungary). The Soviet Union must choose between permitting the Satellites flexibility of action in resolving their economic problems, which are of greater severity than the present economic problems of the Soviet Union and require more drastic immediate measures of reform and adjustment than now being implemented in the Soviet Union, or else adopt a rigid policy which seeks to control carefully the nature of Satellite economic reforms in order

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to prevent a repetition of events such as occurred recently in Poland and in Hungary. This is a basic dilemma, for if the Satellites do not adopt far-reaching economic reforms which will recruit the cooperation of the workers and of the peasants, the economic crisis must continue, but to obtain such cooperation, overall economic and political reforms must be undertaken which would potentially shake the present regimes and weaken Soviet control.

In Poland a situation exists which may be unique among the Satellites. Gomulka has won a begrudging measure of freedom from the Soviet Union. Within this freedom, and with his support from the Polish populace, he may attempt economic measures to create a new economic system, combining central planning, price determination, and direction of the economy with increased incentives to labor, the peasants, and management, and an attempt to relate economic decisions to the interplay of market forces, that is, a more meaningful price system. His economic policy must have several goals: it must give greater weight to living standards in determining the basic perspectives of economic policy, recruit popular support for the regime and support of the new economic program, and obtain more efficient utilization of Poland's limited economic resources. It remains to be seen if a program based upon central planning and control can so recruit popular support and participation while still seeking to maximize economic growth. The Polish government must break new ground in the realm of economic policy, and it must maintain public support in a time of economic crisis. Difficult as are these tasks, even without outside interference, they will be the more difficult since neither the Soviet Union nor the governments of Poland's neighboring states will be likely to ease the task.

S-E-C-R-E-TI. The Policy Conflict between the USSR and Its European Satellites.A. Recent Soviet Policy towards the European Satellites.

The Soviet Union has misjudged the political and economic stability of the Satellites and, by its own statement,\* must re-examine the nature of its relationships with them.

At the Twentieth Party Congress of the Communist Party of the Soviet Union (February-March 1956), it was affirmed that there were many roads to Socialism.\*\* This statement was intended to support Party tactics in Western countries. There is no evidence to suggest that this doctrine was meant to apply to the economic development of the European Satellites. To the contrary, the draft directives on the Soviet Sixth Five Year Plan contained a positive statement concerning the economic consolidation of the Soviet Bloc. In addition, the Congress welcomed economic competition between the systems of capitalism and of "socialism."

At the same Congress, A.I. Mikoyan, one of the founders of the Soviet Bloc system of coordinated economic planning, called for consolidation of the world socialist system to take advantage of a world capitalist system "in crisis, weak, and losing one position after another." In the same speech, however, he stated two theses which were to shake the Soviet hold on the Satellites. In the first, his attack upon Stalin, which preceded that of Khrushchev's, he attacked terrorist methods and the secret police. In the Satellites, this would be interpreted as a softening of the Soviet line. In addition, speaking in confident terms of the ability of the Soviet Bloc to win a struggle of "peaceful" co-existence, he laid to rest the theory of capitalist encirclement. By playing down the thesis of immediate threat, he was attacking the roots of the regimentation of Satellite economic life. This "wartime regimentation" in a time of peace was later attacked by Oskar Lange of Poland in a speech in July 1956.

\* Soviet Statement on Satellite Relations, 30 October 1956.

\*\* A detailed presentation of the Soviet policy statements follows in Appendix A.

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Still pursuing tactics designed to strengthen the new Popular Front line in the West, the Soviet Union held further discussions in Yugoslavia in May and June of 1956. In the Pravda statement concerning the discussions, the thesis of many roads to socialism was extended to the economic sphere in the pronouncement that various ways and means may be used in different countries to solve the specific problems of socialist construction.... This change in the formula was necessary to the justification of the establishment of closer relations with Yugoslavia. There is again no indication that the many roads thesis was intended for the Satellites. Significantly, however, the Pravda statement listed features of the Yugoslav politico-economic system which were by implication acceptable to the USSR:

1. Unity in the chief fundamental matter of ensuring the victory of socialism.
2. Public ownership of the basic means of production, in large-scale and medium industry, transport, the banking system, wholesale trade, and most of retail trade. (Note the exclusions of small industry, some retail trade, and agriculture).
3. The state system is determined by the fact that the working class and the peasantry hold the reins of power. (That is, a Communist Party).
4. Pursuit of a "fitting socialist foreign and domestic policy." (By implication, not going too blatantly against the Soviet line).
5. Extension and strengthening of political and economic ties and cooperation by Yugoslavia with the Soviet Union and the people's democracies.

On 30 October 1956, the Soviet Union issued a statement on its relations with the Satellites. It admitted that the principle of equality had been violated and indicated willingness to re-examine its economic and military relationships with the Satellites. By implication, it

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intended to maintain the Warsaw Pact in force, and accordingly, to maintain Soviet troops in the Satellites. By explicit statement, the Soviet Union would be willing to discuss the recall of Soviet advisers. It is further stated that the Soviet Union is willing to discuss measures in order to remove any possibility of violating the principle of national sovereignty, mutual advantage, and equality in economic relations. By implication, the Soviet Bloc joint economic planning for 1956-60 may be changed in nature and in targets.

This statement does not explicitly extend to Poland or to any Satellite the same latitude of action as previously accepted in the case of Yugoslavia. It does not, however, prevent Gomulka from using the Yugoslav precedent. In addition, the Soviet admission of mistakes and the specific affirmation of the principle of equality in economic relations should strengthen the Polish position.

B. Satellite Reaction to Soviet Policy.

In most of the Satellites, there is a latent economic basis for conflict. The advance in levels of living has been slow; housing accommodations are not satisfactory, and there are food shortages in some Satellites. Even so, discontent has not erupted in some countries which have very low levels of living, but it has in one country with a relatively high level of living (Poland). Discontent with levels of living would likely have the effect of reinforcing discontent arising from political and social motivations.

There is also a basis for conflict in the latent suspicion of Soviet motivations concerning the plans for Bloc-wide economic coordination during 1956-60. While in most cases the various Satellites would find specialization of production to their own advantage, plans involving the allocation of resources at what appears to be Soviet direction introduce the possibility of conflict between Satellite and Soviet policies. Thus the Soviet Union presses for Polish exports of coal to the Soviet Union and to the other Satellites; Poland expresses a



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preference to retain more of the coal for domestic consumption and for sales to the West. When nationalism crystallizes about effective political leadership, as in the cases of Yugoslavia and Poland, the principle of equality in economic and political relationships is zealously preserved; common goals with the Soviet Union are recognized, but the economic relationships must be negotiated and not directed.

Poland tremendously magnifies the problem for the USSR. Polish economists, such as Oskar Lange, who has risen to the influential position of chairman of the finance committee of the legislature, have been in a ferment over the inefficiency and arbitrariness inherent in an economic system that substitutes administrative decisions for a rational price policy as the means by which economic questions are decided. The Lange group is insisting, through Gomulka, both on decentralization of planning and administration, and also on the use of profitability as the criterion for economic policy making.

Yugoslavia, long a disturbing element, has become more of one since its rapprochement with the USSR makes the Yugoslav road to socialism a very real alternative to that of the Soviet Union. Now there are two dangerous precedents for further Satellite defections from the politico-economic community which the Soviet Union had intended to be closely knit.

In its own way, Hungary must also be a dangerous element of instability in Soviet Bloc relationships. An occupied Hungary must represent a drain upon Soviet and Satellite resources. Furthermore, the disturbing weapon of the general strike and of the slowdown has been effectively used in Hungary. In the economic sphere, passive resistance can be potentially disastrous to an unpopular regime. At the present moment (December 1956), East Germany has expressed concern about Hungary's ability to honor its export obligations, not to mention the disruption of transport through Hungary, the rail link between mid-Europe and the Balkans.

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Economic conditions in Czechoslovakia, Bulgaria, and Rumania, while of themselves likely to precipitate a major crisis, would tend to reinforce unrest once it manifested itself.

East Germany exhibits the stability of force, and of force alone. The regime has vacillated between offers of concessions and pronouncement of a hard line. Living standards have aroused discontent, openly expressed in 1953 and now latent. Nevertheless, the presence of Soviet troops and the fear of reunification with West Germany have moved the East German government to adopt a relatively hard line.

Because of the German unification problem, East Germany's position is unique. The economy has been artificially developed as one independent of West Germany. Since much of the metallurgical and fabricating industry must operate at higher cost than the West German counterparts, East Germany would be unable to sustain trade competition with West Germany. In the view of the East German Communist Party (the SED), continued existence of the Party and of the economy, as presently constituted, is dependent upon the furtherance of plans for an integrated Soviet Bloc economy, which would guarantee to East Germany needed materials (especially coal and iron ore) and needed markets for its products. On the other hand, East German pride in German technological achievement is an important stimulus to a German nationalism. On several occasions in the past, East Germany has demonstrated reluctance to share advanced technology with other Bloc countries.

C. Soviet Reaction to Changes in the Satellites.

This is a complex subject, which at the moment is best studied not in terms of generalities, but in terms of the specifics of Soviet relationships to the individual Satellites. If the Soviet Union should decide that countermeasures are necessary, a whole host of countermeasures are available in the economic sphere.

Aside from countermeasures, earlier in the year (1956) the Soviet Union recognized the dilemmas in which the Satellites found themselves

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and offered supplementary aid agreements to Bulgaria, East Germany, Poland, and Hungary. These programs did not go far in terms of equipment and consumer goods made available from the Soviet Union and were perhaps most important for the "free currencies" supplied to the Satellites, presumably for the purchase of needed goods from the West.

It is not likely that the Soviet Union can go much farther in expanding its aid programs to the Satellites, for its own requirements are competitive. The Satellites have acute deficiencies in raw materials, consumer goods, agricultural products, and specialized equipment just as does the Soviet Union. The solution is not likely to be found by reducing the scope of the aid program to the underdeveloped nations, for to a considerable degree the Soviet Bloc is exporting a different class of commodity to these countries, -- the more common types of equipment desired by a country just beginning industrialization.

A unique phenomenon of the Soviet Bloc is Soviet control over the distribution of producer's goods. This control originated from many causes, -- former Soviet ownership of key enterprises in East Germany, Hungary, and Rumania; Soviet aid to expansion in producer's goods industries which was to be repaid in kind by the output of the enterprises if the Soviet Union was not otherwise recompensed; and the artificial stimulation of industries not economically well-founded, which led those industries to look to the Soviet Union to find them both sources for raw materials and markets for finished products. Thus, when the Soviet Union discontinued reparations from East Germany, East Germany had to appeal to CEMA (ultimately Soviet-controlled) to find markets for many categories of equipment.

This factor of control is very important. It put the Soviet Union in a position to choose from two major alternatives of action vis-a-vis its economic relationships with the Satellites. 1) The Soviet Union could channel these investment goods inside its own borders, and 2) The Soviet Union could undertake a Bloc-wide industrial expansion

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program. The latter program would be particularly attractive if it made a larger output of goods available to the Soviet Union and accorded with that country's political interests in the Satellites. There is reason to believe that the Soviet Union did in fact consider this to be the case.\* Adoption of a program involving a high degree of industrial expansion for the Soviet Bloc as a whole, and characterized by increasingly extensive division of labor, required one very basic condition, economic and political reliability within the Satellites. The essential nature of this condition can be seen upon consideration of what would happen if one country significantly underfulfilled the output of commodities on which other countries were dependent for the fulfillment of their own production programs and ultimately of their Five Year Plans. The Five Year Plan is the economic program laid on by the Communist Party for the fulfillment of its policies; thus nonfulfillment of the Plan has serious implications to the strength and the prestige of the Party. If the Five Year Plan of any Communist nation is to become dependent upon another country's fulfillment of its obligations, it becomes a matter of party survival to be sure of the other country's reliability with respect to its obligations.

It is now in the realm of reason that the Soviet Union will start to retreat from alternative (2) (Bloc-wide industrial expansion) to alternative (1) (primary preference for industrial expansion within its own borders), unless the "reliability" of the Satellites can be reestablished, which is not likely even under a Soviet military occupation of Hungary and possibly of Poland. In this event of policy shift an entire sequence of events can be forecast:

1. CEMA could be retained but its activities would be considerably scaled-back and it would begin to look much more like the old CEMA of 1951, a vehicle for the coordination of trade

\* During the period 1951-56, all evidence suggests a degree of investment activity within the Satellites, which was relatively commensurate with the extent of total Satellite industrial production.

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policy in common interests but not an instrument for the detailed coordination of industry. Limited detailed coordination might still develop for a few industrial fields of common concern, but far short of the program planned for 1956-60.

2. The Soviet Union could permit a scaling-down of the Satellite programs for industrial expansion and would even show some reluctance to supply Soviet equipment, raw materials, and technical assistance, while seeking to maximize Soviet internal expansion.
3. The Soviet Union could seek to maximize imports of heavy producer's goods, and of raw materials (such as coal) to the extent of its considerable economic power. This would support internal Soviet development and deprive the Satellites of trade items which the Satellites could otherwise trade to the West in exchange for needed economic assistance. The Soviet Union could maintain a net import balance against write-off of past credits and payment for services.

Implementation of such a revision of the Soviet program would not necessarily require underfulfillment of the Sixth Five Year Plan. The Soviet Union would be relieved of some obligation to supply raw materials and equipment\* to the Satellites and could direct these resources to its own development. The major impact of such shifts would be in terms of lower Bloc-wide industrial production in 1960, resulting from downward revision of Satellite production goals.

There would be serious effect upon the Sixth Five Year Plan, however, if events in the Satellites have forced the Soviet Union to stop its demobilization of military manpower numerically short of its goal for May 1957. This would deprive the Soviet Union of labor reserves

\* These resources would be either of Soviet origin or else Satellite resources directed to Soviet account. This, however, does not necessarily mean that there were net Soviet exports of goods of Soviet origin.

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which it likely must have to fulfill its 1960 output goals. If the situation deteriorates, the Soviet Union may even be compelled not only to stop demobilization but to initiate partial mobilization. Partial mobilization would compel extensive rescheduling of the production and investment programs, likely drawing on agriculture and the services industries (including construction) for manpower and slowing down the investment program, especially the program for expansion in the Far East which has a relatively deferred payoff.

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II. Economic Factors in the Prospects for the Stability and Cohesion of the Soviet Satellite Structure.

A. Outlook for Economic Growth and Improvement of Living Standards.\*

The purpose of this section is to consider briefly the broad prospects for economic growth in the European Satellites, the extent to which such growth is likely to be reflected in living standards, and the general relation of these factors to the internal stability of the countries. While this approach should contribute to an evaluation of probable developments in the Satellites during the next several years, it should be borne in mind that the projections of economic growth are necessarily crude, that living standards may not be allowed to keep up with the growth of the economies, and that improvement of living standards is only one of many factors affecting the internal stability of the countries.

The projections of economic growth which are presented in the next subsection are based on the assumption that a rapid expansion of national products will continue to have a high priority in the Satellites. The effect of this expansion on living standards is more uncertain, however, since it depends on secondary economic policies which have been modified in the past in response to internal or external developments and may be modified in the future for similar reasons. Furthermore, even if parallel development of national products and living standards is assumed, the effect on the internal stability of the countries remains rather problematical. This difficulty may be illustrated by the timing of the riots in East Germany and the later disturbances in Poland and Hungary. The East German riots in June 1953 followed about five years of growing pressure to increase production and socialize the economy and of continuing austerity in living standards. The recent

\* The estimated increases in Satellite gross national product and industrial and agricultural production presented in this section were prepared for ORR Project 10.804, which is attached in draft form as Appendix C. Data relating to plans and plan fulfillment are (with a few exceptions) from official Satellite sources.

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disturbances in Poland and the revolt in Hungary, on the other hand, followed about three years of somewhat more liberal economic policies and an improvement in living standards which probably exceeded in extent that of the preceding three year period.

1. Projected Growth in Gross National Product, 1956-60.

In the fundamental matter of the general growth of the Satellite economies during the period 1956-60, it is estimated that substantial gains will be achieved but that these gains will be somewhat smaller than those believed to have been achieved during the preceding five year period. A projection of gross national product to 1960 has not been prepared for each of the Satellites, however. Instead, combined numerical estimates are presented for Czechoslovakia and East Germany (the most industrialized Satellites) and for Bulgaria and Rumania (the least developed Satellites, excluding Albania), and a qualitative estimate is offered for Hungary and Poland.

The average annual rate of economic growth projected for Czechoslovakia and East Germany is about 5.5 percent and that for Bulgaria and Rumania is about 5 percent. In each instance, the projected rate of economic growth from 1955 to 1960 is considerably lower than the estimated average rate from 1950 to 1955 (see Table II-1). The indicated slackening in growth rates for East Germany and Rumania is especially pronounced because during the 1951-55 period East German industry made a noteworthy recovery from the depressed level of 1950 and both industrial production and agricultural production in Rumania evidently increased substantially. The estimates of economic growth in East Germany and Rumania from 1950 to 1955 may be too high; in any event, such average rates are unlikely to be duplicated or closely approached in the period through 1960.

The population of Czechoslovakia and East Germany is not expected to increase very much during the 1956-60 period because of comparatively low rates of natural increase and the assumption of

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Table II-1

Estimated Gross National Products  
of the European Satellites a/  
1950 and 1955

	Gross National Product (Billion 1955 US \$)		Average Annual Rate of Growth, 1950 to 1955 (Percent)
	1950	1955	
Bulgaria	1.19	1.68	7.1
Czechoslovakia	7.93	11.1	7.0
East Germany	10.8	17.3	9.9
Hungary	2.67	3.62	6.3
Poland	16.7	22.1	5.8
Rumania	2.98	4.48	8.4
Total	<u>42.3</u>	<u>60.3</u>	7.4

a. Excluding Albania.

continuing sizable losses of population through emigration from East Germany. Consequently, the anticipated increase in output per capita from 1955 to 1960 is not appreciably less than the projected increase in total output. The more rapidly growing populations of Bulgaria and Rumania, on the other hand, are likely to reduce the rise in output per capita to about two-thirds of the projected increase in their national products. It follows from this that the already large gap between output per capita in Czechoslovakia and East Germany and in Bulgaria and Rumania probably will be widened rather than narrowed during the period under consideration.

A numerical projection of future rates of economic growth in Hungary and Poland does not seem justified at present in view of the serious disruption of economic activity which has occurred in Hungary and the prospect that general economic policies and specific production goals for the next several years may be modified in both countries. It seems safe to say, however, that whatever the line of economic policy followed -- whether Stalinist, or an expanded New Course with additional benefits and concessions for workers and consumers, or something in between -- the outlook is for average rates of growth in output somewhat lower than those projected for the other Satellites.

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The foregoing projections and judgments are based on limited available data concerning the growth of the Satellite economies since the war and on official announcements of goals for 1960. Previously published production goals for 1960 in Hungary and Poland seem likely to be cut back, and downward revisions which are intended to forestall repetition of the disturbances in Hungary and Poland or which reflect the repercussions of these disturbances through foreign trade may also take place in the other Satellites. The projected growth rates should therefore be regarded only as rough indicators of the probable trend in Satellite output.

By their nature, the projections do not take into account the anticipated plan revisions or the supply difficulties which may occur in the Satellites if deliveries of key products such as Polish coal fall below the previously planned levels. In general, the projected growth rates assume that the increases in industrial production from 1955 to 1960 will be almost as large as those planned. Such gains are not likely to be achieved unless the USSR stands ready to break any serious bottlenecks which develop in Satellite raw material supplies. Failure of the Satellites to carry out joint development projects as scheduled may also affect growth rates significantly.

The agricultural element in the projections of gross national product is based on independent estimates of the outputs of selected agricultural commodities in 1960. The projected increase of a little less than 10 percent is comparable to that estimated to have been attained from 1950 to 1955. Growing difficulty probably will be experienced by these countries in increasing yields per hectare as average prewar levels of output are surpassed, but agricultural policies probably will on the whole be more favorable to the expansion of output than during the past five year period.

2. Implications of Principal Goals of the Current Five Year Plan.

In addition to offering some basis for projections of economic growth, the new Five Year Plans announced earlier this year outline major

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economic goals for 1960 which have certain implications for the internal stability of the countries in the intervening period. A brief discussion of these goals seems worthwhile, but the conclusions reached must be considered as tentative since revisions of these plans are in prospect in at least two of the Satellites.

The first question concerns the general level of the major production goals and the degree of strain on the economy which the effort to fulfill these goals is likely to entail. The planned increases in national income fall within a comparatively narrow range -- 40 to 50 percent for the period 1956-60 (1953-57 for Bulgaria). These objectives are in most cases somewhat lower than the original goals of the first series of long-term plans and considerably lower than the upward revisions of these goals in 1950-51 (see Table II-2). These targets undoubtedly are more realistic than the revised goals of the preceding plans, but it is questionable whether they are much more feasible than the original goals of those plans (which in several countries are estimated to have been far from fulfilled).

Considering the pressure on supplies of raw materials and labor which have already been encountered in the area and the substantial rise in investment expenditures and improvements in planning, management, and labor skills needed to achieve the planned increases in labor productivity, it is believed that the growth in national income will be appreciably less than the rates now scheduled. It seems reasonable to assume, moreover, that the attempts of the regimes to accomplish what appear to be reasonably ambitious objectives will militate against any marked reduction in the degree of state control over the economy. Past efforts to get more and more output from the workers no doubt will continue, but with less reliance on pressures and more use of incentives. Restrictions upon private enterprise and individual initiative, campaigns for increased labor productivity, and the tendency toward increased work norms have, of course, been important sources of discontent among the people.

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Table II-2

Planned and Actual Increases in National Product in the European Satellites  
under First Long-Term Plans and Current Five Year Plans

	Period	First Long-Term Plans			Increases in Percent	
		Planned Increase during Period a/ Revisions of 1950-51		Announced Actual Increase a/	Estimated Actual Increase b/	Current Five Year Plans (1956-60) Planned Increase a/
		Original				
Bulgaria	1949-52 (4 years) c/	63 d/	N.A.	67	20	50 e/
Czechoslovakia	1949-53 (5 years)	48	70	59	46	48
East Germany	1951-55 (5 years)	60	60	62	60	45
Hungary	1950-54 (5 years)	63	130	50	49	40
Poland	1950-55 (6 years)	70-80	112	86 f/	51	50
Rumania	1951-55 (5 years)	100	N.A.	90	50	50

a. Data refer to national income, which (as defined in Communist countries) excludes provision for depreciation and the value of services not connected directly with material production.

b. Data refer to estimates of the total output of goods and services, or gross national product.

c. Period of the plan as completed. The plan originally covered the five year period 1949-53.

d. A calculated goal for the fourth year of the plan (1952), based on the assumption that a steady rate of growth throughout the five years of the original period was planned. The planned increase for the original Five Year Plan was 85 percent.

e. Planned increase for 1953-57, the period of Bulgaria's current Five Year Plan.

f. Provisional estimate by the Economic Commission for Europe.

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The rates of economic growth achieved in the Satellites will reflect in large part their success in fulfilling their goals for industrial production. This, in turn, depends on the realization of the comparatively large planned increases in the productivity of industrial workers shown in the following tabulation:

	Planned Percent Increase in Labor Productivity in Industry, 1955 to 1960
Bulgaria	35 (1953 to 1957)
Czechoslovakia	about 44
East Germany	50 (socialist industry only)
Hungary	36 (state industry only)
Poland	35 (state industry only)
Rumania	45-50

Achievement of such rises in productivity will require a very careful allocation of resources, since it depends not only on high levels of investment (to provide increasing amounts of capital equipment per worker) but also on the morale of workers (and thus in large part on working conditions and living standards). To a certain extent, the one can be favored only at the expense of the other. It seems doubtful whether any pattern of resource allocation will permit rises in labor productivity to the full extent presently planned, although substantial gains are expected and are subsumed in the projected rates of economic growth presented above.

Although the regimes can hardly do much about popular dissatisfaction with the institutional characteristics of their Soviet-type planned economies, achievement of even two-thirds of the planned increases in national income would offer opportunities for a significant (though necessarily gradual) rise in living standards. It seems probable, however, that the average annual gains would not be as large as those of the last three years.

Some impression of the planned distribution of the national products during the 1956-60 period is afforded by the goals for investment and real wages. Real wages are scheduled to increase from 25 to 40 percent in the various countries, compared with the goals of 40 to

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50 percent for national income. The lower rates for real wages (which may be regarded as a rough indicator of the planned increases in consumption) permit planned increases in investment which in several cases substantially exceed the national income targets<sup>\*</sup> (see Table II-3). Even if the national incomes of the Satellites rise only about 30 percent, and investment increases by twice that percentage from 1955 to 1960, average annual increases of 2 to 3 percent in the consumption element of national income should be possible. Gains of this size are comparable to the long-term averages in the industrialized countries of the West.

Even if the expected improvement in living standards is realized, it probably would be a neutral rather than a positive factor in promoting the internal stability of the countries. That is to say, the improvement in living standards probably would not in itself promote any widespread acceptance of the regimes. On the other hand, if perceptible gains are made over a period of several years, living conditions in themselves probably would not be a serious source of disaffection or instability among the population.

Additional impressions of the nature of Satellite economic development through 1960 are provided by the plan goals for the expansion of industrial and agricultural output. The cutback from the previous long-term plans in the size of the planned increases in gross industrial production is somewhat greater than in the case of national income. Except in Czechoslovakia (and Bulgaria, where the current plan ends three years before the others), the planned increases do not exceed about two-thirds of the increases originally planned for the final years of the preceding plans and are of course still smaller in relation to the revised goals of 1950-51 (see Table II-4). Even so, it is considered unlikely that net industrial production (as distinguished from gross industrial production, the customary Satellite measurement)

\* See footnote b/ in Table II-3 for qualifications concerning comparisons of the goals for investment and real wages and footnote f/ for a possible explanation of the small increase scheduled for investment in Hungary.

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Table II-3

Approximate Planned Increases in Investment and Real Wages  
in the European Satellites during the Current Five Year Plans  
1956-60 a/

	Investment b/	Real Wages c/
Bulgaria	100 d/	40 e/
Czechoslovakia	62	33
East Germany	100	30
Hungary	15 f/	25 g/
Poland	45	30
Rumania	67-75	30

- a. Except in Bulgaria, where the period of current Five Year Plan is 1953-57.
- b. Unless indicated otherwise, the percentages indicate the planned increases in average annual investment from the period 1951-55 to the period 1956-60. Since it has not been determined in every case that the increase shown is derived from the same component of investment expressed in comparable prices for the two periods, the figures should be regarded as tentative. These goals are only roughly comparable with those of real wages and national income, since the latter indicate the scheduled increases from 1955 to 1960.
- c. Unless indicated otherwise, the percentages indicate the planned increases from 1955 to 1960.
- d. Planned increase from the four year total for 1949-52 to the five year total for 1953-57.
- e. Planned increase from 1952 to 1957.
- f. Planned increase over the period of the First Five Year Plan (1950-54). Because of the declines in investment in 1954 and 1955, a comparison of the goal for 1960 with actual investment in 1954 or 1955 probably would show a much larger planned increase.
- g. Planned increase in personal consumption.

will increase to the full extent planned for gross production. For the four Satellites other than Poland and Hungary, an increase in net industrial production of 45 to 50 percent is anticipated, compared with the planned increases of about 50 to 65 percent in gross production in the various countries.

Each Satellite has planned larger percentage increases for producer goods than for consumer goods, but the divergence between the goals is in general somewhat smaller than in the earlier plans and is considerably smaller than the differences between the officially announced increases in output in these two sectors of industry during the preceding plans. Assuming no marked shift toward exports of consumer goods, these

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goals indicate an intention to give the improvement of living standards more attention than it received under the earlier plans and seem generally consistent with the goals given in Table II-3 for increases in real wages.

In the previous plan periods, there was an evident large discrepancy between the goals for agricultural production and the results claimed (or estimated) to have been achieved (see Table II-4). Sizable gains in agricultural output are once again scheduled, and it is still very questionable whether they will be realized, in view of past performance and the general difficulty of increasing yields per hectare substantially over a period of a few years. Assuming average weather conditions for the 1960 crop, an increase of 8 to 10 percent in production seems probable over the five year period. Since the population of the area is expected to rise by over 5 percent during the period, only a small increase in food supplies per capita is indicated unless imports are increased appreciably. The conclusion seems justified, therefore, that the food component of personal consumption will continue to be a weak spot in the effort of the Satellite regimes to gain wider support among the people of the area and that the anticipated gradual rise in living standards will take the form primarily of manufactured consumer goods, particularly metal products.

B. Problems of Economic Development in the European Satellites.

The rapid industrialization of the European Satellites during the last five years was achieved by means of extensive regimentation of the economy. Speaking of this period, Oskar Lange wrote in July 1956 the following words, "We directed the economy through methods which are characteristic of a 'wartime economy', i.e., through methods based on appeals of a moral and political character as well as on orders of a legal and administrative character, in other words, through methods based on various means of extra-economic compulsion and not on economic incentives." 1/ A multitude of factors, such as the lessening of the rule by terror in the Soviet Union and the accompanying lessening of



Table II-4

Planned and Actual Increases in Industrial and Agricultural Production in the European Satellites  
under First Long-Term Plans and Current Five Year Plans

	Period	First Long-Term Plans				Increases in Percent	
		Planned Increase during Period a/		Announced Actual Increase a/	Estimated Actual Increase b/	Current Five Year Plans (1956-60)	
		Original	Revisions of 1950-51			Planned Increase a/	
Bulgaria	1949-52 (4 years) c/						
Industry		87 d/	N.A.	130	65	60 e/	
Heavy industry or producer goods		154 d/	N.A.	200	215	78 e/	
Light industry or consumer goods		56 d/	N.A.	100	25	48 e/	
Agriculture		43 d/	N.A.	8	-4	66 e/	
Czechoslovakia	1949-53 (5 years)						
Industry		57	98	102	54	50	
Heavy industry or producer goods		66	133	119	66	57	
Light industry or consumer goods		50	73	80	33	40	
Agriculture		37	71	14	25	30	
East Germany	1951-55 (5 years)						
Industry		90	92	90	84	55	
Heavy industry or producer goods		93	100	94	98	60	
Light industry or consumer goods		86	81	84	54	40	
Agriculture		N.A.	57	44	9	22	
Hungary	1950-54 (5 years)						
Industry		86	210	155	84	47-50	
Heavy industry or producer goods		104	280	188	98	58-60	
Light industry or consumer goods		73	145	127	56	38-40	
Agriculture		42	54	12	10	27 f/	

Table II-4  
Planned and Actual Increases in Industrial and Agricultural Production in the European Satellites  
under First Long-Term Plans and Current Five Year Plans  
(Continued)

	Period	First Long-Term Plans				Increases in Percent
		Planned Increase during Period <sup>a</sup>		Announced Actual Increase a/	Estimated Actual Increase b/	Current Five Year Plans (1956-60) Planned Increase a/
		Original	Revisions of 1950-51			
Poland	1950-55 (6 years)					
Industry		90	136	170 (185 g/)	85	53-57
Heavy industry or producer goods		N.A.	154	(196 g/)	107	53-61
Light industry or consumer goods		N.A.	111	(171 g/)	51	54
Agriculture		36	50	19	18	25
Rumania	1951-55 (5 years)					
Industry		144	N.A.	115	78	60-65
Heavy industry or producer goods		N.A.	N.A.	131 h/	101	70-75
Light industry or consumer goods		N.A.	N.A.	97 h/	51	50-55
Agriculture		88	N.A.	80	48	N.A.

- a. Data refer to gross production, which includes raw materials and intermediate products as well as all final products. Changes in the degree of such double-counting during a period result in percentage changes in gross production which differ from the changes in net production. The increases shown for industry and its components are those announced at the end of the long-term plans. In some instances, cumulation of officially announced annual increases during the period produces a somewhat different total.
- b. Data refer in general to net production. Estimated actual increases in production during the first long-term plans differ from the announced actual increases because of one or (more likely) a combination of the following: (1) changes in the degree of double-counting in the official measurements of gross production, (2) inaccuracies in official calculations of these aggregates or falsification in their publication, and (3) inaccuracies in the calculation of increases in net production as a result of the unrepresentativeness of the sample of products used or deficiencies in the basic data, including estimates of production in physical terms and prices and other data used for weighting purposes.
- c. Period of the plan as completed. The plan originally covered the five year period 1949-53.
- d. A calculated goal for the fourth year of the plan (1952), based on the assumption that a steady rate of growth throughout the five years of the original period was planned. This adjustment permits a more valid comparison of planned and actual increases in production.
- e. Planned increase for 1953-57, the period of Bulgaria's current Five Year Plan.
- f. Planned increase over average output during the First Five Year Plan (1950-54).
- g. Socialist industry only.
- h. Provisional estimate by the Economic Commission for Europe.

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Soviet authority in the Satellites, the reduction of international tensions, and popular discontent with Satellite regimes, have compelled each Government to become more concerned with the problem of stimulating economic incentives to production. In some respects this is a continuation of the New Course begun in 1953, in other respects it goes far beyond. The goals of the New Course were mostly based upon increasing the supply of foodstuffs and other consumer goods, but in 1956, in Poland and Hungary in particular, the drive for economic reform became interlinked with social and political reform movements.

The current economic problems faced by the Satellites tend to reinforce the political and social forces demanding that the welfare of the individual be given greater consideration in the determination of national domestic policy. Continuation of a high rate of economic growth, and the satisfaction of the concomitant necessity to increase exports and to reduce agricultural imports, all depend upon raising productivity in both industry and agriculture. Moreover, limitations of raw materials and of investment resources signify that achievement of these production and trade goals will depend increasingly upon the cooperation and the morale of the individual worker and peasant.

In all the Satellites, the high rate of gross capital investment and defense expenditures from 1951 through the first half of 1953, either restrained or depressed living standards. According to a Polish Sejm Committee, in November of 1956, non-consumption expenditures were a dangerously high percentage in 1953, moreover "The proportion of accumulation in the national income...rose to 47.7 percent of the national income in 1953, and in 1954 and 1955 it amounted to more than 45 percent. The consequences of this were felt in the living standards." 2/

Poland and Hungary have both expressed concern with the impact of a high rate of investment relative to national income and have taken steps to keep the increase in investments during the 1956-60 period relatively small. For the period 1956-60 relative to 1951-55, Hungary

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has planned a 15 percent increase in investment; Poland, an increase of 45 percent, or possibly less. East Germany, however, has planned to double investments, Rumania has planned an increase of approximately 70 percent, and Czechoslovakia an increase of 62 percent.

On the other hand, the expansion of the Satellite economies is limited by raw materials shortages, which can be remedied only by increased imports of raw materials or by intensive capital investment. By way of illustration, Poland expects by 1960 to more than double the import of liquid fuels compared with 1955, to increase the import of metallurgical raw materials by 87 percent, of raw materials for light industry by more than 30 percent, and of raw materials for the chemical industry by 33 percent. Poland's ability to increase the necessary imports is limited greatly by inability to increase exports. Coal exports during 1956-60 will be reduced by 20 million tons compared with the total for 1951-55, in consequence of increased domestic demands. Poland does not expect to be able to increase the export of machines and equipment as much as hoped. Reluctantly, despite Poland's desire to trade, it anticipates the necessity of an expensive development of domestic sources for imported materials (such as iron ores).<sup>3</sup>/This limits Poland's ability to reduce the burden of the investment program upon the rest of the economy. A possible solution would consist of accepting a modest rate of economic growth. In rather similar circumstances, Yugoslavia refused to accept this solution, observing that the plants to become productive in the future would produce the very products that could be exported to cover the imports needed by the economy.

During the last five years, the heart of industrial development in the European Satellites has been the development of heavy industry, in turn based upon the metallurgical industries. The continued expansion of heavy industry can be limited by the following material factors:

1. The supply of iron ore. In 1955, an estimated 60 percent of the iron ore consumed in the Satellites was imported.

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Some 45 percent of the total consumption was imported from the USSR.

2. The supply of coal and power. In the European Satellites, coal is the basis both of metallurgy and of electric power production, since the potential for hydroelectric development is limited. During the next five years, however, Poland must reduce its level of exports to the other Satellites since its ability to increase coal production is limited by investment and productivity problems, since the quality of the coal extracted is declining, and since its domestic requirements are rising. The Soviet Union, which imports coal from Poland, is currently encountering a coal shortage, and can only assist the Satellites to a limited extent. In the European Satellites, shortages of coking coal will tend to limit the expansion of metallurgy. Shortages of coal will further tend to limit the expansion of electric power production and will create additional pressure for the development of the hydroelectric potential of the Danube. Parenthetically, it should be noted that the key project of the Danubian development, the Iron Gate project, would require the participation of Yugoslavia. East Germany may be expected to continue its expensive program for the development of brown coal resources.
3. The supply of capital equipment. As the more industrialized Satellites (Poland, Czechoslovakia, East Germany, and Hungary) expand their metallurgical production and their production of the more basic types of capital equipment, their requirements for investment goods will change. Increasingly, investment goods representing advanced technology will be required as the Satellites turn to the manufacture of more specialized and more advanced engineering items. Satellite

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production of such advanced capital goods is limited, and the Soviet Union is a net importer of this class of equipment; therefore the Satellites must turn to the West for satisfaction of their requirements.

The more industrialized Satellites are finding themselves in the position of Great Britain in the nineteenth century; they have become manufacturing nations to a large degree dependent upon imported raw materials. Their trading relationships are of primary importance to the economy. In this context, they must pay increased attention to the quality of the goods which are produced so that they are acceptable to foreign markets. In a real sense, they must be concerned with the skills and the productivity of the industrial laborer. In addition, if they are to compete in foreign markets, they must be receptive to technological advances and if possible, develop their own advanced technology.

Problems similar to those faced by heavy industry are encountered in light industry. There are severe limitations of raw materials; unsatisfactory expansion of agricultural production in the Satellites limits expansion of the food industry and of those important components of light industry which are based upon agricultural products. The Satellites are increasingly dependent upon imports for expansion in this field; imports of grain, fertilizers, fibers, leather, cellulose, and similar commodities, assume varying importance in the plans of the individual Satellites. Again, if domestic production is to be increased, and especially, if the imports of agricultural commodities are to be reduced, productivity must increase in both light industry and in agriculture.

The twin keys to an increased improvement in the level of living continue to be increased agricultural production and accelerated housing program. In view of the general adequacy of agricultural manpower and ambitious plans for capital investment, the main barriers to expanded agricultural production are the compelling restraints of land and

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agricultural incentive. Little can be done to increase the area of sown land in the European Satellites, but much can be done to improve incentives. All of the Satellites except Hungary and Poland, however, intend to push the collectivization campaign, which may be politically desirable in their eyes but is economically costly. It is estimated that per capita food consumption (caloric value) will rise only slightly in each Satellite, except in East Germany, which will experience an improvement because of probable further losses of population.\* It should be noted that in the present state of affairs, no great reliability should be attached to production estimates for 1960, either in agriculture or in industry. It is, however, extremely unlikely that any Satellite will experience a great improvement in its per capita food supply.

The housing program has been considered elsewhere in this survey.\*\* A sizeable construction effort has been planned for the 1956-60 period, but urban growth and replacement requirements will absorb most of the new housing, leaving little chance of significant improvement in the housing situation, as measured in space per capita. A large-scale housing program is competitive with industrial construction for materials and labor force; as a result, ambitious industrialization plans limit ability to undertake an adequate program in housing. Poland, recognizing this, is now reconsidering its priorities and considering the possibility of restricting industrial construction so that a more adequate housing program might be undertaken.

\* See Table III-1.

\*\* See Section III.

S-E-C-R-E-TIII. The Impact of Living Standards upon Internal Stability.A. General Situation in the Satellites. 1/

In mid-1956, Satellite discontent erupted with the bread riots in Poznan, Poland. From subsequent events, it was seen that more than the food shortage was involved in the pervasive discontent. Food shortages, urban overcrowding, shoddy goods, and limited selections of consumer goods were tangible evidence to the masses of the price paid for regimentation of their way of life, a regimentation that could no longer be justified either by Marxist dogma or by the threat of capitalist encirclement. Similar discontent was prevalent in mid-1953 in many Satellites, but the much-publicized New Course promised to redeem the situation. By 1956, in most of the Satellites it was evident that the New Course either did not go far enough or else that the progress achieved was not nearly that promised.

Discontent with the level of living has already been expressed in Poland and Hungary. A high degree of discontent exists in East Germany but can not be openly expressed. The Czechoslovakian regime is assisted by the fact that the level of living there is quite high relative to most of the other Satellites; but little is being done to increase the material comforts of life. Rumania and Bulgaria both suffer from very low levels of living, but some improvement has been tangible, and discontent does not appear to have crystallized.

Early in 1956, the Satellites individually announced their intention to follow the Soviet lead and to implement a reduction in the work week by the end of 1960. In East Germany, the work week in 1957 is to be reduced to 45 hours and the Czechoslovakian work week has been reduced to 46 hours. Generally, a 48 hour work week has been in effect within the various Satellites. In those cases where workers are unable to increase productivity per hour commensurate with the decline in the working time of the work week, some reduction in real wages is to be expected.



S E C R E T

In most of the Satellites, a prevalent aspect of life is the necessity for women to work in order to furnish a second wage-earner in the family, to ensure the desired level of living. Thus, in East Germany, more than 40 percent of the workers are women.

In the following pages some official claims as to increases in the level of living and in real wages will be cited, in order to illustrate the fact that even official data indicate a noteworthy failure of improvement, or else underfulfillment of plans. Such data tend to overstate the improvement however. Improvement in the food supply has been far less satisfactory than might be inferred from such indexes. Thus a particular effort is made in the following pages to indicate conditions in the food supply for individual countries. Much of the improvement in the consumer goods supply is quantitative and ignores such important factors in consumer dissatisfaction as poor quality, limited assortment, and inadequate distribution which leads to local shortages. Despite official data which show average wage increases, important segments of the labor force in the various countries have had little or no improvement in real wages. In most countries, urban dissatisfaction is more prevalent than might be thought from the official data; the housing problem is most severe in the overcrowded cities, and in countries such as Poland,\* the food collection system has been inadequate and has led to decreases in the urban per capita food supply and increases in the rural food supply.

B. Poland.

1. Food Supply and Food Prices.

In 1956, food prices were so high that a family of four whose head worked in industry would probably have to have a second wage-earner in order to insure adequate diet.\*\* There has been only

\* That is, countries with large urban populations, and with a relatively small collectivized sector.

\*\* 53.7 percent of all workers in socialist enterprises earn less than 1,000 zlotys a month, the minimum cost of food for a family of four.

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slight relief in food prices following the 1953 high point pricewise. In 1955, various urban areas had serious shortages of bread, flour, meat, butter and eggs. In early 1956, meat and potatoes were in short supply in Warsaw.

Poland is plagued by an inadequate food distribution system. In addition, rural consumption of food has risen sharply, as state collections of food have failed to properly channel foodstuffs to the cities. Thus, the supply of food in urban centers is often unsatisfactory, despite the fact that the average per capita availability of food for domestic consumption is above that of any other Satellite and 7 percent above Poland's own prewar average.

Table III-1

Per Capita Diet Estimates for the European Satellites 2/

	Caloric Value		
	<u>Prewar</u>	<u>1955/56</u>	<u>1960 a/</u>
Albania	1,757 <u>c/</u>	1,893 (87 percent bulk) <u>b/</u>	2,200
Bulgaria	2,424 <u>c/</u>	2,632 (88 percent bulk)	2,700
Czechoslovakia	2,514 <u>c/</u>	2,563 (60 percent bulk)	2,600
East Germany	2,813 <u>e/</u>	2,431 (55 percent bulk)	2,800
Hungary	2,633 <u>c/</u>	2,638	2,700
Poland	2,775 <u>d/</u>	2,967 (65 percent bulk)	3,000
Rumania	2,608 <u>c/</u>	2,501 (80 percent bulk)	2,500

a. Estimate based upon announced agricultural plans, estimated fulfillment, estimated 1960 population, and estimated foreign trade pattern in 1960.

b. Bulk diet defined as grains and potatoes.

c. 1933-1937 average.

d. 1934-1938 average.

e. 1935-1938 average.

2. Consumer Goods Program.

The planned increases in level of living have been underfulfilled repeatedly, including the 1949 goals and more recently, the 1955 goals. This has aroused public discontent.

It was planned that by 1949 the average per capita consumption level would be restored to prewar levels, especially for basic articles of food and clothing. According to State Department estimates, the actual 1949 real value of wages was 13 percent below the 1938 level

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and the average worker consumed 20 percent less food and bought 45 percent less clothing than in 1938.

The 1955 goals of the Sixth Five Year Plan (1950-55) for improvement in level of living were not fulfilled, despite the special consumer program undertaken during 1953-55. According to official claims which do not fully portray the situation, the average real wage per worker was only 28 percent above the 1949 level rather than the 40 percent promised. Important segments of the labor force (transport, communications, and consumer goods manufacture) actually suffered a reduction of real wages relative to 1950.

3. Foreign Trade in Consumer Goods.

The export of meat and meat products, chiefly pork, constitutes Poland's most important class of export after coal. Coal exports are nearly half of total Polish exports and make possible raw material imports essential to the industrial program, including the manufacture of consumer goods. On the other hand, when coal production plans are not fulfilled, as has been the case recently, maintenance of export obligations tends to put household fuel in short supply on the domestic market. This was the case in October 1956. Exports of other consumer goods include cotton fabrics (13 percent of the 1954 production), wool fabrics (10 percent of 1954 production), leather and rubber products, sugar products, porcelain items, and industrial consumer goods.

In 1955, Poland imported 64 percent of the necessary raw materials for the leather industry, 75 percent of the wool, nearly 100 percent of cotton requirements, and 60 percent of the cellulose needed for rayon. Imports of finished nonfood consumer goods have been planned to fall from 4.3 percent of total imports in 1955 to 3.9 percent in 1956 and to be an absolute decline.

4. Housing.

During 1956-60, urban housing is to be built at the rate of 240,000 rooms a year, as compared with an annual average of 139,000

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during 1951-55. Polish officials admit, however, that even successful implementation of these plans would at best result in a negligible improvement in the critical urban housing shortage.

The great damage suffered during World War II, the high birth rate, and migration into the cities have all prevented any alleviation of the urban housing shortage. Annual average construction during 1951-55 was more than 100,000 rooms short of the level needed to maintain 1950 housing levels. Despite the great official emphasis upon the new housing program as a major component of the new consumer program, achievement of the 1956-60 targets could at best only partially recover ground lost during 1951-55 and likely will result in little improvement at all. It is estimated by ORR that the program would barely satisfy the requirements of anticipated population increases. In addition, extensive replacement will be required for antiquated and substandard housing.

5. Social Services.

Social insurance coverage has been broadened but inflation has made many benefit payments inadequate to prevent hardship.

Health statistics show great improvement relative to 1938 but mortality rates are still high. Hospitals are overcrowded and the number of physicians per 10,000 people is lower than in any other European Satellite. Rural health service is completely inadequate, -- barely one-sixteenth of the total number of physicians serve more than half of Poland's population.

The drive to eliminate illiteracy and to improve basic education has progressed far. In prewar Poland, only 43 percent of the children attended school through the 7th grade and in 1955 close to 90 percent were completing the 7th grade. Enrollment in institutions of higher learning in 1954-55 was nearly triple the prewar figure. On the debit side, construction of school facilities has not kept pace with the increase in school enrollment. Many classes are overcrowded, and some children have been unable to attend school because of lack of space.

S-E-C-R-E-TC. Czechoslovakia.1. Food Supply and Food Prices.

Immediately after the war, food and living costs were 6 to 7 times 1937 levels, but food prices declined some from 1946 through 1950, then rose during 1951-53 (period during which rationing was ended). Since then prices have been reduced some 13 percent for food, more for clothing expenditures, and yet more for consumer durable items.

During 1956 the food supply has improved. The large urban areas are better supplied than other urban areas. Nevertheless, queues are characteristic of the sale of meat (especially pork) and of butter.

2. Consumer Goods Program.

There has been notable improvement in the supply of nonfood consumption goods during the last two years, despite a serious failure to meet the excessively ambitious goals for the output of textiles. Per capita consumption of consumer durables (washing machines, refrigerators, and the like) is higher than in any other Satellite.

3. Level of Living.

Real wages dropped below prewar levels during 1951-53 though by 1956 they apparently exceeded the prewar level. This rise in real wages and real income has probably served to reduce popular discontent. These increases in purchasing power have been accompanied by a rise in the domestic availability of consumer goods. These goods, however, are of poor quality, and their improvement is a major problem for the 1956-60 plans.

4. Foreign Trade in Consumer Goods.

The immediate availability of consumer goods has not been adversely affected by trade policy. Actually, the importance of the export of light industrial products has declined markedly as these items have been replaced in export importance by products of the engineering industry. (In 1937, light industrial products were 34 percent of total

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exports; in 1948, 27 percent; and in 1956, 10 percent). Presently mostly luxury items and textiles are exported. Imports are important to the level of living; foodstuffs are imported, as well as 75 percent of the fiber requirements and 70 percent of the raw materials needed by the leather industry.

5. Housing.

At the beginning of its Communist regime, Czechoslovakia enjoyed better conditions of housing than any other Soviet Satellite with the possible exception of East Germany. Subsequently, conditions have worsened. The annual average number of new dwelling units built from 1949 through 1955 has not been large enough to meet the estimated net increase in the number of married couples. The Government admits that replacement of old and defective housing has not been adequate. Despite concern with the problem, the Czechoslovakian government acknowledges that the problem of overcrowding cannot possibly be solved during the Second Five Year Plan. Czechoslovakia does not seem as concerned with the housing problem as other Satellites; in comparison its housing problem is not as great. While non-attainment of present housing goals will no doubt affect the prestige of the regime and aggravate present economic problems associated with housing conditions, it is not anticipated that the housing question in the next five years will lead to serious problems of worker discipline.

6. Social Services.

Health. Standards of health care are at a higher level than in any other Satellite (with possible exception of East Germany). They are below the average for Western Europe.

Education. As is the Satellite pattern, great statistical progress has been made in the educational program. Classroom facilities in Slovakia are still notably inadequate, however. Czechoslovakia has had unique disappointments in its program of higher learning. The number of advanced students per 10,000 students has decreased since the early

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postwar period and is lower than in any of the other Satellites, following the Communist "purges" of the "bourgeois" element in the colleges and universities.

D. East Germany.1. Food Supply and Food Prices.

The pattern of price reductions on consumer items has been spotty. The most significant price cuts occurred in 1951 and have been followed by many subsequent cuts, most of which would have only slight impact on reducing the cost of living. Nation-wide rationing is still in effect for meat, fats, and sugar. Winter potatoes are also rationed each year. In the event of local shortages, local or regional rationing is permitted, as was the case for various food products at times in 1955 and 1956. The existence of food shortages so severe as to necessitate rationing has dampened morale. The end of food rationing had been promised for as early as 1953. In March of 1956, Ulbricht and Grotewohl indicated that food rationing would have to continue because of the inadequate food supply and said that prices would sky-rocket if rationing was ended now. Since then, probably as the result of pressure from the populace, the regime has conditionally promised the end of rationing for 1957, possibly April.

Opinions differ as to the severity of the retail food shortage in 1956. The supply of essential foodstuffs is far short of demand and the distribution system is poor. The ration system, however, enables each family to obtain at least a minimum subsistence amount at the low ration prices. In March 1956, the US Mission in Berlin stated that "everything connected with the food situation irritates the population." The comment is still appropriate. Quality is poor, prices are still too high for the average income, except ration prices, and rationing continues. East Berlin is in the best position for food supply and prices. Other areas, such as Dresden, have been burdened with food shortages at times. Many East Germans believe that the food situation now is worse than in 1953 at the beginning of the New Course.

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S-E-C-R-E-T2. Level of Living.

Despite a claimed 40 percent increase in real wages, 1955 over 1952, the level of living of the average middle-income working-class family is not comparable to that of the prewar era. The improvement in level of living, especially in terms of food supply, has not been up to the expectations of the population, based upon the goals of the New Course.

3. Foreign Trade in Consumer Goods.

The East German level of living has become dependent upon imports. In 1955, foodstuffs and beverages were 15.9 percent of imports and 1.4 percent of exports. Grains, meats, fats, oils, and fish are imported. The trend is toward greater dependence upon imports.

Also in 1955, products of light industry were 19 percent of imports and 9 percent of exports. Textiles, ready-made clothing, and footwear are imported; high quality consumer goods are exported. East German light industry is dependent on imports of natural fibers, raw hides, and wood.

4. Housing.

By 1950, while overcrowding in East Germany was not serious by East European standards, the situation had deteriorated considerably as compared to prewar East German standards of housing. During 1951-55, the housing program was not itself adequate to improve the situation, yet improvement did result because of a population decline of 500-800,000 from 1950 to 1955. Nevertheless, housing conditions are still far below prewar standards and remain one of the "critical and chronic problems" of the country. The housing program scheduled for 1956-60, if accomplished, would result in significant improvement but still would not restore prewar housing standards. The housing problem, while severe enough to intensify popular discontent, probably is not in itself enough to lead to serious problems of worker discipline.



S-E-C-R-E-T5. Social Services.

East Germany has an extensive social insurance system, as does each of the other Satellites. Its health facilities appear to be reasonably good, with a few deficiencies, the most serious being a growing shortage of doctors. The educational system is superior to the systems of the other Satellites. In large part as the result of the exodus from the country, the schools are not over-crowded.

E. Hungary.1. Food Supply and Food Prices.

There has been substantial improvement, at least until October 1956, in the food supply after the low point of 1952-53. Careful planning of menus and careful buying is necessary to stretch the food budget of the average family. Some problems are created by inadequacy of retail store facilities in some regions and by poor distribution planning on the part of the retail network.

At the beginning of 1953, food prices were more than double the level of June 1950. Following mid-1953, there has been a gradual reduction of food prices. The prices of non-food consumer goods have not been reduced as much as food prices, partially as the result of the attempt during 1953 and 1954 to distribute non-food consumer goods faster than they were produced.

2. Consumer Goods Program.

The promises of the Communist Party concerning the level of living to be obtained in 1955 were drastically underfulfilled. The average real wage per worker was only 6 percent above the 1949 level, and probably slightly below the 1938 level, despite the efforts of the regime to achieve 1955 real wages some 50 percent above the 1949 level. After serious reductions in the level of living which occurred in 1952 and early 1953, there was some improvement in 1954 as the result of the short-term expedient of reducing investment expenditures and releasing consumption goods from state reserves. Furthermore, large groups of

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workers and employees in the low-wage categories received little or no increase in real wages during 1950-54. Although average family income had shown some improvement by 1956, this was the result of more members of the family working rather than of more earnings per hour of work. In 1956 new measures were undertaken to increase wages, cut some prices, and abolish the peace-loan subscription. Official indexes show that increases between 1949 and 1955 in the real income of the peasants have been well above those of urban workers and employees. In recent years the production of consumer goods has increased sharply, but increases in the export of consumer goods have prevented the domestic retail sales from rising accordingly. In 1956, until October, there had been a substantial increase in retail sales compared with 1955, especially in non-food consumer goods.

3. Foreign Trade in Consumer Goods.

Exports of consumer goods assume increasing importance in Hungarian trade. Hungary now exports textiles, footwear, ready-made clothing, sewing machines, bicycles, radios, and furniture. In 1945, 70 percent of the exports were of agricultural products but the shift to the export of manufactured items has reduced agricultural exports to about one-third of the total. Imports of consumer goods in the past have not been of great significance to the Hungarian level of living. Today, Hungary is in serious trade difficulties which will make it difficult to reduce the export of consumer goods in those cases where the goods earn needed foreign exchange. Hungary is dependent upon the import of bread grains and of raw materials in support of the consumer goods industries, such as raw cotton, leather, and other items essential to the production of textiles, footwear, paper, and wooden articles.

4. Housing.

The statistics indicate that urban overcrowding received no relief during the last five or six years. The long-term plans for 1956-60, unless revised, can achieve no more than to prevent a worsening

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of the situation. The Government admits great concern with the problem but has been unable to promise immediate relief. The housing conditions tend to aggravate worker discontent with the entire failure of the Communist regime to achieve the promised increases in level of living.

5. Social Services.

Hungary has achieved noteworthy gains in social insurance, education, and health compared with prewar circumstances. The rural areas, still of major importance in Hungary, have not gained as much in these respects as the urban areas. Progress in education has been retarded in the last two years by a growing shortage of teachers and of classroom facilities. An interesting development in recent years has been increased emphasis upon the academic competence of students rather than upon their political past or class origin. In addition, Hungarian communism has been depicted as an indigenous Hungarian movement rather than as a "gift of the Soviet Union."

F. Bulgaria.1. Level of Living and Consumer Goods Supply.

Bulgaria's level of living is not high in comparison to the more industrialized Satellites, yet some progress has been made. Furthermore, the regime has not failed to live up to promises as obviously as the regimes in some other Satellites.

Bulgaria does not have a large working class, -- workers are less than 10 percent of the total labor force; therefore trends in real incomes among the farm population are of key significance, and are the most difficult to uncover based upon the scanty information. There seems to have been some improvement in rural real income, following the peasant uprisings of 1952. Agricultural statistics indicate that food consumption per capita in 1955/56 was 9 percent above the prewar level and 20 percent above 1952/53.

The New Course affected Bulgarian light industry only to a limited degree, most of the emphasis being upon improving agricultural

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and livestock production. In 1955, the supply of consumer durables was low but probably sufficient to satisfy the effective demand for such items. Bulgarian consumer goods are also notorious among the Satellites for poor quality and lack of variety. The retail trade network is inefficient and poorly administered.

2. Foreign Trade in Consumer Goods.

Bulgaria's reliance upon imports of raw materials for the consumer goods industry has been declining in recent years, until in 1956 the cotton textile industry had to import only 22 percent of its requirements (prewar - 68 percent), and the wool industry 26 percent (prewar - 63 percent). Imports of materials for the paper and leather industries are of major importance; Bulgaria is highly dependent upon imports of consumer durables. In 1956, exports of cotton cloth, wool and silk fabric are to increase over the 1955 level, despite the fact that domestic consumption of fabrics is at a very low level.

3. Housing.

Bulgaria suffers from severe overcrowding in the urban areas, especially in Sofia, but the impact is lessened by the relatively small share of the population which is urban. If these conditions affected a larger part of the population, the situation would be much more serious in the view of the government. As it is, the 1956-60 plans for construction of urban housing appear inadequate to improve the situation.

4. Social Services.

Bulgaria has improved social services compared to prewar standards. Rapid growth in school attendance, however, has created severe problems of school overcrowding, even in Sofia (this is not the pattern in other Satellites, where the capitals usually enjoy better conditions than the smaller towns and rural areas). Although health conditions remain poor, achievements in public health have been considerable. The number of doctors per 10,000 of population has more than doubled, relative to 1939. Rural medical facilities have shown great improvement.

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S-E-C-R-E-TG. Rumania.1. Level of Living and Consumer Goods Supply.

Rumania is largely rural and agriculture plays a predominant role in the level of living of the people. In 1956, the harvest has been poor, delivery quotas have been high, and food has not been plentiful. Wheat and bread are rationed, vegetables and potatoes are scarce and high-priced. The US Legation has noted a "general feeling of uneasiness on the part of the people and government alike." An inadequate distribution system has aggravated the shortages on a local basis. Rumania has had a long succession of food shortages, in 1946, 1949, 1951, 1953, and 1954. In consequence, food prices have been under great inflationary pressure and extensive rationing of both food and clothing remained in effect until December of 1954 (after which stand-by authority was retained for food rationing). Since more than 25 percent of food retail sales are made in the countryside, farmer to consumer, the rationing system was not altogether effective. After 1954, there has been a slight reduction of food and non-food goods prices.

Food shortages and failure of the consumer goods program initiated in 1953-54 have led to discontent. The average caloric food consumption per capita in 1955/56 of 2,500 calories, was slightly less than prewar and also less than in 1951/52. This typifies the lack of progress which has stirred resentment among the population.

2. Housing.

The urban areas are suffering from acute overcrowding which is getting progressively worse. Present plans for 1956-60 do not schedule enough housing construction to improve conditions. On the other hand, there has been some improvement in rural areas, where the construction results from peasant initiative.

3. Social Services.

The infant and general mortality rates of prewar Rumania were the highest in Europe. The general mortality rate has been cut

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from 19 per thousand to less than 10; the infant mortality rate from 18 to 8. Health conditions in the rural and mountainous areas are much less adequate than those in Bucharest. The hospital construction program has brought progress; Rumania has more hospital beds per 10,000 people than does either Bulgaria or Poland.

As in the other Satellites, Rumania has developed programs for medical assistance, hospitalization assistance, old-age pensions, and other benefit programs. The emphasis during 1956-60 is to be upon developing institutions for the care of old people and invalids.

Despite progress in recent years, the Rumanian educational system lags behind those of the other Satellites. Approximately 10 percent of the population under the age of 55 cannot read or write. School attendance is compulsory in the first four grades; only 62 percent of these graduates continue their studies through the seventh year. Attendance beyond the eighth grade is dependent upon determination of the satisfactory class origin of the applicant or of the political reliability of the parents. Enrollment in institutions of higher learning was 75,000 in the year 1955/56, as compared to 29,000 in 1938.

S-E-C-R-E-TIV. Aspects of Economic Coordination and Integration Among the Satellites.A. Organizational Aspects of Bloc Coordination and Integration.1. The Council for Economic Mutual Assistance (CEMA).

The Council for Economic Mutual Assistance has clearly emerged as the vehicle of the Soviet Union for ensuring coordination of Satellite economic planning with the plans and goals of the USSR. Although CEMA meets as a body composed of representatives of the Soviet Union and of each of the Satellites, Soviet control is assured both through organizational features and through the preponderance of Soviet economic strength relative to any Satellite. The Secretariat of CEMA is directed by a Russian Secretary-General. In addition the economic plans developed in CEMA negotiations are integrated with Soviet domestic plans; in recent meetings of CEMA in East Berlin, a Deputy Chairman of the USSR's Gosekonomkomissiya assumed a leading role. 1/ Officials of Gosplan and the Gosekonomkomissiya have, on occasion, assisted Satellite planners in drafting their annual and Five Year Plans, which then have to receive final approval from CEMA.

It has been the intent of the Soviet Union that CEMA become increasingly concerned with the coordination of the annual and Five Year Plans of the Satellites with one another and with the USSR, within a context of the development of specialization of production. This has involved the coordination of trade planning (including Bloc trade with the West) and of investment planning.

In a sense, the main task of CEMA is to reconcile policy conflicts between the Soviet Union and the Satellites. This can be done on a power basis, or on the basis of negotiation and of mutual interest. The Polish and Hungarian statements of recent months, and the Soviet admissions of the violation of the principle of equality in economic relations, provide strong evidence that unilateral Soviet determination of economic policy has played too strong a role in CEMA negotiations, although discussion has played an increased role in more recent decision making.

S-E-C-R-E-T2. The System of Soviet Advisers.

Until 1954, the Soviet Union maintained relatively direct control over the development of Satellite economies by a complex system of techniques involving Soviet ownership of major industries (in East Germany, Rumania, and Hungary) and the placement of Soviet "advisers" in key positions within the industrial and governmental apparatus. Following 1954, the Soviet Union modified this system, abandoning direct ownership participation in Satellite industry (with limited exceptions) and reducing the visible influence of Soviet advisers. Parallel to these changes, CEMA assumed a more important role in Bloc planning.

In East Germany, Albania, and Hungary, and to a lesser extent in Bulgaria and Poland, the activities of the advisers are now concentrated in the non-production ministries, such as Internal Affairs, Defense, and the State Planning Commission. At this level, the advisers are less apparent to the public but are still in a position to influence the formulation of economic policy.

In the policy statement on Soviet-Satellite relations of 30 October 1956, the Soviet Union expressed willingness to discuss the recall of advisers. It is probable that the visible role of advisers will be further reduced\* but it is far less certain that the Soviet Union will willingly abandon the system of advisers at the higher echelons.

B. Bloc-wide Division of Labor and Specialization of Production.

Soviet leaders recognize the economic advantages inherent in production specialization according to the principle of comparative advantage. They have declared their intention to move toward an economically coordinated and integrated Communist Bloc chiefly by having each country specialize for the benefit of all the Satellites, in those commodities for which it is best suited. Specialization, in practice, has been most often carried out where either a natural resource base or a developed industry

\* That is, advisers at the industrial level and observers in plants may be recalled.



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exists. Examples include coal in Poland, petroleum in Rumania, and chemicals in East Germany. Specialization of this type may be termed "undirected" in that the countries involved might be assumed to continue developing these specialties as a matter of course even without direction from Moscow.

Central assignment by Moscow of specific production tasks to each Satellite may not be a major cause of Satellite discontent -- particularly if the commodity in question is one which the specific country itself desires to produce. It is probable that there is more agreement than not among Soviet and Satellite leaders concerning designated Satellite production tasks.

The natural concomitant to centralized investment planning for the Satellites is centralized allocation of both raw materials and finished products. These two sides of coordinated Bloc planning have been Soviet goals since 1949. It is precisely the central allocation (from Moscow) of goods to which the Satellite leaders seem most to object. It was not the assignment by CEMA for Poland to specialize in producing coal and coke which Polish leaders apparently resented, but rather the unfavorable trade terms to which Polish coal was subjected. Furthermore, Polish leaders were forced to export more coal than they thought was economically wise.

The weakest link in economic coordination of the Soviet Bloc, then, may be the process of central allocation of Satellite commodities toward which the Soviet leaders have been striving these past few years. Consequently, central allocation might be considered a major force behind recent Satellite unrest and might have been a positive contributing factor in the Polish and Hungarian developments; thus Poland preferred greater autonomy in determining the trade pattern for export of Polish coal.

Apart from these broader approaches to specialization of production, considerable progress had been achieved in establishing a number of central production and allocation assignments by mid-1956. In heavy industry, all countries have been developing at least a rudimentary base, simultaneously.

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Czechoslovakia, Poland, and East Germany, for example, have given special emphasis to heavy machinery. East Germany is specializing in heavy tractors and Poland in medium tractors (see Table IV-1).

C. Economic Coordination and Satellite Political Equality.

Future cohesion of the Satellite system may be significantly weakened if one or more of these countries gains greater political and economic independence from the USSR. Assuming greater economic independence for one or more Satellites, several considerations are in order. First, a determination will have to be made as to what effect greater independence for a Satellite will have on its internal economic planning. The second problem relates to the impact of such independence on the part of one Satellite will have on the economy of others. Finally, consideration must be given the effect of these developments on the over-all economic coordination of the entire Bloc as such coordination has been directed and supervised by the Soviet Union.

1. Effect on the Individual Satellite Concerned.

Greater economic independence for a Satellite would no doubt result in a more rational allocation of its own investments, and perhaps the creation of new annual and Five Year Plans. Some evidence points to unwise investments and trade commitments for some Satellites which are economically inefficient, yet which have been forced upon the particular countries in order to round out the scheme of division of labor and production specialization. CEMA ordered Poland, for example, to invest in developing her own oil production, despite a previous finding by the Polish State Planning Commission that such an investment would be less economical than Polish investments in the Rumanian oil industry. 2/ Assignments for a Rumanian factory to produce tractors for Czechoslovakia and a Hungarian factory to produce heavy construction machinery for Czechoslovakia were also considered by the producing countries to be basically uneconomical. 3/

Table IV-1  
Specialization of Production by Industry  
in the European Satellites\*

Product	Czechoslovakia	Hungary	East Germany	Poland	Rumania	Bulgaria	Albania
<b>Coal</b>							
Hard coal	X			X			
Coke	X			X			
Brown coal			X				
<b>Chemicals</b>							
Chemical fertilizers	X	X	X	X	X	X	
Industrial chemicals	X	X	X	X	X	X	
Coal chemicals	X		X	X			
Synthetic organic chemicals	X	X	X	X	X		
Synthetic fibers and plastics	X		X	X	X		
Synthetic rubber			X	X			
<b>Ferrous metallurgy</b>							
Iron ores						X	
Manganese ore					X		
Chrome ore							X
Rolled steel products	X	X	X	X			
Pipes					X		
Alloy steel	X						
<b>Non-ferrous metallurgy</b>							
Alumina and aluminum		X	X				
Bauxite		X					
Zinc and lead				X			
Pyrites						X	
Miscellaneous ores and concentrates						X	

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Table IV-1.

Specialization of Production by Industry  
in the European Satellites  
(continued)

Product	Czechoslovakia	Hungary	East Germany	Poland	Rumania	Bulgaria	Albania
Petroleum							
Oil and oil derivatives					X		X
Bitumen							
Agriculture							
Grain		X				X	X
Medicinal plants						X	X
Tobacco						X	
Heavy industry							
Heavy machinery - general	X		X	X			
Heavy construction machinery		X					
Machine tools							
Metal cutting machine tools	X	X**	X***	X			
Metal forming machinery			X				
Transport vehicles and equipment							
Heavy trucks	X						
Buses		X					
Diesel locomotives	X	X					
Electric locomotives	X		X				
Passenger cars	X		X				
Freight cars	X	X		X			
Heavy tractors			X				
Medium tractors				X			
Tractor and truck spare parts						X	

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Table IV-1.

Specialization of Production by Industry  
in the European Satellites  
(continued)

Product	Czechoslovakia	Hungary	East Germany	Poland	Romania	Bulgaria	Albania
<u>Agricultural machinery</u>							
Grain combines		X	X				
Corn harvesting combines		X					
Potato harvesting combines				X			
All-purpose cultivating tractors	X				X		
<u>Electro-technical equipment</u>							
Electric power plants	X		X				
Electric motors	X	X	X	X			
Precision instruments and optical devices	X		X				
<u>Armaments</u>							
Heavy armaments	X						
Small arms and ammunition	X	X					
Combat aircraft	X			X			
<u>Shipbuilding</u>							
Large ships				X			
Small craft (mainly fishing)							
<u>Light industry</u>							
Footwear, glass, and porcelain	X		X				
Textiles	X	X		X			

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IS-  
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\* Refers to identified CEMA approved specialties rather than production as such.  
 \*\* Primarily single purpose universal machine tools.  
 \*\*\* Including emphasis on automatic lines.

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The new Polish Government evidently intends to reassess its entire economic plan. On October 20, 1956 Gomulka stated that heavy industrial construction would be somewhat demphasized in favor of raising the level of consumer goods investments. 4/ Later, the Polish Communist Party paper stated that Poland is prepared to abandon its current Five Year Plan, possibly in favor of a short-range Two Year Plan. 5/ Even if the present long-term plan is continued, however, in all probability the 1957 investment plan will be altered to grant more immediate consideration to consumer goods. 6/ The path Poland will have to follow to reorient its economic system toward a more equal balance of investment, according to some members of the Polish Society of Economists, is for Poland immediately to abandon its plans for large-scale industrial development, concentrate on consumer and light industry, and alter the general balance of Polish foreign trade. 7/

Any such realignment in Polish trade will no doubt first apply to hard coal. Under assignment by CEMA, Poland has been the main provider of hard coal to the other Satellites and has even exported this fuel to the USSR. Poland has long objected to exporting her coal in excessive amounts. Under CEMA, Polish agreements with East Germany and Hungary provided for shipments of coal to these latter two countries, probably in return for open credits to purchase certain machinery and equipment. 8/ Another source of disagreement in the past has been USSR purchases of Polish coal at a preferential rate below world market prices. In this framework, shipments to the USSR constitute 34 percent of total Polish coal exports. 9/

Since the political developments of October and November 1956, Polish officials are apparently going to review and possibly reallocate their exports of certain commodities. 10/ Persistent reports state that Poland has informed the East German Government that hard coal would no longer be shipped to that country, 11/ although by the first of December, 1956, there was no noticeable reduction of the number of coal trains from Poland to East Germany.

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In response to their paucity of coal, the East Germans appealed to the USSR for assistance. 12/ The USSR, reportedly, has agreed to begin shipping hard coal to East Germany as of 1 December 1956. 13/

It can be assumed that Poland's economic plans will undergo alteration -- particularly with respect to major investments and trade policies with other Satellites. It is apparent that the USSR will ease its demands on the Polish economy -- especially with reference to Polish investments and exports. In fact, Gomulka has recently stated that all Polish-Soviet relations are to be re-examined as parts of the "economic whole." 14/

2. Effect on Other Satellites.

Greater political independence of one Satellite will have significant economic ramifications not only for that country, but for other members of the Soviet Bloc. Rather close coordination of the economic plans of all CEMA members (except the USSR) has been achieved as of mid-1956. Obviously, any unilateral alteration of a single member's annual and Five Year Plans will force an inevitable readjustment of economic plans in at least several other CEMA countries. If the Satellite which first changes its plans is an important cog in the division of labor, then planning, production, and trade within the entire Bloc will face necessary alteration.

In response to the anticipation of cancellation or reduction of Polish coal shipments to East Germany, apparently several plants have severely restricted their operation. 15/ One result of this cutback in coal shipments, reportedly is that the East German State Planning Commission is considering curtailing rail traffic and may even suspend virtually all production in the chemical industry, or cut back light industry. 16/ Several large East German industrial enterprises supposedly will attempt to meet the hard coal shortages by using brown coal for the next three months. 17/

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In countries other than East Germany, any reduction of coal imports from Poland might have a similar effect. When Poland suffered reduced output in its coal industry earlier in 1956, both Hungary and Czechoslovakia felt the pinch, and in Hungary, the reduced imports resulted in a temporary shutdown of some transport. 18/ In Czechoslovakia, reduced imports of Polish coal would affect that country's exports of machinery (for which Polish coal was traded). \* 19/

Serious disruption of Hungarian industry will have long-lasting effects on the industries of all other CEMA members. A statement reputed to be from Ulbricht of East Germany noted the deplorable state of trade between his country and Hungary, following the outbreaks. He stated that the Hungarians could no longer deliver anything and, in fact, East Germany had to deliver commodities to Hungary. 20/

Abandonment by one or more Satellites of the closely-coordinated division of production specialization may not, however, adversely affect every member of CEMA. Some of the countries may use this disruption of their trade plans from the outside as a welcome excuse on their part to increase trade with the West (East Germany seeking hard coal, for example). Finally, the comparative advantage of specialized production and its resultant economic efficiency, may deter a Satellite from rash abandonment of its part in the Bloc-wide division of labor.

### 3. Effect on Bloc Coordination and Integration.

Certain conclusions can be made concerning developments which would stem from greater Satellite independence and at least a partial breakdown of mutually coordinated planning. Ulbricht as the extreme view point has stated that if each Satellite desired economic independence and a co-equal status, the Bloc's mutual economic plans would collapse. 21/ Even a partial collapse of the coordination system would probably mark the death

\* In a recent year, Poland exported 8 million metric tons of coal and over 1 million metric tons of coke to the rest of the Bloc, not including the USSR.



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of any future plans for extensive economic integration of the East European Satellites. CEMA would certainly lose much of the influence and control which it has assumed since 1949. The accompanying structure of a Bloc-wide division of labor and production specialization on which each country has been concentrating in recent years would be seriously and perhaps irrevocably retarded. Even if a Satellite desired to remain within CEMA and to be more or less loyal to the USSR, reduced imports from other CEMA members would force her to de-specialize some of her industry at least for the foreseeable future. The trend followed in recent years in which each CEMA member began to adopt common industrial and managerial standards (usually Soviet ones), would have to be temporarily reversed if not eventually abandoned. Finally, a weakening of economic coordination might well force most of the Satellites measurably to increase their trade with the West and with the underdeveloped nations in particular.

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S-E-C-R-E-TV. Aspects of Foreign Trade Relating to Stability and Cohesion

In a basic sense, this study is concerned with the relationships of the European Satellites with the Soviet Union. The significance of the Satellites to the Soviet Union is manifold, and to a substantial extent the trading policy of the Soviet Union reflects the prevailing Soviet view of the role of the Satellites. This is not the place to study all the permutations of Soviet policy relative to the Satellites, but it may be observed that they can play the following roles, in different combination and with varying emphasis:

1. Buffer against the West (that is, there is a very important geographic consideration involved in Soviet control).
2. Example of the advantages of Communism (in support of expansionist policies).
3. An advanced logistic base for military operations.
4. A source of special natural resources (Poland- coal, East Germany- chemical ores, Hungary- bauxite, Rumania- petroleum and salt, East Germany, Czechoslovakia, Bulgaria, - uranium).
5. A source of advanced technology in the case of East Germany.
6. A source of skilled industrial manpower, in the case of East Germany and Czechoslovakia, and to some extent in Poland and Hungary.

Immediately after the war, the Soviet Union exploited the Satellites, individually and collectively, and accumulated an import balance of immense proportions (when reparations are included as part of the picture). After 1949-50, the Soviet Union began to support the reconstruction of the Satellite economies by supplying raw materials and investment goods in return for machinery, equipment, and such resources as coal and petroleum. During 1951-52, the Satellites undertook, under Soviet instigation, a large buildup of their armaments industry. A Bloc-wide economic adjustment occurred in 1953-54, and in 1955-56 the Soviet Bloc undertook more extensive

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coordination of investment and production planning. In 1955, at least two-thirds of the foreign trade of each Satellite occurred with other Bloc countries, and in every case trade with the USSR was greater than trade with the entire Free World.

In 1954, the Soviet economy was more than twice the size of the combined economies of the European Satellites. Total Soviet trade turnover with the European Satellites was approximately 18 billion trade rubles (probably more than 35 billion rubles at domestic prices). Soviet exports or imports to the Satellites were therefore about 4 percent of the value of Soviet net industrial production but equal to more than 8 percent of the Satellite industrial production. For this reason, the Soviet Union's participation in real economic cooperation with the Satellites is only marginal. Where the Soviet Union undertakes obligations to supply the Satellites with raw materials or machinery, these obligations are minimal for her and do not have great impact on the national economic plan. On the other hand, such supplies are very important to every Satellite because they decisively influence Satellite economic development. Basically, the Soviet economy is also independent of the Satellite economies, which on the other hand are very much dependent upon the economy of the USSR and upon each other.

In 1954, the Soviet Union was a net importer of machinery and equipment from the European Satellites and China to the extent of approximately 900 million trade rubles.\* Since the Soviet Union is a net exporter of these items to China, net imports of machinery and equipment from the European Satellites are probably more than 1 billion trade rubles. Total Soviet exports of machinery and equipment to the Satellites and China are approximately 2.6 billion trade rubles and total imports --

\* In 1954, total trade turnover of the USSR was 25 billion rubles. Imports and exports are assumed to be balanced, as in the Soviet literature, since the USSR is a net importer from the European Satellites and a net exporter to China. According to the Soviet statistical yearbook for 1956 1/, machinery and equipment comprise 32.6 percent of Soviet imports and 21.5 percent of exports. According to Western sources, Western imports of these items from the USSR total \$12 million (48 million rubles) and exports total \$145 million (580 million rubles.) 2/

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3.5 billion trade rubles. Imports of machine tools, chemical equipment, and electrical equipment are of special importance to the Soviet Union.

Eastern Europe is poorly endowed with raw materials necessary to an industrial society and in addition, after diverting productive resources from agriculture to industry, has become dependent on outside sources for much of its agricultural as well as industrial raw material supplies. These requirements have in largest part been filled by the Soviet Union. Ferrous and non-ferrous metals, fuels, and fibers have all been preponderantly supplied to Eastern Europe from Bloc sources, primarily the USSR. In 1955, estimated Soviet exports of iron ore to the European Satellites were more than 8 million tons (12 percent of the Soviet total extraction, or more than 45 percent of the estimated Satellite consumption of imported and domestic iron ore). <sup>3/</sup> In a very real sense, Satellite dependency upon Soviet iron ore gives the Soviet Union control over the development of heavy industry in the Satellites.

In their first long-term economic plans (circa 1950-55), the Satellites undertook rapid industrialization on the basis of the development of heavy industry (and of ferrous metallurgy). The motives were complex, military, economic, political, and nationalistic, but the result was that many Satellites acquired heavy industry which was based on imported iron ore and coal and which was high-cost relative to the world market. This industry could exist under such conditions only within an insulated and isolated Soviet Bloc economic system and tended to facilitate Soviet exploitation. Nevertheless, it became apparent that maximum economic growth of the entire Soviet Bloc would be better achieved if less autarky prevailed in Satellite economic development and if the further expansion of industry were undertaken on the basis of greater coordination of investment and trade planning. Furthermore, by the end of the period (1950-55) the basic autarkic buildup of heavy industry had served its major political and military purposes.

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By 1955, the industrialization programs of the European Satellites had achieved a high level of output for key items, such as coal and steel, but the domestic needs of the producing countries had increased to a larger extent than had been planned. As a result, for example, Poland, which was to have been a supplier of coal for the entire Bloc, was unable to satisfy the import needs of other Bloc countries.

Agricultural development lagged behind plan in all the Satellites; this aggravated a deficit of consumer goods on the market. Poland was unable to export grain and actually had to import it. The USSR itself had to cancel several obligations concerning deliveries of grain and food products and in 1954-55 advised the Satellites to buy grain in the West.

The Satellites became plagued with problems of excess capacity in several industries which had been simultaneously overdeveloped in each Satellite during the frantic industrialization years before 1954. Several countries, for example, had excess stocks of textiles and excess textile producing capacity. To use such capacity, markets had to be cultivated outside of the Soviet Bloc.

Capital investment funds were tied up in idle equipment and incompleting factories, the relics of the excessive, overdiversified, industrialization policy followed in all Satellites. Furthermore, the armaments buildup in the Satellites during 1951-52 had delayed many plants. Other Satellites, deprived of the imports which were to have been supplied by these plants, built their own plants; this in turn removed the justification for several incompleting plants, which were left unfinished.

Current Soviet Bloc trade policy, as envisaged in early 1956, is to concentrate on the following points: 4/

1. Investment planning should be thrifty and selective; costs should be minimized to reduce the burden of investments to the

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economy; idle equipment and capacity should be utilized.

2. Bilateral or multilateral cooperation in specific industries should produce more rational utilization of resources.
3. Excess capacity should be utilized by promoting trade with the underdeveloped nations..

At the meeting of CEMA at Budapest in December 1955, the chairman, Anastas Mikoyan of the USSR, reportedly set forth the following views: 5/

1. Capital investment should favor modernization of plants rather than the construction of new ones.
2. The Satellites are too servile in following Soviet techniques and should avail themselves of Western technology.
3. The Satellites should perform their obligations under the joint planning. (But at this point, conflict arose with the Polish delegate who explained the Polish problems with coal and grain. Actually the surpluses and import requirements of the various Satellites do not dovetail as well as the Soviet Union would like).
4. The Satellites should not expect any deliveries of agricultural products from the USSR in the near future (superseded by agreements made following the bumper Soviet crops of 1956).
5. Satellite trade policy toward the underdeveloped nations would have to be strictly coordinated. The delivery obligations would have to be fulfilled at any price, although if one country should be unable to deliver, another country could assume its obligation. Finally, the Satellite nations should avoid competition among themselves.
6. In planning their trade and production with consideration of trade with the underdeveloped nations, the Satellites should not count on wider possibilities of credit within the Soviet Bloc and each country would have to count upon its own resources.\*

\* The Soviet Union fears shortages of raw materials and capital equipment which might be generated by its own plans for 1956-60. It could maintain an export deficit with the Satellites against past services and credits.

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7. Finally, the context of Mikoyan's statements concerning trade with the underdeveloped nations indicated that the main effort would now be directed toward the Arabic countries while the achievements in India, Burma, and Afghanistan were consolidated.

Although there is now evidence that the Satellites have real fear of the increased economic control centered at Moscow inherent in the plans developed during 1955 and early 1956 for Bloc-wide economic coordination, there is much economic justification for some form of economic cooperation among the Satellite countries. Specialization for a Bloc-wide market would help to make Satellite production more efficient, and to make their exports more competitive in the total work market, and thus to facilitate the coming-of-age of the infant industries. Increased economic coordination makes possible a more orderly planning of trade patterns which is very important to a planned economy such as any of the European Satellites. Each Satellite, however, is possessed of its own immediate economic problems and has occasionally sought to solve them in competition with another Satellite for a given contract or source of supply. Evidence of such inter-Satellite competition, especially in intra-Bloc trade, has grown more scarce and in mid-1956 was largely confined to the chronic complaints about delivery delays or unfilled quotas. To the extent that Satellites such as Poland and Hungary pursue an independent economic policy, there is likelihood that frictions will increase both in intra-Bloc trade and in the internal planning of other Bloc countries such as East Germany. This would generate pressures from all the other trading partners to negotiate economic coordination at least on the level of common interest.

Trade with the underdeveloped countries, although promoted by the Soviet Union for purposes largely political, offers the prospect of long-run economic gains. In exchanging their own industrial products for the agricultural and other raw material exports of the underdeveloped countries, the Satellites are alleviating their own chronic material shortages,

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employing productive capacity which might lie idle, and are moreover lessening the pressure on the Soviet Union's resource endowment. There is even the possibility of circumventing some of the Soviet control over the Satellite economies through the importation of iron ore from India, Liberia, and Brazil instead of from the USSR. The benefits to the Satellites from such exchanges have been felt only partly, for many of the exports from the Satellites have involved an extension of credit, and thus the return flow of raw materials has not yet been completed.

The amount of benefit which the Satellites have derived and will derive from an extension of their trade with the underdeveloped countries depends upon the terms of trade, the prices of their exports as compared with the prices of their imports. Present information does not yet permit assessment of the economic gain or loss to the Satellites of the current programs. To some extent, the Satellites would be willing to undergo short-term costs in order to develop a long-term market, which is a normal trade phenomenon.

The development of trade with the underdeveloped countries can provide greater freedom in the financing of Satellite foreign trade. For complex reasons bound ultimately with the exploitation of the Satellite economies, the USSR has in the past never encouraged intra-Bloc multilateral settlements and has encouraged bilateral barter agreements.\* The Satellites have not been satisfied with bilateral balancing, which becomes very difficult to administer and is not economically advantageous to them. They have begun to achieve de facto multilateralism in the form of commodity shunting: the import of a commodity from one country in order to export it to another from which something more necessary can be obtained.\*\*

\* Bilateral trade negotiations permit the USSR to use its full economic weight against a single country at a time, should that expedient be necessary. In addition, multilateral clearing would tend to prevent the USSR from maintaining a net import balance from the Satellites since there would be a tendency for the Satellites collectively to import from the USSR up to the limit of their exports to the USSR.

\*\* In a sense, even China has done this. In 1954, when rubber shipments to China were embargoed but were legal to the USSR, China procured rubber and shipped it to the USSR.

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Extended participation of the Satellites in Free World Markets has broadened their opportunities for such de facto multilateralism. On the one hand, certain of their non-Bloc trading partners (such as Ceylon) have objected to the restrictions of bilateralism with the result that pressure for some form of intra-Bloc clearing of accounts has come from outside the Bloc. On the other hand, new opportunities for commodity shunting and multilateral uses of bilateral clearing accounts have been developed and utilized by the Satellites.

Trade with the underdeveloped countries has yet another attraction for the European Satellites. To an increasing degree the economic development of the underdeveloped nations is occurring under some form of economic planning. Both parties then find it desirable to conclude trade agreements based upon a planned and frequently medium-term (2-5 years) exchange of goods, insulated against market fluctuations to the extent agreeable to both sides. In such cases, both parties are concerned by sharp movements in Western market prices and are susceptible to fears of the trade barriers existing in the larger nations of the West<sup>\*</sup>; their trading relationships potentially fulfill common needs.

The expansion of Satellite trade with the underdeveloped countries, while desirable from the viewpoint of the Satellite economies, would not solve all the basic trade questions. To the extent that Poland, East Germany, Czechoslovakia, and Hungary have completed much of their basic industrial buildup, they have become increasingly interested in advanced technology and advanced equipment. For these, they have turned increasingly toward the industrialized countries of the West. Rumania submitted to US Ambassador Thayer an impressive list of equipment which it would like to obtain from the West. The Soviet Union also desires an impressive list of such equipment. 6/ The Satellites have been unable to satisfy their desires in this respect both because of Western Cocom controls and

\* Especially those barriers erected during a decline in business activity.

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because of their limited ability to market goods in such countries as Great Britain and the United State.

If it should so desire, the Soviet Union possesses significant ability to limit Satellite trade relations with the industrialized West by channelling to itself those few items which have ready markets in the West, -- such as Polish coal, chemicals and fertilizers from several Satellites (especially from East Germany), and foodstuffs. As the dominant trade partner of each of the Satellites it is in position to do this, and doubly so as a major creditor.

The Soviet Union can further influence the economic development of the various Satellites through its re-direction of the basic commodities received as privileged export shipments from other Satellites. These shipments of machine tools, chemicals, electrical equipment, synthetic rubber, and the like, and which are of Satellite origin, are essential to the development and operation of the industries of all the Satellites. The USSR received priority claims on exports of these products either by virtue of past ownership of the producing enterprise (as was the case with the former Soviet-owned enterprises in East Germany, Hungary, and Rumania) or in repayment of investment credits granted to all the Satellites. It is in this context that the Polish government sees the importance of the Soviet cancellation of the 2.4 billion ruble credit repayment obligation due the Soviet Union from Poland.\* This debt was in every sense a Soviet mortgage on the Polish economy.

\* This debt was cancelled in November 1956 against Polish claims for compensation arising from Soviet underpricing of Polish coal shipments to the USSR and against Polish reparations claims against East Germany which were exercised by the USSR.

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VI. Economic Reforms.A. Decentralization.

One of the economic reforms which has been going on within the Soviet Bloc deals with limited decentralization in the managerial direction of the economy. This movement was apparently initiated by the USSR early in the 1950's. Several Satellites (Czechoslovakia, Poland, Hungary, and East Germany) have instituted somewhat similar measures.

The Soviet model for decentralization is reflected in organizational and operational changes in the economic managerial structure which have been carried out within the past few years. A number of economic ministries have been partially decentralized, chiefly by reorganizing some all-union ministries into union-republican and transferring a number of enterprises from national to regional control. In planning, the central apparatus of the Soviet Government now restricts itself to broad target figures, and has granted considerable responsibility to union-republics, ministers, and plant directors to draw up their annual plans. Planning authority remains strongly centralized, however. Ministerial reorganizations and the delegation of planning details have been coupled with a general increase in the economic role and responsibility of the union-republics. Finally, plant directors have steadily gained power more commensurate with their earlier responsibilities.

The Yugoslav model for decentralization has also involved the delegation of detailed planning to lower level organizations. It has gone considerably further than the Soviet pattern, however. Since 1950, Yugoslavia has had a system of worker's councils. These councils in the individual plants constitute one of the main pillars of economic-managerial decentralization in that country. The councils elect a management board to run the plant in conjunction with the director. 1/  
The legal powers of the worker's councils include the following: 2/

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1. Select and dismiss the plant director.
2. Fix wages, prices, and establish certain working conditions.
3. Formulate operating plans and supervise balance sheets.
4. Distribute the income of the plant among wages, amortization, etc.

Theoretically, at least, the worker's councils control the management and, in general, run the enterprise. In practice, the councils are not as active in daily management as their legal charter would imply. The councils appear to follow the suggestions of the director and the party leaders, the latter frequently working through the plant union. <sup>3/</sup> This lack of direct control by the council is further displayed by party control of the list of candidates, who are later elected to the worker's council by the plant personnel. <sup>4/</sup> In addition, a plant is rather strictly supervised by the local branch bank, and any financial difficulty in which it finds itself subjects it to a peculiar form of central control, termed "socialist sequestration." <sup>5/</sup> Finally, the plant manager, particularly since he is probably a communist, has the official right to make final decisions in the plant.

Czechoslovakia has been one of the most advanced Satellites in introducing decentralization. In this country, the Soviet model has been generally followed in such specifics as delegation of planning detail \* and the grant of rather extensive powers to plant directors. In fact, Czechoslovakia has apparently given more powers to plant directors than have other Satellites or even the USSR. <sup>6/</sup> Regional and district authorities have also been strengthened. More state farms, for example, will in the future be subordinate to national committees. Also, area administrations of certain ministries have been or will be transferred to regional national committees. <sup>7/</sup>

Poland, like Czechoslovakia, has carried out general reforms in extending powers of plant directors, such as granting to enterprises the

\* The annual plan for 1957 will reportedly contain only four-fifths the number of target figures compared to the 1956 plan.

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right to formulate their detailed plans on the basis of central targets. Recently, the Polish Sejm dissolved the State Economic Planning Commission and replaced it with a smaller planning body having much more limited powers. This new organization will have no authority to issue "binding directives" to ministries and people's councils, 8/ as apparently its predecessor had. Ministries and lower-level councils will probably benefit from this development by enjoying more freedom of operation. Somewhat contrary to the Soviet model, however, Poland seems to be following the Yugoslav pattern of establishing worker's councils in individual enterprises. These councils appear to have powers and responsibilities similar to those found in Yugoslavia. 9/

Hungary has also instituted general administrative improvements along the Soviet pattern, but like Poland, appears to be following the Yugoslav model in setting up worker's councils in the enterprises. 10/ In addition, a number of enterprises have been transferred to the jurisdiction of the county and town councils--in seeming agreement with the Yugoslav system. 11/

East Germany, like Czechoslovakia, follows more the Soviet rather than the Yugoslav model of decentralization. Thus, planning is to be simplified and local ministers and plant directors are to receive additional powers. 12/ However, the East German Communist Party has felt it necessary to give some deference to the Yugoslav system of worker's councils. East Germany will probably establish "worker's committees" in each enterprise, but probably will withhold significant powers from them. 13/

B. Labor Reforms. 14/

During 1956, the European Satellite regimes took action on an unprecedented scale to improve the economic welfare and working conditions of the industrial labor force. These actions were motivated in part by the necessity for devising ways to increase labor productivity and in part by the need to placate restless populaces. Although the

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particular measures taken differ widely in scope and content among the countries, the net result in each case is some improvement in the lot of the industrial worker; the net effect on productivity cannot yet be determined.

Labor laws and practices in the Satellites are patterned more or less after those of the USSR. Liberalizing measures in the labor field taken by the USSR during 1956 for economic motivation undoubtedly stimulated Satellite actions along the same lines. In addition to the Soviet example, however, the particular pattern of reform adopted in each Satellite was also influenced by its reaction to the Soviet repudiation of Stalin and by its own complex of events, including the extent of worker unrest.

Four of the Satellites cut the regularly scheduled workweek from 48 to 46 or fewer hours; in Bulgaria and Czechoslovakia a general 46 hour workweek was established, while in Hungary and Rumania the reductions applied only to designated industries. Although East Germany and Poland did not reduce working hours during 1956, they have indicated an intention to do so during the current five year plan periods.

Each of the countries took action of some kind to raise wages of various categories of workers and to adjust work norms. East Germany, Hungary, Poland, and Rumania made general, across-the-board increases in basic minimum rates, thus giving substantial wage increases to the lowest-paid workers. In Bulgaria wage increases were few and benefited an insignificant number of workers, whereas in the other countries wage adjustments had more significant impact. Poland, for example, accorded wage increases to some 4 million workers, nearly two-thirds of all non-agricultural employees. Increased work norms in some industries, particularly in East German industries, negated the benefits of the wage adjustments to workers' total earnings. All countries have plans for further wage and norm reforms during the next few years.

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Each Satellite has improved its social security system, which provides temporary disability benefits, family allowances, and pensions. All of the countries except Hungary have effected substantial increases in old age, disability, and survivors' pensions by establishing higher minimum pensions for each category. Hungary improved temporary disability benefits somewhat. A comprehensive revision of the entire social insurance program is scheduled to become effective in Czechoslovakia on 1 January 1957, and Poland plans to raise family allowances on that date.

Most of the Satellites have taken steps to liberalize the existing, highly-restrictive laws governing absenteeism, job-transfer, and other forms of labor discipline, although East Germany and Czechoslovakia have taken no action in this respect. Rumania repealed laws that had permitted compulsory transfer of workers on government order and had prohibited voluntary leaving by the worker. Poland and Hungary abolished criminal penalties for absenteeism and other infractions of labor discipline. Several of the countries are engaged in comprehensive revisions of their criminal and labor codes.

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APPENDIX A

RECENT SOVIET POLICY STATEMENTS CONCERNING  
SOVIET-SATELLITE ECONOMIC RELATIONSHIPS

In order to examine the points of difference and the points of common interest in the foreign policies of the Soviet Bloc countries, several pertinent policy statements will be examined.

1. Soviet Economic Policy (Twentieth Party Congress). In February and March 1956, the Soviet Union once more affirmed the priority of the policy of maximizing economic growth, with special emphasis upon the growth of heavy industry, over the policy of consumer satisfaction. Nevertheless, extensive measures have been undertaken, especially in agriculture and housing, in order to improve living standards:

"The chief task of the Sixth Five Year Plan for the development of the national economy consists of insuring the further mighty growth of all branches of the national economy, on the basis of preferential development of heavy industry, uninterrupted technical progress and increase of the productivity of labor, of realizing an abrupt increase in agricultural production, and on this basis, of insuring significant increase in the material welfare and cultural level of the Soviet people." 1/

2. Many Roads to Socialism (Twentieth Party Congress). The Congress reaffirmed an old Lenin statement, "All nations will come to socialism; this is inevitable; but they will not all come in in quite the same way, each will make its own contribution...." The Congress then went on to say, "It is perfectly logical that the forms of the transition to socialism will be still more varied in the future." 2/

3. Soviet Bloc Economic Cooperation.

"The fulfillment of the tasks of the Sixth Five Year Plan will be a great contribution to the cause of the further consolidation of the entire socialist camp. The Soviet Union will expand in every way its cooperation with the People's Democracies in the field of the most rational utilization of the economic resources and production capacities in common interests, by way of the coordination of the development of individual branches of the national economy, by way of specialization and cooperation in production, and also, by way of exchanging scientific and technical achievements and advanced production experience." 3/



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A comparison of this statement with paragraph 2, above, indicates that the thesis of many roads to Socialism applied to the political sphere more than to the economic sphere, was the intent of the Twentieth Party Congress. If rational utilization of economic resources was to become the Soviet Bloc joint policy, some type of central decision making body was to become effective, which is now known to be CEMA (Council for Economic Mutual Assistance) and the important Soviet organizations linking CEMA planning to Soviet planning.

4. Economic Competition between the Soviet Bloc and the Capitalist Nations.

"The Twentieth Congress of the CPSU considers that the Soviet nation now has all the conditions necessary for accomplishing, by means of peaceful economic competition and in historically the shortest time, the main economic task of the USSR -- to overtake and surpass the most developed capitalist countries as regards per capita production." 4 /

In retrospect, the speech of A.I. Mikoyan before the Twentieth Party Congress was one of the most important statements containing the true goal of Soviet economic relationships with the Satellites. Strangely enough, the same speech helped to unleash two concepts which were to shake the Soviet Bloc. The following paragraphs deal with this topic (paras. 5-7):

5. Consolidate the Bloc and Divide the West.

"The inception, growth, and strengthening of the mighty camp of socialism is the principal factor in the fundamental changes in the international situation. A socialist society has been built in the Soviet Union; great China and the People's Democracies are marching with rapid steps along the path of the building of socialism. A world socialist system has been established and consolidated and is developing, while the world capitalist system is in a state of crisis; it has weakened and is losing one position after another." 5 /

Parenthetically, it should be noted that a Marxist discussing the socialist system and the capitalist system is discussing economic systems as well as political societies. For this reason, the statement should be read with paragraph 3 in mind (preceding page of this report). In addition, it is significant that the statement was made by Mikoyan, who is one of the authors of the Soviet Bloc's coordinated economic planning system.

S-E-C-R-E-T6. The Attack on Stalin and the Cult of the Individual.

The sharp remarks contained in Mikoyan's speech ante-dated Khrushchev's more famous speech upon the same subject. It is not likely that Mikoyan realized the weakening impact that the attack upon Stalin, and the campaign against the secret police, would have upon Soviet authority in its relations with the Satellites.

7. Burial of the Thesis of Capitalist Encirclement.

"The time is past when the Soviet land of socialism was isolated, when we were an oasis in the capitalist encirclement." Now the Soviet Union is joined by a system of socialist states and is no longer alone. In addition, Mikoyan added, Socialism is already incomparably stronger than capitalism in the minds of men. "This is why it is not for us to fear a struggle between the ideas of socialism and those of capitalism." Now the struggle can be conducted in terms of peaceful coexistence. 6 /

In replacing the fear of capitalist encirclement with a call for competitive peaceful coexistence, the Soviet planners encounter a basic problem which was graphically illustrated in subsequent events, especially in Poland. The problem is this, to compete with the Western world, the Soviet Bloc must continue its program of forced-draft industrialization. Yet to a high degree, in the past, this rate of economic growth was achieved only by regimentation within the various states. This regimentation was facilitated both by fear of Soviet authority and by fear of capitalist encirclement. Weaken these fears, the regimentation is then weakened, and the rate of growth suffers, unless incentives to individual performance can replace the whip of authority. This point was well recognized by the Polish economist Oskar Lange who wrote in a Polish periodical in July of 1956, "We directed the economy through methods which are characteristic of 'wartime economy'", i.e., through methods based on appeals of a moral and political character as well as on orders of a legal and administrative character, in other words, through methods based on various means of extra-economic compulsion and not on economic incentives." 7 / (Underlining added.)

S-E-C-R-E-T8. Many Roads to Socialist Construction.

After the Soviet-Yugoslav talks held in May and June of 1956, the Soviet reaffirmation of the principle of many roads to socialism was extended to the economic sphere, in what was to become an extremely important extension. The old Lenin statement (see Para. 2, above) was hauled out once more, but the following words were added by the editors of Pravda:

"The historical experience of the Soviet Union and of the people's democracies shows that, given unity in the chief fundamental matter of ensuring the victory of socialism, various ways and means may be used in different countries to solve the specific problems of socialist construction, depending upon historical and national features. 8/

In the same editorial, the following features of the Yugoslav politico-economic system appeared to be set forth as features acceptable to the Soviet Communist Party:

- 1) Unity in the chief fundamental matter of ensuring the victory of socialism.
- 2) Public ownership of the basic means of production, in large-scale and medium industry, transport, the banking system, wholesale trade, and most of retail trade. (Note the exception of small scale industry and of some retail trade.)
- 3) The state system is determined by the fact that the working class and the peasantry hold the reins of power. (I.e., a Communist party).
- 4) Pursuit of a "fitting socialist foreign and domestic policy."
- 5) Extension and strengthening of political and economic ties and cooperation by Yugoslavia with the Soviet Union and the people's democracies. 9/

These principles are of extreme importance. At the time, they were extended to Yugoslavia only, and there is no evidence that the Soviet Union anticipated extending them to any of the Satellites. Yet a major precedent had been set. It is further of note, that the reforms proposed by the new Gomulka government in Poland do not violate these principles openly, except only by strict interpretation of such a

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clause as 4) which contains the deceptive word "fitting." On the other hand, the changes proposed by the Nagy government in Hungary went far beyond these limits.

9. Soviet Statement on Satellite Relations, 30 October 1956. 10 /

This statement was an admission by the Soviet government that the principle of equality had been violated in relations with the other Bloc countries. In addition, the USSR indicated willingness to reexamine the subjects of mutual relations in the military and economic spheres. Nevertheless, the USSR indicated that it would take a rigid position in defense of its military interests by indicating that withdrawal of Soviet troops from any country which is a member of the Warsaw Pact could be only with the consent of all the other signatories. The USSR would be willing to discuss the recall of Soviet advisers, and the wording indicated that some concessions would almost certainly be made along this line.

This statement must have been made under some duress. While it is not basically a definitive restatement of Soviet policy vis-a-vis the Satellites, it is a confession of mistakes (a dangerous precedent) and an admission that there exist basic areas of friction between the Soviet Union and the Satellites (and apparently not limited to Hungary and Poland, judging from the context).

The section relating to economic frictions is of particular interest.

The Soviet government is ready to discuss with the governments of other socialist states measures insuring the further development and strengthening of economic ties between socialist countries, in order to remove any possibility of violating the principle of national sovereignty, mutual advantage, and equality in economic relations. This principle should extend also to advisers.

If this statement is compared with the statement of the Twentieth Party Congress concerning Soviet Bloc economic cooperation (Para. 3, above), it becomes evident that the nature of joint planning for the period 1956-60 may be subject to significant change, and that there may be revision of the 1960 economic targets in several Satellites.

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Significantly, this statement does not specifically grant Poland the same latitude of action as previously accepted in the case of Yugoslavia. Yet Gomulka, by treading the Yugoslav line, has a strong precedent. In addition, the Soviet admission of mistakes and the specific affirmation of the validity of the principle of equality in the sphere of economic relations should serve to strengthen Gomulka's theoretical position.

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APPENDIX B

THE DISCUSSION OF REFORM IN THE POLISH ECONOMY

Statement of Purpose.

Poland is now in a unique position among the countries of the Soviet Bloc to attempt new approaches to stimulate the interest of the workers and peasants in their tasks specifically and in the economy generally. This unusual opportunity afforded Gomulka and his economic advisors, including Oskar Lange, is furnished by the popular support on which the new regime rests, and without which it must fall, and by Soviet acceptance of the new regime, however reluctant. If a high degree of interest on the part of the workers and peasants is aroused and maintained, the Polish experiment may become increasingly tempting to other peoples of the Soviet Bloc and may lead to a reduction in the pervasive role of authority in other Communist states.

Although the present opportunity to experiment is new, the economic crisis, rooted in shortages of raw materials and advanced capital equipment and in the growing apathy of the workers and peasants, is not novel. As a result, for several months preceding the Gomulka regime, Polish journals were deeply involved in developing the concepts of a new economic program. The issues raised in this continuing discussion are examined in the following pages.

In addition to drastic revisions which have been and are still being made in the order of priority tasks originally set by Poland's Five Year Plan, various reforms in making and implementing economic policy have been provisionally adopted in the hope of curing certain basic economic ills: the low productivity of socialized industry and agriculture, the uneconomic use of the resources Poland has available, and in general a high cost of production, to which is attributed the necessity of subsidizing many industrial enterprises and most cooperative farms. This section proposes to discuss the possible consequences of such reforms, or of the failure to carry them out, in a period of expected transition

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from a system in which compulsion has played the major role to one based on a freer interplay of economic forces.

There has been a growing disposition over the past six months to assign the above maladies a dual basis: centralism in administering the economy and lack of adequate incentives to produce. Insofar as the solutions proposed for them may be reduced to a single denominator, however, decentralization is their frame of reference.

1. Reorganization at the Apex of the Political Economy.

The desire of Polish economists to simplify and streamline the running of their economy was dramatically symbolized by the liquidation of the State Economic Planning Commission, which took place November 15, 1956, and the reorientation of its functions within a Planning Committee attached to the Council of Ministers which was established in its place. Potentially the most significant change that occurred in this transfer of functions was the abolition of the SEPC's power to administer indirectly all units of the economy by issuing binding directives to the various ministries on operational questions. As a result of this shift, the manpower of the former SEPC has been reduced from 1700 to 1000, and the original 40 departments within the SEPC have been cut to 29.

As the Planning Committee assumed a subordinate and advisory role, the power of the ministries was correspondingly strengthened, and the Council of Ministers has taken on the operative function lost by the SEPC. The Council has been reorganized into three sections, one for industrial production, construction, and transportation, one for agriculture, and one for welfare and services. The Planning Committee, on the other hand, submits proposals regarding the supply of food and consumer goods, problems of prices and wages, economic incentives, and investment and foreign trade policy.

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The importance of the Sejm, too, has been heightened with regard to planning. From a short-range point of view this has come about accidentally, arising from the nature of Gomulka's strongest weapon against Soviet control over the direction of Poland's economic growth, his popular support. The Sejm has as a consequence taken on the aspect of a debating chamber after the Western model, a sounding board for the multitude of suggestions regarding industrial management and planning which have been advanced by worker delegations. Proposal and counter-proposal on possible changes in the Five Year Plan have been permitted, perhaps in part with the hope that the best way out of Poland's economic difficulties will be discovered by this means. Efforts which are being made to legalize and perpetuate this de facto situation apparently stem from the fact that the country's economic needs require a more flexible National Economic Plan, and that this can best be achieved by continuous supervision of plans and performance by the Sejm and its committees. It is held that the latter should work out future long-term plans in conjunction with the various ministries, and the Sejm as a whole should be given the power to confirm plans on an annual basis.

Formal recognition has thus been extended to the traditional distinction between planning and decision-making. This appears to be an important step toward economic decentralization because it has taken place on the highest level. It should be kept in mind, however, that in practice the line between these functions becomes blurred at that level under conditions of forced growth. Rapid growth has not been repudiated, and it is probable that its rate has only temporarily subsided. At the moment it may be not only desirable but quite possible to separate the executive from the legislative functions, but once the breathing spell ends, the same forces which produced an SEPC combining both functions may again reassert themselves and the trend toward unification of both these kinds of power in a single body may reappear.



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Nonetheless, these changes are significant in the short-term in that they attest to the regime's present intentions to relax the grip over the economy which has been maintained by the mechanism of administrative decision making. More interaction among alternative "decisions", an opportunity for which has been given by the Planning Commission's reorganization, will inevitably color the results of planning with some degree of unpredictability. Further, the Sejm's new watchdog role will have a restraining effect on the tendency, characteristic of an administered economy, for decisions which look well on paper to be carried through arbitrarily regardless of their harmful economic and political consequences. As long as it is the regime's desire to obviate that possibility, greater scope may be permitted to nationally responsible discussion of broad alternative policies, just as is intended, on a more restricted scale, within the Council of Ministers.

2. Territorial Decentralization.

In the area where decentralization of planning merges with that of management, some changes have been confirmed which parallel those adopted in the USSR since the Twentieth Party Congress. More power to make short-range plans and operational decisions has been given the Central Boards (analogous to the Soviet "chief administrations") within the ministries. In addition, a wider role than hitherto has been assigned to the lower territorial subdivisions of the State, administered by the People's Councils. Responsibility for local light industries, for locally derived building materials such as quarries, brick kilns and the like, for food processing, and for the entire retail network, has devolved upon the provincial, county and parish People's Councils. Revenue for conducting these activities is to be drawn not from the central budget, as formerly, but from all the forms of tax levied on enterprises subordinate to the People's Councils, taxes which are no longer, therefore, channelled into the State Treasury. On the

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basis of these sources of revenue the Councils may now adopt their own budgets.

This reform appears to be designed to simplify the central government's problem of supervising economic activity; it is not calculated to be a stimulus to local self-determination, however much it savors of democratization. The local People's Councils are in charge, for instance, of the restoration by local craftsmen of their workshops, fallen into disrepair as the craftsmen were forced out of business over the past decade. They are in charge of the carrying out of policy, in other words. Similarly, they are permitted to invest at their own discretion only within the framework of the gross quantities allotted specifically for these purposes by the national plan. And, to make this limitation all the more binding, although these local bodies can make changes in their planned investments, they can only do so if no expenditure of money or material is required beyond that approved by the plan. Lastly, the national plan defines for the economy subordinate to the People's Councils all economic tasks of national significance. This can be a rather flexible criterion.

The over-all pattern of reforms under consideration was set forth in the report to the Sejm on November 7 of Lange's budgetary and finance committee. Besides urging the decentralization and simplification of planning (such as a reduction in the number of indexes centrally determined) and an enlarged role for the People's Councils, the committee advocated greater autonomy for socialist enterprises, a greater scope for worker self-government and a rise in material incentives to stimulate the worker's interest in the results of his labor. Such a general solution to Poland's ills has been under discussion over a relatively long period of time -- even before the Gomulka regime -- and whatever action is taken will undoubtedly fall within its framework.

Thus, Workers' Councils within industrial enterprises have been recognized and encouraged to put forward whatever changes they deem desirable in the policies or the running of such concerns. Official

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sanction has been given to the implicit assumption that the entire range of industrial management and labor relations is within the province of low-level discussion and even action, in that delegations presenting programs based on such wide perspectives have obtained sympathetic hearings in the press and within the government.

3. The Prerogatives of Workers' Councils.

Among the powers these councils have been granted are the right, in principle, to approve the detailed production plans, both in physical and financial terms, which are annually handed down by the Central Boards within economic ministries, and the right unilaterally to introduce changes in production methods without changing the entire plan.

In the foreground of demands preoccupying the workers but not yet sanctioned by the government are the following:

- a. Power to control the wage fund and to set norms and wage differentials.
- b. The right of advising as to the distribution of all profits, both planned and unplanned. A typical recommendation runs as follows: of total profits from the former category, 70 percent is to be turned over to the State, 10 percent is to be directed into the works fund (analogous to the Soviet "director's fund"), and 20 percent to the wage fund. Of profits on excess production, 50 percent would go to the State, 10 percent to the works fund and 40 percent into wages.
- c. Final authority in the selection of a director for the enterprise and residual control over his decisions, including the right of demanding his recall.

In addition to the above ideas, there is a group of recommendations of even more vital concern to the principle of planning than those which have to do with the wage fund and profit sharing. They include:

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- a. Greater freedom for the enterprise in determining the scope and placement of its investments. Some degree of control by the national plan is conceded.
  - b. Control over price policy. The reform envisioned here is to make the sales price more realistic in terms of the factory price, i.e., to narrow the margin created by turnover tax and profit. It is difficult to discern if this reform is meant to apply to producer goods or consumer goods, or to both.
  - c. The privilege of making non-planned deliveries to both socialized and private concerns, and, beyond this, the right of selecting the plant's own suppliers and customers.
4. Improvement in Efficient Use of Resources.

It is noteworthy that a rise in labor productivity, usually very much in evidence in similar Soviet programs, figures at best only as one implication of the final proposal. This can be traced to Oskar Lange's conviction that reforms should be directed not primarily to a quantitative increase in overall production but to an improvement in quality, a decrease in plant production costs, and in particular the husbanding of raw material resources and a reduction in the costs of producing or obtaining them. Gomulka laid heavy stress in his October 20 speech to the Eighth Plenum on the dearth of industrial raw materials which puts Poland at a disadvantage in trade with the West, and called attention to the necessity, for regular production, of building up adequate reserves in these basic resources.

It is hoped that several of the reforms in decentralizing responsibility will help correct this deficiency. Cutting the red tape that discouraged initiative in originating and carrying out improvements in production methods should lead to savings in materials and their fuller utilization, where this is possible. In the realm of incentives, it is planned to provide premiums out of the works fund for savings in raw

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materials. Worker motivation toward this end would be heightened by a liberalized basis for profit sharing, such as that mentioned above. In general, greater responsibility by the workers, engineers, technicians, and economists representing the enterprise on the Workers' Council over the setting up of the original production targets would afford an opportunity of forestalling the uneconomic use of materials. The proposal, not yet approved, to allow a plant unplanned disposal of the revenue on 30-40 percent of the year's output would also be conducive to the most efficient utilization of resources, since the plant would try to maximize profits, and would have the further advantage of helping to eliminate bottlenecks in production elsewhere, or, in the case of consumer goods, in the distribution system. Two objectives are involved, therefore, in liquidating the problem of material scarcity, one being cost considerations, the other stockpiling to insure rhythmic production. Decentralization, a greater stake in profits for the plant, and something less than total allocation of output or the revenue thereof, all help to solve that problem. These solutions, however, call into play certain economic forces, which, once released, are to a certain degree uncontrollable, and may react unfavorably on other problems the economy is facing.

One such problem is unemployment. According to a report in the June 10 issue of Po Prostu, there were then 300,000 unemployed workers, of which two-thirds were women. At the same time it was estimated that worker "superfluity", or underemployment, amounted to two million. Granting to this estimate a large measure of exaggeration to buttress a point, it still is undoubtedly true that a considerable number of workers, in particular women, are unproductive most of the time, though on the pay roll. One major cause of this is the necessity in many families for all adult members, including the aged and the women, to hold jobs in order that the family maintain a minimum standard of living. Measures to raise pensions and minimum wage levels, and to afford some tax relief, will have the effect of removing a few workers from the labor force.

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Basically, however, the need is to use the labor force more efficiently, not to reduce it. A more constructive measure to curb underemployment follows from the decision to reverse the previous policy of centralizing industrial production in Poland's large urban centers. That policy had led to the liquidation of such small-scale, local enterprises as quarries, sawmills, breweries, and handicrafts such as textile workshops, causing in the process local labor surpluses. The concept of regionalization behind it, in their words, the "equal distribution of production" between city and country, is now unfavorably contrasted to a "rational distribution of production", which is designed to encourage local industry and private handicrafts, thus absorbing local surpluses when they exist and, presumably, creating small vacuums to be filled by underemployed personnel in socialized industries. A step designed to stimulate a resurgence of handicrafts is a two-year tax exemption for any shop employing no more than one hired laborer. In order further to encourage the development of the capacity of these localities to absorb labor, the government has made available to them investment money to the extent of 100 million zlotys in 1956 (most of which has by now been allocated), and 200 million zlotys in 1957. These policies will make for a geographic decentralization of the economy parallel to that envisaged in the sphere of decision making.

5. Some Basic Economic Problems.

There are many obstacles to the solution of the underemployment problem, including some created by the policy of decentralization. In the first place, the materials situation will probably remain static, or improve only slowly, despite the savings effected by greater efficiency. In order to obtain a steady flow, in quantity, of her materials requirements, Poland must export in quantity and thereby stabilize her balance of payments. The only product she can handle this way which is in great demand throughout Europe is coal, and the likelihood is that exports of this commodity will continue to diminish for some time.

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Secondly, it may be assumed that in order to economize on resources as much as possible, the opportunity afforded by quasi-autonomy on the production unit level will be utilized to make wiser choices between alternative solutions to investment and production problems. Hence high production costs, a salient target of Poland's new economic policy, will be lowered. This measure may reduce employment in some plants.

Thirdly, the reduction of high production costs through efficiency will be meaningless unless some stable, predictable relationship is established between these costs and the sales price. This applies especially to consumer goods industries, where political consequences tread more closely on the heels of economic policies than in the producer goods area. Since at the plant level the emphasis of this new policy is on profitability, rather than on a continuance of quantitative overfulfillment of plans, an effort will probably be made to cut down the number of subsidized--unprofitable--plants. Lange has underlined the need to hold industrial enterprises accountable for the amounts invested in them. In the discussion over policy it has even been advocated that an interest rate be charged on funds allocated for capital investment.

These policies are intended to raise labor productivity. The supply of raw materials, however, will not be adequate to meet the subsequent heightened capacity of Polish industry to absorb materials, despite the possible reduction in the total number of production units through the elimination of those which are now subsidized. Unless the newly resuscitated private and handicraft sectors can provide for the surplus labor resulting ultimately from the attempt to conserve materials, raise quality, and reduce costs through decentralization and enterprise autonomy, there is likely to be an unemployment problem after 1960, when the total labor increment will amount to more than 500,000 in subsequent five year periods.

S-E-C-R-E-T6. Special Economic Problems of a Planned Economy.

The specifically economic theme running through all these changes, both adopted and proposed, is increased profitability in all sectors of the economy. It is most obvious in agriculture, where the situation calls for the most drastic measures. Gomulka and his advisors have taken their stand on the abolition of subsidization of cooperative farms. If their number decreases in the short run, that is not a vital set-back, they maintain. What is essential is that the most economic means of production be found. Of course, there is an important limitation on this policy, for it is not intended to threaten the "social" goals of communism. But from a short-term viewpoint, higher productivity, with the goal of greater efficiency, is seen as having a close relation to profitability. This idea is carried over into industry.

Now if the market place is to be the test for this, the price system must be altered to allow competitive pricing among industrial enterprises. The possibility of this occurring is doubtful, for it brings the threat of "monopolist exploitation" of the market. The principle of centrally manipulating the price system is still adhered to in Poland, but the regime does intend to adjust prices to cost, for it recognizes the necessity of finding out how much has been expended or saved in the production process in order to determine where savings may best be effected. Real production costs are determined by the "change of prices in goods turnover between enterprises", Gomulka stated in his October speech, referred to above. The guarantee that such changes will not be "fictitious", he went on to say, is the enjoyment of full economic accountability by the individual economic units.

If this assertion is to be taken at its face value, it brings the problem full circle again. Fluctuations in the demand for a plant's products are of course first felt by that plant. Carrying this premise to its logical conclusion, Polish economists admit that to make the proper and timely adjustments in output or in assortment, an enterprise



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should be in close touch with its customers, "not only with another state enterprise, another organization receiving its products, but with the actual consumers", as the president of the Polish Economists Society recently said. This implies contractual freedom by an enterprise in obtaining supplies and in disposing of its products. This freedom can only operate efficiently within a framework of equilibrium prices, i.e., prices which equate supply and demand and are responsive to changes in supply and demand. There has been no indication in Polish discussions to date of an intent to achieve this kind of price equilibrium. In addition, it is questionable that this could be achieved by central planning, even if attempted. In sum, while political imperatives militate for the immediate satisfaction of demand, the Soviet-style quest for rapid economic growth creates pressures in favor of an administered economy.

A satisfactory solution to the perennial problem of reconciling centralized authority in policy making with delegated authority in carrying it out is thus being sought more intensely and on a wider scale than heretofore in Poland. This is taking place at present on two broad fronts, the industrial and the administrative, and is based on a general conviction among the proponents of Gomulka's policies that to encourage the anti-centralist, and indeed syndicalist, tendencies which are so patently obvious throughout the country, is both economically desirable as a means of reducing inefficiency and increasing the profitability of socialist enterprises of all descriptions, and politically mandatory as a means of retaining support for the regime. It is on the first of these fronts that the desire for widespread democratization has taken a clear-cut, programmatic and specifically economic form in the Workers' Councils which have sprung up in most Polish plants.

The Workers' Council movement promises two positive gains for the regime; first, it fosters the political support by the workers upon

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which the Gomulka regime depends; second, it should enlist the more enthusiastic participation of the workers in production, on which depends the hope of the regime for an increase in labor productivity. On the other hand, the degree and scope of authority and power which the Workers' Councils have been demanding are incompatible with the managerial efficiency which the Gomulka regime is urgently seeking. Therein lies Gomulka's dilemma.

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APPENDIX C

SURVEY OF ECONOMIC DEVELOPMENTS IN THE EUROPEAN SATELLITES

UNDER THE FIRST LONG-TERM PLANS

(Draft of ORR Project 10.804)

14 DECEMBER 1956

(Two copies of draft  
submitted to ONE  
only as APPENDIX C)

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