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European Review

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25 September 1985

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25 September 1985
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European Review [redacted] 25X1

25 September 1985

[redacted] 25X1

The recent conclusion of a rescheduling agreement with Western governments has done little to brighten Poland's financial outlook. Warsaw will be hard pressed to meet the payments required under this agreement and those made with banks. Poland probably will not achieve its planned hard-currency trade surplus for 1985, and creditors remain reluctant to extend enough loans to cover the financial gap. Difficulties will increase in 1986 as more repayments of principal fall due on previously rescheduled debt. The regime probably will try to bridge the gap by favoring payments to banks over governments with the hope that the Paris Club will not call default for nonpayment. Another possibility is for Warsaw to request a further rescheduling of repayments due on the 1981 and 1982 agreements. [redacted] 25X1

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[redacted] 25X1

The competitive elections for the National Assembly and local governments this summer—a novelty for Hungary and the Soviet Bloc—were a limited success for the Kadar regime. While presenting little risk to the party, they won Budapest favorable publicity in the West as the most moderate and "democratic" regime in the Soviet Bloc, provided it a better measure of popular attitudes and grievances, and paved the way for reforms to revitalize the country's legislative and local administrative bodies. But they apparently have done little to enhance the regime's legitimacy—one of the major objectives of the experiment. The regime's turn toward limited political reform at a time of economic stagnation may reflect insecurity about its relationship with the Hungarian people and concern about the viability of the Kadarist social contract that has helped preserve social stability for the past three decades. [redacted] 25X1

Slovenia, Yugoslavia's most economically advanced republic, has become an increasingly vocal player in the debate over changes in the country's political and economic systems. In an officially Communist state, Slovenia routinely blocks efforts to centralize power in Belgrade, resists federally sponsored redistribution of resources to the poorer southern republics, and staunchly defends its Western cultural heritage and unique language. The republic will continue to exploit the decentralized post-Tito system to protect its interests but will press for market-oriented reforms and efforts to streamline the cumbersome federal bureaucracy. [redacted] 25X1

Some articles are preliminary views of a subject or speculative, but the contents normally will be coordinated as appropriate with other offices within CIA. Occasionally an article will represent the views of a single analyst; these items will be designated as uncoordinated views. Comments may be directed to the authors [redacted] 25X1

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Briefs

West Germany

Social Democratic Infighting

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A draft paper by Social Democratic Party (SPD) security expert Andreas von Buelow has provoked a storm of public criticism and controversy within the SPD. The paper proposes turning the Bundeswehr into a Swiss-style militia and cutting military service time in half. It suggests that these and other measures could induce the Soviets to withdraw their troops from Eastern Europe by the end of the century, after which the United States could remove its forces from West Germany except for a symbolic contingent in Berlin. The paper has no official party standing, but the Christian Democrats are branding it as further evidence of SPD hostility to NATO and the United States 25X1

Social Democratic moderates leaked the paper to the press in order to isolate von Buelow, whom they suspected of wanting to force leftist foreign policies on Johannes Rau in his race for chancellor in January 1987. The SPD leaders, however, generally defended von Buelow both within the caucus and in Bundestag debate, although they disavowed the notions of US troop withdrawals and turning the Bundeswehr into a militia. As a result, party moderates reportedly doubt whether Rau will be able to buck the leftist trend in the Social Democratic leadership. As a precondition for accepting the nomination for chancellor, Rau has demanded that the party stem its drift toward anti-Americanism and reaffirm its strong commitment to NATO, according to the source 25X1

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Foreign Affairs Appointments

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The Kohl government has finally filled two major foreign policy posts vacant since early this year. Hans Stercken will replace the late Werner Marx as head of the Bundestag Foreign Affairs Committee, and Lutz Stavenhagen will take over from the late Alois Mertes as parliamentary state secretary in the Foreign Ministry. The new appointees are both members of Chancellor Kohl's Christian Democratic Union and have been in the Bundestag since 1976 and 1972, respectively.

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Initial reactions to the appointments have been somewhat skeptical because neither has had much experience in foreign affairs. One conservative newspaper lamented in particular their inexperience in dealing with Eastern Europe and the Soviet Union. Stercken at least served on the Foreign Affairs Committee and gained some exposure to West European, African, and Israeli affairs. Stavenhagen, on the other hand, has a predominately commercial background and has focused in parliament on fiscal and research policy. It is too early to predict what effect these appointments will have on the formulation and conduct of Bonn's foreign policy, particularly since the chancellery retains a pivotal role. In any case, Kohl and his advisers clearly wanted to keep these posts in the hands of Christian

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Democrats despite the party's dearth of foreign policy expertise. Nevertheless, the upshot may be a freer hand for Foreign Minister—and Free Democrat—Hans-Dietrich Genscher, especially in the realm of *Ostpolitik*. [redacted] 25X1

Netherlands

Peace Movement Against Cruise Missiles [redacted] 25X1

The Coordinating Group of the Dutch Peace Movement has launched a two-month national petition to defeat a decision on INF deployment to be taken by the government on 1 November. The group hopes to reach a minimum of 80 percent of the 5.2 million Dutch households between 7 and 29 September and will present the results to Prime Minister Lubbers on 26 October at a mass rally. Mass signature campaigns are uncommon in the Netherlands, and historical precedent shows a mixed record of success. An August poll by the NIPO Public Opinion Polling Agency indicated 51 percent of the Dutch population will sign the petition. [redacted] 25X1

The petition, we believe, is not likely to prevent a favorable government decision on INF basing. Prime Minister Lubbers has stated repeatedly that his government will accept the deployment of cruise missiles if, by the decision date, the number of Soviet SS-20s exceeds 378. A successful petition drive, however, could jeopardize parliamentary ratification of the decision next year by increasing anti-INF tendencies in the Christian Democratic Party, the government's senior coalition partner. [redacted] 25X1

Romania

Export Push [redacted] 25X1

Bucharest has increased bonuses for managers and technicians whose enterprises exceed export and energy plans and has imposed stiffer fines for underfulfillment in an all-out effort to avert a financial crisis this fall. The decree, which will remain in effect for the rest of the year, also stipulates equivalent fines—the loss of up to 50 percent of wages—for managers of enterprises failing to make timely deliveries of raw materials and other goods to firms producing exports. [redacted] 25X1 25X1 [redacted] exports had recovered from the serious disruptions of last winter, increasing 11 percent in the second quarter compared to the same period in 1984. [redacted] 25X1 substantial shortfalls in planned energy production continued to hamper export production well into the summer. [redacted] 25X1

Bucharest must boost export earnings because prospects are uncertain for a $150 million commercial bank loan needed to meet debt repayments due this fall. The new measures are unlikely to increase exports of most goods because shortages of raw materials and intermediate goods caused by import restrictions are the chief constraint on export production. The regime, however, may augment exports of refined petroleum products by cutting allotments to the domestic economy, leaving the country vulnerable to severe energy shortages comparable to those suffered last winter. [redacted] 25X1

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Hungary

Banking Reforms 25X1

Hungary is moving ahead cautiously with its program to create a less centralized and more competitive banking system. According to the US Embassy in Budapest, the government recently created eight new institutions to finance technological development and foreign trade for state enterprises and cooperatives. The new banks will be allowed to peg their interest rates up to 1.5 percentage points above the base rate set by the National Bank. In addition, Budapest approved Citibank's plan to open in January 1986 a joint venture bank, after the IMF persuaded senior National Bank officials that the plan would not weaken their control over hard currency debt. The joint venture—of which Citibank will own 80 percent and the National Bank 20 percent—will engage in both domestic and international banking operations. Finally, the Foreign Trade Bank is to enter the domestic lending market while the State Development Bank can now issue bonds and establish joint ventures and financial institutions. 25X1

Budapest hopes these measures will improve the efficiency of credit allocation in the economy, but its wariness of excessive decentralization will limit the activities of the new banks. The National Bank will need to develop new policy levers to regulate financial institutions that are not its own subsidiaries. The new banks probably will remain cautious in their lending until they develop expertise in judging the creditworthiness of firms and the likely profitability of investment proposals. 25X1

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Poland: Financial Crisis Continues

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The recent conclusion of a rescheduling agreement with Western governments has done little to brighten Poland's financial outlook. Warsaw will be hard pressed to meet the payments required under this agreement and those made with banks. Poland probably will not achieve its planned hard currency trade surplus for 1985, and creditors remain reluctant to extend enough loans to cover the financial gaps. Difficulties will increase in 1986 as more repayments of principal fall due on previously rescheduled debt. The regime probably will try to bridge the gap by favoring payments to banks over governments with the hope that the Paris Club will again not call default for nonpayment. Another possibility is for Warsaw to request a further rescheduling of repayments due on the 1981 and 1982 agreements.

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Table 1
Poland: Debt Service Due [a]

Million US $

	1984	1985	1986
Total	**15,750**	**14,797**	**4,835**
Paris Club	12,602	12,807	2,109
Of which:			
Arrears	9,717	11,649	
Banks	1,185	1,570	2,014
Other	1,963	420	712

[a] Polish financial data.

25X1

Financial Situation in 1985

Poland signed an agreement with the Paris Club of 17 Western government creditors in July—after more than a year of talks—to reschedule all $11 billion in principal and interest due during the period 1982-84. By eliminating Warsaw's massive arrearages to Western governments, the agreement was a vital step toward normalizing relations with creditors. The two sides had initialed terms in January, but formal signing was delayed when Warsaw tried to obtain new credits from the governments and failed to make required payments on arrears from the 1981 rescheduling agreement. The Poles claimed that without new credits they could not meet payments required under the agreement. Warsaw signed the accord only after Western creditors agreed to reconsider the situation if problems develop.

25X1

The Paris Club extended very generous rescheduling terms to the Poles. The overdue debts were rescheduled for 10 years with a five-year grace period ending in 1990. Half of the interest due this year was rescheduled over four years; subsequent interest payments will be paid in full when due. To implement the agreement, the Poles must pay 50 percent of the 1981-83 interest arrears on the 1981 rescheduling agreement—about $200 million—and conclude bilateral agreements with the individual governments. Warsaw must also come up with approximately $1 billion in interest payments due for this year on its two rescheduling agreements with the Paris Club. New credit commitments will be decided between Poland and Western creditors during bilateral talks in the coming months.

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Financing Sources

Warsaw probably lacks adequate resources to meet these payments plus its obligations due under bank rescheduling agreements. Excluding the $11.6 billion in debt relief from the Paris Club, we estimate Poland's sources of financing at $2.4-2.6 billion compared with Warsaw's projection of $3.6 billion. The Polish estimate for a hard-currency trade surplus of $1.5 billion seems overly optimistic because the surplus in the first seven months of 1985 was $589 million, about $300 million less than the same period last year. Warsaw, so far, has not cut imports as in past years to meet its surplus goal. Imports in

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Table 2
Poland: Sources of Financing

Million US $

	1984 [a]	1985		1986	
		Polish Estimate	CIA Estimate	Polish Estimate	CIA Estimate
Total	**3,917**	**15,264**	**14,064-14,264**	**5,202**	**3,622-3,822**
Earned [b]	2,035	1,900	1,500-1,700	2,050	1,700-1,800
Hard currency trade	1,456	1,500	1,200-1,400	1,650	1,400-1,500
Exports	5,828	6,300	5,700-6,100	6,850	6,000-6,400
Imports	4,372	4,800	4,500-4,700	5,200	4,600-4,900
Services and transfers, net	396	500	400	500	400
Interest earnings	183	−100	−100	−100	−100
Borrowed	1,882	13,364	12,564	3,152	1,922-2,022
New credits	218	1,000	200	1,830	600-700 [c]
Recycled interest [d]	240 [e]	815 [f]	815 [f]	440	440
Credits extended, net	−176	−100	−100	−100	−100
Debt relief	1,600	11,649	11,649	982	982
Banks	1,600 [g]				
Paris Club		11,649 [h]	11,649 [h]	982	982

[a] Polish financial data.
[b] Earned payment capacity equals the current account balance excluding interest.
[c] Assumes $400-500 million in credits from the IMF.
[d] Separate agreements during the bank rescheduling accords of 1982, 1983, and 1984 provided that certain percentages of interest payments be re-lent in the form of short-term loans.
[e] Net figure: The Poles received $1.18 billion in revolving credits in 1984 but repaid $940 million.

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[g] The bank rescheduling of July 1984 covered payments due between 1984 and 1987.
[h] Includes rescheduling of about $10.3 billion due in 1982-84, and $1.4 billion due in 1985.

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January-July were up about 11 percent, with purchases of capital equipment rising more than 25 percent due to the regime's lack of control over investment. Exports to the West decreased 2.5 percent, with sales of coal and chemicals falling because of production and transportation problems caused by the extremely cold winter. Warsaw, which was relying on a large rise in machinery exports to meet its surplus target, was able to increase sales of these items only by marginal amounts.

Requests to Western governments for $600-800 million in new credits seem to have fallen on deaf ears. By the end of August, only Austria had signed a bilateral rescheduling accord with the Poles and provided $20 million in new commodity credits—less than 15 percent of Warsaw's original request—and a $20 million extension of an existing line of credit for agricultural items. The Dutch, Belgian, Swiss, Italian, and Canadian bilaterals, however, were held up due to disagreements over the rates of interest that would apply. If the accords are signed, West Germany may grant $30 million, Switzerland $20 million, and France about $10 million, but only after the 1985 rescheduling accord is signed and all payments are completed. The British, Italians, and Swedes also may grant some trade credits. The Belgians, Portuguese, Greeks, and Canadians have yet to decide on granting 25X1

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new loans while the Japanese, Danish, and Spanish governments claim they will extend no new credits. [redacted] 25X1

Obligations
Even with the rescheduling of 1982-84 debt and assuming the rescheduling of all 1985 maturities, Poland owes about $3.1 billion,[1] leaving a financial gap of $500-700 million. In addition to payments to the Paris Club, Warsaw owes bank creditors $1.6 billion and other creditors over $400 million. Poland's payment schedule will be particularly difficult over the next few months. Payments include:

- $286 million for 1984 interest on the 1981 government rescheduling agreement now due.
- $220 million for 1985 interest on the 1981 government accord due 30 November.
- $284 million for principal on the 1981 bank rescheduling agreement due 10 December.
- $586 million for 1985 interest on the 1982-84 government rescheduling due 31 December. [redacted]

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The Poles already have failed to pay the governments completely the interest arrears on 1981 debt. As a result, the September Paris Club meeting to finalize a 1985 rescheduling accord was postponed as well as bilateral talks with several governments concerning the 1982-84 accord. [redacted] some bankers, however, expect Poland to make the December payment to the banks on time, despite shortages of hard currency. They believe that Warsaw will continue to favor the banks over Paris Club governments because of the lesser risk in failing to pay official creditors. [redacted] 25X1

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Warsaw also may have some hidden payment reserves that do not show up in the projections provided to creditors. The Polish people have about $1.2 billion in hard currency deposits in their domestic state banks, including $340 million put in earlier this year as a result of increased interest rates and incentives for travel. Data from the Bank for International Settlements (BIS) showed Polish deposits in Western banks at $1.6 billion in March 1985. Warsaw claims these deposits are "working balances" for banks and enterprises. Although the Poles do not consider these items as reserves, Warsaw probably could draw upon some of this money if forced to do so. [redacted] 25X1

Financial Situation in 1986
The gap between sources of financing and payments due probably will widen in 1986. Warsaw will owe about $4.8 billion next year assuming Western governments reschedule almost $1 billion due in principal and interest on original maturities. Banks and Paris Club governments are due about $2 billion each under previous rescheduling agreements, and other creditors are owed over $700 million. The bank payments include $568 million in repayment of principal under the 1981 agreement and $316 million from the 1982 accord, while repayments to the Paris Club include $550 million in principal due from the 1981 agreement. [redacted] 25X1

We estimate that Poland probably can pay only $3.6-3.8 billion next year, although the Poles project covering all payments. We believe Warsaw is once again being overly optimistic in its projections of the trade surplus as well as the amount of IMF credit available in 1986 if readmission is granted. Warsaw projects a trade surplus of $1.65 billion with exports increasing by 9 percent and imports by 8 percent. Based on 1985 performance, exports are likely to rise only half that amount mainly due to a continued lack of raw materials and quality goods to sell in the West. Imports probably will be lower than the Polish plan because of the lack of hard currency revenue. Thus, the surplus is likely to rise only slightly above the 1985 level of $1.2-1.4 billion. [redacted] 25X1

Poland is not likely to receive the large amount of credits it projects for 1986. Warsaw is counting on readmission to the IMF early in 1986, from which it hopes to obtain over $1 billion in new credit next year. However, the regime most likely will have access to no more than $400-500 million in IMF loans after entry, not the estimated $1.1 billion in standby credits. Moreover, before receiving a larger amount of IMF money, Poland would have to negotiate a stabilization program. Such a program would require the support

[1] Private banks in July 1984 rescheduled $1.6 billion of debt due during the period 1984-87. [redacted]

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of workers whose continuing demands for increased consumption would conflict with IMF requirements for greater austerity to improve Poland's capacity for debt repayment. [redacted] 25X1

Near-Term Outlook

While the recent Paris Club agreement has created the impression of progress on Poland's debt problems, Warsaw continues to be mired in a financial crisis. Its lack of funds to make payments on its rescheduling will force the regime to choose one or more of these options:

- ***Pay the banks, not the governments.*** The Paris Club allowed Poland to run up arrears of $12 billion in 1982-84 without calling Warsaw in default. As a result, Poland most likely will delay payments to Paris Club members, hoping for the same outcome. [redacted] 25X1 25X1 The Paris Club most likely would protest such a choice as well as continued payments to other creditors, but the governments have no real leverage over Warsaw.

- ***Cut imports.*** The regime slashed imports in 1983 and 1984 to achieve targets for hard-currency surpluses when exports did not reach planned levels. Warsaw apparently is holding off on this option in 1985, hoping exports will increase.

- ***Keep pressing for new credits.*** Another round of requests for loans from Western governments—without more serious attempts by Poland to improve its trade performance—is not likely to have much success.

- ***Request a further rescheduling of the 1981 and 1982 bank and 1981 government agreements.*** Poland owes about $1.2 billion in principal to banks from these agreements and $550 million to governments in 1985 and 1986—about the sum of the financial gaps in both years. Creditors would not welcome such a request, and, [redacted] 25X1 25X1 Warsaw has given no signals that it would ask for such a package. A rescheduling of the agreements would require the cooperation of banks and governments in the sharing of Poland's payments—which has not occurred up to now. If Warsaw enters the IMF in 1986, the Fund could play a role in guiding future negotiations. The IMF probably would press governments and banks to provide more debt relief and new credits before extending its own loans under a standby program. [redacted] 25X1

In any case, these options will provide just another short-term solution to most immediate financial problems. Warsaw has not made the policy changes necessary to stimulate hard-currency exports and escape the endless cycle of requiring more credit and debt reschedulings. An adjustment policy formulated by the IMF in cooperation with the regime may offer some hope of improvement, but any progress will be slow. [redacted] 25X1

[redacted] 25X1

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Hungary: Multiple Candidate Elections

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The competitive elections for the National Assembly and local councils (local governments) this summer—a novelty for Hungary and the Soviet Bloc—were a limited success for the Kadar regime. While presenting little risk to the party, they won Budapest favorable publicity in the West as the most moderate and "democratic" regime in the Soviet Bloc, provided it a better measure of popular attitudes and grievances, and paved the way for reforms to revitalize the country's legislative and local administrative bodies. But they apparently have done little to enhance the regime's legitimacy—one of the major objectives of the experiment. The regime's turn toward limited political reform at a time of economic stagnation may reflect insecurity about its relationship with the Hungarian people and concern about the viability of the Kadarist social contract that has helped preserve social stability for the past three decades. 25X1

The Election Results

The elections presented no risk to the leadership. Thirty-five of Hungary's most prominent regime-approved personalities were placed on a "national list" and ran without opposition. In the competitive electoral districts, the Patriotic People's Front (PPF), Hungary's umbrella front organization, organized nominating meetings and put forward the names of two candidates to compete in the election. In addition, nominations could be submitted from the floor, but all candidates had to openly accept the program of the PPF, and only those who captured at least one-third of the votes at two or more nominating meetings were allowed to stand for election. 25X1

The authorities carefully controlled the nominating process by employing such techniques as orchestrating the debates at the nominating meetings, packing the halls with party supporters, introducing other candidates to dilute the vote, and moving the meetings without providing sufficient advance notice. In this way, the regime was able to prevent the most objectionable candidates from standing for election. Of the 873 candidates who cleared the nominating process for the Assembly election, only 78 (9 percent) were nominated from the floor (43 were eventually elected to serve in Hungary's 386-seat Assembly). Similarly, of nearly 90,000 nominees for the local government positions, only about 4 percent were proposed by the voters. 25X1

Despite the regime's precautions, several well-known retired and active officials were defeated in the election, some rather soundly. Two prominent retirees, former Politburo member and reputed conservative Bela Biszku and former premier and reform advocate Jeno Fock, lost their races as did five retired county first secretaries, including one who received only 16 percent of the vote. In addition, three of the 21 active party officials running for office were defeated. But the candidates who fared least well in the elections were the trade union representatives. The head of the Iron and Steel Workers Union was defeated as were 10 of the 17 union delegates running for election. 25X1

International Reaction

Western observers reacted favorably but guardedly to the elections. They applauded the existence of multiple candidates but pointed out that there were no true opposition candidates in the field. And while many conceded that the elections might be a small step in the direction of democracy, they questioned whether a greater role for the National Assembly would automatically ensue. 25X1

Overall, most observers concluded that the elections constituted an unusual experiment in Eastern Europe and compared them favorably with electoral practices of other Bloc states. The Hungarian media gave prominent place to Western press accounts, but objected to the Western focus on the fate of the "independent" candidates, and chided those Westerners who dismissed the elections because they brought no change in power. 25X1

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Reporting in the Bloc press was more restrained, with most party newspapers—including *Pravda*—simply noting that the elections demonstrated the unity of the party and the people and affirmed the decisions taken at the Party Congress last March, without mentioning the multiple candidates. Only the Polish press went into any detail on the new election law and the results of the election. 25X1

Domestic Reaction

The Kadar regime's major domestic goal probably was to enhance its legitimacy. After the trauma of the 1956 revolution, Kadar sought popular acceptance of his government on the basis of a "social contract" under which it provided the people with economic benefits and social freedoms that were not available in the other East European states. The economic stagnation that has bedeviled Hungary in recent years has clearly undermined the regime's credibility. Budapest appears to believe that limited political reforms, of which the multiple candidate elections form only one part, are needed to take up the slack. 25X1

The leadership apparently hoped that the appearance of a choice and the actual opportunity to vote officials out of office would elicit more voter participation. Postelection assessments in the Hungarian press centered on assertions that the elections had indeed engendered greater public interest in political affairs and had thereby contributed to national unity. 25X1

Turnout figures suggest, however, that this may be an overly optimistic interpretation. In the previous parliamentary election, 97 percent of the eligible voters cast their ballots, but only 93 percent did so this time. Moreover, only 83 percent of those eligible voted in the byelections held later in the month. 25X1

The regime also hoped that greater participation would help it get a better grasp of popular attitudes and grievances. The Central Committee, in a recent statement, directed the newly elected members of the National Assembly and the local councils to make use of all proposals raised at the nominating meetings. Some in the leadership, however, appeared disappointed with the outcome of the electoral debates. Istvan Horvath, a Central Committee secretary, worried openly in his report to the Central Committee on the elections that the large number of local issues raised during the parliamentary campaign would hinder the Assembly's ability to consider the good of the whole nation. Horvath apparently had hoped that the National Assembly election would identify major national issues and that matters of purely local interest would be raised in the local council elections. 25X1

New Roles for Old Institutions

The competitive elections may also have been intended to set the stage for changes in the now largely moribund National Assembly and local governments. According to the Central Committee, the leadership wants the National Assembly to play a more active and visible role in discussing important social issues, in defining major new policy measures, and in monitoring policy implementation by government bodies. Although the party appears unwilling to give the Assembly greater policymaking authority, it apparently wants to increase its credibility as a means of legitimizing the policies that it votes into law. The regime took a step in this direction last year by creating a constitutional council within the parliament to review laws and regulations made by local government organs and central ministries for consistency with the constitution. 25X1

The regime also apparently intends to expand the role of the local councils. These local government bodies are expected to do more to identify and discuss important local interests, to exploit local resources, and to stimulate greater popular participation in civic affairs. The authorities have already moved to give the councils more authority by abolishing the administrative districts that had existed between the local councils and the counties; the granting of increased financial and policy autonomy to the councils also has been discussed. Such measures are considered to be the logical outcome of the greater independence assigned to economic enterprises as a result of Hungary's economic reforms. 25X1

A Regime Ill At Ease?

Budapest's search for new ways to increase its legitimacy and open new lines of communication to the people suggests an uneasiness with its position. In

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particular, the leadership seems to feel it is losing touch with the mood of the country and thus risks being surprised by destablizing social developments. The population's longstanding cynicism toward politics and reluctance to participate in the officially directed political process have contributed to the regime's uneasiness. 25X1

Further reflecting its concern, the regime also has ordered local party organs to take greater note of important social issues at party forums and to be better prepared to explain and defend central decisions. In addition, Kadar, himself on several occasions, has expressed concern over public discontent with stagnating living conditions and a growing alienation among various sectors of society. 25X1

The regime's anxiety level will rise even higher as the succession to the 73-year-old Kadar grows nearer, and could lead to more daring measures as the leadership tries to maintain its social contract with the Hungarian people. 25X1

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Yugoslavia: Slovenia's Role in the Reform Debates

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Slovenia, Yugoslavia's most economically advanced republic, has become an increasingly vocal player in the debate over changes in the country's political and economic systems. In an officially Communist state, Slovenia routinely blocks efforts to centralize power in Belgrade, resists federally sponsored redistribution of resources to the poorer southern republics, and staunchly defends its Western cultural heritage and unique language. The republic will continue to exploit the decentralized post-Tito system to protect its interests, but will press for market-oriented reforms and efforts to streamline the cumbersome federal bureaucracy. 25X1

Opposition to Federalist Reforms

Leaders of the more centralist-oriented Serbian republic and some federal officials have introduced the major proposals in the national reform debates, while Slovenia has assumed a leading role in opposition. Slovenia, not surprisingly, favors change that would shift Yugoslavia closer to Slovene practices. Its leaders argue for greater political freedom including more open public debates and more objective media reporting. They back greater reliance on market forces in the economy, and, according to US diplomats, would restrict federal regulation to monetary and fiscal policies that provide a framework for market-based decision making.

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Slovene opposition centers on efforts to block federalist proposals for granting greater power to central authorities:

- Slovene leaders frequently attack Serbian proposals for constitutional amendments enlarging Belgrade's authority in both political and economic affairs.

- In cooperation with Croatia, the Slovenian republic has vigorously countered Serbian-backed proposals of the federal government to centralize control over hard currency earnings. The two republics last spring took the unprecedented step of drafting alternative legislation on the foreign exchange system for the Federal Assembly.

- The Slovenes have sought a reduction in federal control over mandatory aid to the poorer southern republics and have demanded smaller aid quotas.

- Slovenia's state president has denounced a proposal made in the Party Central Committee last summer for federal legislation to control locally determined wages. 25X1

The Roots of Slovene Behavior

Long a part of Catholic Central Europe, Slovenia is more Western in culture than most other republics. Slovenia also industrialized earlier than most of the rest of the country and has remained more closely linked with Western economies. The republic's distinct language and cultural isolation from the rest of the Yugoslav federation have allowed Slovene politicians to expand the limits of acceptable Yugoslav Communist behavior. The result is a republic where dissent is generally tolerated, relations with the Catholic Church are cordial, and skill and efficiency are bywords of economic management.

The Political Leadership 25X1

Slovene leaders differ from those of other republics in several ways, particularly in their openness to new blood and extensive interaction with Slovenian society. 25X1

Mobility and Diversity. Slovenia invests more authority in its cadre of young, pragmatic technocrats. US diplomats note that in recent years the Slovenes have favored younger, market-oriented officials with reputations for able management. Both the young and old Partisan generations have diverse professional backgrounds: labor, journalism, business, party and state bureaucracy, academia, and even the internal security apparatus. 25X1

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Prominent Slovenian Leaders

France Popit, 64, Republic President

Most influential figure in Slovenia . . . vocal advocate of republic interests.

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Milan Kucan, 44, Member of Federal Party Presidium

Trained as lawyer . . . . critic of constitutional change and political interference in economy.

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Andrej Marinc, 54, Republic Party President

Postwar politician . . . professional party man . . . defender of decentralized status quo and Slovene economic practices.

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Mitja Ribicic, 66, Member of Federal Party Presidium

Liberal, but republic leaders publicly disavow his most radical statements.

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Joze Smole, 58, Ljubljana Party President

Longtime journalist . . . outspoken defender of political tolerance.

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Stane Dolanc, 59, Member of Federal State Presidency

Partisan generation . . . far more conservative than most Slovenes . . . little power base at home.

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Diffuse Authority. Slovenia has long avoided concentrating political authority, and no single body seems capable of dictating policy. Senior officials share substantial decisionmaking power with local party officials, republic legislative bodies, and enterprise managers. US diplomatic reporting indicates that even groups normally subordinate to the party—including the Socialist Alliance of Working People (a party-organized front organization) and the Socialist Youth League—exercise considerable autonomy. 25X1

Fundamental Agreement on Issues. US diplomats say that the Slovenes demonstrate virtual unanimity on political and economic reform issues and that occasional disagreements apparently cut across generational lines. The US Consulate in Zagreb reports that Republic President France Popit appears to have widespread support in the republic. 25X1

Limited Participation in the Federation. Many Slovenes reportedly prefer a confederation to the present federal structure. Slovene leaders reportedly have gone so far as to suggest that the Army—generally considered the final guarantor of Yugoslav unity—be disbanded in favor of a stronger regionally based militia. Slovenia's choice of persons to serve on federal executive bodies who do not reflect mainstream Slovene thought suggests a low priority on participation at that level. Instead, Slovenia appears to rely almost entirely on its representatives in the Federal Assembly and Party Central Committee to block undesirable policies. 25X1

Role for Public Opinion. The Slovenians have gone further than other republics in allowing public opinion a role in the political process. One member of the republic state presidency told US diplomats recently that Slovenian officials are particularly sensitive to public opinion. The press frequently debates political, social, and economic issues. 25X1

Political Tolerance. Slovenes are proud of their relatively liberal political system and are quick to defend their practices against outside meddling. US diplomats report that the public regards mutual tolerance and respect as fundamental values. Senior politicians frequently say publicly that they see no point in suppressing different ideas or in keeping silent on current problems. 25X1

The Economy

Since the 1970s the Slovene economy has done well by Yugoslav standards. Slovenia is the most industrialized and least dependent on agriculture of the Yugoslav republics. With only 8 percent of the national population, Slovenia provides 15 percent of national output and 25 percent of the country's hard currency earnings. Worker efficiency is the highest in Yugoslavia, and unemployment stands at only 2 percent. In the first half of 1985, Slovenia was the only republic to record an increase in real wages. 25X1

Nonetheless, the Slovenian economy faces underlying problems. The US Embassy in Belgrade reported last spring that Slovenian officials are worried over long-term economic prospects, noting the need to modernize the republic's industrial base. A Croatian official told US diplomats five years ago that official data showed that Slovenia's capital stock was among the oldest and most exhausted in Yugoslavia; yet during the period 1977-82, investment in industry and mining dropped by roughly one-third. 25X1

Although Slovenes generally agree on economic policy, implementation has not always been smooth. According to diplomatic reporting, former republic Premier Zemljaric told the Slovenian Party Central Committee in late 1980 that only nine of the republic's 64 active investment projects appeared geared to needed export growth; a senior Slovene official told US Embassy officers early this year that bad investments continue to haunt the Slovenian economy. Public comments by politicians and businessmen also suggest that the Slovenian market has been weakened by its fragmentation into many small markets controlled by local politicians and business monopolies. 25X1

The Culture

A militant popular commitment to Slovene culture and language also appears to influence republic resistance to increasing outside political and economic interference. US diplomats reported early this year that Slovenia was gripped by an angst resulting in large part from cultural concerns. 25X1

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Historically, Slovenia has been the most ethnically homogeneous republic, and its small population still worries about being overwhelmed by the Serbo-Croat majority to the south. Over the past few years, Slovenia has imported many workers from the south to supplement its undermanned labor force; a Croatian news magazine reported in early 1984 that immigrants had grown to 20 percent of Slovenia's population. 25X1

Slovenia and Future Debate

As the national debate proceeds, Slovenia will continue to resist central authority in Belgrade. Over the next several months, Slovenes will fight to dilute federal government legislation to centralize control over foreign exchange and will work through party channels to kill the current southern-backed federal wage system proposal. While Yugoslav politicians are likely to propose many changes to strengthen the central party before its congress next summer, the Slovenes will seek allies in other republics to prevent any loss of power at the regional level. And the post-Tito political system, which yields decisive power to the republics, will enable them to block most of the changes they find unacceptable. At the same time, Slovenia will continue to lead the country in the implementation of market-oriented reforms called for by the party in 1983 and will probably support efforts to streamline the Party structure. 25X1

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Economic News in Brief

Western Europe

Surge in new domestic orders probably strengthening West Germany's resolve not to reflate . . . 5.1-percent jump in July follows solid 2.1-percent gain in second quarter . . . spurt in domestic sector joins robust exports. 25X1

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Direct foreign investment in Spain totalled $1.2 billion first half of 1985, down 2 percent from same period last year . . . foreign investment on Madrid stock exchange doubled to $160 million . . . Madrid expects recently liberalized regulations to boost foreign investment activity in second half of 1985. 25X1

Portugal announced a general reduction and reform of domestic interest rates . . . basic discount rate cut by 2 percentage points, loan rates by 2.5 points, and deposit rates by 3 points . . . aimed at promoting private investment, increasing industrial production, and improving the flexibility of financial markets . . . with national elections on the horizon, government intent on improving economy's performance. 25X1

Malta has lifted trade, travel restrictions on Italy imposed last October . . . Rome will reactivate military mission in Malta, negotiate financial aid . . . economic problems, impending elections prompting Malta to mend fences. 25X1

Eastern Europe

Bulgaria has announced new measures to cope with shortages, poor industrial performance . . . prices raised for electricity, gasoline, heating oil, drinking water, construction materials, luxury foods . . . staple prices held constant to avoid criticism. 25X1

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