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Soviet Consumer Services: Prospects for Change Under Gorbachev [Redacted]

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A Research Paper

This paper was prepared by [Redacted]

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[Redacted] Office of Soviet Analysis.

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Comments and queries are welcome and may be directed to the Chief, National Issues Group, SOVA,

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**Soviet Consumer Services:
Prospects for Change
Under Gorbachev** []

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Summary

*Information available
as of 2 September 1986
was used in this report.*

General Secretary Gorbachev has made the improvement of consumer services—from beauty parlors to laundries to auto repair shops—a prominent part of his highly publicized commitment to improve Soviet living standards. He told the party congress in February that he wants “decisive measures” to modernize the service sector and to bring supply into line with demand. He was even more strident in July when he told Khabarovsk party workers that “all our plans are doomed” unless the country decisively stops the longstanding practice of treating services and other consumer problems as a secondary priority. []

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The General Secretary’s public concern is well founded. He and other Soviet officials clearly recognize that deficiencies in consumer services impose serious political, social, and economic costs:

- The paucity of supplies and the daily frustrations of dealing with the ineffective state service sector lower morale and waste consumers’ time. It is estimated that Soviet consumers spend about 40 billion man-hours annually shopping for goods and services with about one-half that time spent standing in lines or traveling to and from the service shops.
- The lack of consumer services in rural and remote regions makes it difficult to attract and retain workers.
- The scarcity and poor quality of state services spawn corruption and help create a large underground private sector where illegalities such as theft of state property and tax evasion are common. []

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There are no easy solutions to the sector’s problems. While Gorbachev and other officials would prefer to improve the existing system first, past attempts to adjust plan indicators and managerial incentives in the state service sector have done little to improve performance. Additionally, the new leadership’s commitments to industrial modernization limit its ability to increase the share of labor or investment devoted to services. []

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Measures to expand the role of personal initiative and the rewards accruing to successful entrepreneurs in the service sector offer the greatest potential payoff, and reform-minded officials and economists have put forth several such proposals:

- Expanding the use of “collective contract” arrangements, which allow groups of workers in the state sector to have greater control over their operations, paying all expenses and pocketing a large share of the profits.

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- Emulating Hungary and East Germany in giving more scope to individual and family-run businesses.
- Reviving the independent, member-run cooperatives employed by Lenin in the 1920s as part of his New Economic Policy. [redacted]

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Gorbachev's public remarks indicate that he favors this approach. While in Khabarovsk he called for a search for new forms of "individual work activity" in the service sector and raised the issue of reviving cooperatives. Also, in remarks to Leningrad party workers in May 1985, he suggested that the regime should take a more "realistic" attitude toward the activities of individuals moonlighting in the service sector. [redacted]

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As in other controversial areas, Gorbachev has been slow to back his rhetoric with concrete proposals. His caution probably reflects the substantial political and economic risks attendant to any attempt to tamper with the centralized control and wage egalitarianism that underpin the Soviet system. Conservative officials have specifically warned that measures of the sort proposed by reform-minded economists could result in:

- Loss of state control over resource allocation decisions.
- Diversion of workers from labor-short state industries to more lucrative opportunities in the service sector.
- Garnering of "unjustifiably" high incomes by service-sector workers.

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The leadership is apparently attempting to reconcile these concerns by moving simultaneously along two tracks. A Politburo decision last March linked measures to expand the role of personal initiative with other steps that would reduce the level of unauthorized private activities. The regime has already moved ahead on the latter track with a series of decrees cracking down on "unearned" income. Although progress on expanding the role of personal initiative appears to be coming more slowly, the regime has recently taken some tentative steps. Remarks by Soviet officials indicate that new legislation regulating individual work activity could emerge in the next few months. More details concerning the guidelines for the formation of cooperatives approved by the Politburo in August should also be published soon. [redacted]

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Even if the regime enacts measures favored by reformers, it must also tackle associated problems that have stymied past reform efforts to ensure that any new steps have a significant impact:

- *Ensure operating autonomy.* Gorbachev would have to ensure that central authorities give contract collectives, cooperatives, and private individuals freedom to run their businesses profitably. This should include the power to expand operations, control the number of employees, and adjust prices to reflect supply and demand.
- *Provide facilities and supplies.* Gorbachev would have to back up new organizational arrangements with operating facilities and adequate sources of supply. The chronic shortages of materials, spare parts, and equipment that now plague the service sector can prevent state-run, contract, cooperative, or individual operations from working profitably.
- *Increase incentives.* Gorbachev will have to ensure a more equitable division of profits between workers and the state by reducing the currently high marginal tax rates on the profits of private operators and by preventing officials from continuing to confiscate the earnings of highly profitable operations.

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Given the limited resources available to devote to improving consumer welfare, we believe the Gorbachev regime will run the political risks associated with an expanded role for personal initiative in the services area. Efforts to enact truly effective measures that address the fundamental problems of independence, supply, and incentives will surely encounter formidable resistance from bureaucrats and conservatives who believe the risks outweigh the potential gains. Progress on such measures is likely to be deliberate at best, but to a population long accustomed to leadership indifference, even small steps could provide a psychological boost.

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Scope Note

The services we assess in this paper correspond roughly to the US definitions of "personal services," "automotive repair services," and "miscellaneous repair services." These include laundry, drycleaning, barber, beautician, and public bath services; repair of clothing, consumer durables, and housing; and a variety of other services such as rentals of consumer durables. Professional services such as health care are not addressed in this paper because they are classified by the Soviets under other statistical categories. Our judgments, though based on a study of Soviet statistics compiled on the narrower Soviet definition, generally apply to other service sector activities as well. 

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Soviet Consumer Services: Prospects for Change Under Gorbachev

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Consumer Services in the USSR Today

The Sorry State of Consumer Services

In Mikhail Gorbachev's Soviet Union, where criticism of economic performance is the order of the day, few sectors provide as much grist for the leadership's mill as that of consumer services. Premier Nikolay Ryzhkov frankly acknowledged the underdevelopment of this sector in a December 1985 speech in which he labeled the state of basic services as "embryonic." Deficiencies in the supply and quality of consumer services reflect poorly on the Soviet system abroad and, in the judgment of Soviet leaders and public figures, are costly in political, social, and economic terms. Improving the service sector is essential to addressing problems of sagging morale and productivity at home and to enhancing the image of the Soviet economy abroad.

Party chief Gorbachev has given a great deal of rhetorical emphasis to the service sector, stressing its importance to his overall economic goals. He told the party congress in February that the service sector must be brought up to date as quickly as possible and that "decisive measures" are needed to bring the supply of services into line with demand. In a July speech to Khabarovsk party workers, Gorbachev demanded an end to the longstanding practice of treating the service sector as a secondary priority and stressed that, if social problems such as consumer services are not solved, "all our plans are doomed." At the same time, he expressed his conviction that boosting the output of services is a key factor in improving labor productivity.

The leadership's concern is well founded. Although per capita availability of services has roughly doubled in the past two decades (see table 1), per capita expenditures on consumer services amount to roughly only one-quarter of the level Soviet economic

Table 1 Percent
**Growth in Real Per Capita
Consumption**

	Average Annual Growth		
	1971-75	1976-80	1981-85
Total consumption	2.6	1.9	1.0
Personal care and repair services ^a			
Total (includes private sector) ^b	4.4	4.1	3.1
State sector only	6.8	5.8	4.2

^a Figures are computed according to the methodology in "An Index for Consumption in the USSR," in *USSR: Measures of Economic Growth and Development, 1950-80: Studies Prepared for the Use of The Joint Economic Committee, Congress of the United States*, December 8, 1982. Adjustments made to official data on the state service sector include the removal of services sold to enterprises and institutions and the addition of the cost of materials used in providing services.

^b As is true of all activity in the so-called second economy, estimates of the value of private-sector services are necessarily imprecise. We estimate that the private sector currently provides about a quarter of the total. This is based on a figure for private services of 5-6 billion rubles given in *Izvestiya*, 19 August 1985. We assume a per capita growth rate of these services of 1 percent annually, which seems consistent with the rise in money incomes.

planners regard as the "rational" standard of consumption.¹ (See inset on US-USSR Comparisons.)

In the USSR—as in other countries—consumer services are most highly developed in the cities, but, even in the largest Soviet urban areas, service outlets tend

¹ The planners set "rational norms" for consumption, which provide standards for how much an average Soviet citizen should consume in food, housing, clothing, and other goods and services. They generally represent a comfortable living standard, albeit a lower one than in the West.

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US-USSR Comparisons

Services in the USSR compare poorly with those in the United States. In 1984, for example, Soviet per capita expenditure on consumer services was only about 25 percent that of the US level.^a These services constitute only about 2.5 percent of total personal consumption in the USSR. In the United States, the proportion is about 7 percent. The USSR, with a population of about 280 million, has about one-third the number of service establishments of the United States, whose population is about 240 million. Compared to the United States, the USSR has one-tenth the number of photography studios, less than two-tenths the number of barbers and beautician shops, and less than one-twentieth the number of furniture repair and reupholstery shops. [redacted]

^a Excluding automotive services, consumption of which was only about 1 percent of the US level. [redacted]

To avoid overstating the Soviet position, we have attempted to delete expenditures on activity not classified as services in the US accounts but included in everyday services (see appendix A for a discussion of differences between the US and Soviet definitions). [redacted]

to be scarce. According to Soviet commentators, moreover, service outlets within the cities are poorly distributed. It is not unusual to find drycleaning service available only in one part of town, shoe repair in another, and watch repair in a third. Even in Moscow, which Soviet citizens generally regard as the country's most livable city, only one or two repair points exist for some kinds of household appliances, and customers are forced to travel many miles. In a city of more than 8.5 million people, Moscow has fewer than 4,000 service enterprises. [redacted]

Despite Soviet efforts to correct the imbalance, the picture remains even bleaker in rural areas. In recent years, per capita consumption of services in rural areas has been growing faster than in urban areas but by 1984 had attained only 60 percent that of the urban level (see table 2). The range of services offered in rural areas is not as wide as in the cities. Laundry,

Table 2
Growth of Per Capita State-Provided Services^a

Percent

	Average Annual Growth		
	1971-75	1976-80	1981-84
Rural	8.0	10.0	4.9
Urban	6.2	5.3	4.0

Sources: 1975 and 1984 *Narkhoz*.

^a Soviet data exclude housing construction and repair services. Otherwise, the adjustments to the data referred to in table 1 have not been made here.

[redacted] 25X1
drycleaning, and beautician services are particularly poorly developed in Soviet rural settlements² (see table 3). [redacted] 25X1

According to Soviet statistics, the availability of consumer services varies widely in different republics and regions of the USSR. Residents of the European republics enjoy the greatest per capita availability of services, while the Central Asian republics and Azerbaijan offer the fewest services (see table 4). The differences among the republics, moreover, are wide, ranging from 69 percent above the national average in Latvia to 36 percent below in Uzbekistan. [redacted] 25X1

The multitude of consumer complaints appearing in the Soviet press makes it clear that the quality of state-provided consumer services also leaves much to be desired. About one-third of some 2,800 Soviet emigrants participating in an interview project conducted by Western academics reported that they were "somewhat" or "very" dissatisfied with the time it took to have repairs done by state shops. In Latvia, a

² Available data preclude firm estimates of the amount of services purchased by rural and urban residents because Soviet data on sales of services in rural and urban areas represent total purchases in the respective areas, rather than total purchases by their residents. Many rural residents travel to urban areas to purchase services. [redacted] 25X1

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Table 3 *Percent*
**Per Capita Sales of Selected Services
in Rural Areas as a Share of
Per Capita Sales in Urban Areas ^a**

	1975	1984
Shoemaking and repair	48	70
Tailoring and clothing repair	45	59
Knitting and knitwear repair ^b	93	144
Home appliance repair and manufacture of metal articles	40	41
Repair and maintenance of automobiles	20	51
Repair and production of furniture ^b	104	160
Drycleaning and dyeing	14	24
Laundries	08	14
Photography	40	46
Baths and showers	31	35
Barbers and hairdressers	18	22
Rental of durable goods	13	23
Hauling services	63	92
Residual ^c	80	90
Total	44	60

Source: 1984 *Narkhoz*.

^a Adjustments to data referred to in table 1 have not been made here.

^b Rural expenditures per person exceeded that of urban in 1984 for knitwear repair and knitting and in 1975 and 1984 for repair and production of furniture. We can only speculate on the reasons. Production of furniture may fill in gaps left by the inadequate retail trade network in rural areas. Residents in remote areas would surely have trouble buying furniture and transporting it home. As for knitwear, such activity requires no equipment and minimal materials and is something a single employee of a rural services outlet could easily spend time on.

^c Includes funeral services and some agricultural services.

[Redacted]

1983 survey revealed that frustration with the long delays in filling orders, poor quality of workmanship, redtape, and rudeness of service employees had prompted many consumers to refuse to patronize local state service shops. What the survey found in Latvia is reportedly common to other areas of the USSR as well (see inset on laundry service, p. 5). [Redacted]

Inconvenient operating hours pose another obstacle to the potential consumer of state-provided services. A survey conducted in 1983 showed that a large majority of service enterprises open at 0900 or later and

Table 4
**Per Capita Sales of State-Provided
Services, by Republic, 1985 ^a**

	Relative Level (index: USSR = 100)	Urbanization (per- cent share of urban population in total)
European republics		
Latvia	169.1	70.5
Estonia	161.1	71.4
Lithuania	125.4	66.7
Belorussia	127.5	62.0
Moldavia	85.8	44.7
Transcaucasus		
Georgia	120.3	53.8
Armenia	94.7	67.6
Azerbaijan	67.4	53.7
Central Asia		
Kirghizia	76.3	39.6
Uzbekistan	64.5	41.9
Tadjikistan	68.7	34.2
Turkmenia	68.4	47.4
RSFSR	103.4	72.6
Ukraine	105.2	65.4
Kazakhstan	85.5	58.4

Source: 1985 *SSSR V Tsifrah*.

^a Adjustments to data referred to in table 1 have not been made here.

[Redacted]

close by 1800—hours most Soviet citizens are at work. Under former party chief Andropov, an effort was made to force service enterprises to stay open longer hours, but recent press reports indicate that many enterprises have reverted to their former schedule. The major obstacle to lengthening operating hours is probably the lack of an incentive for managers to do so; those who can fulfill their sales plans and earn the regular bonuses during the shorter hours have little reason to stay open longer. Service employees are also reluctant to work hours that are not compatible with schedules for transportation, day-care centers, and shops. Efforts to encourage factories and enterprises to open on-site service outlets for their employees have met with little success. [Redacted]

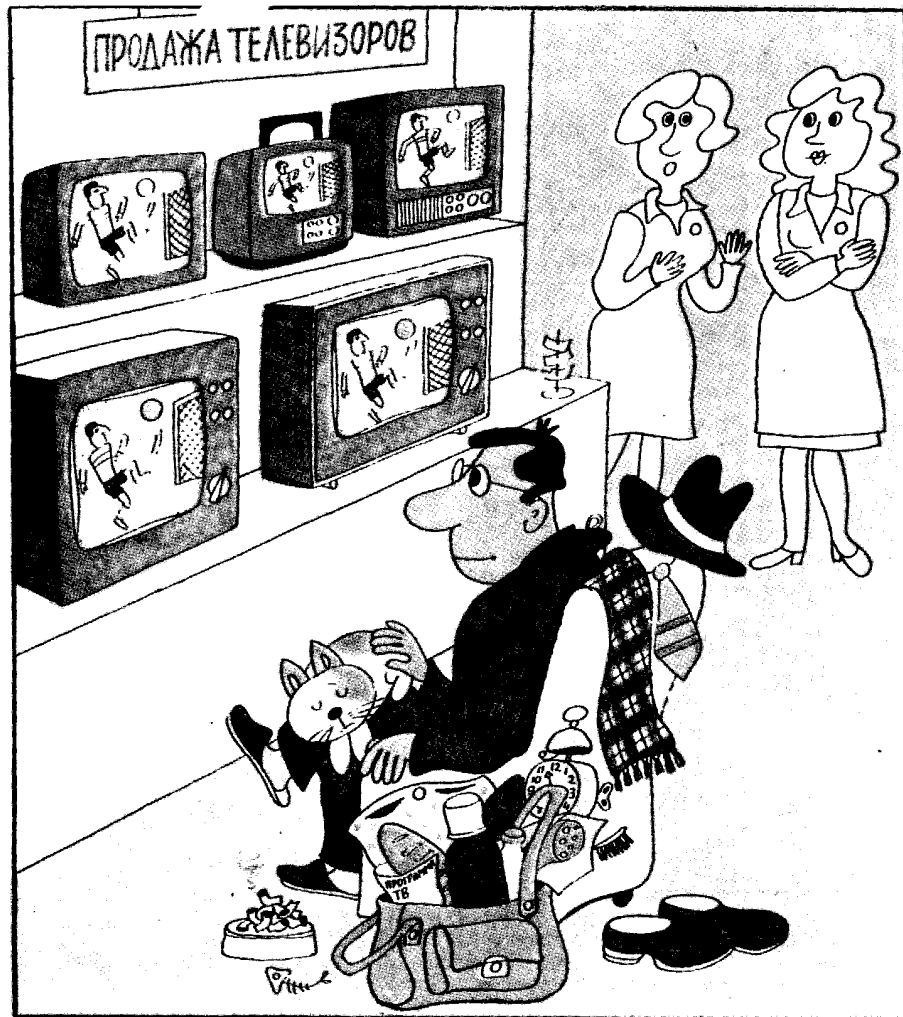
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Figure 1. Television Repair in the USSR—The Waiting Game
— Is this the second month this shopper hasn't left our store?
— His television set is at the repair shop."



— И что этот покупатель второй месяц не выходит из нашего магазина?
— А у него телевизор в ремонте.

Krokodil 1983

Services—The Stepchild Sector of the Soviet Economy
Central planners have traditionally given the service sector low priority, neglecting its resource needs in favor of developing other sectors—industry, energy, agriculture, defense—that they regard as more crucial. To judge from articles in Soviet journals and the popular press, vast increases in labor and capital investment would be needed to create a network of state enterprises capable of adequately meeting the Soviets' own standards for consumption of services. According to a recent article in *Kommunist*, for example, the State Planning Committee's (Gosplan)

Scientific and Research Institute of Economics has calculated that the sector would need to double its present labor force to meet "rational norms" of consumption for the output of services. An August 1985 *Izvestiya* article estimated that, given its present mode of operation, the service sector would require an immediate infusion of 4 million more workers and 5 billion additional rubles' worth of material resources to meet consumer demand.

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Laundry Service—Soviet Style

Checking on complaints of poor-quality services in Orenburg, several Soviet reporters visited a laundry, and then described for their readers what they found:

The first thing they did was to hand us a razor blade and needle. After managing to cut the buttons off the coats we had brought to be cleaned, we began sewing on the tags we had been given. The people, about 40, in the line behind us began to raise a fuss and urge us to hurry.

We barely finished our sewing when the clerk disappeared into the back room. . . . When she returned 15 minutes later, she didn't even look at our coats. She tossed them onto a single pile on the floor, next to some greasy quilted jackets.

The journalists did not reveal how their experience ended, but, presumably, they got their coats back, unlike some Moscow consumers who wrote local papers complaining that state laundries had lost their clothes.

At present, however, the service sector receives only a tiny sliver of the investment pie—less than one-half of 1 percent of total investment in 1966-80, according to a 1983 *Voprosy ekonomiki* article, and there is no evidence that its share increased in 1981-85. Investment in services often falls short of targets set in the five-year plan because construction organizations as a rule find it easier to fulfill their plan targets by building large, industrial projects rather than smaller service-sector jobs. In 1976-80, for example, capital spending on consumer services totaled 2 billion rubles, although the plan had set a target of 2.3 billion.

Despite its labor-intensive nature, the service sector has also been a stepchild with respect to the supply of labor. According to Soviet statistics, about 2.4 percent of state workers (some 2.8 million persons) are employed in furnishing consumer services, up from 2.1 percent in 1970.

The low priority of the service sector is reflected in the low wages and poor benefits provided its employees. As a result, the sector suffers a shortage of trained personnel, particularly qualified appliance repairmen whose technical skills can get them more prestigious, better paying jobs in industry. According to a 1983 survey of Moscow service employees, 27.5 percent of those surveyed had no professional training, including approximately 30 percent of all hairdressers, 15 percent of radio repairmen, and 75 percent of shoe repairmen. In addition, the service sector suffers a very high rate of worker turnover—nearly 25 percent a year according to some Soviet estimates. Workers leave for jobs with higher pay, greater prestige, and better fringe benefits (like access to housing) that are often available in higher priority sectors. The workers who do remain tend to be the poorly educated, who cannot qualify for better jobs elsewhere.

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According to Soviet media commentary, shortages of materials and equipment chronically hamper the operation of state service enterprises. Reportedly, service shops frequently refuse to do repairs because they cannot get the required spare parts. The head of the Belorussian Republic's system of radio and television repair, for example, complained in a September 1985 article that his organization received less than one-half its scheduled allotment of integrated circuits to repair new model televisions. The Russian Republic (RSFSR) Minister of Consumer Services complained in a television interview that the machine-building ministries fail to keep service enterprises supplied with spare parts, diagnostic equipment, and technical manuals needed to repair the consumer appliances they produce.

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Although shortages of machinery and spare parts are endemic to the Soviet economy, they evidently are especially acute in the service sector, where enterprises often depend on suppliers that specialize in products unrelated to their needs. More than 20 ministries produce machinery and equipment used in service enterprises. Drycleaning and laundry equipment, for example, are produced by factories under the Ministries of Aviation Industry, of Construction,

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...и только приемник молчит!
Рисунок Г. АНДРИАНОВА.

Figure 2. Soviet Repair Services—The Missing Spare Part Krokodil 1983

“— No more spare parts!
— We did everything we could!
— We repaired it the best we could!
— ... Only the radio is silent.”

Road, and Municipal Machine Building, and of Machine Building for Light and Food Industry and Household Appliances. Such equipment is a sideline for those factories, and, according to numerous press reports, their managers and parent ministries give priority to fulfilling the plans for their primary product line—on which their bonuses depend. As a result, the service shops are undersupplied and reportedly must frequently purchase equipment secondhand from nonservice enterprises.

Flaws in the Soviet incentive system also reportedly have a detrimental effect on the behavior of consumer service enterprises. Enterprises are rewarded for fulfilling targets set from above rather than for satisfying the demands of their customers (see inset on shoe service). The main target that central planners set—

total value of enterprise sales—encourages state service shops to behave in ways that go against planners' wishes. According to numerous press reports, for example, in an effort to achieve their total sales targets, consumer care and repair shops tend to:

- Concentrate on providing high-cost services, even if they are not in demand, because such services are the quickest path toward fulfillment of targets for total sales.
- Produce for bulk consumers rather than individual consumers. (Service outlets are authorized to sell services and a limited amount of goods to institutions: hospitals, boarding schools, hotels, and factories. The share of sales to institutions has been rising, even though official policy has decreed its decline.)³
- Produce goods rather than services. (The service shops find it easier to meet output targets through the material-intensive route of manufacturing products rather than by just providing services. Soviet statistics indicate that production of goods now accounts for about 40 percent of the sales of service enterprises.)⁴
- Mass-produce goods rather than turn out custom-made items for individuals, although the latter are supposed to account for most of what the outlets produce. The quality of this mass-produced output

³ Sales of services to institutions rose from some 4 percent of total sales of services in 1965 to about 21 percent in 1982, according to the Soviet press. As one service enterprise employee said in a letter to a Soviet newspaper in 1983, “Our repair brigades are all too eager to service various organizations, but they don't want to serve the public because it is easier for them that way. Why replace a broken belt in a washing machine or do minor repairs on an electric razor? It's bothersome and it only yields a few kopecks, while working in a hospital or a kindergarten you can fix all the appliances in a block order and there's your plan fulfilled. You receive bonuses . . . and then many of the figures for service organizations are switched to the consumer services account.”

⁴ We lack sufficient data to delete production activity from our estimates of consumption of services. Although this means that our estimates of the amount of services purchased are biased upward, the growth of services is more on target because the share of production activity in total service enterprise sales has been fairly constant since 1975. The only service shops where the share of goods output in total sales has grown—from 22 percent in 1975 to 31 percent in 1982—are those that work on consumer durables. These shops may be increasingly engaged in production of spare parts.

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The Shoes That Never Returned—Neglecting the Service Consumer

The Soviet press reported the case of a Moscow man who answered a knock on his door to find employees of a nearby state shoe repair shop soliciting shoes in need of repair. It was near the end of the month, and the shop apparently had not fulfilled its monthly sales quota. Gratified by the unusual exercise of initiative by state workers, the man handed over a pair needing repair and, according to the customary procedure, paid for the repairs in advance. Months later the shoes were still in the shop, the repairs unfinished. Once it had the money in hand and fulfilled its sales quota, the repair shop had no further interest in the customer or his shoes. [redacted]

is poor, and the Soviet public reportedly finds it to be as unappealing as that produced by light industry.⁵

[redacted]

The Costs of an Underdeveloped Service Sector

In the judgment of Soviet officials and economists, the deficiencies of the state service sector impose serious political, economic, and social costs. Among them:

- Inconveniences in state consumer services result in a great deal of wasted time. It is estimated that Soviet consumers spend about 40 billion man-hours annually shopping for goods and services with about one-half of that time spent standing in lines or traveling to and from the service shops. Because few shops stay open after normal working hours, the time lost is often work time.
- The scarcity of household services adds to the already heavy burdens borne by Soviet women and contributes to marital and family problems. Soviet

⁵ This production activity makes a relatively small contribution to total Soviet output of such goods. We estimate that in 1984 everyday service shops provided less than 10 percent of the value of total shoe and clothing output and less than 5 percent of all knitwear. *Vestnik statistiki*, no. 5, 1983, p.79, and no. 7, 1985, p. 80; [redacted]

calculations indicate that women can rely on the state service sector to assist them with only about 3 percent of household chores.

- The lack of consumer services in rural areas and remote regions of the country makes it difficult for farms and factories in those areas to attract and retain skilled workers.
- Poor appliance and auto repair service takes a toll on the state's resources because repairing an item is often more cost effective than producing a new one.

[redacted]

The scarcity and poor quality of state consumer services also have reportedly fostered rampant corruption, contributing to a mood of cynicism and apathy among the populace, which, in turn, lowers worker productivity and undermines public respect for law and order. According to numerous press reports, customers must frequently pay under-the-table mark-ups to service personnel to obtain high-quality work or repairs that require scarce materials or parts. Sometimes state service enterprises brazenly engage in practices akin to extortion. A Moscow car owner, for example, complained to the press that a state auto repair shop charged him double the official rate to install a scarce part. [redacted]

There have been frequent press reports that service personnel customarily supplement low wages by working off the books and skimming a portion of enterprise receipts. According to a 1977 article in one economic journal, service enterprises end up with 50 to 100 percent more sales revenue on days when they are audited by State Bank officials as compared with ordinary operating days when employees apparently often fail to issue receipts for purchases and pocket the money instead.⁶ [redacted]

⁶ This suggests that the level of services reported in Soviet statistics may be biased downward, although it is not clear to what extent. We assume that the growth of services is unaffected as long as there is no acceleration or deceleration in the tendency to pilfer from the state. [redacted]

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The Private Sector—Filling the Void

The deficiencies of the services provided by state enterprises have caused consumers to turn to the flourishing private sector where, as a well-known Soviet economist has acknowledged, service is often better quality and takes about half the time. Because much of the activity takes place “underground,” the size of private-sector services is difficult to estimate accurately. Recent Soviet press comments, however, suggest that the private sector may provide more than a quarter of all personal care and repair services. In an article in *Voprosy ekonomiki*, Soviet economist V. Dmitriev suggested that the private sector was about 30 percent as large as its official counterpart. A larger estimate was provided in an August 1985 *Izvestiya* article. According to the authors of this article, the private sector provides 5-6 billion rubles’ worth of services annually, or 50 to 60 percent as much as reported sales in the state sector in 1984.⁷ Some 17-20 million workers—14 to 17 percent of all workers and employees in the state sector—participate in the private sector, mostly on a part-time basis. They provide 50 percent of all shoe repairs, 40 percent of auto repairs, and 30 percent of appliance repairs in urban areas. *Izvestiya* estimated that the share of private services in rural areas is as high as 80 percent in some categories. [redacted]

Some types of services can be legally provided by private individuals who register with the state and pay taxes on the income earned. These services include tailoring, carpentry, metalworking, watch repair, ceramics, repair of motor vehicles, hairdressing, and painting. Proscribed services include processing of agricultural and food products and transporting passengers or freight. Republic-level Councils of Ministers and local authorities may add to or delete from the list of proscribed services; the definition of what is legal varies from one area to another. [redacted]

⁷ These figures presumably include some private housing construction and repair, which we subtract to make our definition of private services comparable to that of state services. [redacted]

The private purveyor of services operates in an uncertain environment often subject to arbitrary action by local officials. Republic criminal codes, for example, forbid activity engaged in for the purpose of obtaining “unearned income,” vaguely defined as income incommensurate with the individual’s labor contribution. Hence, determination of what constitutes unearned income is often left to the discretion of law enforcement authorities. Unregistered private operators working full-time outside the state sector also risk running afoul of laws against “parasitism.” [redacted]

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Even legal private activity, moreover, is often associated with illegalities such as theft and tax evasion. Often the only method of obtaining tools and materials is theft from state enterprises. State taxes on income derived from private handicraft or trades rise to 60 percent of amounts over 3,000 rubles (compared to only 13 percent for income from state-sector employment) and 65 percent of amounts over 5,000 rubles. Consequently, many private operators either underreport their earnings to minimize the tax or fail to pay taxes at all [redacted]⁸

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Searching for a Solution

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While Soviet officials have long acknowledged serious problems in consumer services, agreeing on a solution has proved to be difficult. Before Gorbachev came to power, Moscow initiated some cautious experiments in the state sector, and reform-minded economists began to propose measures that involved more far-reaching changes. The experiments did little to solve the problems, while the economists’ proposals have aroused considerable controversy. [redacted]

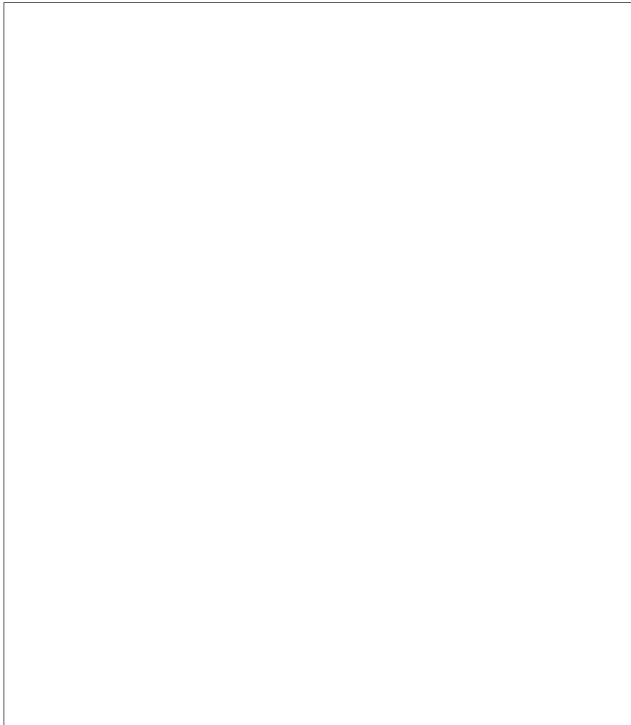
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⁸ A 1983 *Pravda* article, for example, stated that only one of the 48 craftsmen registered in one district in Estonia paid taxes on his private income. Some individuals do not even register for licenses. [redacted]

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One such administrative measure in the program is a requirement that all enterprises, regardless of their main product line, set up facilities to provide services to their own workers and the public at large. Similar measures have been tried in the past with little success.¹⁰ Although the authorities have vowed to make provision of services a mandatory planning assignment, this additional action is unlikely to lead to a substantial increase in output. Managers will probably remain unwilling to divert labor, space, or materials to providing services at the risk of failing to meet their main production targets. [redacted]

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The Consumer Services Experiment

The Soviets have also attempted to better the consumer's lot by implementing experiments designed to improve the performance of the state service sector through minor changes in planning and management procedures. A large-scale experiment was launched in several areas of the RSFSR in July 1984 and expanded to areas in the Ukraine and the Republics of Belorussia, Latvia, and Estonia in early 1985. According to a November 1985 *Izvestiya* article, the experiment was to be expanded throughout the USSR in 1986. Its key provisions include:

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The Consumer Goods and Services Program

Preparation of a new package of measures for the development of consumer goods and services began in September 1983 with the establishment of a Politburo commission. By September 1985 the Soviet leadership had approved a series of targets for the provision of goods and services during the period 1986-2000. The targets themselves—an increase in sales of services of 40 percent by 1990 and 140 to 150 percent by the year 2000—were ambitious, but, as two Soviet experts on the service sector complained in a January 1986 article in *Kommunist*, the authorities appear to have avoided the question of providing the service sector with additional resources to pay for the planned increases. Instead, they made the achievement of the program's goals dependent on gains in efficiency not previously achieved⁹ and on administrative measures similar to those that have failed in the past. [redacted]

- A reduction in the number of plan targets that service enterprises must meet and the introduction of a new target—sales of services to individuals, rather than institutions—as a measure of enterprise success.
- An expansion of enterprise rights to use their profits to expand production or pay bonuses to workers.
- Increased use of collective contracts: arrangements that pay small groups of workers according to performance.

¹⁰ For example, resolutions issued in January and March 1983 called on ministries to expand the provision of services at sites of employment. However, the ministries did not set plan targets for services output as they will under the 12th Five-Year Plan. [redacted]

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⁹ Increased output is to result primarily through "improvement in production organization, more efficient use of capacities, modernization and retooling of enterprises, the use of modern materials, reduction in the material-intensiveness of output, and more economical use of resources." [redacted]

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- Intensified recruiting of fully employed persons who wish to moonlight, as well as pensioners, students, and housewives, for part-time work in the services sphere.¹¹ [redacted]

The experiment has received mixed reviews. A January 1986 Central Committee resolution evaluating the performance of the service sector in the RSFSR credited the experiment with increasing growth rates but noted that it has not yet brought about a turnaround in service quality. Some observers have complained that, despite the introduction of the new plan target for sales to the populace, total sales remain the main success criterion for service establishments. As a result, enterprises reportedly continue to neglect the public in favor of pursuing easier means of fulfilling their sales targets. Other commentators have charged that service enterprises have been unable to use their newly granted freedom to spend their profits on new equipment and supplies because these resources are simply not available for purchase. Furthermore, as in similar experiments in industry, the profits of successful enterprises have frequently been siphoned off by the ministries to subsidize unprofitable enterprises.

[redacted]

Initiatives to increase the use of pensioners and part-time labor could provide some relief for the labor-intensive services sector. Perversities in the incentive system, however, have prevented managers from actively recruiting part-timers. Managers reportedly complain that the use of part-time workers complicates the computation of bonus payments and, because part-timers tend to be less productive, hampers the enterprise's ability to fulfill labor-productivity targets. Furthermore, individuals hoping to moonlight in the state sector may be discouraged by the bankers' hours kept by most service enterprises. [redacted]

¹¹ Efforts to increase employment of part-time workers include decrees issued in January 1983 and March 1983, and the Comprehensive Program discussed earlier. In addition, in July 1983 the Council of Ministers approved measures allowing pensioners who work at consumer service enterprises to receive their full pension (previously they could not retain their full pensions if they earned more than 120 to 150 rubles a month) and permitting individuals to work a second job in a service enterprise for as much as half their normal work time if the primary place of employment and its trade union approve. [redacted]

Proposals for Expanding the Private Sector

Some Soviet economists have advocated a more radical approach: allowing the private sector to play a broader role in providing services as has been done for years in Hungary and East Germany (see inset on services in Hungary and East Germany). Legalizing and expanding the private sector, proponents argue, could provide several benefits:

- Bringing the private sector above ground would reduce the level of bribery and corruption currently connected with the purchase of state services and raise public morale.
- The private sector could better mobilize currently underutilized resources such as pensioners and moonlighters.
- A decentralized network of private service outlets could respond more promptly and flexibly to changes in consumer demand and, with a larger number of small shops, bring services to locations more convenient to consumers. [redacted]

Economist Abel Aganbegyan, an informal adviser to Gorbachev, has been a prominent advocate of adopting the East European model. Aganbegyan has argued in newspaper articles that allowing private operators to rent and run "miniservice points," and expanding opportunities for individuals and groups to provide services outside the state sector, could do much to improve the quality and availability of services. [redacted]

Some Soviet economists have also proposed following the Hungarian model of allowing individuals to work semi-independently, under contract with state service enterprises. Such arrangements could provide legal channels for private activities that are currently conducted underground and enable the regime to regulate and extract a share of private-sector earnings, which at present escape taxation. The state, for its part, would surely have to provide incentives to persuade individuals to give up their lucrative underground operations and sign such contracts. Among the incentives it could provide are access to premises, equipment, training, and supplies and coverage for social insurance, vacation, sick leave, and pension benefits. [redacted]

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Personal Services in Hungary and East Germany

For years Hungary has relied on legally operating private businesses to provide a sizable share of its personal consumer services. Much of this private business consists of moonlighting state workers and pensioners working on a part-time basis. Measures introduced in 1981 allow private entrepreneurs to lease service shops from the state and hire up to 12 workers to run them. Workers may form cooperatives to go into business on their own or under contract with their state enterprise employer to do additional work after normal working hours. Many simple repairs are done by individuals who work on contract for state service shops. [redacted]

Similar arrangements exist in East Germany, where large numbers of private hairdressers, tailors, shoemakers, and auto and appliance repair shops flourish. These establishments, which can be cooperative or individual operations, perform about 75 percent of consumer services. Individuals can hire up to 10 workers—some 82,000 private operations employ 255,000 people. The state makes credit available to craftsmen, and supplies and materials can be purchased through cooperatives engaging in wholesale trade. Prices are set by craftsmen themselves and must be approved by local authorities. Cooperatives are subject to greater state regulation and are presented with annual plan output goals. The work of private craftsmen is not subject to the state plan. [redacted]

Conservative Resistance. Aganbegyan and other advocates of expanding the private sector have encountered strong opposition from officials who see dangerous social and political consequences attending any such moves. In a June 1985 *Pravda* article written under the pseudonym O. Vladimirov, Boris Rakhmanin, the first deputy chief of the party Central Committee's department for relations with the "socialist bloc" and a prominent spokesman for conservative views, called proposals to expand the private sector "revisionist" and fraught with serious economic, social, and ideological consequences. Officials such as Rakhmanin take a dim view of developments in

Hungary, East Germany, and especially China, where measures to privatize certain types of economic activity have gone the farthest. They argue that expansion of the private sector in China has produced corruption, speculation, inflation, and a growing social stratification that, in their view, creates a potential for class conflict. Ideologically minded officials also have complained in the press that the private sector lives as a parasite on the state economy, plundering state property, benefiting from subsidized rates for premises, heat, electricity, and transportation, and pocketing "superprofits which no capitalist ever dreamed of." [redacted]

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Even among reformers, moreover, the question of how much of a role the private sector should be allowed to play is controversial. Prominent academic Tatyana Zaslavskaya, author of the iconoclastic 1983 "Novosibirsk Report," which criticized systemic failures of the Soviet economy and was widely circulated in the West, has argued in recent press articles that expansion of the private sector would increase the level of "injustice" in Soviet society. In her view, the private sector is unjust because private incomes are derived through exploitation of market scarcities rather than through hard work. Seeing an increase in the number of individuals living off such "unearned" income would, Zaslavskaya argued, further demoralize honest state workers who must live on what they earn. [redacted]

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Popular Skepticism. Many ordinary Soviet citizens also balk at proposals to expand the private sector. Frequent complaints to Soviet media concerning high prices for scarce food items in collective farm markets, where prices are set by supply and demand, testify to a widespread public suspicion of free markets and market prices. Yevgeniy Ambartsumov, a senior researcher at the Institute of the Economics of the World Socialist System and a prominent advocate of expanding the private sector, told US Embassy officials that his articles supporting privatization of services have drawn a huge volume of mail split almost evenly between support and opposition. In Ambartsumov's view, the nay-sayers represent a deep popular fear that privatization would lead to a revival of capitalism and to "one man becoming richer than another" [redacted]

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The Tallin Experiment—Allowing Firms To Pocket the Profit

Izvestiya reported that a state radio and television repair association has leased a fully equipped workshop to a team of repair technicians. The team pays for everything out of its own pocket—rent, utilities, new equipment, supplies, and janitorial services. Like other state enterprises, the team has a plan assignment, but, in a departure from the usual practice, planners have promised the team a stable plan, that is, plan targets will not be increased as profits increase. The plan requires the team to pay 650 rubles per month per man to the state. The team keeps 70 percent of everything earned above the plan assignment. A team leader and council determine wages and decide how to run the operation.

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Although proponents of the private sector see many economic benefits coming from expansion, other officials evidently worry about the economic costs that might attend such a move. In articles in the Soviet press, for example, managers have expressed the fear that opening up opportunities in the private sector will divert manpower from the state sector. Similarly, officials and fellow workers have complained that individuals attracted by the possibility of large earnings in the private sector lose interest in contributing to the state sector or sometimes do not contribute at all. In late 1985, the official newspaper of the Young Communist League published several articles calling for greater regulation of the private sector to ensure that opportunities to earn money there do not undermine incentives to work in the state sector.

According to the authors of the Izvestiya report, the new system has transformed the way the shop operates. Average repair time has been cut from two weeks to three days, and the shop gets few returns since shoddy repairs reduce the team's earnings. Paying the bills gives the team an incentive to economize, and team members have cut consumption of utilities and spare parts. They also let the janitor go, deciding they could keep the shop clean themselves. The team rented a second service truck and hired a driver to drum up more business, and, when members discovered the receptionist's rudeness was driving customers away, they fired him. The technicians' earnings have increased to the point where they are no longer interested in doing repairs "off the books."

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Collective Contracts: Personal Incentives in the State Sector

Service-sector officials in Estonia claim to have found another way to stimulate personal initiative in the state service sector. As part of the extension of the consumer services experiment to Estonia in January 1985, republic officials began an experiment with the use of collective contracts in radio and television repair service. The Estonians claim that the quality of

repair service has been vastly improved, because the contracts not only make workers responsible for costs but also allow them to retain a large share of profits. An enthusiastic account of this experiment published in *Izvestiya* in August 1985 demonstrates how the collective contract works under ideal conditions (see inset on Tallin experiment).

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Despite high-level endorsements and enthusiastic press articles, collective contracts do not appear to have made much of a splash elsewhere in the service sector. Use of collective contracts was endorsed in the consumer services experiment, but press reports indicate that collective contract arrangements in services and other sectors have encountered many obstacles. Ideological conservatives reportedly object to the high incomes earned by contract workers. Some officials fear that the contract arrangements could lead workers to become preoccupied with making a profit and to lose sight of the interests of the enterprise and the economy as a whole. [redacted]

Press reports indicate that collective contracts frequently cause problems for planning officials and factory managers, who find themselves compelled to violate the contracts when unforeseen circumstances require revision of plan priorities or reassignment of workers. For their part, the workers find they have no recourse when management violates the contract, even if management reneges on promised wage payments. Contracts stipulate that management is to provide the collective with necessary supplies, but managers have little control over sources of supply outside the enterprise. Frequent supply disruptions can stop work in the collectives and prevent them from earning the large amounts they anticipated. In view of these difficulties, it is not surprising that collective contract arrangements often do not work. [redacted]

Cooperatives—Halfway Houses for Personal Initiative

Given the formidable ideological barriers to anything that resembles individual private activity, it is not surprising that reform-minded economists have tried to find a way to get around these barriers. Several recent press articles have called for reviving cooperatives, which played a large role in the economy in the 1920s. Proponents argue that such a move would provide a quick fix for the service sector while requiring few additional resources and avoiding the undesirable side effects that conservatives argue would accompany a large-scale expansion of private activity. [redacted]

Proponents of cooperatives may be talking about something comparable to the old style cooperatives or artels that existed before the revolution and were revived as part of Lenin's New Economic Policy in the 1920s. These organizations operated much differently than the cooperatives in the USSR today. They were independent, self-governing associations of large and small groups of workers that enjoyed genuine autonomy from the state—members ran the operation and divided profits among themselves. By the 1930s, however, independent cooperatives were either abolished or taken over by the state as a result of Stalin's imposition of central control over the economy.¹² Their descendants, organizations of the Union of Consumer Cooperatives that today conduct trade and provide services mainly in rural areas of the USSR, are cooperatives in name only. With few exceptions, they operate like ordinary state enterprises having little operational autonomy and working under plan assignments that leave little or no profit for the members. One of the exceptions is a roadside restaurant recently set up in the Georgian Republic (see inset on cooperative restaurants). Although restaurants do not fall strictly within our definition of consumer services, the case of the Georgian restaurant illustrates the advantages proponents see in a revival of independent cooperatives. [redacted]

As proponents see it, allowing the revival of old style, truly member-run cooperatives in the service sector would have several advantages:

- Cooperatives encourage higher labor productivity than state enterprises and can more easily make use of the labor of pensioners, the disabled, teenagers, and women with young children.
- Cooperatives have a political advantage: They are seen as ideologically "superior" to private ownership (although inferior to state ownership) because they preserve the collective nature of work and control. Additionally, in taking this road the Soviets could argue that they are drawing on their own experience of the 1920s and therefore developing a distinctively Soviet model rather than imitating the Chinese or Hungarians. [redacted]

¹² Statistical handbooks for some of the Baltic republics indicate that, at least in these areas, cooperatives existed in industry up to 1960. [redacted]

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Cooperative Restaurants Don't "Cook the Books"

According to reports in the Soviet press, a roadside restaurant set up in 1984 by the Georgian Republic Union of Consumer Cooperatives operates on a collective contract that gives it wide-ranging economic independence. Employees do the purchasing and set prices themselves, and prices have gone down. The restaurant delivers a fixed amount of its profits to the state, but it is free to use above-plan profits any way it chooses. Most of the above-plan profit is shared among employees. [redacted]

According to media reports, customers claim the food is better and more varied than the usual fare in state-run restaurants. Sales are up, and, with no increase in staff, the restaurant is now turning over to the cooperatives union four times the profit it earned before. Employees earn two to three times their former salaries, and the restaurants' defenders insist that these are achieved without shortchanging the customer, doctoring the books, or dodging government auditors. [redacted]

Despite the advantages claimed by proponents, proposals to revive the cooperatives have encountered opposition from conservatives who oppose any departure from state ownership as a retrogressive step. They see cooperatives as just another way of opening the door for "exploitative" profits and "unjustifiably" high earnings that might lure workers away from labor-short state industries. [redacted]

Policy Directions Under Gorbachev

The Available Options

To judge from the range of experiments tried and proposals aired in recent years, the new leaders are likely to choose one or a combination of the following options for improving consumer services:

- Seek solutions on the cheap: attempt further adjustment in the management mechanism combined with disciplinary measures to exact better performance

from workers and managers. This could involve further adjustment of the planning and management system as well as attempts to more strictly enforce plan assignments for the provision of services such as the requirement that all enterprises provide consumer services.

- Increase funding for the state service sector: provide it with a larger share of labor, capital, and materials.
- Enhance the role of personal initiative: expand the use of collective contracts and create opportunities for cooperative or quasi-private arrangements.

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Seeking Solutions on the Cheap. Recent events suggest that the regime is likely to try to get maximum mileage from efforts to improve the existing system before it resorts to more costly measures. In a speech to the Supreme Soviet on 18 June, for example, Premier Ryzhkov announced that machine-building enterprises are being ordered to set up factory service networks to improve repair service and give the enterprises a greater stake in the quality of the consumer goods they produce. Four defense industry ministers were publicly rebuked in June for paying insufficient attention to the production of consumer goods at enterprises they supervise. This action suggests that the leadership may attempt to force ministers and managers to do a better job on other consumer-oriented assignments. [redacted]

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We cannot rule out the possibility that, despite the regime's rhetoric on services, it is not prepared to take economically or politically costly steps and will go no further than attempting to make the existing system work better. The long-term economic gains from these measures, in any case, are likely to be small. To be effective, Gorbachev would have to resort to disciplinary measures more severe than public reprimands, but it seems improbable that managers in high-priority industries would be severely penalized for failing to meet assignments for the provision of services. [redacted]

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Funding the State Sector. A substantial increase in the share of resources allocated to the service sector could bring a considerable improvement in the supply of consumer services. Labor is particularly important in the services sphere. The leadership plans to allocate the entire increment (3.2 million persons) to the work force in 1986-90 to the "nonproductive sphere," which includes health, education, and services. Premier Ryzhkov told the party congress in March that any labor freed up in industry by modernization is also slated for these areas. It is not clear, however, how much of this additional labor is actually earmarked for the service sector. [redacted]

Rhetoric aside, there is no sign that the leadership is prepared to substantially increase the share of labor or investment devoted to services. Indeed, in light of the large, long-term commitments that Gorbachev has made to his industrial modernization program, his endorsement of the food and energy programs, and the continuing needs of Soviet defense, the service sector is likely to fare poorly in the competition for resources for at least several years to come. Providing additional resources, moreover, would do little to remove the perversities of the incentive system or to encourage service-sector enterprises to make efficient use of resources and serve their customers better. [redacted]

Increasing the Role of Personal Initiative. Although politically controversial, arrangements designed to stimulate personal initiative among workers in the service sector appear to offer the greatest potential economic gain for the least economic cost. Many obstacles would have to be overcome, but collective contracts, independent cooperatives, and quasi-private arrangements have the potential to provide workers with sufficient scope and effective personal incentives to produce major improvements in the quality and quantity of personal services. [redacted]

Gorbachev's Policy and Perspectives

Sanctioning arrangements that allow a greater role for personal initiative in the service sector would require strong backing from Gorbachev. He has not taken a clear and consistent public stance in support of expanding personal initiative, and, in view of the controversy surrounding such measures, he may well wish to avoid doing so. Nevertheless, there is evidence indicating that Gorbachev favors expanding the role of personal initiative:

- During his tenure as party secretary for agriculture, he took a favorable view of citizens' private plots. His call for a "realistic" evaluation of the role of moonlighters in housing repair in a speech to Lenin-grad party workers in May 1985 also suggests that he is sympathetic to expanding the role of personal initiative in services.
- In his speech to the 27th Party Congress in February, he called for new arrangements that would allow private individuals to provide services under contract with state enterprises. He echoed these sentiments in a July speech to Khabarovsk party workers, calling for a search for "new forms of individual work activity." Both at the congress and in Khabarovsk, Gorbachev endorsed expanding the role of cooperatives in the service sector. He did not make clear, however, whether he had in mind the present ersatz cooperatives or more vigorous, independent entities.
- He and other Politburo members have repeatedly endorsed collective contracts. He told the June 1985 Conference on Science and Technology that such contracts should be boldly expanded to become the main form of management. It remains to be seen whether he will be willing or able to force planning and ministerial officials to give contract collectives elsewhere the degree of operating autonomy and resource support that make the Tallin experiment work. [redacted]

The General Secretary's statements on the broader topics of economic reform and ideology suggest that he has little sympathy with conservative arguments that an increased role for personal initiative in the service sector is ideologically unacceptable. Gorbachev has repeatedly expressed his views on the need to expand the role of workers' initiative in the economy and to create a sense of "socialist enterprise" among workers. His remarks have more than once suggested an impatience with ideological obstacles that stand in the way of change. Gorbachev warned in Khabarovsk during his Far East tour that he would not allow dogmas that conservatives regard as "eternal truths of socialism" to become an obstacle to progress. He has given little attention to other, practical obstacles, such as the problems of supply, taxation, and price setting, that will also have to be dealt with to successfully foster personal initiative in the service sector. [redacted]

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Whither the Gorbachev Regime?

Recent events have added to the uncertainty about what Gorbachev and his colleagues have in mind for the service sector. Reiterating his determination to address the problems of the service sector at the party congress, Gorbachev proposed a two-part agenda. He linked his endorsement of cooperatives and individual arrangements to measures to crack down on illegalities and abuses in services and other sectors of the economy, calling for legislation to eliminate "unearned" income, theft, and corruption. Shortly after the congress, the Politburo seconded Gorbachev's proposals and ordered the drafting of new legislation in both areas. [redacted]

One part of Gorbachev's agenda was fulfilled in late May with the publication of a series of decrees on "unearned income" and corruption (see inset on unearned income). Although the decrees contain no new prohibitions on private activities, they increase penalties for violations of regulations already on the books, such as tax evasion and theft of state property. At a minimum, these decrees create a climate in which private activity is viewed with suspicion and may be increasingly subject to arbitrary actions of local officials. If vigorously applied, these measures could significantly reduce the overall supply of services available to Soviet consumers by making it risky for underground private operators to continue to do business. Although the decrees pay lipservice to the need to expand the supply of spare parts and construction materials sold to the population through legal channels and to move quickly to expand the supply of personal services, they provide few clues as to how, if at all, the leadership intends to accomplish these tasks. [redacted]

As yet there has been little progress on cooperatives and individual labor arrangements—the second half of this legislative agenda. The Politburo approved guidelines in August on the formation of cooperatives, but the guidelines have not yet been published and there are few clues as to how far they go. It is likely that conservative resistance is delaying progress on new legislation to expand individual labor activity in services. Evidence indicates, however, that discussion of such legislation is proceeding within the regime. Aleksandra Biryukova, newly appointed Central

Key Provisions of Decrees on Unearned Income

The decrees contain a variety of measures to further General Secretary Gorbachev's anticorruption campaign, including steps against corruption by officials and ordinary citizens. Those measures that will have the greatest impact on private-sector economic activity include:

- *Closer monitoring of individual income to identify those receiving money from illegal sources.*
- *Increased financial penalties for violation of laws on taxation and licensing of private artisans and craftsmen.*
- *More detailed accounting by state enterprises of supply inventories to curtail theft by personnel.*

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Committee Secretary in charge of the consumer sector, said in a speech on 20 May that legislation to encourage citizens' individual labor in services is being drawn up. Oleg Bogomolov, director of the Institute for Economics of the World Socialist System, told Austrian journalists in April that measures to permit the formation of small family businesses in the service sector would be forthcoming. [redacted]

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Prospects

Enactment of genuinely effective measures to expand the role of personal initiative in consumer services will be a severe test of Gorbachev's leadership ability and commitment. Arrangements designed to stimulate personal initiative will have little effect if they are not accompanied by effective steps against some of the planning and management problems that have stymied past attempts at reform in services and other sectors. Problems that would have to be addressed include:

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- Ensuring operating autonomy—overregulation by central planners and ministerial officials often deprives the collective contract of its incentive effect. The same fate could befall cooperatives and even private individuals if they are not given sufficient independence to run their businesses profitably and

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serve their customers well. This should include the power to expand operations, control the number of employees, and adjust prices to reflect supply and demand.

- Providing facilities and supplies—chronic shortages of materials and equipment make it difficult for any type of enterprise to operate profitably. Frequently, self-financing arrangements are rendered meaningless, for example, because construction resources and equipment needed to modernize or expand operations are generally unavailable for purchase. Creation of adequate legal sources of supply will be essential to the success of contract, cooperative, or individual operations.
- Increasing incentives—private operators working legally are now required to pay 60 to 65 percent of their profits to the state in taxes. If private initiative is to be encouraged, provisions would have to be made for a more equitable tax rate aimed at encouraging individuals to operate legally rather than underground. The regime would likewise have to set the level of taxes or deductions from profits of cooperatives and contract collectives at a reasonable level and prevent planners and managers from adjusting it upward.

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Movement to increase the role of personal initiative may become increasingly attractive if, as we believe, efforts to improve the system on the cheap fail to produce a major improvement in consumer services. However, in view of the serious economic and political obstacles to personal incentive measures, change will probably be slow in coming.

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Appendix

Definition of "Everyday Services"

The services we deal with in this paper largely coincide with the items in the Soviet category "everyday servicing of the population." In US national accounts, these services are classified as "personal services," "automotive repair services and garages," and "miscellaneous repair services."¹³ There are noteworthy exceptions, however, which mean caution must be used in making US/Soviet comparisons in this area:

- The Soviets include some private housing construction and repair, which, partly for the sake of manageability and partly because construction is not a service, are excluded from this study.
- The Soviet category "everyday services" includes a substantial amount of activity that is not actually a service, but production of goods.¹⁴ According to Soviet definitions, the purpose of the service sector, apart from providing services, is to provide the population with a source of high-quality, nonstandardized goods. Production activity therefore is legitimate in the eyes of authorities if it is done by individual order of customers and is of high quality.
- Soviet data do not accurately represent expenditures by households on these services because the basic data exclude materials (such as cloth used by tailors) and also include purchases of services by state enterprises and institutions. [redacted]

The category "everyday services" encompasses over 900 types of activities, the largest of which are shown in table 5. [redacted]

¹³ *Standard Industrial Classification Manual*, Office of Management and Budget, 1972, pp. 298-314. [redacted]

¹⁴ In contrast, US accounts separate production activity conducted in service establishments from service activity. [redacted]

Table 5
Everyday Services Sold in State Enterprises and Estimated Shares of Total Sales, 1985

	Million 1981 Rubles	Percent Share
Total sales	9,677	100.0
Shoemaking and repair	956	9.9
Tailoring and repair	1,801	18.6
Knitting and repair of knitwear	461	4.8
Repair and production of household appliances	1,126	11.6
Repair and servicing of automobiles	538	5.6
Repair and production of furniture	402	4.2
Drycleaning	219	2.3
Laundries	435	4.5
Photographers	463	4.8
Baths and showers	217	2.2
Beauticians and barbers	868	9.0
Rentals of consumer durables	270	2.8
Hauling services	541	5.6
Funeral services ^a	406	4.2
Processing of agricultural produce and other agricultural services ^a	764	7.9
Other	210	2.2

Sources: *Vestnik Statistiki*, no. 7, 1985, p. 80; and 1985 SSSR *V Tsifrah*.

^a Values for funeral services and processing of agricultural produce and other agricultural services are estimated based on their shares of the total for 1984.

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Table 6
Growth of Everyday Services
Provided by the State *Percent*

	Average Annual Growth			
	1971-75	1976-80	1981-84	1985
Repair of:				
Shoes	3.0	5.1	5.5	NA
Clothing	2.6	3.4	3.8	NA
Knitwear	NA	12.5	4.1	NA
Durables (household appliances, tools, radios, televisions)	10.5	13.5	10.5	NA
Furniture	NA	13.0	7.2	NA
Automobile repair and servicing	NA	22.7	13.7	12.1
Production of:				
Shoes	9.3	9.4	6.0	NA
Clothing	5.3	4.2	0.5	NA
Knitwear	13.0	9.8	6.0	NA
Metal items	NA	22.2	12.2	NA
Furniture	15.9	10.2	7.4	NA
Other services:				
Drycleaning	9.4	5.2	3.2	3.8
Laundry	10.3	6.3	2.8	4.3
Photography	11.3	7.1	5.4	7.7
Public baths	0	2.6	2.4	5.3
Beauticians and barbers	5.3	5.6	5.7	6.2
Rental of durable goods	19.4	14.3	12.0	11.6
Freight hauling services	NA	7.4	7.0	3.2

Sources: *Vestnik Statistiki*, no. 5, 1983 and no. 7, 1985; 1983 *Narkhoz*; and 1985 *SSSR V Tsifrahk*.

The repair and rental of durable goods (including automobiles) is the largest and fastest growing sector in "everyday services" provided by the state, accounting for about 20 percent of the total in 1985 (see table 6). Their swift increase reflects the rapid rise in Soviet production, and hence the stock of durable consumer goods.¹⁵ It also is in keeping with the official policy (originated under Krushchev) of trying to limit the demand for durables by encouraging the public to rent rather than buy them. The Consumer Goods and Services program announced in late 1985 also emphasizes the need for more repair and rental services.

Despite rapid growth of repair services, the leadership has far to go to meet Soviet norms for these services. According to one Soviet publication, only 15 percent of the planned consumption norm for repair services is being met, as compared to almost 50 percent of the norm for customized production and 21 percent of that for personal services.

¹⁵ Automobile repair services in particular are in short supply and are the subject of much lament in the Soviet press. In 1982 the level of car servicing was less than one-tenth the planned norm. The Soviet consumer's insistence on keeping his long-awaited and expensive automobile past the planned service life of nine to 10 years is aggravating problems with auto servicing. Because retirements are low, the car inventory is growing in excess of plan, causing the inventory of service stations to fall even further behind demand. See "The Consumer and the Automobile—What Future?" *USSR Review*, February 1985.

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