
East European Economies Facing the "Eighties"

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The overall economic performance of Eastern Europe in the 1971–1975 period, when most of the countries in question enjoyed relatively high rates of growth coupled with rather substantial improvement in the standard of living, revealed also a number of significant weaknesses menacing the future. Indeed, already the second half of the 1970s contrasted sharply with the first one. The rate of growth of national income for the area as a whole was lower than at any time since the establishment of the communist system: the aggregate for the six "people's democracies" (Bulgaria, Czechoslovakia, German Democratic Republic, Hungary, Poland and Romania) was below 4% annually as against almost 7% in the plans; even leaving aside Poland which virtually collapsed towards the end of the decade, the combined rate for the remaining five countries was only about 4,5% annually. The record varied for individual countries; however in all cases without a single exception there was a marked slowdown not only in comparison with the preceding five-year period, but also with the plans which were supposed already to account for some negative factors (as, for instance, the impact of the rise in world energy prices). Unlike the slowdown during the so called "New Course" after the death of Stalin, when it was linked to a deliberate re-direction of resources towards consumption, this time the deceleration was accompanied by an even less favourable movement of real incomes of the population: Poland ended the quinquennium with dramatic shortages of basic consumer goods, Bulgaria, Czechoslovakia and Hungary had real wages practically stagnant (around 1% annual increase), and only GDR and Romania recorded figures anywhere near the original plans. Outside the Comecon, Yugoslavia fared better in respect of the overall growth (over 5% annually on average in 1976–1980), but real wages fell strongly in 1980 reducing the

average annual change for five years to about 1%, with very high inflation, and unemployment hovering around 10% of the non-agricultural workforce.

The question which must be posed is how to interpret these phenomena: are they only a more or less temporary twist in the path of development, or a reflection of deeper processes which signal a consistent trend? A categorical answer would be obviously too much to expect here, but some hypotheses can be formulated.

To begin with, the planners themselves threw some light on the prospects for the 1980s. The plans for 1981–1985, either in the preliminary or in the final versions, carried a quite unequivocal message: in every “people’s democracy” the past retardation of growth of national income was projected into the future, resulting in a combined annual rate of growth for five countries (we are again leaving out Poland) by approximately one-fifth lower than the respective rate over the years 1976–1980. Yugoslavia too planned growth (in this case in terms of Gross National Product) at a lower annual rate than previously (4,5%). Paradoxially, the expectations were not so pessimistic for the less predictable agriculture, but in industry each country again planned output targets below those actually recorded in the preceding period. The practice of setting targets in the consecutive plans below the previous record was very much present in Soviet post-war economic history, where it reflected a virtually relentless deceleration of growth in every single quinquennium since 1950, save the 1966–1970 period. In the second half of the 1970s the Soviet average annual rate of growth of national income dropped almost to one-third of that of the beginning of the 1950s – a remarkable vindication of the theory of the “*potukhayashchaya krivaya*” (literally – the “dying-out” curve) which was so vehemently denied by the official Soviet economics in the inter-war years.

All this suggests that the East European results for 1976–1980 were not a freak, but rather a symptom of a more profound change; this change might have surfaced earlier if not for the massive influx of external resources in the first half of the 1970s. This hypothesis seems to concur with what is generally known about the poor prospects of drafting-in new resources, and the insufficient progress in more intensive utilization of the existing ones. The supply of labour was on the whole diminishing both for general demographic reasons, and for the fact that despite the still relatively high proportion of agricultural population the potential and the benefit/cost ratio of migration from the countryside to the towns was declining. Increases in labour productivity unassisted by more capital remained largely unsatisfactory, and the rising rate of substitution of capital for labour makes growth more expensive in terms of investment per additional unit of national income. Similar effects resulted from the need to reach less accessible natural resources, and to develop infrastructure often neglected in the past. Energy and material input/output ratios remained excessive. Relief from imports did not come easily as it required frequently resorting to more costly exports. On the other hand, times have passed when the growth-hungry

political leaders and their planners could simply turn the screw on the consumer and safeguard ambitious targets by raising the share of accumulation in the national income. Whatever the failure to keep the glowing initial promises, consumption standards have increased in Eastern Europe over the past years, and consumer aspirations have increased even more strongly. This restricted the former freedom to take away resources from agriculture and related industries, even if they are highly capital intensive. Even private motorization started posing problems: the number of passenger cars in five countries – not counting Bulgaria and Romania – rose from 750 thousand in 1960 to 3,5 million in 1970 and 10 million in 1980, which began to affect the balance of petrol in these oil-poor countries, despite the fact that the private share in overall petrol consumption was still of the order of 10% only.

Retardation of growth came, therefore, as no great surprise. But does it actually matter? Should the East European communist leaders worry about the diminishing rates and make efforts to stop the rot? After all, taken at face value, the East European rates of growth remained still higher than the West European ones, and an absolute fall in national output in any East European country was still regarded as exceptional, unlike the recessionary phenomena in the West.

However, this kind of argument – although continued to be used in the countries of the Soviet bloc – brings probably small consolation to the party leaders, both for ideological and for pragmatic reasons.

Ideological implications are manifold. The claim of communism's superiority over capitalism rests heavily on the former's ability to secure long-term rapid growth, uninterrupted by crises. For generations the steeply rising statistical curves served as the most popular and seemingly irresistible propaganda asset. Rapid growth was regarded as the paramount factor of "catching-up and overtaking" the developed capitalist countries, and of the transition to full communism. It was the assumption of an 8,5% annual rate of growth sustained over 20 years since 1960 that underlay the Khrushchevian plan of ushering the Soviet Union into the era of full communism by 1980 – and it was the obvious failure to achieve it that must have prompted Brezhnev to switch to the formula of "advanced socialism" of undetermined duration, and without any quantitative commitments. References to the increasing costs of non-renewable resources or to the unfavourable movements in the world markets don't save the day: whatever their relevance, they carry a message that abolition of capitalism has not in itself brought about the removal of all fetters to economic development, and that planned economies are also very vulnerable to the impact of external factors. Acceptance of the sharply diminished and still falling rates of growth – even if long term objective factors were to blame – must be taken as refutation of the entire Marxian concept of human progress so strongly linked with the prospect of abundance.

Ideology apart, pragmatic considerations make the diminishing dynamism even more worrying. There are several interconnected reasons why growth is of greater importance for East European than for

Western economies, and why rates of growth which would be regarded as at least acceptable in the West might cause justified concern or even prove unbearable in the East. The overall lower than in the West level of economic development combined with the still felt consequences of the income-squeeze in the past results in personal wealth and some elements of social infrastructure (housing in particular) weighing considerably less in the standard of living of the population than in Western countries. This places a greater burden on *current income* which in turn is, *ceteris paribus*, a function of growth. In the initial stage of industrialization when a strategy of rapid *acceleration* of growth prevails, there is a sharp conflict between growth and immediate consumer interests because of the rising share of accumulation in national income. At a more advanced stage the position becomes different if an economy is able to *sustain* an approximately steady rate of growth with a corresponding more or less steady share of accumulation: then the rate of growth of output (national income) determines the rate of increase of real incomes of the population. Incapability of sustaining such a rate creates grave problems for the regime: to maintain the rate of growth of consumption with a falling rate of growth of national income would require a reduction of increase in investment, but this would depress the dynamics even further, engendering some sort of a downward spiral. To save growth at the expense of consumption cannot be ruled out, however in view of the enhanced dependence of the communist regimes' legitimacy on their ability to "deliver the goods", constraints are clearly much stronger now than in the past. Attempts to apply such manoeuvres on a wider scale and for a longer period might not only prove dangerous or simply unfeasible politically, but also self-defeating economically because of the high probability of a negative feed-back as far as productivity is concerned. On the other hand, slack development adversely affects social mobility which in the past was such an important feature of East European societies, compensating to quite an extent for many other deficiencies; the need for continuation of this process is still pressing, particularly in the less developed countries of the region, and the diminished opportunities may significantly add to social frustrations. In the Yugoslav case this aspect is linked with the problems of fighting unemployment.

There other causes for concern too. In some instances – contrary to expectations – deceleration has not alleviated but exacerbated the imbalances usually plaguing the Soviet-type economies; a new economic term even emerged – "the bottleneck multiplier" – to characterize the aggregate loss in production caused by reduction of output in a particular sector. This was especially conspicuous in the case of Poland in 1980/81, but by no means confined to that country alone. Finally, in economies lacking excess resources, lasting retardation of growth cannot be regarded with indifference by those in charge of the military potential.

It is with all these matters in mind that the Soviet and East European leaders of the communist parties, including probably the Yugoslav

ones, must have viewed the Polish Summer of 1980 and its aftermath.

Certainly, over the entire post-war period Poland time and again emerged as a special case. She was strongest of all in the resistance to the imposition of the communist order in the aftermath of the war. Later, the single open attempt to oppose stalinization within a Communist party came in Poland (Gomulka's "right wing and nationalistic deviation"). Even at the peak of Stalinism the pressure for mass collectivization was unsuccessful, and the country's agriculture remained predominantly private. The idea of a market-oriented economic reform and of workers' participation in management found an early, widespread and persistent support in Poland. The Catholic church not only retained a position unique in the communist world, but over time gained immensely in stature. The degree of intellectual freedom, and of what may be termed "openness to the outside world" was as a rule higher than elsewhere. And perhaps most important – twice before 1980 major workers' revolts forced a change of government with far reaching consequences for the operation of the regime in general, and for the management of the economy in particular. Under the circumstances, the ruling elite could have perhaps alleviated the mounting conflicts by becoming genuinely more reformist, more accommodating to people's attitudes, beliefs and aspirations. When this had not happened and instead the unwieldy economic system was in the 1970s overburdened with hyper-expansion and overexposed to pressures stemming from reckless borrowing in the West – the scene was set for an explosion. The economic catastrophe sparked off a popular reaction which presented the most fundamental, so far, challenge to the established principles of communist order in Eastern Europe.

Yet, despite the undeniable peculiarities, it would seem wrong to separate in essence the Polish case from the rest of Eastern Europe. Such separation would be obviously unwarranted not only for the main period covered by this history; but also at the end of the 1970s and the beginning of the 1980s, when events took a different turn in many respects. The basic structural problems appeared to be the same *kind*, varying mainly in *degree*. This applied to the latent socio-political conflicts as well, although the Polish economic misery which followed the 1980 revolution had made it easier for the other East European countries to avoid the danger of a spillover. By the same token, however, the arrest and reversal of the slide of the East European economies becomes in the longer run more indispensable than ever.

The obstacles to the achievement of this objective are compounded by factors not at all dissimilar to those at work in the Polish case. Most of the East European countries which resorted at the beginning of the 1970s to Western loans in order to supplement resources and to gain access to higher technology they were unable to develop domestically, found themselves at the outset of the 1980s in substantial financial difficulties. The indebtedness kept growing, and whereas in the first half of the decade this was the result of the wish to avail themselves of

extra-opportunities for expansion – in the second half the clear reason was the inability to produce the expected returns. Net indebtedness of the five East European members of Comecon – Poland excluded – increased from 1975 to 1980 by more than 2,5 times (from some 12 to about 30 thousand million US dollars – of current value, however). The Yugoslav net foreign debt increased at least as fast, reaching 15 thousand million dollars by 1980. When calculated per head of the population, by 1979 Hungary and the German Democratic Republic (and Yugoslavia) were more indebted than Poland.

Although the Hungarian and the East German (and the Yugoslav) ratio of maturing payments to earnings from exports to the West (the so called debt-service/export ratio) was much better than the Polish one, and their credit standing and overall economic position substantially more favourable – the underlying weakness was there, too: insufficient capability to increase export outlets to the Western markets (admittedly more difficult because of the recession) despite the massive import of technology and know-how in the first half of the 1970s. This is true in relative terms even for the GDR, her privileged position in the intra-German trade notwithstanding. External factors will continue heavily to affect most of the East European countries in the 1980s: all of them entered the decade with a deficit with the West on current account; this means that even a *slowdown of the increase* of the debt would require exports to go up faster than imports from the West until balance is reached. Assuming balanced foreign trade with other partners (socialist and developing countries), this would render the rates of growth of national income *for domestic use* (distributed – i. e. the sum total of domestic consumption and capital formation) *lower* than that of produced national income. Bearing in mind how low the latter are planned (the figures shown above referred to national income *produced*), the consequences for the dynamics of both components of domestic utilization must be serious indeed. Such a relationship between the rate of growth of national income produced and for domestic use appeared already in the latter part of the 1970s decade, contributing to the inferior record in the growth of consumption compared with the overall indicators of performance. Its continuation in a period when the rates of growth of national income produced are expected to be lower, places so much greater a strain on the economy and on social relations. The proportions of the necessary excess of the rate of growth of exports over that of imports depend on the time allowed for achieving the balance on current account. Assuming 1990 as the target date, and a certain relationship between the planned growth of national income and the necessary imports (the so-called import elasticity of growth), some Western sources estimated the difference at 2,5 percentage points (exports would have to increase by 6% annually in real terms, imports by 3,5%). The difference which this would cause between the rates of growth of national income produced and that for use would be lower than 2,5%, none the less it would be tangible. It should not be forgotten that under this assumption the debt would continue to grow throughout

the 1980s, levelling off by 1990 with a sum-total for the five East European countries (Poland excluded) more than twice the level at the beginning of the decade; this would still leave for the 1990s the burden of interest, not to speak about the repayment of the principal. Attempts to bring closer the target date, and to reduce the debt mountain would require an increase in the export surplus; attempts to postpone it would require the willingness of both creditors and borrowers to accept a further substantial rise in indebtedness.

Apart from the problems involved in coping with the consequences of reducing (and later – eliminating) a foreign trade deficit in a supply-determined economy, there are problems connected with the way such a development can be brought about: by maintaining imports at a level sufficient to satisfy the normal needs (the level of “normal” import dependence from the West must have increased substantially since the beginning of the 1970s) at the cost of a correspondingly larger increase in exports, or by cutting imports to the bone in order to adjust them to the limited export capabilities. Some reduction of the current account deficit in the later 1970s was obtained mainly in the second way; this started already to produce the “bottleneck multiplier” effects, although, as emphasized, on a scale much smaller than in Poland. If this method were to continue, let alone intensify, the effects would be considerably harder to contain. An inward turn – increase in the share of intra-Comecon economic relations – was likely under these circumstances (including Yugoslavia’s closer ties with Comecon); this could perhaps improve the position of a particular country, but it would be difficult to see this as a factor producing a strong positive effect for the group as a whole, especially as at least for some time Eastern Europe will have to cope with the economic consequences of the Polish crisis. Several East European countries had at the beginning of the 1980s a quite unusually high level of accumulated trade deficit with the Soviet Union, which hardly augured well for the prospects of substantial relief from this side. Eastern Europe faces a serious energy crisis, and no encouragement was offered by the Soviet Union as far as an increase in oil deliveries to Eastern Europe was concerned; the slight advantage in price of oil bought from the Soviet Union was likely to diminish in the first half of the 1980s. On the other hand, an end to the Western recession might ease access to these markets somewhat, although tougher competition is also likely (particularly from the Far Eastern countries and from the new members of the EEC), and the behaviour of the terms of trade remains unpredictable.

Everything hinges, therefore, on the possibility to lift substantially the level of performance of the domestic economies, especially to make them more sensitive to costs and to quality in the broad sense, the technical modernness of the products including. Unfortunately, plans of four East European countries (Bulgaria, Czechoslovakia, Hungary and Romania) for the period 1981–1985 revealed a continuation of the preceding quinquennium’s rise in the so called ICOR (incremental capital/output ratio – the amount of investment expenditure needed for

a given increase of national income). Should this prove irreversible, and should the use of energy, basic raw materials and of course labour remain excessively high in relation to output, the prospects would look sombre indeed.

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This leads to the question of the likelihood of institutional changes which would promote greater efficiency and spur innovations; in other state of affairs by mid-1970s. At the outset of the 1980s, conditions for relatively radical economic reform have emerged in Poland under the pressure of a powerful popular movement of truly revolutionary dimensions, despite the military clamp-town in "Solidarity". However, even if these conditions were successfully utilized, the crisis that country had to extricate itself from was so deep that one could hardly expect the Polish results over the decade to contribute to the brightening of the aggregate picture of the East European economy. Thus, the problem must be posed for the other countries.

One common element for all East European countries (including the Soviet Union in some respects as well) was a further relaxation of the attitude towards private economic activity in the second half of the 1970s. This applied in the first place to agriculture – both to the private plots within collective farms, and to private farms in Poland and Yugoslavia. In some countries this was accompanied by a more liberal policy towards small business outside agriculture as well (private, cooperative and local state enterprises); in Hungary where the boost to private and particularly cooperative economic activity created initially by the New Economic Mechanism seemed to have been arrested around 1975, the policy returned gradually to the original direction. This trend looked likely to continue into the 1980s, and although no spectacular effects could be expected (especially in the GDR and Czechoslovakia), some relief might come from these quarters. Attempts to open the door to enterprises funded jointly with or by foreign capital might also be more successful in some countries than in the past, when the economic effects were largely negligible.

It was clear, however, that regardless of the actual impact of other sectors, the decisive importance would still lie with the way the dominant state (or social – as the Yugoslav terminology goes) economy functioned. The measures which had actually been taken or envisaged in connection with the new five-year plans for the years 1981–1985 created a rather firm impression that changes might be expected as a rule within the already existing framework only. Neither the Yugoslav market socialism, nor the Hungarian NEM intending to combine central planning with regulated market mechanism, nor finally the centralistic (command) system of Bulgaria, Czechoslovakia, GDR and Romania were set to remain immutable, but it looked unlikely for any of the countries in question to move across what might be called the demarca-

tion line, at least not in the medium term. In Yugoslavia one could expect the continuation of the search for less vague forms of "self-management *planning*" – in order to reduce the negative consequences of over-reliance on the operation of the market. In Hungary the clear tendency was to try to overcome the systemic difficulties by more consistent application of the principles of NEM: phasing-out the individualized financial shelters for enterprises which should be made to face the consequences if unable to stand up to economic conditions (bankruptcy including); linking much closer than before domestic with foreign markets by appropriate changes in price structure and the use of uniform exchange rates (with gradual broadening of the sphere of convertibility of the currency); further reforming of the investment system in order to stem the continuously excessive pressure for funds by strengthening the financial responsibility for the projects (the suggested solutions were the least clear here – not surprisingly in view of the complexity of the problem). As for the countries preserving the command system, the emphasis since the end of the 1970s was on net (value added) instead of gross output indicators, on somewhat closer links between profitability and incentives, on reduction of the number of obligatory targets; in some countries of this group certain organizational forms were strengthened (Kombinate in the German Democratic Republic), longer term norms substituted for the annual ones (Czechoslovakia), and even bodies of employee-participation in management instituted (Romania, but hardly more than in a consultative capacity). The basic principles of target-planning and physical allocation of main producer goods were being preserved, as well as the hierarchical subordination structure.

The institutional changes surveyed above might have some positive influence on efficiency. The developments in Hungary seemed in themselves to be the most promising, but the country – very dependent on foreign trade, and with few indigenous primary resources – faced formidable tasks. The command economies could benefit somewhat from the shift to net output and greater attention to financial results of the enterprises, particularly in terms of savings in inputs. On the whole, however, the changes seemed to be marginal, and they could hardly be expected to bring more than only marginal effects.

Is there not a chance of more comprehensive reform in the command economies? Such possibility can never be ruled out completely, and the Polish experience may become a factor prompting some reconsideration on the upper levels of the East European political hierarchy. Of course, not in the sense of imitating, but to the contrary – of avoiding the Polish course of events. In the light of the Polish experience, a Hungarian-type economic reform and perhaps the "Kadarist" model as a whole might become more acceptable to the Kremlin and the sub-Kremlins of Eastern Europe. After all, Hungary has remained relatively stable politically, while Poland may be viewed as an exemplary lesson of a time-bomb produced by blocking more moderate reforms at an earlier stage. Should this lesson be driven home, the pragmatic

approach to economic reform might gain ground, and this in turn could affect economic performance – if not in the first half, then perhaps in the second half of the decade. Needless to say, the East European power elites might not go along with this way of thinking, let alone acting . . .

This note on the economic history of communist Eastern Europe over a quarter of a century* ought not to be read as a simple prediction of doom. With luck, the East European economies may muddle through the decade of the “Eighties” without another major breakdown, and some of them may even do better than planned by an odd percentage. What they are, however, unable to do in their existing shape – is to present their own people and the world at large with an attractive prospect for the future, and the more so to gain credibility for the worn out millennial promise of communism.

* Postscript to “Economic History of Communist Eastern Europe”, to be published in 1983.