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Economic Developments in Eastern Europe

Every spring, the Department of Socialist Countries and East-West Economic Relations at the HWWA-Institut für Wirtschaftsforschung-Hamburg submits a summary of the past year's economic developments and of current trends in CMEA countries.¹ The main results are presented here.

USSR

The new Five Year Plan period got off to a promising start. In the wake of the Chernobyl shock the Soviet economy faced the difficult task of allocating a considerable amount of additional resources to eliminate the damage done. For the time being it looks as if the problem has been coped with quite well. According to the 1986 plan fulfilment report it was possible to stop the trend towards declining growth. Higher growth rates than during the previous year were achieved for the overwhelming majority of targets. In some major sectors the growth rates corresponded to the average levels envisaged in the Five Year Plan. For the first time there was reference in the 1986 plan fulfilment report to the development of produced national income. The increase of 4.1 % even meant an overfulfilment of the plan target level (+ 3.9%). Applied national income, on the other hand, only increased by 3.6 % (plan: + 3.8 %).

The foreign trade turnover fell by 8 %, primarily as a result of the dramatic decline in prices on the crude oil market. There was a further shift towards trade with socialist countries. The USSR once more recorded a considerable import surplus vis-à-vis Western industrialised countries. The deterioration of the terms of trade is a bitter blow for the Soviet Union, since for the planned modernisation of its economy the Soviet

economy relies not only on the priority development of the mechanical engineering industry but also on the importation of Western technologies. The effects of the marked bias in the Soviet export structure and the lack of competitive strength of industrial products are now being felt more severely.

The satisfactory development of the agricultural sector, where the production increase of 5.1 % almost reached the planned target, should be emphasised. The substantial increase in the cereal harvest was a major contributory factor. The development in this sector improved the Soviet Union's difficult foreign trade situation, since less foreign exchange was required for food imports from the West.

The population's standard of living in 1986 developed as follows: The increase in money incomes exceeded the plan target, and the substantial increase in residential building corresponded to the plan target. The plan was not fulfilled, on the other hand, with regard to the increase in per capita incomes. Although the 10.2 % increase in the services provided against payment for the population was also below target level (+ 14.2 %) it must nevertheless rank as a respectable result. On the whole, consumer demand for goods and services could not be fully satisfied.

As in previous years the industrial sector also recorded substantial growth in 1986 (+ 4.9%). The inability of individual sectors to fulfil plan targets often was the cause of a deterioration in delivery discipline in comparison with the previous year.

As opposed to the impressive performance in quantitative terms, the planned modernisation and qualitative reorganisation of the Soviet economy failed to make the desired progress. The urgently needed

¹ Klaus Bolz (ed.): Die wirtschaftliche Entwicklung in ausgewählten sozialistischen Ländern Osteuropas zur Jahreswende 1986/87, Verlag Weltarchiv GmbH, Hamburg. The report on the GDR was written by Peter Plötz, that on the USSR by Sybille Reymann, that on Poland by Andreas Polkowski, and that on Rumania by Petra Pissulla, all from the HWWA-Institut für Wirtschaftsforschung-Hamburg. The contribution on Bulgaria was written by Ilse Grosser of the Wiener Institut für Internationale Wirtschaftsvergleiche, Vienna. The author of the report on Czechoslovakia was Franz-Lothar Altmann, Osteuropa-Institut, Munich. The report on Hungary was contributed by Andreas Wass von Czege, University of Hamburg.

concentration of investments on essential projects did not take place, and the inability to meet deadlines remained a serious problem. Nor were the efforts to save raw materials and fuels – priority target in the current Five Year Plan – everywhere successful to the planned extent. At the same time, the quality and range of many Soviet products frequently failed to meet requirements.

On the whole, developments in 1986 suggest that considerable efforts are still needed in order to effect the envisaged restructuring of the Soviet economy. Despite various reform measures already carried out in 1986 it was not yet possible to achieve the qualitative targets in all fields. The hopes, therefore, have now turned to 1987. The growth rates fixed in the 1987 plan are generally higher than in the 1986 plan, yet by and large lower than the results achieved in 1986. Produced national income is planned to increase by 4.1% and industrial production by 4.4%.

German Democratic Republic

The East German economy is currently moving along a stable growth path; the 1986-1990 Five Year Plan period began successfully. The increase in produced national income in 1986, i.e. the increase in all goods produced for private and government consumption, investments and exports, was 4.3% compared to the 1985 figure and thus only 0.1 percentage points below the target fixed in the National Economic Plan. According to the plan fulfilment report the increase in national income was, for the first time, exclusively due to the increase in the productivity of labour.

Once again, industrial production increased at a faster rate than planned. The productivity of industrial labour continues to follow an upward trend.

As in previous years the development in the agricultural sector helped stabilise growth. The performance in crop production clearly surpassed the plan target. The result in 1986 was only 3.5% lower than in 1985 – the record year so far in the GDR's agricultural sector. There was also a continuingly positive development in animal production.

Whereas the increases on the production side by and large corresponded to plan targets this was not the case with regard to the application of national income. International merchandise trade expanded more slowly than planned, although the lower growth rate is due to a considerable degree to a decline in the prices of key imports and exports (crude oil and mineral oil products).

According to the Minister of Trade, Gerhard Briska, the GDR's foreign trade turnover (exports plus imports) increased by 3% (plan: 5%). Due to the lack of corresponding data no statements can be made on the global development of exports and imports and thus on the corresponding balances.

Investments have benefited considerably from overall economic growth. Instead of the increase of 0.8% planned for 1986 in comparison to the 1985 figure investments actually expanded by 5.8%. This marked expansion would indicate that the GDR has modified the investment strategy – scarce investment funds and more extensive utilisation of production plants – pursued during the last Five Year Plan period. Besides, it is not unusual in a centrally planned economy if at the beginning of a medium-term plan period the growth rate for investments is clearly above the annual average target level for this period.

The East German population benefited from the stable development of the economy as a whole during the last plan year. Private consumption, measured in terms of retail trade turnover, increased by 4.1% in nominal terms (plan: 4.0%). This growth rate is virtually the same as in 1984 and 1985, which means that private consumption has caught up with the average annual growth rates recorded during the second half of the 1970s.

The 1986 plan fulfilment report shows that plan target growth rates were again achieved for produced national income, industrial production, the agricultural sector and private consumption. During the current intensification phase of the GDR economy an overall economic growth rate of over 4% is a lasting success, a success which, in addition, exclusively results from a more efficient utilisation of resources. The expansion of investments provides favourable growth conditions for the future. Furthermore, the population did not suffer from bottlenecks last year of the kind experienced, for example, in 1982. All in all, the central political and economic leadership of the GDR can look back on a "normal" year with a good growth performance.

The GDR intends sticking to its course this year. This is indicated by the increase in produced national income planned for 1987 and the envisaged application of that income. In terms of performance in 1986 the calculation of plan targets can be termed "normal". They roughly correspond to the target figures for the current Five Year Plan period.

The produced national income is planned to grow by 4.5% in comparison to 1986, industrial production by 3.8%. In line with the economic concept of the political

and economic leadership in the GDR, a steady improvement in the supply situation of the East German population is again intended for the current year in order to stimulate the achievement motivation of the workforce. Retail trade turnover as well as the net money income of the population are planned to increase by 4%. This means that – due to the expected price increases for higher-quality consumer durables and non-durables – the increase in private consumption in real terms will not match the growth of overall output.

The expansion of foreign trade is planned to be accelerated; the foreign trade turnover is to increase by 6%. Although export and import targets for 1987 have – as usual – not been published, the difference between the planned increase in produced national income and planned national application (growth of overall investments and retail trade turnover) indicates that exports are planned to increase more than imports.

Poland

The Polish economy requires a decisive turn. Although production increased in all sectors, especially in the agricultural sector, in 1986 the quantitative increases could not disguise the unsatisfactory performance with regard to the internal and external equilibrium and the intensification of production. Produced national income exceeded the plan target, but was still five percentage points down on the figure in 1979, the last pre-crisis year. The situation on the domestic market clearly shows that the increase in produced income was achieved via an increase in the production of producer goods (Department I) at the expense of consumer goods (Department II). The supply did not match monetary demand. The supply gap was estimated at 150-200 billion zloty in 1986 and was primarily noticeable in the field of consumer durables.

The efforts by the government to reduce the state budget deficit by restricting subsidies have been unsuccessful since 1982, which makes it more difficult to strengthen the achievement principle in production and bring about a recovery of the domestic market. Poland's growing indebtedness, while representing a serious national economic problem in itself, also has adverse effects on production and the domestic market as well as on exports.

It is hoped that economic reform will foster a process of restructuring, modernisation and greater efficiency in the Polish economy. Spurred on by the spirit of reform in the Soviet Union the party and the government have committed themselves to the continuation of reform.

The second stage of the reform, whose content was outlined during the III. plenum of the Central Committee of the PUWP in December 1986 and the main points of which were listed and presented for discussion by the Commission for Economic Reform in April 1987, represents a renewed and this time more dramatic attempt to save Poland from a continuing economic decline. As often emphasised by the government this is not a new reform, but simply an attempt to apply existing principles and mechanisms more rigidly and single-mindedly with the aim of raising quality and efficiency. Whether the sixth attempt at reform in Poland's post-war history will produce a breakthrough remains to be seen.

Czechoslovakia

Although overall economic growth was on the whole satisfactory in 1986 (3.4% increase in national income) there were complaints about deviations from plan targets, imbalances and other shortcomings. Contrary to plan specifications investments again increased at a faster pace, but progress in the field of modernising machinery and equipment was only hesitant, and there was once more an increase in the number of unfinished projects. The fact that it was not possible to accelerate the enterprises' innovation activities and save more materials costs was particularly criticised. Altogether, a quarter of all industrial enterprises were unable to fulfil their plan targets in 1986. Light industries revealed particular weaknesses. As a result there was no significant improvement in the supply quality and range for the domestic as well as the export markets.

As regards foreign trade a surprisingly high deficit was recorded primarily in CMEA trade, especially in visible trade with the Soviet Union. In trade with non-socialist countries there was an overall surplus due to the substantial export surplus in trade with developing countries. Visible trade with Western industrialised countries, whose share in Czechoslovakia's total foreign trade fell from 23.1% to 16.1% between 1980 and 1986, experienced a slight deficit for the first time since the end of the 1970s. Czechoslovakia's net hard-currency indebtedness, therefore, probably increased slightly to approx. \$ 2.8 billion by the end of 1986.

The fact that a plan for 1987 has not been published only allows but few statements to be made on the – undoubtedly existing – plan targets. The aforementioned imbalances, however, have apparently led to more modest targets than the annual averages derived from the Five Year Plan.

The performance figures of the first few months of 1987 also indirectly confirm the assumption that targets

have been fixed more cautiously. The considerable production shortfalls recorded for the industrial and construction sectors cannot be solely blamed on the cold weather in January. It is interesting to note that the corresponding shortfalls in Hungary, the GDR and Bulgaria were much lower despite similarly poor weather conditions. In Czechoslovakia these shortfalls would therefore appear to indicate problems of a more serious and fundamental nature. This was particularly apparent in the development of foreign trade. Over half of the production plants were unable to fulfil their export plans in January 1987. The extreme supply backlogs of the Czechoslovakian industry even led to a downward revision of the 1987 export targets for trade with the West (from an originally planned annual increase of 4.2 % to 0.6 %) and in its wake of the 1987 import targets too (from 5.8 % to 3.9 %). The 1987 plan targets for visible trade with socialist countries (annual increases of 2.8 % for both exports and imports) were not revised during the first few months of the year despite an equally apparent non-fulfilment of plan targets.

In the Czechoslovakian economy, too, a process of renewal, involving greater independence for enterprises, a more pronounced participation of industrial producers and buyers in foreign trade activities as well as the acceptance of joint ventures, has begun. There are plans to elaborate a corresponding legal framework by the end of 1987.

Hungary

The hopes of Hungarian economic policy planners for a recovery of economic growth have remained unfulfilled to date. Produced national income, which had already in 1986 increased only by 0.5 % to 880 billion forint and was thus still lower than the 1984 level, was also unable to achieve the desired growth rates during the first few months of 1987. Despite administrative restrictions on imports and price increases in many sectors, on the other hand, it was still not possible in the first few months of the year to bring the population's consumption level and business investments adequately under control, whereby consumption level and business investment increases in 1986 had already markedly exceeded plan targets, which meant that applied national income increased by 3 % to 895 billion forint and there was a convertible currency deficit on current account for the first time in years. The balance of trade in convertible currencies, which in 1986 showed a deficit of over US \$ 400 million instead of the planned surplus of \$ 350-400 million, deteriorated even further in the first quarter of 1987. Contrary to the intentions of economic planners,

Hungary's indebtedness increased on international financial markets.

This year's plan targets, which assume relatively modest growth rates of between less than 1 % (in the case of real per capita income) and roughly 5 % (gross agricultural production) and which envisage a surplus of only US \$ 130-180 million for exports in convertible currencies in comparison with the US \$ 500-600 million specified in the 7th Five Year Plan, are hardly likely to be fulfilled. This, however, has not yet been officially admitted. The assumed non-fulfilment is based on the trends in industry, which were unable to match expectations regarding production and, above all, export increases during the first few months of the year, as well as in the agricultural sector, where a long-lasting frost during the early months of 1987 meant that a large part of the wheat sown in the autumn was destroyed and now has to be replaced by an increased sowing of maize and sunflower seeds.

As could already be observed in 1986, the stimuli emanating from the demand side are relatively weak in all sectors of the economy. The inability of Hungarian products to assert themselves on international markets, and thus the stagnation of production and turnover, are still primarily caused by supply-side shortcomings – the low productivity of labour, outdated technologies, the obsolete plant and equipment, and the lack, or poor quality, of raw materials and semi-finished goods caused to a considerable degree by existing import restrictions. Key efficiency criteria for economic activity – specific materials usage, capacity utilisation and labour productivity – were unable to reach the targets set by national economic planners in both 1986 and during the first six months of 1987. Hungary's economic policy planners, therefore, already no longer rule out the possibility that this year's budget deficit, which already has a very high plan estimate of 43.8 billion forint, may turn out to be much higher than planned, especially since the actual deficit in 1986 was over 40 billion forint as opposed to the target figure of 22.5 billion forint.

In view of the current crisis-prone development of the Hungarian economy the efforts of the economic policy planners concentrate on re-establishing external economic equilibrium via import restrictions and, at the same time, by increasing the volume of exports and adjusting the range of exported articles to world market demand. Meanwhile, domestic consumption, which according to the national economic plan should not exceed the 1986 level, is to be pushed back via price increases, subsidy cuts and obstacles to investments. The introduction of a system of self-administration for state enterprises, the creation of a bankruptcy law, the

transition completed in January 1987 to a two-tier banking system, and the extensive tax reform and reorganisation of company law planned for the near future all represent significant steps towards a market-oriented and decentrally coordinated economic system. This process of economic reform in Hungary, however, is not inconsiderably impaired by the country's current domestic and external instability, a situation which is viewed with growing concern not only in Hungary itself.

Rumania

The first quarter of 1987 ended with the same complaints by Ceauşescu about serious plan arrears in Rumania's industry as the year 1986, although the exact details were not quantified. Above all, export production again seems to have lagged far behind expectations. Although plan arrears are nothing unusual in Rumania the fact that its internal and external economic development was already extremely problematic last year explains why the continuing difficulties in increasing the efficiency of the Rumanian economy are a cause for concern.

In mid-1986 Rumania again ran into serious external payments difficulties. These were caused not least by oil-price-induced export shortfalls and the liquidity problems of Middle Eastern trading partners. Towards the end of the year the miserable domestic supply situation led for the first time to bitter public protests by the population despite the officially recorded high overall economic growth rates of 7.3% for national income and 7.7% for industrial production.

Although agricultural production also increased substantially in 1986 (by 12.8% in gross terms and 13.3% in net terms) due, *inter alia*, to favourable weather conditions, and record yields were reputedly achieved for almost all crops, the supply situation of the population has not improved.

Particular criticism was levelled by Ceauşescu against the development of foreign trade in 1986. Although industry and agriculture recorded high production increases, total exports fell in real terms by 11.6% and imports by 5.5%. Data are not yet available on the development of hard-currency trade in 1986; however, the OECD nine-month figures indicate that the balance of trade surplus in convertible currency has probably again decreased in comparison with the previous year. Although Rumanian exports to western industrialised countries during the first nine months of 1986 rose in comparison with the corresponding period

in 1985 by almost 9% to \$ 2.7 billion, imports again increased substantially for the first time, namely by almost 30% to just under \$ 1.3 billion. There was therefore a surplus of approx. \$ 1.4 billion vis-à-vis this group of countries. However, as the Rumanian balance of trade vis-à-vis developing countries is traditionally negative due to oil imports, the overall surplus in convertible currency may be expected to be much lower.

In view of last year's plan arrears Ceauşescu has called for a "radical improvement in all industrial activities" in 1987. Above all, he has insisted that an improvement of the frequently poor product quality and a reduction of production costs are essential. The renewed plan arrears at the beginning of 1987, however, would indicate that neither the planned increase of industrial production in 1987 (6-7%) nor the increase in net production (9-10%) can be achieved. This also makes the fulfilment of the plan target of between 8 and 9% for national income seem doubtful.

Bulgaria

In 1986 national income growth increased to 5.5% (plan: 4%) following the 1985 low (1.8%), the wide fluctuations in agricultural production being a decisive factor in both years. However, little progress (if any) was made towards the goal, of a "new quality" of economic growth: the amount of idle equipment is still substantial, including 230 programme-controlled machine-tools, and the performance of those in operation suffers because of poor software; the share of products unsaleable due to poor quality increased, and defective products were returned from abroad; delays in putting new capacities into operation were most conspicuous in key development branches (chemicals, biotechnics, metal casting, toolbuilding and automation, machine-tools and robots, metallurgy).

Bulgaria was hit by several calamities in 1986: the Chernobyl radioactive fallout, a violent earthquake and a disastrous industrial accident at one of the biggest chemical combines in Devnya.

Gross industrial production increased by 4.3% (1985: 3.5%). As usual, engineering – including electronics – showed one of the highest growth rates (9.3%), this time joined by the coal industry (10.2%). Extraction of coal reached a record level of 36.8 million tons (+13.3%), sustained by a capacity increase in the biggest open cast coalfield of the country. However, (electric and heat) energy production sold continued to decline (-3.8%); electric power production stagnated (0.5%), remaining 6.3% below its 1984 level. Consumption of electric energy is still rationed.

Agricultural production increased by about 10.5% (plan: 7.4%), not quite making up for the 1985 shortfall (-12.2%). In crop production (20.6%) the grain harvest can be estimated at 7-8 million tons. The extremely bad 1985 harvest (5.5 million tons) required substantial grain imports (3 million tons in 1986). Despite additional imports in fodder concentrates, animal holdings in the socialist sector were further down with regard to cattle (-1.3%) and sheep (-2.6%). The number of hogs (1.9%) and poultry (2.5%) increased. Animal production as a whole grew by 3.2%.

Investment growth decelerated sharply to 2.0% in nominal terms (1985: 8.6%), the aim of reducing the share of unfinished construction was missed by a wide margin.

On the consumption side, retail trade turnover and average wages and salaries increased by 7.3% and 5.4% respectively in nominal terms. Due to the lagged effect of the 1985 autumn price hike, real rates of growth will be markedly lower. There were serious shortages on consumer goods markets, including those for some basic foodstuffs.

In foreign trade, Bulgarian imports nearly stagnated (+0.2%) while exports decreased by 2.9% - the overall balance of trade deficit more than doubled to 762 million foreign-exchange Leva. In a regional breakdown, the 1985 pattern persisted: while exports were increasingly orientated towards the socialist countries (+4.5%), imports were partly shifted to the non-socialist countries. The balance of trade deficit with the industrialized West soared up to about US \$ 1.5 billion (exports -26.4%, imports +11.5% on US \$-basis, i.e. including the oil-price and exchange-rate effects).

Bulgaria's net hard currency debt is likely to have risen to about US \$ 3.2 billion by the end of 1986 (1985: US \$ 1.9 billion). As opposed to 1985, when Bulgaria had raised \$ 475 million on the international financial markets, only one syndicated loan (\$ 45 million) was reported in 1986.

The personal re-shuffles and institutional changes before the 13th Party Congress of the BCP (April 1986) were followed by a series of organizational changes throughout the year. In December 1986, the 1986-90 five-year plan was adopted as a law - it entails an upward revision of most growth targets as against the (ambitious) draft plan: national income growth is to accelerate to 5.4% p.a. (1981-85 actual: 3.7% p.a.). At the same time, another round of economic reforms was launched. In a preliminary assessment, the determination of the leadership to bring about a more comprehensive reform seems more serious. However, despite some improvements, the reform concept itself is still of a rather ambiguous nature.

For 1987, Bulgarian planners envisage an increase in national income produced of 5.2% - 1986 having been a rather exceptional year, the aim of almost keeping up the rate of economic growth seems at least hard to achieve. Economic policy measures recently decided upon comprise the obligation for enterprises to operate in at least two shifts (three shifts for those producing extremely scarce goods), and the introduction of state control of product quality. "Concrete measures" were announced to close down unprofitable enterprises, to shift production to places with an adequate labour supply, and to speed up the completion of investment objects.

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