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COMMITTEE ON SOVIET ECONOMIC POLICY
ECONOMIC DIFFICULTIES IN THE SATELLITES

Note by the Secretary

The attached paper prepared by the International Staff is circulated for information and for discussion at the next meeting of the Committee.

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ECONOMIC DIFFICULTIES IN THE SATELLITES

I. THE BACKGROUND TO THE PRESENT DIFFICULTIES

A. 1948 - 1953

1. The attempt by the satellite governments to industrialise their countries and to establish a communist pattern of society was bound to lead to economic difficulties. But these difficulties were accentuated by the speed with which these changes were carried out and by the decision to copy blindly the policies followed in Russia in the early thirties, irrespective of whether these policies were suited to the special problem of each of the East European countries.

2. The agricultural policies of the satellite regimes have been one of the main causes of popular discontent. The promises made after the war that the property rights of the peasants would be safeguarded were broken, and around 1948 drives were launched everywhere to bring the land under collective ownership. The collective enterprises, which had to deliver the bulk of their produce to the state at low prices, remained poor and inefficient; the peasants who remained outside the collective farms were hounded by the government and frequently deprived of essential supplies of fertilizers and machinery. As a result agricultural output suffered; in 1955 food output did not exceed two-thirds of the pre-war level.

3. The industrial workers, the favoured children of communism, fared little better. The fall in agricultural output made it impossible to provide the rapidly growing cities with sufficient food. Retail trade was disorganized by the campaign to eliminate private shops, and the few goods which were available were badly distributed. Housing construction remained very low, and in some countries it did not compensate for the losses through obsolescence of existing dwellings. As the industrial labour force grew, the cities became badly overcrowded. In the factories the workers suffered a great deal from crude incentive schemes. Being denied the right to strike, they were defenceless against sudden increases in working hours and arbitrary cuts in wages.

4. What made these hardships even more intolerable is that they were not the result of a national revolution, as in Russia, but of a revolution imposed from abroad. The exaggerated praise given to the Soviet Union was a constant reminder of the subordinate condition of the satellite countries. The stock phrases about the "generous help of our great Soviet friend" must have sounded ironic to the numerous officials who were aware of the cost to their countries of Soviet exploitation and of Soviet imposed policies.

5. One example of this cost was the heavy burden of military expenditures imposed on the satellites after the outbreak of the Korean war. According to figures disclosed by the former chairman of the Hungarian planning board military expenditures may have approached 20% of the Hungarian national income. This heavy burden prevented any improvement in standards of living; it overtaxed productive capacity in the satellite countries, in particular in the engineering industries, and made it extremely difficult for them to sustain their programmes of economic development out of domestic resources.

6. When the satellites were driven to ask for Russian aid, they received loans and not grants. In addition, she continued to exploit them, directly by exacting reparations from her former enemies, and less openly by setting up Russian controlled joint companies and by imposing grossly unfavourable terms of trade in her agreements with them. Men like Kostov in Bulgaria were executed for, among other things, bargaining too hard; the recent Russo-Polish protocol implicitly recognised that low-priced exports of coal have caused Poland to lose some 600 million dollars.

7. The policy of autarchy within the Eastern bloc which Russia has enforced has also aggravated the economic problems of the satellites. While it would evidently be wrong to attribute the whole of the reductions in East West trade between 1948 and 1953 to this factor, there is no doubt that in important instances the satellites have reduced their imports from the West against their own advantage. An example of this is the shift of Czech and Polish iron ore imports from nearby Sweden, their traditional supplier, to the distant Ukrainian mine at Krivoi Rog.

8. While Russian imposed policies have subjected the economies of the satellites to severe stresses, it cannot be denied that there have been substantial achievements. In an area which was largely agricultural, powerful heavy industries have been created. Total production has risen rapidly, at a rate far exceeding anything achieved in pre-war years.

9. However, the policies through which these achievements have been secured have been partially self-defeating. The concentration on investment and on defence has left the people with the feeling that they could derive no benefits from the government's policies. There is little doubt that failure to provide for a gradual betterment of the consumers' lot in the years preceding the death of Stalin has gravely jeopardised the chances which the communist regimes might have had of winning over the allegiance of the satellite people.

B. Changes in economic policies since 1953

10. By 1953, it was becoming evident that the burden of re-armament and of sharply increased programmes of investment was proving too heavy to bear, and that the increased production targets announced after the outbreak of the Korean war would not be reached. Heavy industry was hampered by shortages of energy in several countries of the Soviet bloc. Popular resistance was increasing and in the first seven months of 1953 there were workers' or peasants' riots in East Germany, Czechoslovakia, Hungary and Rumania.

11. The first "thaw", associated with the name of Malenkov, was hastened by the death of Stalin; but some relaxation in economic policies would probably have been necessary in any event. Within a few months the governments of the USSR and of all the satellites announced reductions in retail prices, some changes in the pattern of investment in favour of light industries, and in some countries, even reductions in investment. The existing discriminations against independent peasants, traders and artisans were reduced in most countries.

12. These policies were only partly successful. The problem of shifting the pattern of industry in favour of light industry had been underestimated and the shortage of energy continued to impede the expansion of industry. Agricultural output remained low, and the USSR and the satellites were forced to step up their imports of food in order to satisfy the increase in demand which followed the reductions in prices. As exports did not increase to a corresponding extent, the larger imports had to be paid for in gold. In view of the bloc stocks of consumers' goods seem to have been drawn on to a substantial extent in order to meet the rising demand of the population.

13. These difficulties contributed to the further revision in policies which followed the rise of Khrushchev and Bulganin in the USSR, and similar political changes in the satellites. Under the new leadership, emphasis tended again to be laid on heavy industry, though the production of consumers' goods continued to receive more attention than under Stalin's rule. In addition a determined attempt was made to overcome the weaknesses which had thwarted Malenkov's policies. Measures were taken to increase energy supplies and agricultural output, while the Soviet economic offensive in the underdeveloped countries and in Europe helped to raise exports to a level where they could finance much larger imports of raw materials and capital goods.

14. These policies were reflected in the five-year plans announced by the satellites in 1956. These plans, while paying lip service to the need to improve standards of living, in fact gave even higher priority to heavy industry over light industry and economic expansion over consumers' satisfaction. There seems to have been hesitation about the speed with which the remnants of the private sectors were to be socialised; in Rumania and in Bulgaria collectivisation of the land was planned to be greatly accelerated but in other countries the announced goals were less drastic.

15. The plans followed closely the pattern laid down in the Russian Sixth five-year plan and in pronouncements by Russian leaders. There was evidence, however, of an attempt to understand and to solve the special difficulties which have hindered the economic development of Eastern Europe. Whereas each country had hoped, in the past, to be planning to become self-sufficient on the Russian model, the new plans showed a trend towards specialisation between countries. To further this purpose, the Council of Mutual Economic Assistance, hitherto dormant since it was set up in 1949, met early in 1956. For the first time the five-year plans of the satellites were synchronised, so that each country could harmonise its objectives with the needs of its neighbours. This experiment does not seem to have been very successful, and in view of recent events in Poland and in Hungary it may be that many of the agreements concluded will not be carried out.

16. The plans stressed the need to develop trade, especially with the underdeveloped countries. Several of the satellites have made efforts to reach agreements with Western countries providing for repayment of previous debts, and clearing the way for an increase in trade. This reflects greater recognition of the cost to the satellites of the disruption of their traditional trade ties with the West. Russia has not always been able to supply the raw materials which they needed, and there is also evidence that the

satellites have not been able to sell within the bloc all their exportable surpluses. A greater volume of East West trade would provide alternative outlets and sources of supply in the Free World, and give more flexibility to economic planning.

C. The 1956 economic crisis in Hungary and in Poland

17. At the start of 1956, the satellite governments began to implement the harsher policies provided for in their plans for 1955-60. Substantial increases in investments were decreed, ranging from 30% to 40% in most countries. The renewed drive to collectivise agriculture resulted in a substantial rise in the area under collective ownership. The greatest progress was reported by Bulgaria, where by April 1956 socialised agriculture accounted for four-fifths of the available land area.

18. This shift to harsher policies was particularly ill-timed in Poland and in Hungary, where the political situation was already becoming unstable. Inside the Polish Central Committee there was open disagreement between those who advocated continued economic austerity and those who wished to grant concessions to the population. The latter policies, advocated by Cyrankiewicz in the Committee and Gomulka outside it, enjoyed wide popular support. In Hungary the debate over the five-year plan provided Imre Nagy and his supporters with an opportunity to criticise the leadership of Rakosi. In both countries the governments were forced to make token reductions in the five-year plan targets, though they remained unwilling to make substantial concessions to the public.

19. This reluctance to make concessions is largely explained by the economic difficulties experienced by both countries during 1956. Both countries appear to have been in the throes of severe balance of payments difficulties. Poland's exports of coal, which account for close to half of total exports, remained substantially below the planned level. The first instalment on repayment of loans received from Russia in 1949 and 1951 was due during the year. It is reported that the pressure on her balance of payments even forced Poland to refuse delivery of Soviet equipment and raw materials contracted for at an earlier date. Less is known about Hungary's balance of payments, but official spokesmen have stressed the burden which the country's indebtedness laid on her economy. In addition, Hungarian industry suffered from a severe shortage of energy, due to a reduction in Polish coal supplies and a fall in domestic oil production.

20. In the light of these difficulties it is evident that the Polish and Hungarian governments were unable to promise an immediate rise in standards of living. Soviet aid alone could have eased their problem, but this was not forthcoming on a sufficient scale. Russia agreed to postpone the first repayment on the loans to Poland, but it was not until the uprising in Poznan and after three Polish requests that the Soviet government agreed to grant a small loan, amounting to 25 million dollars. At the same time, Russia continued to import Polish coal at less than market prices, and required Poland to participate in her programme of aid to Yugoslavia. Hungary was even more badly treated, and received no aid until October 4th, 19 days before the Budapest revolt.

D. Future possibilities

21. In the light of last year's events, Russia seems to have accepted that hard fisted policies may not be the most economic ones in the long run. She has cancelled Polish debts amounting to 100 million dollars to make up for the losses incurred by Poland in earlier years when she was compelled to sell coal to Russia at low prices. The USSR has also abandoned part of her claims arising out of last year's sale to Rumania of her share in the Soviet Rumanian Oil Company (Sovrompetrol)(1), and agreed to sell her share in another Soviet Rumanian company producing uranium ore. The price of uranium ore supplied by Czechoslovakia has been raised. Within a few weeks Poland, Rumania, Bulgaria, East Germany, and Hungary have been granted plans amounting to over 500 million dollars (2).

22. The total cost of the concessions made by Russia since last October may approach 2 billion dollars. It is to be expected that further concessions will be made within the next few months; Hungary, in particular, will require additional help, and the Polish government has let it be understood that more aid was wanted to help Poland solve her present difficulties. The cost of economic assistance to the satellites is proving substantial. Indeed the possibility cannot be excluded that the Soviet leaders will try to revert to Stalinist methods, refuse to make more concessions or to grant additional aid, and again rely on force to impose their will.

23. Up to now there is, however, no sign that Russia is giving up her attempt to prop communist regimes in Eastern Europe by economic means. The Soviet economy is strong enough to support quite a large programme of aid, though in particular respects existing plans will be affected. The commitments to deliver five million tons of grain to Eastern Europe are bound to conflict with the plans to build up adequate reserves of grain. The reduction in Hungarian coal output and in Polish deliveries to Eastern bloc countries is affecting the already difficult coal supply situation, and will force the coal industry in West Russia to make an extraordinary effort to solve the fuel shortages in the Baltic States, in East Germany and in Hungary.

24. There is little doubt that the five-year plans announced this year by the satellites will be modified substantially to make room for additional concessions to the consumers. It has been already announced that the Polish plan would be revised; and early the Hungarian plan is obsolete. According to some reports, Rumania and East Germany will announce shortly the revision of their plans. Even Russia has announced a forthcoming revision of the sixth five-year plan, which provides for some reduction in investment and in a number of output targets:

-) Russia has agreed that Rumania need not pay for German assets in Rumania worth \$700 million, which Russia had seized after the war and which had formed the major part of her contribution to the capital of the Company.
-) Including \$275 million to Poland, \$50 million to Hungary, \$85 million in free foreign exchange to East Germany, \$50 million in free foreign exchange to Hungary, wheat and investment goods worth \$110 million to Rumania, and a small grain loan to Bulgaria.

25. However, both revision of the five-year plan and Soviet aid can provide only temporary relief. A decisive improvement in living conditions can probably be achieved only through the release of some of the latent energies which have been suppressed by an excessively centralised system of planning. Though any statement on this is, of course, pure speculation, it may well be that other countries will follow Poland's lead in giving up collectivisation of agriculture, reducing discriminations against artisans, and in giving greatly increased responsibilities to workers' councils in the direction of factories.