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8892	PAPER	MOSCOW AND THE INTERNATIONAL COMMUNIST MOVEMENT: DISUNITY, DETERIORATION, AND LOWERED EXPECTATIONS <b>R 12/13/2007 F06-114/6</b>	6	ND	B1
8890	MEMO	MATLOCK RE PAPER "GORBACHEV'S ECONOMIC AGENDA: PROMISES, POTENTIALS, AND PITFALLS" <b>PAR 11/16/2015 F2006-114/6</b>	1	9/11/1985	B1
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*the International Communist Movement*

THE WARSAW PACT AND [SOVIET--EAST EUROPEAN RELATIONS]

*Moscow and Eastern Europe*

[Overview]

Soviet leaders see the maintenance of the Warsaw Pact military alliance and the continued existence of pro-Soviet regimes in Eastern Europe as a priority second in importance only to the preservation of communist rule in the USSR itself. Eastern Europe plays a critical role in Soviet calculations, serving both as a security buffer between the USSR and NATO, and as an extension of Russian domination and influence westward.

Moscow has used the existence of the "socialist commonwealth" and its "fraternal allies" in Eastern Europe to buttress its claims about the legitimacy of communist rule at home and abroad. The suppression of popular challenges to Soviet-style dictatorships--in East Germany (1953), Hungary (1956), Czechoslovakia (1968) and Poland (1956, 1970, 1976 and 1981)--has [effectively] undermined the value of such claims abroad, [although not among a majority of Soviet citizens.]

Nationalist ideas have [at the same time] influenced the East European regimes themselves to varying degrees, and fostered challenges to Soviet authority that have been somewhat more successful. At [the] one extreme, the communist parties of Yugoslavia and Albania have never been under Moscow's control, and have pursued independent policies for decades.

The remaining six regimes, while under more effective Soviet domination, have all at one time or another carried out internal or external policies that departed from Soviet wishes. Romania's President Ceausescu has pursued a

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relatively autonomous foreign policy since 1964, while maintaining strict dictatorial rule at home. Several other regimes--Hungary, the GDR, and even Bulgaria--have also taken cautious steps in recent years to distance themselves from Soviet foreign policy positions. Nevertheless, all must be sensitive to Moscow's outlook and the pressures that the Soviets can apply.

The basic lessons of the past 40 years of Soviet domination of Eastern Europe appear to be:

- [First,] that Moscow will not tolerate the overthrow of a communist regime, and will use military force where necessary to preserve or re-establish communist rule.
- [Second,] that Moscow will tolerate--though with great reluctance--some independence on the part of these communist regimes, and will not use force simply to bring such a regime back into line.
- [Third,] that Moscow will continue efforts to impose its will on these countries, even if they often provoke counteractions stemming from nationalist sentiments in Eastern Europe.

Early indications are that Gorbachev is trying to restore tighter Soviet control over Eastern Europe after several years of slack reins resulting from leadership turnover in Moscow. He has pressured <sup>General</sup> Jaruzelski, for example, to crack down even harder on domestic opponents of the Polish regime. [Given the historical record of 10 major challenges to Soviet domination in Eastern Europe since the war, the odds favor another such political crisis by the end of this decade and its suppression, although Soviet success in defusing Poland may dampen rebellion elsewhere.]

The Warsaw Pact

The Soviets see the Warsaw Pact both as a means of enhancing their own security, and as a mechanism for preserving communist rule in Eastern Europe. To Moscow, these two goals amount to the same thing.

The seven countries making up the Warsaw Pact officially are equals in its policymaking bodies, including its highest [ranking] organ, the Political Consultative Committee, which is composed of the top party leader from each country.

During peacetime, the national armies remain under the formal control of their respective regimes, <sup>but</sup> [At the same time,] the Warsaw Pact's unified command and staff coordinate bloc military policies and oversee training. This unified command is dominated by Soviet officers, and operates in effect as an extension of the Soviet General Staff.

[Soviet control over the East European armed forces would become even stronger] in wartime. <sup>+</sup> The Soviet Supreme High Command would assume direct command of the Pact's combined armed forces [well in advance of hostilities, placing East European forces under unilateral Soviet orders. This could deprive the East European regimes of the right to decide on their own whether to go to war, and undercut their ability to influence events in a crisis.]

The Soviets also exercise considerable control over East European weapons procurement, and seek to ensure that all Pact armies are equipped with weapons of standard design. [Yet] despite considerable pressure from Moscow, the East Europeans have chronically failed to devote the resources necessary to stay in step with Soviet military modernization programs. Even the more advanced East European army units are typically five to 10 years behind their Soviet counterparts, [for example,] and some units are still equipped with World War II vintage tanks.

These growing disparities between Soviet and East European forces, as well as among the East Europeans themselves, undercut Soviet efforts to achieve Pact-wide uniformity [in military equipment] and frustrate their attempts to prepare the Warsaw Pact as a whole to conduct combined operations against NATO. [Despite these problems, the Warsaw Pact's war plans envision the East European armies participating in offensive operations alongside Soviet armies or on separate axes.]

Soviet leaders apparently perceive most of the Warsaw Pact armies as dependable, at least in the initial stages of an East-West war.

- They probably regard the Bulgarians and the Germans as their most reliable allies, with the Czechoslovaks and Hungarians next in line.
- Soviet confidence in the reliability of the Polish armed forces is more open to question. As the second-largest Warsaw Pact army, <sup>however,</sup> the Poles are still expected to carry out important offensive missions on their own in the event of war.
- The Soviets undoubtedly rate the Romanians as the least dependable member of the Pact. Romanian forces are not subject to wartime Soviet command and control, and they do not participate in major Warsaw Pact combined exercises.

*Integrated Economics*  
Economics

The Soviets have long favored increased economic integration with Eastern Europe to accomplish several goals:

- Enhance bloc cohesion as well as their own hegemony;
- Constrain the pull of East European trade toward the West;
- Reduce bloc vulnerability to Western economic leverage;

-- Increase the economic return to the USSR from intrabloc trade.

Most of the East European regimes (for their part continue, as they have for years, to) resist Soviet efforts to strengthen the powers of the Council for Mutual Economic Assistance (CEMA), Moscow's primary mechanism for controlling their economies through joint planning.

The Soviets are running certain risks in putting pressure on the East Europeans to tie their economies more closely to the USSR, and must calculate the trade-offs involved in trying to curtail East European dealings with the West. The Soviets recognize that the East Europeans need to trade with the West in order to shore up their economies, satisfy consumer expectations, and thereby preserve domestic political stability. They also recognize the value of such East-West trade for technology acquisition, which can be transferred back to the Soviet Union. Moscow has been unwilling, moreover, to sacrifice its own trade with the West, or pay too high a price in subsidies to the East Europeans to promote economic integration.

The Soviets have moved in the last few years to reduce their subsidies to the East European economies and improve their terms of trade. In return for Soviet-supplied oil and other raw materials, Moscow wants the East Europeans to raise the quality and increase the volume of their exports to the USSR-- chiefly food, consumer goods and machinery.

The Soviets have pledged to maintain oil deliveries to all CEMA countries at their present level through the end of the decade. Falling Soviet oil production puts their ability to keep their word in doubt, however, and they failed to keep a similar pledge during the first half of the 1980s. Moscow has also made it clear that such deliveries will hinge in part on East European investment in Soviet extraction and delivery projects, including the

construction of another natural gas pipeline from northwest Siberia to Eastern Europe. Again, however, Moscow must strike a balance between meeting its own needs and jeopardizing political stability in Eastern Europe.

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Popular Attitudes

Soviet imposition of communist rule in Eastern Europe following World War II strengthened long-standing anti-Russian sentiments in some countries, and provoked such attitudes in others where they had not existed before.

For their part the Russians typically feel that East Europeans still owe a debt of loyalty for Soviet sacrifices in defeating Nazi Germany and "liberating" these countries. To this should be added a measure of jealousy that East Europeans--save in Romania, Albania and perhaps Bulgaria--have higher standards of living, and conceit among Soviet party leaders that the USSR is entitled to bloc leadership as the first, biggest and most "advanced" communist society. [The result is that few Soviets have any qualms about imposing their will--where they deem necessary--on Eastern Europe.]

[Soviet views about Eastern Europe contain an element of self-deception and naivete. Soviet leaders are well aware of the existence of anti-Russian and anti-communist attitudes throughout Eastern Europe. But they appear to dismiss such hostility as a passing phenomenon that is artificially excited by Western propaganda and subversion. They may not fully realize how quickly the East Europeans would leave the Warsaw Pact and CEMA if free to do so. In any event, they have no intention of tolerating the bloc's collapse.]

Bilateral Relations

[Generalizations about Soviet interactions with and perceptions of Eastern



Europe as a region can only go so far, before one must look as well at Soviet relations with each specific country. ]

### Poland

[ Soviet perceptions of Poland are colored by antagonisms that date back hundreds of years. Soviet leaders recognize the strength of Roman Catholicism in Poland as well as the strength of Polish nationalism and anti-Russian attitudes. They seem unable to understand, however, why the Polish communist party cannot control the Church the way Moscow controls religion in the USSR. ]

While the Soviets have been on the whole satisfied with Jaruzelski's performance since the inception of martial law, they appear uneasy about the extent to which military officers still occupy key posts throughout Poland, and would prefer to see the civilian role in the party leadership strengthened. The Soviets were also unhappy with the public denigration of the secret police following the murder of a Polish priest earlier this year.

### East Germany

Despite the Soviet line that East Germany has nothing in common with earlier German regimes that attacked Russia, the privately expressed views of Soviet officials and ordinary citizens alike still reflect a wide-spread, deeply-seated animosity toward all Germans.

Because the GDR owes its existence to the USSR, subservience to Soviet wishes has been the standard prerequisite for East German leaders. The regime's cautious flirtation with German nationalist ideas in recent years has drawn Soviet suspicion and public criticism.

Moscow openly pressured East German President Honecker to cancel a

scheduled visit to the FRG in September 1984, temporarily forcing him to abandon efforts to isolate GDR-FRG relations from the general East-West climate.

The hard-working character of the German people has considerable Soviet respect, with the GDR providing the bloc with its strongest economy and the Soviets with their most important and dependable supplier of modern machinery and advanced technology.

Soviet military forces stationed in East Germany serve as the USSR's first line in the event of war in Europe. These 400,000 Soviet troops--more than twice the size of the East German army--are also Moscow's ultimate guarantee of a loyal regime in the GDR.

Romania

Romania has unquestionably been the greatest East European thorn in the Soviet side. The Soviets have repeatedly made their displeasure clear over independent Romanian positions across nearly the entire foreign policy spectrum.

Moscow has tolerated Bucharest's independent ways, however, because the repressive Ceausescu regime poses no attraction to Soviet citizens, and because the Romanian president's erratic and egotistical style has prevented him from becoming the leader of wider East European resistance to Soviet wishes.

The chief unknown factor in the equation of Soviet-Romanian relations is the stability of the Romanian regime, which Ceausescu has tended to treat as a family preserve. Ceausescu's declining health--reportedly he is suffering from a very serious prostate problem--may present Gorbachev with an

opportunity to back a possible successor less fixated on demonstrating Romanian independence on the world stage.

Bulgaria

Soviet relations with Bulgaria benefit from ties dating back to Imperial Russia's assistance in freeing the country from Turkish rule in the 19th century. A shared Slavic heritage and cultural affinity provide the only instance of reality coming anywhere close to matching the propaganda claims of friendship between Soviets and East Europeans.

While traditionally the Soviets' most dependable supporter on the international scene, the Bulgarians have taken cautious steps toward a more independent foreign policy in recent years. Bulgarian enthusiasm for a Balkan nuclear-free zone has not been matched in Moscow, for example. This could be related to reported Soviet desires to deploy short-range nuclear-armed missiles here--public reports of which the Bulgarian regime was quick and emphatic in denying.

Czechoslovakia

The Soviets squandered traditional friendly relations with Czechoslovakia in crushing the "Prague spring" of 1968. The Husak regime has subsequently been slavish in supporting the USSR externally, while pursuing unimaginative conservative policies internally. The Czech economy--once the most advanced in Eastern Europe-- has stagnated under a regime afraid to undertake reform.

The true feelings of the Czech people have been best exemplified in the unofficial country-wide celebrations of the national hockey team's occasional victories over the Soviets. The hostile reception given visiting Russian

teams--which the regime is powerless to prevent--have drawn vigorous complaints from Moscow. The national mood, however, is one of resignation rather than rebellion.

### Hungary

The Soviets have tolerated Hungary's market-oriented economic reforms and relative cultural freedom over the past 15 years because Hungarian leader Kadar has been careful to make no claim for the broader applicability of these experiments beyond his country's borders. The Hungarian regime has also demonstrated its loyalty and dependability by faithfully following the Soviet international line.

Reform-minded Soviet economists have long been interested in the Hungarian experiments as possible models for the USSR. This attractiveness, on the other hand, has earned Budapest the suspicion of more conservative Soviet leaders.

Open Soviet-Hungarian polemics broke out in early 1984, however, when a senior Hungarian party official publicly set forth a detailed justification for independent domestic and foreign policies that applied to all East European regimes. There had been earlier signs of Soviet desire to deploy short-range nuclear missiles in Hungary, which Budapest--like Bulgaria--was successful in resisting.

*The Warsaw Pact and the International Communist Movement*

**MOSCOW AND THE INTERNATIONAL COMMUNIST MOVEMENT:  
DISUNITY, DETERIORATION AND LOWERED EXPECTATIONS**

*The International Communist Movement*

Communist philosophy and economic theory <sup>conception</sup> [posit] a utopian future society. Karl Marx's <sup>visions</sup> [visions] of universal equality first found expression in the late nineteenth century with the founding in London of the First International (1864-1876), an association of European labor leaders pledged to destroy the [then-prevailing] capitalist system. A loosely organized and informally coordinated group of [the] major socialist parties of western and central Europe constituted the Second International (1889-1914), which fell apart with the start of the first world war. The Third International, better known as the Comintern, emerged after the Bolshevik revolution to carry out the objectives of the new Soviet state on a global basis. It was formally dissolved by Stalin during World War II.

No true international center ever emerged to replace the Comintern. The Soviet party's authority in the Communist movement has since been exercised primarily through ideological support and training, discreet wielding of Soviet state power, clandestine operations and assiduously cultivated contacts, overt and covert. But as [the] foreign parties assumed national identities of their own over the years, their willingness to give Soviet interests priority over all else eroded markedly. In particular, they have resisted formation of any center which might allow Moscow to reassert an institutionalized control over the movement.

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The Comintern and the Roots of Communist Discord

The decline in the solidarity of the international communist movement, and in Soviet authority over it, is dramatic when viewed from a historical perspective. The Comintern, which provided the organizational skeleton of the international movement from its foundation in 1919 to its dissolution in 1943, was entirely a Soviet creature and Soviet control over it was virtually absolute. Its headquarters were in Moscow, the bulk of its leadership and staff was Soviet, and the primary condition for membership was unqualified acceptance of Lenin's Twenty-One Principles, a list of organizational and ideological rules designed to ensure that foreign parties were cast in the mold of the victorious Russian Bolsheviks.

In fact, foreign parties were in large part mere carbon copies of the Russian party. Tendencies toward independent thought and action were effectively discouraged by domestic repression -- which deepened the dependence of many foreign communists on Soviet support for their very survival -- and the Stalinist purges, which struck foreign parties almost as severely as they did the Soviet. Internal dissension within the parties themselves also proved a weakening factor.

The dissolution of the Comintern in 1943 was a Stalin gesture to his wartime allies, and had little immediate effect on the reality of Moscow's dominance over foreign communists. In 1944-45 Moscow could still compel the massive Italian and French parties to dismantle the large armed resistance movements they controlled and join in conservative-dominated governments of national unity as part of the USSR's grand alliance tactics. In July 1945, it could order the US communist party to purge its ranks of officials such as Earl Browder who were identified with party lines no longer in favor in the Kremlin.

Moscow's control was demonstrated even more tangibly in 1947 with the creation of the Cominform, a truncated replacement for the Comintern which united the parties of Europe, this time in an all-out struggle against the Marshall Plan. It was again a mark of Soviet authority that the French and Italian parties obediently fell into line, withdrawing from the national unity governments and consigning themselves to domestic political isolation.

With the benefits of hindsight, this can now be seen as the high-water mark of Soviet ideological hegemony, however. Within a year the monolithic facade of the communist world had cracked: Titoist Yugoslavia openly defied Moscow and asserted the right to define its own national policies. That blow to Soviet authority within the communist movement has since been followed by many others.

The post-Stalin Soviet leadership under Nikita Khrushchev was itself instrumental in contributing to more fissures within the movement. Khrushchev's efforts to discredit his predecessor at the 20th party congress in 1956 shattered the faith of many communists in the infallibility of the Soviet party and its leaders. Palermo Togliatti, head of the Italian party and a former Comintern agent, shortly after that congress proclaimed the doctrine of "polycentrism", which held that each national party should be free to chart its own road to communism rather than obey the dictates of a single center - i.e., Moscow.

Challenges to Soviet Leadership

Moscow has never succeeded in closing the Pandora's box opened at the 20th congress. The bloody suppression of the Hungarian revolt shortly thereafter (November 1956) cost the movement even more adherents and led to further questioning of the moral basis of Soviet authority. The open eruption of the Sino-Soviet dispute in 1959 added to the disarray; the major non-bloc parties resisted all Soviet efforts to formally excommunicate the Chinese and even today see the Chinese as a useful counterweight to the Soviets in the movement.

A decade later, the Soviet occupation of Czechoslovakia in 1968 temporarily halted what Moscow saw as dangerous liberalizing trends in Eastern Europe, but at the cost of further strains to relations with non-ruling parties -- and of stimulating the spread of Eurocommunism. More recently, a broad sweep of events, beginning with the Soviet invasion of Afghanistan in 1979, punctuated by the declaration of martial law in Poland (December 1981), and culminating two years ago with INF deployment and the Soviet walkout from the Geneva talks, added more fuel to the controversies within the movement and sparked polemics among Eastern bloc states themselves.

International Conferences Mark Decline in Soviet Authority

The progressively less impressive results of the international communist conferences which have taken place since the 20th party congress chart the erosion of Moscow's authority over the international communist movement. The conference of 81 parties held in Moscow in 1960 produced a document which was a carefully-worded compromise between the positions of the Soviets and the Chinese. It was, however, more memorable as the last such meeting attended by the Chinese and as the scene of a violent debate between the Soviet hosts and their Chinese guests. The next -- and last -- World Communist Conference met in 1969, five years behind schedule. It was boycotted by most of the important Asian parties, and produced a final document which many European parties refused to endorse in full.

Moscow had to resort to regional gatherings in 1976 and 1980 to get the European parties together as a show of "proletarian internationalism" -- its ideological codeword denoting the obligation of all communists to give priority to Soviet interests. But even those gatherings only highlighted the the CPSU's inability to reassert its authority over dissident European communists. The Soviets and some of their allies have since occasionally broached the idea of convening another European, and possibly a world conference, and each time ran into objections from major Western parties opposed to

giving Moscow any opportunity to re-establish its sway over other parties. Continuing foreign communist opposition to Soviet policy in Poland and Afghanistan still ensures that any such international gathering would produce less of a show of unity than Moscow could tolerate.

Sources of Communist Disunity

The sources of disunity within the communist movement are many. What was once an international coterie of believers in one faith has increasingly devolved into a collection of individual parties moved by parochial considerations of political advantage. The Soviets themselves contributed to this trend. They long ago transformed the concept of proletarian internationalism from "one for all" to "all for one" -- the one being the USSR.

In the 1920s and 1930s, the moral authority which accrued to the USSR as the homeland of communism and the dependence of foreign communists on it for financial and organizational support combined to bind foreign communists to this tenet. The German party's suicidal refusal to join with the socialists to fight the Nazi menace in 1933 and the shifts imposed on the French and Italian communists in the immediate postwar years were alike dictated by Moscow's view of its own needs rather than by political reality in the countries involved.

The notion that the preservation and strengthening of the Soviet state took precedence over all else could be maintained without difficulty only as long as the Soviet Union remained the world's only communist state. As the communist bloc expanded to include many other states, it has become steadily more difficult to sustain the obvious clashes of state interests. The Sino-Soviet feud in particular, and the periodic convulsions which have shaken Eastern Europe and Moscow's responses to them, further contributed to an erosion of the CPSU's moral authority within the movement. It has become increasingly difficult for the Soviets to justify their actions in terms of common interests of all communists; indeed, their positions on a host of domestic and international issues have come under direct attack from erstwhile comrades. The negative Eurocommunist reaction to Moscow's stationing of nuclear missiles in East Germany and Czechoslovakia in response to INF deployment illustrates this point graphically.

The Situation Today

*Begin* → *The International Communist Movement*  
Despite the ideological and political convulsions that have shaken the world communist movement, the CPSU still recognizes and maintains relations with some 80 nonruling communist

*Outside Eastern Europe*



parties in Asia, Africa and Latin America. More than a third are illegal or restricted from participating in local electoral politics.

While retaining their Leninist organizational structure and authoritarian style, several nonruling parties in Western Europe, India and Japan have evolved into mass parties attracting broad electoral support and winning parliamentary representation. These in particular assert their independence from the CPSU on a range of issues, both to establish national identities and better to resist direct Soviet pressure.

The nonruling parties vary greatly in their dependency on the CPSU and their willingness to support Soviet policies. Nevertheless, all of them, including even the largest and most independent, seemingly feel a need to retain ties to the CPSU and remain within the international movement, bound by an ideological vision in which the eventual triumph of "peace, freedom and socialism" is secured by the weakening and eventual destruction of Western democratic values and institutions. Even when little else is agreed on, this shared vision provides the basis for political cooperation with Moscow against the West, particularly the United States.

At the same time, it is those parties' conviction of Moscow's readiness to subordinate the needs of the international movement -- or rather the needs of foreign communists -- to the dictates of Soviet foreign policy which keeps them determined to oppose Moscow's efforts to reassert leadership of the movement.

#### Autonomy Remains the Central Issue

The issues which divide the Soviets and the large foreign parties are often expressed in terms of ideological conflict, e.g., a struggle between the proponents of "orthodoxy" and "revisionism." On the issue of autonomy, these parties vehemently insist on the right to define their own interests and pursue them with their own tactics. The Soviets, for their part, insist that the interests of any single party must be subordinated to the common interests of the movement, and that as the senior member of that movement, they have the major voice in defining what these common interests are. Moscow thus continues to attempt to assert its leading role among all parties and to ignore in practice its rhetorical endorsement of diversity and separate roads to socialism.

Consequently, disunity within the world communist movement promises to remain a fact of life. Formation of a new international center is highly unlikely; indeed, Moscow's

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incurable propensity for meddling in other parties' internal affairs argues the likelihood of more defections by smaller nonruling CPs and aspiring socialist groups. Thus the movement seems condemned to perpetual fragmentation and polemics. But as long as the Soviet party considers the movement important to the interests and future of the Soviet state, it will never abandon efforts to keep foreign communists harnessed to its cause -- and will always find some who will go along willingly and tactics to persuade others.

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*Fine paper, but  
not for  
introductory behind.  
purposes - aimed  
more for the  
specialist.*

*J.P.*

(b)(3)

Central Intelligence Agency



Washington, D.C. 20505

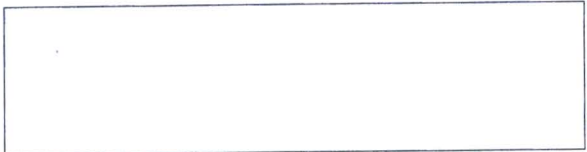
11 September 1985

*J.P.*

Ambassador Jack Matlock  
National Security Council

*JACK -*

Attached is the final draft of a forthcoming memorandum, "Gorbachev's Economic Agenda: Promises, Potentials, and Pitfalls." The analysis identifies and critiques key elements of General Secretary Gorbachev's economic strategy. We conclude that Gorbachev can make a difference in the short run, but will have to address fundamental obstacles to modernization most importantly the limited investment funds available to underwrite the modernization effort. To this end we address potential alternatives open to Gorbachev, including a reduced flow of additional investment to defense.



Chief, National Issues Group  
Office of Soviet Analysis

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**Gorbachev's Economic Agenda: Promises,  
Potentials, and Pitfalls** [redacted]  
**Intelligence Assessment**

This paper was prepared by [redacted] Office  
of Soviet Analysis, with contributions by SOVA analysts [redacted]

[redacted] Comments and  
queries are welcome and may be directed to the Chief, Economic Performance  
Division, SOVA, [redacted]

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Gorbachev's Economic Agenda: Promises,  
Potentials, and Pitfalls [redacted]

Key Judgments

Information available as of 6 September 1985 was used in this paper.

Since coming to power Mikhail Gorbachev has set in motion the most aggressive economic agenda since Khrushchev. The key elements are:

- o A reallocation of investment resources aimed at accelerating S&T and modernizing the country's stock of plant and equipment.
- o A revitalization of management and planning to rid the Soviet bureaucracy of incompetence and petty tutelege and put more operational control of enterprises in the hands of managers on the scene.
- o A renewal of Andropov's anticorruption and discipline campaigns, coupled with a new temperance campaign, to increase and perhaps improve worker effort.

All of Gorbachev's initiatives are aimed at raising productivity and efficiency throughout the economy by matching more and better equipment with a motivated work force and enlightened managerial cadre. He has put his finger on the very tasks that the economy has never done well and has become progressively less able to do as it has grown in size and complexity. [redacted]

Although Soviet economic performance has improved in recent years from the low levels of 1979-82, Gorbachev still faces an economy that cannot simultaneously maintain rapid growth in

defense spending, satisfy demand for greater quantity and variety of consumer goods and services, invest the amounts required for economic modernization and expansion, and continue to support client state economies. Gorbachev, in our view, has a clear understanding of these limitations; he is obviously extremely impatient that they be addressed now.

Soviet officialdom probably was caught off guard by Gorbachev's sweeping condemnation of past economic policies, particularly considering the recent economic rebound, and were surprised that he apparently was ready to take action so early in his tenure. Despite the urgency of his rhetoric, he seems aware that implementing his programs too rapidly carries substantial economic and political risks:

- o He has prepared the party and bureaucracy for substantial change by bluntly laying out the need for management reorganization and renewal, but has yet to provide specific details on controversial issues that would provide a basis for organized resistance.
- o He has moved aggressively to replace old-line economic managers, but has yet to replace Council of Ministers Chairman Tikhonov, regarded by most Soviets as a major political obstacle to economic change.
- o He has talked about the potential need for "profound" changes in the area of economic reform, while strongly supporting the need to maintain central control. (C NF)

Program specifics will be announced by next February along, we judge, with Tikhonov's replacement. It is unlikely that they

will contain any radical departures from what Gorbachev has already announced. At present his game plan seems to be a realistic assessment of what can be done in the short run while planning and developing a consensus for more radical change over the long haul if he deems that it is needed. [redacted]

Success with the initial stages of Gorbachev's program could provide a relatively immediate growth dividend that could be used to bolster worker morale and underwrite future growth. How much economic improvement will occur and how long it can be sustained, however, is very much an open question. Modernization is slow by nature in any economic system and in the Soviet case will run into the perennial conflict between meeting output goals and reequipping enterprises with new equipment and technology. Streamlining the bureaucracy will be resisted by countless officials whose jobs and perquisites are threatened, and a new set of incentives must be instituted to motivate a new type of Soviet manager. Discipline campaigns can go only so far in energizing a cynical work force. [redacted]

Gorbachev will be hard pressed to find the resources necessary to underwrite his modernization goals. The economic dividend from management reforms and the discipline campaign will not substantially relieve the basic scarcity of resources nor obviate the need for fundamental systemic change:

- o Improving worker morale and management effectiveness will require an effective incentive system and a greater availability of high-quality consumer goods at a time when the investment sector will be oriented toward

producer goods and new defense programs will be coming on line. In fact, Gorbachev's investment program implies a potential decline of some 60 percent in the investment increment going to consumer-oriented sectors.

- o The regime's plan to hold energy's share of investment constant comes at a time when demand for energy will grow and the cost of offsetting declining oil production will be rapidly rising. If the requisite investment is not forthcoming, the current decline in oil production could become precipitous.
- o The increased managerial independence necessary to spur effective technological development and utilization is inconsistent with a centrally planned pricing and allocation system, leading to the likelihood of management disillusionment and subsequent reversion to the very methods that have led to waste, fraud, and mismanagement for years. [redacted]

Gorbachev could employ various options to address these issues but all contain serious pitfalls. East European countries could be ordered to shoulder a larger part of the economic burden, including increased exports of equipment to the USSR, but own deep economic problems increase the likelihood of confrontation between Moscow and its allies. A drive to increase imports of Western technology would come at a time when the prospects for expanding hard currency exports, particularly oil, look dim. A shift of resources from defense to civilian uses could have considerable positive impact over the long run, but



even the suggestion of such a shift might damage Gorbachev's relations with the military and risk deep divisions within the Politburo. Finally, major economic reforms to promote managerial effectiveness would encounter strong resistance on political and ideological grounds, particularly since they threaten the institutional prerogatives and thus the privileged position of the Soviet elite. [REDACTED]

Indications that Gorbachev has decided on and gained consensus for more radical changes could include:

- o New, dramatic initiatives to reach an accord at Geneva and concrete proposals for reduced tensions at the November meeting between the US President and the General Secretary, which might signal a willingness and desire to reduce the Soviet resource commitment to defense and create an atmosphere for expanded commerce with the West.
- o Select legalization of private-sector activity, particularly in regard to consumer services, which would indicate a willingness to confront past economic orthodoxy in order to improve consumer welfare and thereby economic performance.
- o Breaking the monopoly of the foreign trade apparatus, which would signal an increased reliance on managerial independence at some cost to centralized control.

Continued reliance on marginal tinkering despite clear indications that the plan for economic revitalization is faltering would indicate that Gorbachev, like Brezhnev before him, has succumbed to a politically expedient but economically ineffective approach. [redacted]

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Gorbachev's Economic Agenda: Promises, Potentials,  
and Pitfalls [redacted]

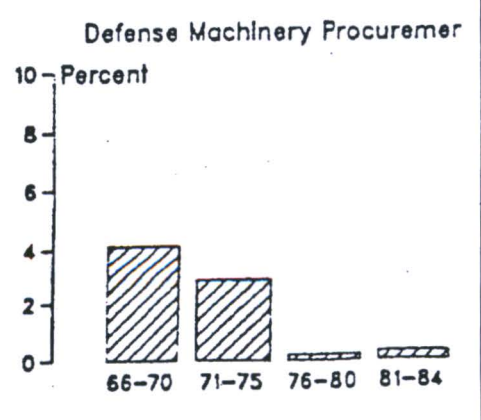
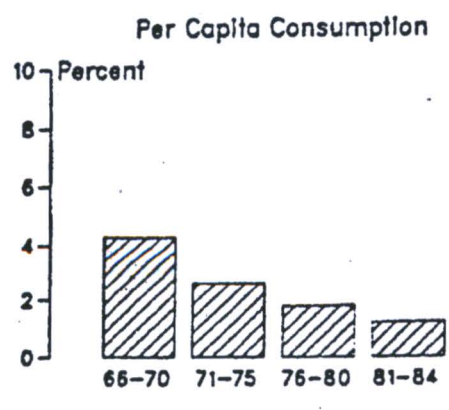
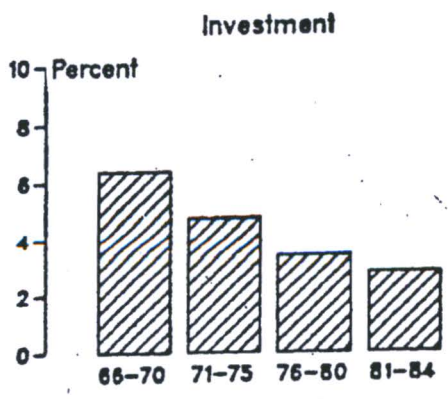
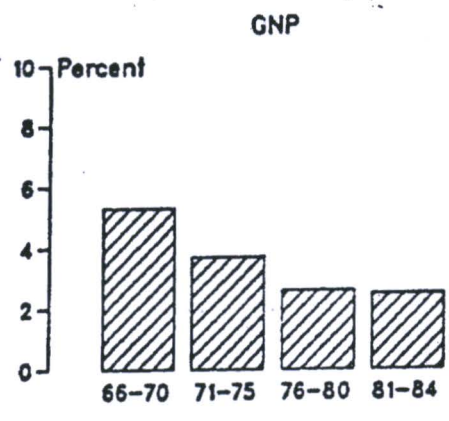
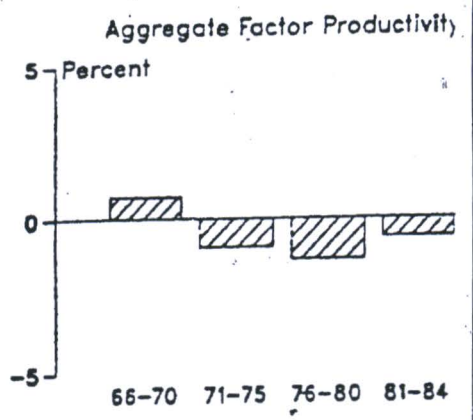
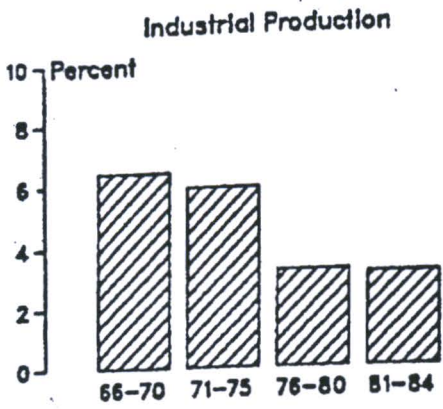
Gorbachev's Economic Heritage

In March 1985 Mikhail Gorbachev inherited a technologically backward economy that had experienced a decade of slowing growth punctuated by harvest failures, industrial bottlenecks, labor and energy shortages, low productivity, and declining efficiency of investment (see figure 1). The simple growth formula that had propelled the USSR to a major world power in the postwar era--ever-increasing inputs of labor and capital resources--by the mid-1970s was no longer effective. [redacted]

During the 1950s this growth formula resulted in rapid gains in output because of the very low level of GNP in the early postwar period and the relatively high efficiency of new fixed investment in reconstruction and repair of war damage. As the USSR moved out of the reconstruction phase in the 1960s, however, highly effective investment projects became more difficult to identify, and centralized planning and management of a burgeoning economy became more cumbersome and inefficient. Unable to improve their ability to deal with an increasingly complex economy, Soviet leaders had little choice but to sustain the large commitment of resources to investment if economic growth was to continue apace. In addition to maintaining larger annual flows of investment, Soviet planners have swelled the expansion of plant and equipment by:

~~Confidential~~

Figure 1  
USSR: Key Economic Indicators,  
Average Annual Growth Rates



- o Holding retirement of equipment to a minimum.
- o Prolonging the service lives of technologically obsolete capital through repeated extensive repairs.
- o Continually expanding new construction projects, thus channeling the bulk of investment into buildings and structures rather than into new equipment, the principal carrier of new technology. [REDACTED]

Sustaining a high level of increase in total capital assets by these methods enabled the Soviets to achieve high rates of growth and to support an enormous defense establishment, but also impeded technological progress and productivity gains. Efforts to increase the quality and quantity of output and make better use of available resources in the economy continued to be frustrated by a backward technological base, inflexible production processes, and, perhaps most important, a cumbersome and inefficient system of planning and management. [REDACTED]

These problems were well understood by Gorbachev's predecessors. Rhetorically at least, Brezhnev recognized that in the future the economic system would have to operate differently if it was to meet the needs of the Soviet polity and society. Various Central Committee and Council of Ministers' decrees were promulgated to address these problems, but Brezhnev in his waning years lacked the energy and political will to follow through on his diagnosis. As a result of this administrative lethargy and the endemic nature of many of the problems facing the Soviet economy, Brezhnev's successors were saddled with:

- o A technologically antiquated industrial base and a burdensome defense sector that has systematically siphoned off high-quality resources needed for economic revitalization.
- o An energy sector beset by stagnation and decline in production of its major fuel--oil--and a 30-year pattern of energy use that inhibits the rapid transition from oil to other fuels.
- o A level of technology that generally lags that of the West. Even in military applications the Soviets have encountered technological problems in recent years that are sharply driving up costs and delaying new sophisticated weapon systems, thus creating a further drain on available resources.
- o An inefficient farm sector that despite large investments still employs one-fifth of the Soviet labor force, is bereft of an adequate storage and transportation system, and is unable to produce grain and meat in sufficient quantities to meet rising domestic demand.
- o A hidebound bureaucracy whose rigidities contribute to irrational investment decisions, retard scientific-technical innovation, and encourage high costs and massive waste of resources. [REDACTED]

Moreover, by the end of the Brezhnev era a growing malaise had spread through much of the work force, not only because gains in living standards had slowed, but also because workers believed that the system was incapable of bringing any meaningful

improvement. This attitude--reflected in the rise of alcoholism and related health problems--exacerbated the corruption and inefficiency that had permeated the Soviet economic bureaucracy from farmhand to factory worker to the ministerial superstructure. Workers and managers alike spent increasing amounts of time and effort trying to insulate themselves--often through illegal means--from the effects of shortages in both the home and factory. This reduced productivity on the job and promoted greater shortages of goods and services throughout the economy, especially for individuals and enterprises with little or no "special access." [redacted]

While Andropov's ascension to power gave a glimmer of hope for change, his tenure was too short and he had too little personal energy to reverse the decades of abuse and mismanagement tolerated by his predecessors. Anticorruption and discipline campaigns stimulated some improvement in economic growth but made only minor ripples across the surface of the deeply entrenched system of planning and management. Chernenko, for his part, paid little more than lipservice to these initiatives. [redacted]



The Gorbachev Agenda

When Gorbachev came to power, many Soviet officials--except those of the old guard, who felt threatened--had high expectations for a vigorous revival of Andropov's anticorruption and discipline programs, as well as a stepped-up pace of personnel change. But, with economic growth having recently accelerated from the unusually slow rates of 1979-82, many probably felt that he would avoid sharp changes in resource allocations. [redacted]

Gorbachev, however, has taken little solace in recent economic improvement; by all indications he realizes that long-term gains will require solving endemic problems that for the last decade have prevented the economy from simultaneously sustaining:

- o Continued rapid growth in defense spending that had proceeded unabated since the mid-1960s.
- o Greater quantity and variety of consumer goods and services demanded by an increasingly discriminating population.
- o Rapid growth in investment goods for economic modernization and expansion.
- o Increased support for client states whose own economies are coming under increasing strain. [redacted]

In little more than five months, Gorbachev has demonstrated that he is the most aggressive and activist Soviet leader since Khrushchev. He is taking power by virtue of his strong, assertive personality and by aggressively inserting his own cadre

into key positions. Moving forcefully to place his personal stamp on economic policy, Gorbachev has repeatedly told managers that they must change the way they do business or "get out of the way":

- o He has assailed managers by name for lack of innovation, laziness, and poor management and has strongly implied that they will be removed. He has attacked the complacent attitude toward corruption within the party bureaucracy and called for promotion of younger and more competent officials at all levels. While such rhetoric is not new in itself, he has already underscored his intention to back up his tough rhetoric with dismissals (see inset "Gorbachev's Hit List").
- o He has returned for revision the centerpiece of the planning system's raison-d'etre, the draft five-year plan, demanding specific changes--so far unspecified--in the planned pattern of resource allocations for 1986-90. [redacted]

Gorbachev is determined to deal with the economy's underlying problems. He has thrown down the gauntlet on issues as controversial as the allocation of investment, broad gauge management reform, and a complete purging of incompetent and corrupt officials from the system. While the details of his economic game plan probably will await the new draft of the 12th Five-Year Plan (1986-90) to be announced at the 27th Party Congress in February 1986, the broad features of his program are already emerging. All are aimed at raising productivity and

## Boxed Text 1

Gorbachev's Hit List

Gorbachev has made it clear he intends to overcome entrenched resistance to his domestic programs by cleaning house:

- o He has named eight new economic ministers since coming to power, including those in charge of oil and steel production.
- o He has replaced three Central Committee department chiefs who oversee the machine-building, construction, and trade and services sectors. [redacted]

In addition, he has supervised an extensive turnover among regional party first secretaries--who play a critical role in implementing economic policies, are spokesmen for local economic interests, and act as facilitators in overcoming economic bottlenecks. Already over 20 such officials have been appointed, nearly one a week since Gorbachev came to power, and more changes are likely during the party elections that will precede next February's party congress. [redacted]

Gorbachev probably also has other high-level changes in mind:

- o Reports persist that he intends to retire Premier Tikhonov at the congress or perhaps even sooner. Some Soviet officials claim that Gorbachev might take the job himself, while others indicate that he will give it to a close ally like RSFSR Premier Vorotnikov or Secretary Ryzhkov.
- o Several Soviets have strongly implied that State Planning Committee Chairman Baybakov is on the hit list, and Gorbachev indirectly criticized him in June for undermining an economic experiment being implemented in major industrial sectors.
- o Gorbachev may also want to go after the remaining dozen or so top economic officials who have been around since the beginning of the Brezhnev era. [redacted]

He has already shown his intention to reassert party control over the vast economic bureaucracy, which had grown accustomed to Brezhnev's benign neglect. The firings so far have probably sent an unmistakable message to economic officials that they must toe the mark or face disgrace and forced retirement. [redacted]

End Boxed Text

efficiency throughout the economy--something the system has never done very well and has become progressively less able to do as it has grown in size and complexity. He has called for annual growth in national income of at least 4 percent. If this plan were achieved, growth in real GNP as measured in the West would also amount to an increase of about 4 percent per year--a healthy increase above the good performance of 1983-84 (see inset "Measuring Soviet Economic Growth"). He plans to achieve this goal by pursuing an ambitious strategy for modernizing the economy's stock of plant and equipment and by raising the level of effort and sense of personal responsibility of managers and workers alike. [redacted]

Gorbachev personally has provided a pointed example of how critical a substantial improvement in productivity and efficiency is to his entire program. In his June speech to a special science and technology (S&T) conference, the General Secretary indicated that an additional 8-10 million people in the labor force and an average annual growth in investment of 5 1/2 to 7 percent during every five-year period would be required to achieve his goal of 4-percent annual growth in national income in the absence of a substantial increase in the combined productivity of land, labor, and capital. Both he and his audience probably were aware that less than 4 million people will be added to the labor force in 1986-90 and a 5 1/2 to 7 percent increase in the rate of growth of investment would put severe strains on the other resource claimants--defense and consumption. They also probably recognized that productivity

## Boxed Text #2

Measuring Soviet Economic Growth

The principal conceptual difference between GNP and Soviet reported national income is the latter's exclusion of (1) most personal services as well as services provided by the government (for example, health, education, housing, personal transportation and communications, recreation and personal care, government administration, credit and insurance, research and development, and military personnel costs) and (2) depreciation on fixed capital. Because Soviet growth statistics measuring achieved national income overstate performance by including new product price inflation, a 4-percent planned increase in national income, if fulfilled, would be equivalent to about 5-percent growth in achieved national income. Moreover, growth in achieved national income has been about one percentage point higher than growth in GNP as measured in the West. Over the past 20 years this has resulted in an annual exaggeration of economic performance by about one percentage point. Therefore, a 4-percent annual growth in planned national income, if achieved, would amount to real GNP growth also at 4 percent. [redacted]

End Boxed Text

increases will not be easy--growth in combined productivity of land, labor, and capital has been consistently negative for the last decade. [redacted]

To help address these issues Gorbachev has appointed several economic advisors who have long advocated a major overhaul of the economic system: substantial increases in investment in machine building, changes in the incentive structure, a greater role for private activity, and more devolution of authority and personal responsibility to enterprise managers (see inset "Reform-Minded Economist Advising Gorbachev"). The ascent of such reform-minded economic advisers to policy-level positions is a signal of Gorbachev's commitment to finding ways to make the system work better. At present these include accelerating S&T progress, restructuring investment, implementing management reforms, and tightening discipline. [redacted]

Accelerating S&T Progress.

Gorbachev views a modern, efficient industrial base as crucial to the success of his economic program. A special conference was held in June to develop a comprehensive strategy for accelerating technological progress. In addressing the conference, Gorbachev focused on the need for the rapid introduction of new production technology, insisting that the Soviet Union must launch a revolutionary program to reequip its factories and farms with the most up-to-date machinery. He recognizes that acceleration of S&T progress depends critically on the success of other elements of his strategy. As he pointed out at the conference:

## Boxed Text #3

Reform-Minded Economist Advising Gorbachev

The prominent and controversial economist Abel Aganbegyan has become an influential informal adviser to General Secretary Gorbachev. The longtime director of an economic institute in Novosibirsk, he recently moved to Moscow to head a committee of the Academy of Sciences. Aganbegyan has a history of involvement in controversy with conservatives over his criticism of the workings of the economic system. Several changes he has proposed, which include accelerating the modernization of industry through retooling and a streamlining of the Moscow-based bureaucracy, have become major themes in Gorbachev's recent speeches on the economy. [redacted]

Aganbegyan's new status is another indication of Gorbachev's intention to shake up the economic establishment. At age 52, Aganbegyan's ties with Gorbachev date back to Moscow University days in the 1950s. As an adviser to Gorbachev, he is likely to reinforce the party chief's determination to look for new approaches to economic planning and management. [redacted]

There have also been indications that Tatyana Zaslavskaya, a well-known sociologist and close colleague of Aganbegyan, may now have a stronger voice in the academic community, if not an advisory role in the government. In a recent interview in Izvestiya, she reiterated arguments originally made about the inappropriateness and ineffectiveness of the centralized economic system in a confidential document that was leaked to the Western press in April 1983. [redacted]

End Boxed Text

- o In carrying out the S&T revolution the commanding key role belongs to machine building....First and foremost machine building itself must be reconstructed....In the years 1986-90, capital investment for the civilian machine-building ministries should be increased by 80-100 percent.
- o The acceleration of S&T progress insistently demands a profound reorganization of the system of planning and management....Without this, everything we are talking about today may remain but a fond hope. [redacted]

Restructuring Investment.

Gorbachev recognizes that his call for accelerated technological progress is only possible with a major alteration in investment priorities. Currently, 30 to 40 percent of all Soviet equipment has been in operation for more than 15 to 20 years. By 1990, Gorbachev declared, one-third of the fixed capital stock--including one-half of all machinery--must be "new." He urged that special priority be given to the "development and introduction of fundamentally new systems of machines and technologies" and called for a 50-percent increase in expenditures for retooling existing enterprises financed, in part, by a cutback in new construction. [redacted]

In his June address Gorbachev accused the State Planning Committee (Gosplan) of paying "verbal tribute" to the role of civilian machine building while continuing to starve it of resources and suggested that his call for nearly doubling investments for this sector in the 1986-90 period could be



achieved by the partial redistribution of capital investments from the industries that use the machines. This "suggestion" was presaged in a particularly forceful statement in a speech to an ideological conference last December, where Gorbachev insisted that the longstanding practice of allocating economic branches the same proportions of new investment from one plan to another must be "changed decisively." [redacted]

In this context, Gorbachev hinted that the need to supply additional resources to machine building might affect the priority status of two of the biggest claimants on investment resources, energy and the agro-industrial complex:

- o He suggested that the share of investment in energy could be "stabilized" by giving greater attention to conservation.
- o He indicated that the present level of investment in the agro-industrial complex is adequate and that it is the return on this investment which continues to be unsatisfactory.

He has not addressed how other major claimants on investment-- such as defense--will fare. [redacted]

#### Reorganizing Management and Planning.

Gorbachev has been particularly critical of intermediate management bodies that choke off initiative and has hinted that they should be streamlined or eliminated. His aim is to rid the system of some of the massive bureaucratic apparatus whose petty tutelage in implementing Central Committee decisions defeats the purpose of the decisions. [redacted]

The level of specificity in his June speech in Dnepropetrovsk suggested that plans for such a reorganization have now reached an advanced stage and will include the creation of superministerial bodies, starting with agro-industrial and machine-building sectors. His speeches also suggest that these superministries will be restricted to "strategic" planning and leave operational control of enterprises in the hands of the managers on the scene. [redacted]

Gorbachev's first move to give greater operational independence to enterprise managers was to expand the economic experiment, begun in January 1984, giving enterprises greater control over investment and wage funds and making fulfillment of contractual sales obligations the prime indicator for evaluating enterprise performance (see inset "Managerial Initiatives"). He has also implemented a far-reaching experiment at the Tolyatti Automotive Plant that increases the plant's authority for its own management and for making purchase and sales agreements with foreign firms, without the direct participation of the ministries or foreign trade associations. [redacted]

Gorbachev has also endorsed Brezhnev's 1982 Food Program, which, as party secretary responsible for agriculture, he helped formulate. In this connection he has supported increasing the authority of the regional agricultural production associations (RAPOs)--an innovative form of administration that cuts across ministerial lines and concentrates authority at the local level for coordinating the activities of farms, agricultural service agencies, and processing enterprises in a given district. [redacted]

Boxed Text #4

Managerial Initiatives

The Soviets have announced a major expansion of the experiment in industrial management that began on 1 January 1984 in five all-union and republic-level ministries and was extended this year to 20 additional ministries. The experiment will extend to all machine-building ministries and many consumer-related industries in 1986 and to all of industry in 1987. [redacted]

The experiment's aim is to improve the central planning and management system by reducing the number of success indicators used to evaluate enterprise performance and by slightly increasing the enterprise's limited control over wage and investment funds. The decree to expand the experiment presents measures to improve product quality and further increase enterprise control over plant operations:

- o Enterprises of the machine-building sector producing products judged to be of highest quality will be able to increase their earnings by raising prices up to 30 percent. Enterprises producing lower quality goods will have to cut prices by up to 30 percent and then reimburse the state for lost revenue with money taken from their worker and manager bonus funds.
- o Enterprises will have increased authority to spend limited amounts of investment funds at their own discretion for industrial renovation and for construction of housing or other consumer-related undertakings. The state planning and supply organs have been instructed to give such projects priority.
- o Penalties for delays, nondelivery, or delivery of inferior goods will be increased, and rewards for timely provision of satisfactory products will be implemented.

[redacted]

Moscow has also announced a managerial reorganization program--described as a model for the rest of the economy--for the Ministry of Instrument Manufacturing (Minpribor). The program includes:

- o Eliminating the management level that lies between the enterprise and the ministry.
- o Creating additional scientific production associations to spur R&D and prototype production. [redacted]

End Boxed Text

Tightening Economic Discipline.

Gorbachev is banking on improved worker effort to immediately bolster economic growth. Because he needs the support of both managers and workers, he has appealed directly to them to buy into his program. He has pledged to increase both the material rewards for good performance and the penalties for violations of economic discipline. [REDACTED]

Much of Gorbachev's campaign for improved worker effort, however, will rest on the more vigorous implementation of programs initiated before his tenure. These include:

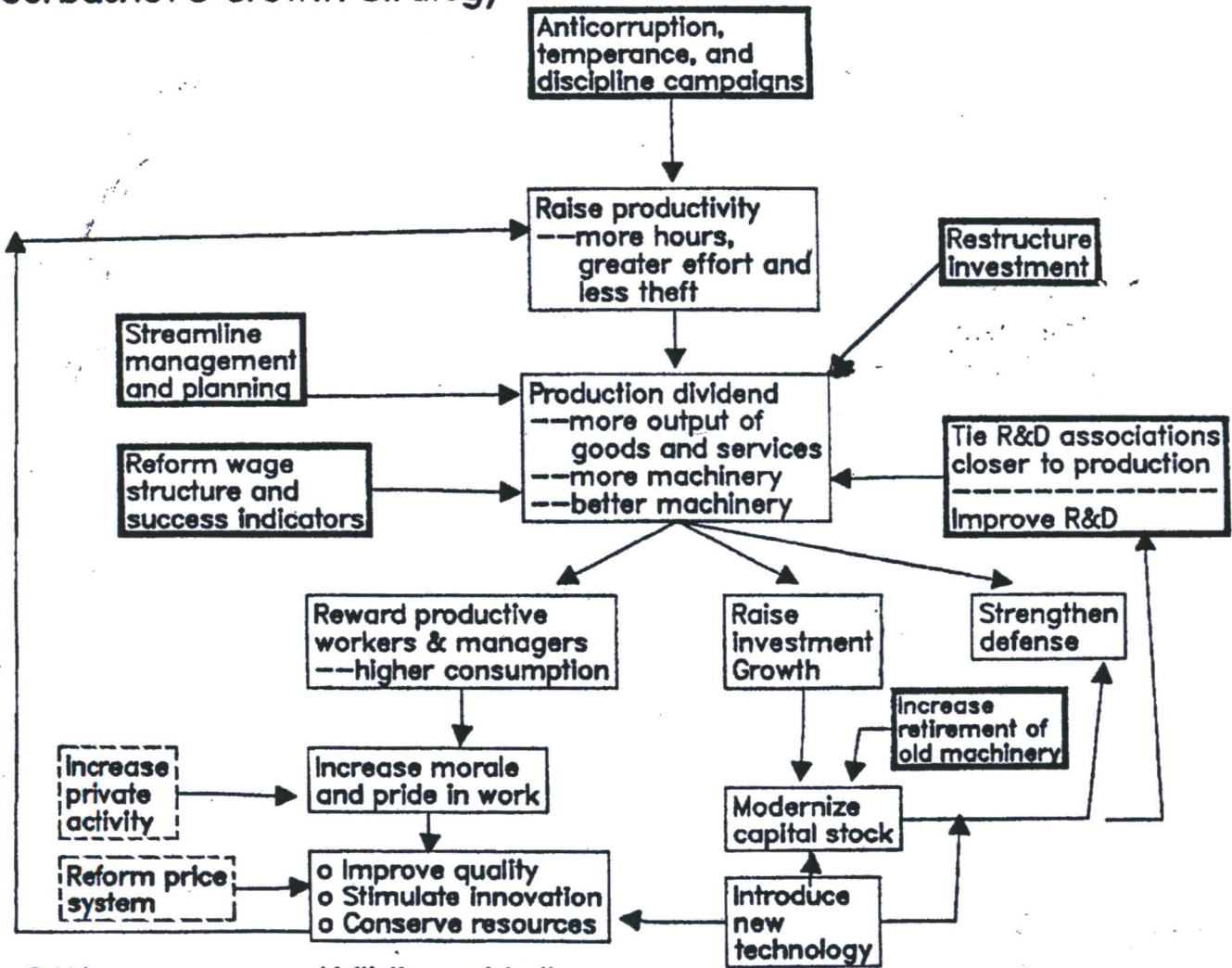
- o Improving labor productivity by reviving the discipline campaign, which Andropov initiated but which flagged somewhat under Chernenko. Gorbachev has already initiated a vigorous antialcoholism campaign which is serving as a daily reminder of the new leadership's seriousness and intensity in attacking problems of both a social and economic nature.
- o Tying workers' earnings more closely to their output, through greater differentiation of wages and expanded use of contract brigades--small groups of workers whose earnings depend on fulfillment of contractual obligations to management. [REDACTED]

An Integrated Approach

On balance, Gorbachev's game plan reflects an appreciation of what we and many Soviets believe to be many of the economy's fundamental problems. Moreover, he recognizes that all elements of his program cannot be implemented immediately and simultaneously across the economy. The centerpiece of his modernization strategy, replacing the economy's stock of machinery and equipment and improving management techniques, will require years of effort. Nevertheless Gorbachev probably feels that unless he starts now in earnest and maintains constant pressure on his economic managers, the future will continue to be hostage to indecision and inaction. [redacted]

Gorbachev, in essence, is proposing an integrated approach for the resurgence of economic growth (see figure 2). Anti-corruption and discipline campaigns are aimed at reducing worker apathy, which, together with the attendant massive waste and theft of resources, have held down growth in productivity throughout the economy. Some success here, along with some redirection of investment resources, fewer layers of bureaucratic tutelage, and a more equitable system of rewarding productive workers and managers, is geared to provide a growth dividend that can be used both to bolster worker morale (via more and better consumer goods and services) and to underwrite further growth. Gorbachev appears to be counting heavily on a synergistic effect among the several parts of his program to provide even greater dividends in the years ahead, returning the economy to an upward

Figure 2  
Gorbachev's Growth Strategy



Bold boxes are announced initiatives or intentions  
Broken boxes are potential future initiatives

growth path and, perhaps, providing him with justification for future fundamental changes in the centralized control of the economy, if needed. [redacted]

Gorbachev's strategy is not without substantial economic and political risk, particularly as he is seeking to change an economy that has recently been on the upswing. In public statements, Gorbachev has so far focused on the general themes of his economic program rather than on specific measures that could galvanize opposition. He may well have decided to refrain from translating vague expressions of support for controversial measures into specific proposals until he has more fully formulated his plans--in part by encouraging public dialogue and selectively testing some options--and consolidated his political strength. He has not openly challenged the legitimacy of centralized economic control, including such fundamental obstacles to the success of his program as the arbitrary nature of Soviet prices which prevents planners from making economically rational decisions, or the lack of sufficient consumer input into production decisions. A Soviet political commentator privately characterized Gorbachev's current approach as one of first adopting noncontroversial economic measures while simultaneously working on a long-range and more far-reaching program. Gorbachev may be refraining from more radical measures because he hopes that the steps he has already proposed will be sufficient to remedy the economy's ills. [redacted]

Whether he will be able to achieve his economic goals in the absence of additional, bolder changes--moves toward market

socialism, for example--is problematical. There have been hints in Gorbachev's past and recent speeches and in the statements of some knowledgeable Soviet officials that he may eventually be willing to make such changes. In his Lenin Day address in April 1983, for example, Gorbachev stressed the importance of greater reliance on prices as an economic lever. He returned to this theme in his June 1985 address to the S&T conference, calling for a more decisive shift from administrative to economic methods of regulating the economy. In the same address he also called for an end to "the domination of the consumer by the producer." [redacted]

[redacted]

There is also growing evidence that Gorbachev favors an expanded role for private initiative as a way of alleviating consumer problems without much additional investment or change in the way the socialized sector is organized and managed. In the past Gorbachev has been a staunch supporter of expanding production on private agricultural plots, and in his speech to the Central Committee plenum in April he twice referred to the contribution that the private farming sector can make to improving the quality of life. In May he returned to this subject in a speech in Leningrad and expressed disagreement with the Politburo's recent handling of the issue. He contrasted the Politburo decision to earmark land for an additional 1 million private market gardens with Soviet citizens' requests for some 15 million new plots. "Mathematically," he noted with evident sarcasm, "our approach to this problem is fundamentally weak."

[redacted]



Gorbachev's remarks in Leningrad also lend credibility to earlier reports that he favors the more controversial policy of allowing a greater role for private initiative in the service sector. He called for a "more realistic evaluation" of the major role "moonlighters" currently play in providing such services as home repairs and seemed to suggest that the state should not just tolerate such activity but should actively support it. Materials used, he said, are generally stolen and "come from the state anyway." In this context, Izvestiya acknowledged in August that illegal private services are too widespread to stamp out and called for their legalization under contract to state enterprises. [redacted]

Favorable Short-Term Outlook

Gorbachev needs some near-term success to sustain his early momentum for change, particularly since he is seeking major changes in an economy whose performance has improved in recent years. To this end he made it clear at a recent Central Committee meeting that the 1986-90 Five-Year Plan must get off to a fast start. He should be able to capitalize on the aura of change and rejuvenation he has created in the early months of his regime to elicit some genuine increase in effort by at least part of the work force. Moreover, the discipline campaign, which was evidently an important factor in the economic upswing during Andropov's tenure, could again have a favorable impact on economic performance (see inset "Potential Gains From Increased Discipline"). This, together with a new set of Gorbachev appointees--who probably have the energy and determination to use the carrots and sticks available to them with greater consistency than their predecessors--could promote at least some short-run gains in economic performance. Although Gorbachev is gambling heavily on the impact of his early initiatives--a risky approach given that previous attempts to implement similar changes have been frustrated by entrenched bureaucratic interests--his prospects for near-term success should not be underestimated. [redacted]

[redacted] Gorbachev's program also may get a short-run boost from the upsurge in machinery production that occurred in 1983-84 and a particularly favorable harvest this year. Growth in production

Boxed Text #5

Potential Gains From Increased Discipline

According to Abel Aganbegyan, writing in the Soviet labor newspaper Trud in 1981, one-half of the decline in growth of labor productivity that occurred in 1976-80 compared with 1971-75 was due to "people's attitudes toward their work." Andropov recovered some of the earlier momentum with the initiation of a tough discipline campaign in 1982; labor productivity rose by 3.2 percent in industry in 1983 as slackers were forced to actually be on the job during the time they were counted as being there. Gorbachev may be able to recoup even more of the momentum with his revival of the discipline campaign and his strong stand on temperance. Indeed, the reduction in absenteeism due to drunkenness may have a potential for achieving a greater increase in actual hours worked than was achieved under Andropov. Moreover, Gorbachev's direct appeal to workers, together with his other initiatives, may elicit a more responsible effort--at least in the short run--from many who might otherwise merely put in their time. [redacted]

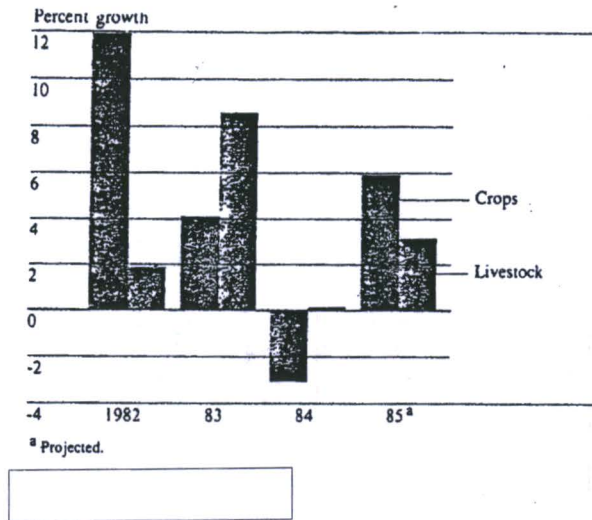
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of machinery picked up sharply in 1983-84, registering annual increases better than 5 percent, after averaging about 3.5 percent per year in 1981-82. The added machinery could help raise growth in investment enough to get Gorbachev's modernization program moving. Moreover, the outlook is for a substantial increase in crop production and livestock products this year after a dismal performance by the farm sector in 1984 (see figure 3). A better harvest this year would help hold down queues for food, provide workers fewer excuses to be away from their jobs during working hours, improve consumer morale, and reduce hard currency outlays for grain.<sup>1</sup>

<sup>1</sup> Moscow also should enjoy the benefits of a buyers' market this year in the international grain trade. World supplies are expected to continue to be abundant, largely because of a bumper crop in the United States and reduced Soviet demand for grain.

Figure 3

USSR: Agricultural Performance



### Long-Term Uncertainty

How much economic improvement will occur and how long it can be sustained, however, is very much an open question. Short-run gains alone will not ensure success. For longer term aspects of the program to succeed, many things must go right for Gorbachev-- some he can control, others he cannot. Moreover, the synergism he appears to count on may not develop, especially in the short run. For example, he hopes to pair improved worker initiative with a modernized industrial base. But this will require redirecting investment resources, which, in turn, could lead to bottlenecks in industries whose investment allocations are squeezed. Any campaign-style modernization program could create imbalances in new capacity and encounter lengthy delays in achieving results. [redacted]

Moreover, if plants are forced to shut down production lines to permit renovation, short-run performance indicators will be adversely affected. This, in turn, might provide ammunition for Gorbachev's opponents, who could contrast 1983-84 industrial production gains with a poor output record of newly renovated enterprises as evidence of harebrained or misguided programs. In the long run, each of Gorbachev's initiatives faces particularly challenging problems that will take more than strong rhetoric and willing hands to overcome. [redacted]

### Problems Facing Industrial Modernization

Renovation. Renovating existing enterprises rather than building new ones is a key element of Gorbachev's modernization strategy. He is likely to find, however, that this approach is

fraught with difficulty. Plans to concentrate investment on renovation have been touted by Soviet leaders for more than 15 years but have never been effectively implemented. The strategy has been resisted by enterprise managers because the downtime required to replace old machinery, as well as the uncertainty inherent in new production processes, threatens their ability to achieve short-term performance goals. Maintenance and support for new processes--particularly highly automated processes--are essential, but problematical in the Soviet economy. It has always been safer from a manager's perspective to build a new production plant or add to an existing plant than to renovate an operating facility. . [redacted]

Moreover, the renovation approach is not effective for large areas of the country. According to Soviet literature, many of the existing industrial facilities are so decrepit that renovation--if possible at all--will be extremely costly and time consuming. Modern equipment requires facilities that have a broad assortment of heating and ventilation features. Most old buildings in the USSR cannot be easily converted to accomodate such equipment. This is especially relevant to the thickly populated regions of the European USSR, the Urals, and the Donetsk-Pridnepr' Basins--the old industrial core of the Russian empire, which accounts for about 75 percent of total Soviet industrial production. [redacted]

In addition, the emphasis on renovation could exacerbate the ever-present tension in resource supply throughout the economy.

For example, as production lines are shut down for renovation, the lost production will have to be made up by other plants if supply bottlenecks are to be avoided. Too much simultaneous renovation could lead to shortages of key industrial materials. Indeed, many of these materials are already stretched so thinly that even small shortfalls are magnified as their impact ripples throughout the system. [REDACTED]

Machinery Production. Gorbachev plans to underwrite industrial renovation by a rapid expansion in output of high-quality equipment. To achieve his announced goal of 50 percent "new machinery" by 1990, he must manage an acceleration in the annual output of producer durables to rates unmatched since the early 1970s. Additionally, the machines must be tailored to meet the unique needs of the wide variety of plants being remodeled--a difficult task for an industry accustomed to manufacturing large lots of a small variety of equipment for use in plants being constructed under highly standardized designs. Indeed, the increased pressure on Soviet machine builders to boost output probably will reinforce the tendency to reproduce the same pattern of output that has prevailed for years, only faster and--unless major gains are made in quality control--perhaps in a more slipshod manner. [REDACTED]

Advanced Technology. In addition to rapidly expanding machine-building capacity, Gorbachev must turn around a system characterized by its relative failure to create and use technically advanced equipment. [REDACTED]



recent Soviet assessments by industry and foreign trade specialists conclude that the quality of Soviet machinery is well below world standards.<sup>2</sup> The geographic and bureaucratic separation of research organizations from production enterprises impedes introduction of new technology into the production process. Insufficient funding of research--most noticeably in the machine tool industries and in the ministries responsible for producing agricultural machinery--contributes to poor performance. Finally, the Soviet system of bonuses--with its inherent bias toward volume of production and apparent rather than real quality change--is a de facto barrier to the production of better capital equipment. According to one high-ranking Soviet official, only 15 percent of wage and performance bonuses are keyed to the introduction of new technology and equipment.

[REDACTED]

Many Soviet officials probably view Gorbachev's modernization strategy with pessimism. A "Business Club" roundtable discussion that Pravda held recently, for instance, pointed to major difficulties in implementing the ongoing renovation program in the Ukrainian Republic (home for about 20 percent of Soviet industry). The program--developed along the same lines as Gorbachev's strategy--is failing, it was concluded, because of:

<sup>2</sup> - Evidence also suggests that average leadtimes for using new technology are much longer in the USSR than in the West. Data show that about 50 percent of US and West German inventions are implemented in about one year compared with three years for Soviet inventions. At the end of two years, the US implements about 66 percent, West Germany 64 percent, and the USSR 23 percent. [REDACTED]

- o Perverse incentives that discourage construction ministries from undertaking reconstruction.
- o Inadequate funding for installing equipment.
- o Lack of qualified workers.
- o The inability of the machinery industry to keep pace with the increased demand for more efficient, specialized equipment needed for renovation. [redacted]

While Gorbachev may ultimately be able to overcome some managerial biases by changing success criteria (which he has not yet done) and appointing new managers, he cannot overcome the economic realities of outdated plants and limited investment resources. In the final analysis, no matter how hard Gorbachev pushes, modernization will occur only slowly and must come from new construction as well as renovation. Substantial results can not be expected for several years. Even now, signs are emerging that some aspects of Gorbachev's early initiatives are backfiring and inhibiting rather than stimulating high-quality production (see inset "Reforms To Spur Innovation Backfire"). Part of the problem is the intricate layering of the managerial bureaucracy, which Gorbachev is still a long way from purging. Decades of bureaucratic development have created a labyrinth of buck-passing and indifference that will probably take years and thousands of key personnel changes to rectify. [redacted]

Revitalizing Management

Streamlining the bureaucracy, refurbishing its ranks with his allies, and developing better management skills are critical to the success of Gorbachev's plan to stimulate higher

Boxed Text #6

Reforms To Spur Innovation Backfire

Central authorities are attempting to stimulate high-quality production by assigning higher prices. Enterprises producing a new product or one judged of the "highest quality" are able to increase earnings by raising the price by up to 30 percent. This is leading to actions that planners did not anticipate, and innovation is the loser. [redacted]

For example, the Noril'sk Metallurgical Combine responded to the leadership's call to innovate by manufacturing an improved copper cathode. Once produced, it had to be inspected by central authorities to be certified as being of the highest quality. The State Price Committee then had to review a formal petition for a price adjustment. When the higher price was approved, central planners readjusted the combine's sales targets to take into account the increased revenues the superior product should generate. Production plans were formulated and sales targets finalized before industry's demand for an improved copper cathode was tested. [redacted]

When finally put on sale, the high-quality cathode was rejected by most domestic customers in favor of the cheaper, less advanced version that has been used for years. If the price were reduced by having the copper cathode recertified at a lower quality level, the combine would not be able to achieve its sales output target, which was set on the basis of the higher price. Thus, for all its trouble to produce a technologically advanced product, the combine now finds itself in a no-win situation-- unable to sell the more expensive higher quality copper cathode but also unable to cut its price and still achieve performance targets. Thus, the inflexible and formalistic procedures characteristic of centrally controlled prices and output targets continue to undermine even seemingly sensible measures to encourage innovation. [redacted]

End Boxed Text

productivity. The General Secretary has already managed to firm up his base of support in the Politburo, and [redacted]

[redacted] he intends to replace 28 to 36 ministerial officials and 48 to 60 members of the Central Committee with his own aides between now and the party congress next February. Nevertheless, his plans to streamline the industrial ministries, remove unnecessary bureaucratic linkages between enterprises and ministries, and increase the autonomy of enterprises will not be welcomed by many officials whose jobs, and perquisites, will be threatened. In the meantime, Gorbachev runs the risk of having his directives ignored, misinterpreted, or even reversed (see figure 4). [redacted]

In addition to cleansing the bureaucracy of redundancy, indifference, and gross incompetence, Gorbachev must also come to grips with an incentive system that stifles initiative and fosters corruption. Reducing the myriad of success indicators and tying wages closer to productivity, as Gorbachev has called for, will help. But the real trick will be to develop a set of success indicators that are beneficial both to the individual and to the economy. This, however, can only happen as a result of a major change in the Soviet economic system that will induce producers to respond to consumers and allow prices and wages to reflect consumer preferences.<sup>3</sup> As long as a set of detailed

<sup>3</sup> Consumer means any purchaser of goods or services--individual or enterprise. [redacted]

Figure 4

USSR: Bureaucracy Run Amok



national preferences (reflected in five-year and annual plans) is imposed on producers, and prices and wages are set and changed at the discretion of central planners, the managerial initiative Gorbachev seeks to develop--despite some likely early success--will eventually succumb to the waste and inefficiency engendered by the conflicting interests of enterprise managers and central planners.<sup>4</sup> [redacted]

Tying workers' wages more closely to productivity will have some beneficial effect in the short run. Wage incentives, however, will only be effective in the long term if there is a substantial increase in high-quality consumer goods available for purchase. Indeed, Gorbachev has personally identified himself with an expanded commitment to consumer-goods production. A 7 billion ruble program to modernize and increase shoe production has already been announced. According to one Soviet official, action to bolster output of household durables and materials for housing construction soon will follow. But much more investment is necessary to substantially improve the provision of consumer goods, and, given the strain already being put on investment resources, it seems unlikely that consumer-goods sectors will benefit from much additional investment during the next few

<sup>4</sup> Enterprise managers with increased autonomy, for example, will place new and perhaps excessive demands on local suppliers for raw materials and semi-finished goods. Suppliers, on the other hand, will still be functioning under the direct control of central authorities and may be unable to reconcile the demands of their customers with the directives and resource allocations of their masters. As a result, both producers and suppliers may become disillusioned and may once again resort to the very methods that have led to waste, fraud, and mismanagement for years. [redacted]

years. In fact, a high-ranking Soviet official recently acknowledged that problems will continue in the consumer sector and few additional resources will be made available to overcome them. [redacted]

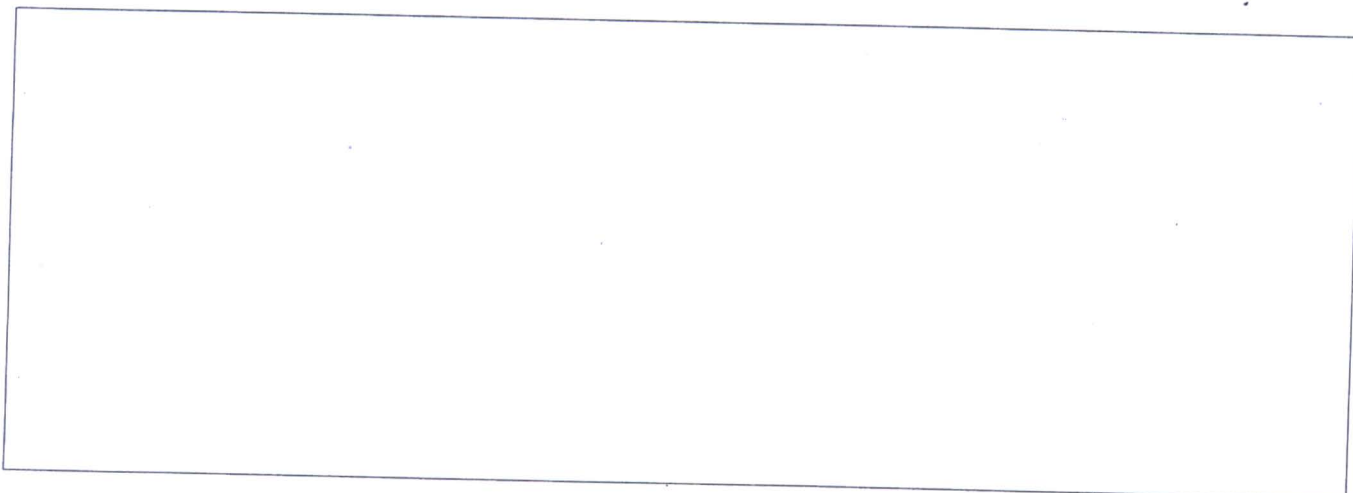
Dealing With Finite Resources

Gorbachev will be hard pressed to find the resources necessary to underwrite his goal of developing a modernized industrial base. The economic dividend from management reforms and the discipline campaign, while potentially substantial, will not come close to meeting these resource needs. Increased discipline, less corruption, greater temperance, and new management will help to raise labor productivity but will do little to offset the declining trend in capital productivity. Given enough time and investment resources, the modernization program could eventually pay off. While five years may be enough time to make a substantial dent in the stock of plant and equipment that needs to be modernized, there is simply not enough investment to go around. [redacted]

Although the Soviets have not formally revealed their investment plans for the 12th Five-Year Period, [redacted] [redacted] total

investment will increase by about 4 percent annually.<sup>5</sup> At the same time, Gorbachev has indicated that investment in civilian machine building will nearly double, while agriculture and related industrial support will maintain a large share. This will leave little room for increases in other sectors. The consumer may be especially hard hit in the nonfood areas. Gorbachev also will have to deal with pressures to expand investment in other areas, as:

- o Oil and natural gas exploitation moves further northward into the offshore areas of the Arctic and deeper into the Precaspian Depression.
- o Demand for roads, railways, and other infrastructure development--projects with heavy up-front costs and long leadtimes--increases in more costly and inhospitable regions.
- o Expensive new conventional and strategic weapons that have completed or are about to complete testing enter series production on a large scale. These include the Blackjack bomber, the AS-15 cruise missile, the SS-X-24





and SS-X-25 ICBMs, and the SU-27, MIG-29 and MIG-31 fighter aircraft. [redacted]

Gorbachev's announcement that energy's share of investment should be stabilized during 1986-90 carries special risks. Oil production has already begun to fall, and without substantial increases in investment, the production decline could become precipitous (see inset "Implications of Stabilizing Energy's Share of Investment"). Electric power, too, will need large increases in investment resources to meet the increased power requirements that will accompany the modernization effort. Coal production--the USSR's best long-term source of energy--has been slighted in investment allocations for years and will need a major increase to adequately exploit the large Siberian and Kazakh basins. Thus, if the energy sector has to make do with the same share of investment it received in 1981-85, likely production shortfalls could knock Gorbachev's modernization program into a cocked hat. [redacted]

The leadership seems to be counting heavily on its ability to increase energy efficiency enough to offset any production shortages that might arise. Retooling and installing more energy-efficient equipment promises substantial savings, but only in the long run and after considerable expense. The share of energy consumed by Soviet residential, commercial, and transportation sectors, which present relatively greater opportunities for immediate cutbacks, is comparatively small.

Boxed Text 7

Implications of Stabilizing Energy's Share of Investment

We estimate that to keep oil production from falling below about 11 million barrels per day (b/d) by 1990, investment in the oil sector alone during 1986-90 would have to increase by about 45 billion rubles from the 1981-85 level. We estimate that this is more than twice the investment increment that would be allocated to the entire energy sector in 1986-90 if Gorbachev stabilizes energy's share of total investment. If the needed investment in oil is not forthcoming, production could fall to less than 10 million b/d by 1990. Such a drop in production would be greater than total hard currency exports of oil in 1984. [redacted]

Boxed Text End

Department stores consume over one-half of the fuel used residentially, and most of them burn low-grade coal or firewood. Trains rather than trucks provide the dominant mode of Soviet commercial transport and are already the most energy-efficient in the industrial world. Private automobile use will remain far below levels in the developed West through 1990. [redacted]

[redacted]

Industry and electric power generation are the principal energy consumers in the USSR. The Soviets are world leaders in cogeneration--the production of steam for space heat at thermal electric power plants--which has raised considerably the total efficiency of those power facilities in comparison with power plants in the West. Some Soviet basic steelmaking processes are also relatively energy efficient. Additional major energy savings in industry therefore must come through massive capital investment for the production and/or importation of more energy-efficient equipment. [redacted]

However, the production of more efficient equipment is a difficult and time-consuming task. Machine builders--having had little incentive to produce energy-efficient machinery in the past, will have to start virtually from scratch. Payback is uncertain, and delayed until new equipment can be designed, produced, and put into operation--often a process of at least six to eight years. As a consequence, given Gorbachev's announced growth goals, the mix of Soviet output over the next five years is likely to become more, rather than less, energy intensive. [redacted]

### A Rocky Road Ahead

Gorbachev probably believes that if he can kick-start the ponderous economic machinery hard enough, and sustain the momentum long enough, the early gains he achieves are likely to stimulate lasting improvement. Indeed, because of the strong interdependence among his plans for energy savings, industrial modernization, managerial renewal, higher productivity, and an improved work ethic, a large dose of early success in some areas could promote success in others. The longer he can sustain the early gains, the better the chances for long-term progress. This same interdependence, however, increases the risk of failure; because so many things that have gone wrong for so long must now go right, the likelihood is high that some will continue to go wrong and thereby impede progress. [REDACTED]

Reducing waste, fraud, and mismanagement and directing available resources to their most productive uses will contribute substantially to the modernization program. But the economic dividend from management reforms and the discipline campaign will not come close to meeting the economy's resource needs. The key to success will be Gorbachev's ability to cope with some fundamental paradoxes, and he will have to do so sooner rather than later:

- o Improving management efficiency and worker morale will require an effective incentive system and increased availability of high-quality consumer goods at a time when the investment sector will be oriented toward

producer goods and new defense programs will be coming on line. Based on Gorbachev's program for redirecting investment, we project that the increment in consumer-oriented investment during 1986-90 could be some 60 percent less than that for 1981-1985.

- o Energy's share of investment is to be held constant at a time when demand for energy will grow and the cost of offsetting declining oil production will be rapidly rising. The implications of a redirection of investment away from other sectors, particularly consumer-oriented sectors, may be equally ominous.
- o The increased managerial independence necessary to spur effective technological development and utilization is inconsistent with a centrally planned pricing and allocation system, leading to the likelihood of management disillusionment and subsequent reversion to the very methods that have led to waste, fraud, and mismanagement for years.

Gorbachev's approach in resolving these issues could have strong political and strategic implications; failure to resolve them will stymie his modernization effort. [redacted]

He could, and likely will, seek some relief from the economic dilemma by demanding that Eastern European countries, which have benefited from Soviet economic largess in the past, shoulder a greater part of the burden. Imports of equipment from Eastern Europe accounted for one quarter of total Soviet

machinery and equipment investment in 1983, and Gorbachev will likely push for an even higher flow in the future while reducing Soviet deliveries of costly raw materials. East European leaders, beset with their own deep economic problems and popular expectations, are likely to strongly resist such suggestions, paving the way for growing confrontation between Moscow and its allied states. [REDACTED]

Gorbachev may also increase imports of Western technology to secure state-of-the-art equipment in key areas. A marked rise in imports, however, would require a substantial increase in hard currency expenditures at a time when the USSR is facing a decline in the production of oil, its major hard currency earner. While Moscow has the capability to expand imports by markedly increasing its hard currency borrowing, such an expansion would create a potential vulnerability to Western exporters, lenders, and their parent governments that past Soviet regimes have sought to avoid. [REDACTED]

Gorbachev could attempt to reallocate resources away from defense to provide some relief to the civilian economy, but he probably would encounter stiff opposition if he attempted major adjustments in defense allocations. Currently about 30 percent of all machinery output probably goes to support defense production. Moreover, this share generally represents the highest quality products and newest technological processes in Soviet machine building. The military sector also receives the most capable managers. Some labor, materials, and components

could be readily shifted to civilian uses, but most defense industrial plants would require extensive, time-consuming retooling before they could productively turn out much civilian production. Nevertheless, in the long-run many defense resources could be applied productively in the civilian economy. [REDACTED]

Although military leaders recognize that the long-term strength of the Soviet military depends largely on the country's economic health, the Soviets are committed to programs for modernizing their offensive and defensive strategic forces, as well as their conventional weapon programs. In addition, the US defense modernization and the long-term implications of the Strategic Defense Initiative (SDI) probably are being cited by Soviet military leaders as justification for higher growth rates for defense spending. The rate of growth of defense spending since the mid-1970s has been a relatively modest 2 percent, and military leaders probably already feel that defense has accepted slow growth in resources for as long as it can, given the extensive requirements for upgrading weapon systems. [REDACTED]

The institution of major economic reforms such as private enterprise and market determined prices and allocations could, over time, markedly improve economic efficiency, consumer welfare, and technological adaptation. They would encounter strong resistance on political and ideological grounds, but Gorbachev has already shown that he will aggressively tackle the problems he has inherited and, like Khrushchev more than two decades ago, use his considerable power to force the pace of change (see inset "The Krushchev Analogy"). [REDACTED]

## Boxed Text #8

The Khrushchev Analogy.

Nikita Khrushchev, during his 11 years at the top (1953-64), launched his own "revolution" in Soviet politics. Crude, boisterous, and aggressive by nature, he bullied and cajoled his colleagues and the bureaucracy to adopt his vision of the Communist future. He made catching up with the United States a major goal and enshrined it in the utopian party program of 1961. He eliminated terror as an instrument of everyday politics, brought Stalin's police apparatus under effective political control, and publicized some of the crimes and abuses of power of his former mentor. (These revelations were a tremendous shock to the Soviet people and to Communist sympathizers around the world.) He made dramatic changes in economic policy and management--abolishing the same central ministries that now so trouble Gorbachev, reorganizing the party apparatus that oversees them, and changing economic priorities almost by fiat. He dramatically increased Soviet involvement in the Third World and vigorously stepped up Soviet competition with the United States for power and influence around the world. His risky political course both at home and abroad--along with his nonconsensus style--ultimately led to his ouster by the very people he brought into power.

The most striking similarity between Gorbachev and Khrushchev is their informal, populist style of leadership. Like Khrushchev, Gorbachev has made an effort to show that he is accessible and interested in the views of normal citizens. He has made forays into the streets and visits to factories to engage in unrehearsed, well-publicized exchanges with the assembled crowds. The informal style of both leaders is also evident in their willingness to make extemporaneous remarks during their prepared speeches as well as in the public role for their wives and families. The similarities between both leaders are particularly pronounced when compared to the cautious, stiff, and highly formalized style of Brezhnev that was the norm for the past 20 years.

At the same time Gorbachev--more polished and educated than Khrushchev--appears to have learned from Khrushchev's mistakes and is using very different tactics in pressing his agenda for change. When Khrushchev was removed, his successors accused him among other things of "hare brained scheming, immature conclusions, and hasty decisions and actions divorced from reality, bragging and phrase-mongering." These accusations stemmed from his efforts to hastily push through major reforms that were not well thought out and his highly personalized style of leadership that was based more on confrontation than consensus.



~~SECRET~~ [REDACTED]

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While Gorbachev appears equally determined to overhaul the system, he has gone about the task much more deliberately and cautiously than Khrushchev. His signals to the bureaucracy are clearer and make it easier for lower level officials to calculate what is expected from them and to respond accordingly. Instead of presenting specific proposals for reform, as did Khrushchev, Gorbachev has defined the general directions of the changes he would like to accomplish and encouraged further discussion of the optimal ways to achieve them. At the same time he is systematically building political support for his agenda by installing loyal officials in key positions and removing those who might thwart his plans. [REDACTED]

End Boxed Text

~~SECRET~~ [REDACTED]

Premier Tikhonov almost certainly will be replaced at or before the congress in February by Gorbachev himself or an ally. The leadtime to the congress will also give Gorbachev the opportunity to more thoroughly clean out the deadwood from the party and governmental bureaucracies and bring in a management team more sympathetic to his policies and better equipped to carry them out. Over the next year, indications that he is moving ahead with his economic agenda could include:

- o A clear delineation of winners and losers in the 1986-90 plan for investment allocations. Besides machine building, sectors such as ferrous metals and chemicals must receive a greater share of the investment pie for the modernization program to have any chance for success.
- o The creation of superministries, for example by combining ministries in the agricultural area, with a concomitant reduction in ministerial control of enterprise operations.
- o Specific changes in managerial incentives (for example, tying bonuses to the share of new equipment installed) to promote modernization of plant and equipment.
- o The replacement of Gosplan Chief Baybakov with an outsider (possibly even Nikolay Ryzhkov) who would enhance the political stature of Gosplan and signal increased emphasis on long-term strategic planning rather than detailed annual planning.

- o A reduction in reported resistance to the ongoing industrial management experiment coupled with measured gains in productivity. [redacted]

Moreover, with his own people in place, Gorbachev should be able to build a consensus behind the more far-reaching proposals that he has only hinted at to date. Indications that he has decided on and gained consensus for more radical changes could include:

- o New dramatic initiatives to reach accord at Geneva and concrete proposals for reduced tensions at the November meeting between the US President and the General Secretary, which might signal a willingness and desire to reduce the Soviet resource commitment to defense and create an atmosphere for expanded commerce with the West.
- o Select legalization of private sector activity, particularly in regard to consumer services, which would indicate willingness to confront past economic orthodoxy in order to improve consumer welfare and thereby economic performance.
- o Breaking the monopoly of the Foreign Trade apparatus, which would signal an increased reliance on managerial independence at some cost to centralized control.

Continued reliance on marginal tinkering, despite clear indications that the plan for economic revitalization is faltering, would indicate that Gorbachev, like Brezhnev before him, has succumbed to a politically expedient but economically ineffective approach. [redacted]