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Gorbachev: Steering the USSR Into the 1990s

Key Judgments
*Information available
as of 30 June 1987
was used in this report.*

In the next year, Soviet leader Mikhail Gorbachev and his Politburo will have to agree on adjustments to the current (1986-90) five-year plan to cope with emerging shortfalls and to correct imbalances. Meanwhile, the future of economic reform is being worked out, and the Soviet leaders will be attempting to formulate their resource allocation guidelines for the 1991-95 plan. The USSR's planning cycle calls for these guidelines to be given to the economic planners by about mid-1988. This will be a tough call because not all the returns will be in from measures already implemented.

Adjusting the 1986-90 Plan

The present five-year plan has virtually no slack that would permit more attention to one of the major sectors of the economy without some impact or offsetting adjustments in other areas. For example, the growth in overall volume of investment, while higher than in the two previous five-year plans, still appears low in comparison with the production targets. Taken at face value, the plan indicates that the Soviets expect a sharply increasing ratio of output per ruble of investment. But if the efficiency gains from the "human factor" campaign do not materialize, the leadership will have to decide whether to push for faster investment growth in the present plan to keep its industrial modernization program on track. Such a step could force the USSR to consider permitting a buildup of debt to the West to finance more imports. And sustained higher rates of investment would not be feasible, in our view, without holding military procurement relatively flat.

Similarly, allocations to the consumer in the current five-year plan, particularly goals for consumer durables, have been held down against a promise of better things to come in the 1990s as the hoped-for benefits of industrial modernization are realized. The leadership, however, will have to be careful to avoid the kinds of shortages that in the past have had a dampening effect on labor incentives—particularly because so much of the present plan appears to bank on increasing productivity through a motivated work force.

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In the case of reforms, what has been accomplished so far amounts to a set of partial measures. Soviet leaders will need to consider adjustments to those measures already implemented and how to implement the more comprehensive changes in the organization and management of the economy that Gorbachev called for at the Central Committee plenum in June 1987. It will be particularly important for the leadership to avoid the kind of backsliding that has brought past reforms to a standstill. Gorbachev has been searching for a formula that encourages more initiative at lower levels while permitting control to be maintained from the center. This is a delicate balance at best; early in the 1965 and 1979 reforms, for example, the ministries began to reassert their control over enterprises by multiplying the number of plan targets and limiting their use of discretionary funds. And the natural inclination of local party officials will be to exercise the same kind of petty tutelage over enterprises that they have in the past. Preventing this will require a fundamental restatement of the responsibilities of ministries and party organizations. [REDACTED]

According to guidelines approved by the Central Committee on 26 June 1987, the next phase in improving organization and management will involve curbing the powers of central economic authorities, developing genuine wholesale trade, reforming the price system and financial and credit institutions, and introducing stronger incentives for enterprises to use their increased independence in ways that satisfy the guidelines set out in the state plan. Gorbachev could also expand the permissible boundaries of private production and allow greater wage differentiation. Even with the best leadership intentions, improving worker incentives will depend mainly on whether workable arrangements in these areas can be developed and on how the labor force reacts to them. Elastic work rules and narrow wage differentials have become an important part of the "social contract" in the Soviet Union. [REDACTED]

Formulating Resource Guidelines for 1991-95

The leadership's perception of progress on the industrial modernization program—especially in the machine-building sector—will be a critical factor in its outlook on the next five-year plan. If by next year this program does not appear to promise growth large enough to give generous increments to consumers and defense as well as investment, the leadership will

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be forced to decide whether civilian machine building should get more funding in the 1991-95 plan. Another factor that could contribute to pressures for higher investment than originally envisaged for 1991-95 would be a dwindling of the impetus to growth from tightening labor discipline and weeding out poor managers. And a key unknown may be whether the construction and machine-building base will be adequate in scale and quality to support a large increase in investment without a cutback in the defense plan submitted by the General Staff. ■■■

Foreign Help

So far, Gorbachev has had little success in obtaining help for his economy from abroad—either from Eastern Europe or the West. The Soviets have had trouble getting their East European allies to shoulder more of the burden of the USSR's resource development and the Warsaw Pact's force modernization. Meanwhile, although the extent to which the leadership planned on increasing imports from the West during the 1986-90 plan period remains an unsettled question, Moscow's ability to buy more Western machinery or farm products has eroded badly because of the decline in world energy prices and the lower value of the dollar. At this juncture, the Soviets appear to be counting heavily on joint ventures with Western firms. They are currently negotiating with about 100 Western companies, although only a few of these negotiations appear to be in their final stages. ■■■

The Potential Pitfalls . . .

A wide range of special interests and sensitivities will impinge on Politburo decisions over the next few years. First of all, military support for the modernization of civilian industry could erode substantially if the external threat assessment now being offered by military leaders becomes starker because arms negotiations fail to constrain NATO defense programs and bilateral US-Soviet relations worsen. In the reform arena:

- A relaxation in the tautness of the economy would help innovation and ease a transition to new economic arrangements, but Gorbachev stands in the way. From his first days in power he has stepped up the pressure on workers, managers, and bureaucrats.

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- Ministries are not likely to easily accept a lesser role in administering the economy. They probably will try to entrap their enterprises in a new web of rules and requirements, while ideological conservatives will fight an expansion of private economic activity.
- Genuine elections for party-state offices would evoke the specter of factionalism and be seen as a threat to the top-down direction of the society and the economy that has characterized "democratic centralism" for 60 years.

... And A Helpful Environment

The investment/defense decisions to be made would, of course, be generally much easier if economic growth turned upward sufficiently to ease the resource bind and diminish some of the fears of the fence sitters in Gorbachev's Politburo. At the same time, arms control agreements and improved US-Soviet relations that reduced both the momentum of NATO military programs and the influence of the Soviet military-industrial complex would give Gorbachev more room to maneuver. Soviet success in these areas would in turn raise Western interest in granting credits to Eastern Europe and establishing joint ventures in both the USSR and Eastern Europe.

Somewhat paradoxically, however, better economic performance and a favorable international climate would both strengthen and weaken the case for more ambitious economic reform. Reform is easier to implement when annual GNP growth is high, but the urgency attached to a reform program tends to fade when the economy is doing relatively well.

Gorbachev's Next Steps

At considerable risk to his political future, Gorbachev is gambling that his policies will rejuvenate the USSR's economy and society. The problems he is encountering have not yet derailed his program or diminished his determination to change the system radically. But even his supporters are concerned that he will need to win new victories before long if he is to sustain the momentum for change he has generated.

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Thus, we believe that Gorbachev cannot work out the next steps toward renewal at his leisure. Developments during the past year have increased the chances that he will act boldly to sustain the momentum of his program. Because he seems determined to protect a modernization program that is already underfunded and because the milestones for fashioning the 1991-95 economic plan are fast approaching, Gorbachev is likely to seek arms control agreements in the final years of the Reagan administration rather than wait for the next election. Moreover, the weaknesses of the reform measures undertaken thus far are likely to become clearer over the next few years. We think Gorbachev is likely to move forward rather than retreat and push through more radical reforms so that they will be in place for the 1991-95 plan period. In this context, Gorbachev sees publicity and elections at lower levels as a way of exposing and disciplining those who will not or cannot implement his program. In the economy, workers probably will have a greater say in choosing trade union officials, foremen, and even managers.

The Consequences of Failure

Gorbachev has already asked the military and the population to curb their appetites in return for more later. If his programs do not work out, other leaders could appeal to these constituencies. The risks in a more radical reform and a rewrite of the social contract are that confusion, economic disruption, and worker discontent will give potential opponents a platform on which to stand. Gorbachev's position could also be undermined by the loosening of censorship over the written and spoken word and the promotion of limited democracy. If it suspects that this process is getting out of control, the party could well execute an abrupt about-face, discarding Gorbachev, along the way.

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