

On *Perestroika*: Analyzing the "Basic Provisions"

John E. Tedstrom

THE MAIN document ratified by the June 1987 Plenum of the Central Committee of the Communist Party of the Soviet Union and entitled the "Basic Provisions for the Radical Restructuring of Economic Management" represents the product of more than two years of effort on the part of General Secretary Mikhail Gorbachev and his allies to effect a radical reform of the Soviet economic system. The most extensive such measure since the Khrushchev reforms, perhaps even since the New Economic Policy (NEP) of the 1920's, the "Basic Provisions" is but one part of a broad Soviet reform effort that includes the reshaping of the social and political environment as well.

The timing of the "Basic Provisions" is quite significant. Faced with an increasingly outdated economy that has reduced Soviet ability to compete on the international market, Gorbachev has not only called for the restructuring of the economy, but has demanded that it occur at an *accelerated* pace. A whole section of the "Basic Provisions" is devoted to laying out specific deadlines for the implementation and completion of the various economic reform measures.

Given the importance and urgency of the "Basic Provisions," I shall attempt a brief analysis of the document in terms of the consistency and cohesiveness of its six major provisions. After summarizing each provision individually, I shall proceed to analyze its content and feasibility.¹

John E. Tedstrom is a Research Analyst for the Hudson Institute's Center for Soviet and East European Studies (Indianapolis, IN). The author would like to thank his colleagues Hans Heymann and Ralph Raymond for their thoughtful comments and to express his special gratitude to Professor Robert Campbell.

I. To Switch to the New Economic Mechanism of Enterprise Activity.

Calling for "a most favorable economic environment for the enterprise," this provision establishes the enterprise as the primary economic actor in the Soviet economy and as the foundation upon which the restructuring of the economy is predicated. Essentially, it promises enterprises more economic independence than ever before, including responsibility for transferring to full cost-accounting and self-financing; providing for effective worker incentives within the enterprise; stimulating production within the consumer sector; ensuring resource savings; and introducing more extensive use of scientific and technological innovations. Furthermore, it charges enterprises with the independent drafting of their own five-year plans, which are to be based on state orders, direct orders from other enterprises, and consumer demand. Finally, it makes enterprise work collectives responsible for electing their leaders from among a broad field of competitors.

Clearly the responsibilities given to the enterprises under this provision far exceed the degree of independence granted them. In the Soviet Union, full cost-accounting (*khozraschet*) implies economic and financial *accountability*. In other words, an enterprise operating under this system must be essentially self-sustaining. The state will no longer subsidize enterprises that cannot generate revenues to finance their own activities; they will be forced to declare bankruptcy.

Although Western economists may at first applaud this development as a rational way to weed out ineffi-

¹My analysis of the "Basic Provisions for the Radical Restructuring of Economic Management" is based on the text of that document published in *Ekonomicheskaya Gazeta* (Moscow), No. 27, July 1987, pp. 11-14. For an English translation of that text see Foreign Broadcast Information Service, *Daily Report: Soviet Union* (Washington, DC), June 30, 1987, pp. R/1-22.

ciency, one should not forget the conditions under which these enterprises may soon be operating. Much of this will be discussed later, but a few general comments are warranted here.

First, uniform application of the principle of economic accountability is unlikely. In all probability, ministries will not allow crucial enterprises to declare bankruptcy but will ensure that important but unprofitable enterprises continue to receive subsidies. Enterprises within the military-industrial complex (VPK) will probably continue to receive preferential treatment, forcing their suppliers to operate irrationally in order to meet overly tight production and delivery schedules, and so constricting the flow of supplies to the civilian sector of the economy.

Second, the fact that this provision states that "control figures, long-term economic norms, state orders and allocations are [to be] the initial data and basis for drafting the enterprises' five-year plan" casts doubt on the significance of the touted horizontal linkages between enterprises. How are the enterprises to make their own purchasing and output decisions if they must still base their plans on centrally established control figures, and state orders and allocations? And what role can consumer demand play in the product mix if orders from above predetermine that mix? These key issues in the development of any decentralized, efficiently operating economy are not resolved in the reform plan.

Finally, this provision will force enterprise managers and other vested interests to try to reconcile competing (and perhaps irreconcilable) goals—that is, to improve economic efficiency in the marketplace on the one hand, and to satisfy central command on the other. In addition, they will be held accountable for poor economic performance. Given that ultimate control and authority still rests in the center, there is little doubt as to which goals most managers will feel compelled to achieve. Such exceptions to the application of the new economic mechanism will necessarily reduce its impact on economic development and growth.

II. To Raise the Efficiency of Centralized Economic Guidance Through Methods of Economic Management.

According to this provision, guidance from the center must be "perfected" so enterprises can operate more freely and effectively. From now on, instead of micro managing the economy, the USSR State Planning Committee (Gosplan) is to focus its efforts on "implementation of the state's strategy of economic, social, scientific and technological development, [and] the adjustment of national economic processes on the basis of com-

plete and reliable economic balance." Four aspects of the centralized planning mechanism are targeted for improvement: planning methodology, provisions for the material and technical supply of enterprises, price formation practices, and policies regarding financing and the granting of credit.

Planning methodology. This section states that annual, five-year, and longer-term (usually 15-year) plans will continue to be the framework for the development of the Soviet economy. All five-year plans are to be based on input from the enterprises, ministries, the State Planning Committee, and the Council of Ministers, and are to be ratified at congresses of the Communist Party of the Soviet Union (CPSU). The main change in the planning process is to be the transition to "economic methods of planning the activities of enterprises on the basis of planned targets, long-term stable economic standards, and state orders and allocations." According to the provision, planned targets "... should not be directive in nature and should not restrain the work of the collective in the elaboration of the plan, giving it wide scope for the choice of solutions and partners when concluding economic contracts."

This reform has two salient implications. First, because plan targets are no longer to be "directive," the enterprises will be ostensibly allowed more freedom to choose suppliers and to make operational decisions without direct influence from the center. Managers—those who are most familiar with the operations and problems of their enterprises—will now be free to make more decisions.

Second, vestiges of the old planning methodology will apparently remain in existence. For example, the continuation of the practice of centrally adopted plan targets virtually guarantees that managers will continue to work toward centrally established production quotas regardless of any promises by the center to the contrary. (By contrast, the essence of the Hungarian reforms was the complete elimination of central target figures.) Furthermore, although they now have the legal right to do so, enterprises will probably not change their suppliers since, in the heavily concentrated Soviet industry, the number of suppliers to choose from is very limited. Since incentives for suppliers to compete for business on the basis of price or quality also remain low, most industrial activity will continue to be centrally determined.

In short, the predominance of state orders and allocations over consumer demand will continue to bias the output mix of the economy. As a result, managers will be overly sensitive to centrally established gross indicators and less sensitive to issues of quality and resource-conservation.

Material and technical support. This section of the second provision calls for a "radical reorganization of the means of material and technical support" entailing a transfer to wholesale trade (*optovaya trgovlya*) between organizations instead of central allocation. Wholesale trade is now to be carried out through "free purchases and sales under direct contracts [*po priyamym dogovoram*] between producers and consumers . . ." Designed to enhance the role of the purchaser and to accord enterprises more flexibility in obtaining material and technical support, this transition to direct wholesale trade relations is scheduled to be completed within four to five years. Special provisions permit "the filling of and support for orders placed by the state." According to these provisions, centralized economic management bodies may place state orders with enterprises, and, if necessary, may also list "the enterprises, organizations, and institutions having a right to purchase products made under the orders."

This provision is designed to enhance the managers' freedom of decision-making. Practically speaking, however, the present central supply system (Gossnab) will continue to be the single largest obstacle to enterprise autonomy. Central control over production quotas cannot exist without central determination of supply markets, since the bulk of output is fed back into the production process in the form of inputs. Thus, the continued ability of Gossnab to determine buyer-seller relationships will impede the Soviet quest for an efficient economy. There is little indication so far that the Soviets plan to initiate any meaningful changes in the supply system in the near future.

Price formation. The system of price setting, one of the weakest links in the Soviet economic system, has been the subject of much debate and controversy among Soviet economists and planners, some of whom have come to accept the concepts of scarcity pricing and marginal costs as fundamental components of an efficient economic system. In fact, in the case of several economic activities, the algorithms the Soviets use to form prices attempt to achieve marginal cost pricing (*zamykayushchyye zatraty*). These prices, however, tend to serve as theoretical reference points and are not generally used in actual transactions. The section of the second provision addresses the problem and provides for the integration of prices at all levels of production, from research and development to retail sale, in order that they may reflect more accurately the cost and societal value of each commodity.

The pricing issue has proven so controversial that the June plenum could not arrive at any consensus. Consequently, this section mostly calls for further discussion of

the pricing issue on a country-wide basis. It also charges the USSR State Committee for Prices to prepare and carry out a radical reform of the system of price formation. Furthermore, this section notes that there is a need for a single system of control over prices, to overcome any inclination on the part of the newly empowered enterprises to increase prices, to eliminate any tendency toward monopolism, and to shield the producer from consumer pressure under the new conditions of self-financing.

It is probably unfair to comment critically on the new program of price formation when details have yet to be worked out. Yet there exists sufficient information to make a few general critical observations. First, although the Soviets want the price reform to accomplish a more accurate representation of marginal cost and marginal benefit and hence facilitate more "rational" economic activity, they fully realize that this is likely to conflict with one of the basic tenets of socialism—economic equality. Increased wage differentials in many sectors of the economy have already threatened economic equality and have raised concern among academicians and the populace as well. Clearly the Soviets have yet to determine how best to use price formation reform to achieve greater efficiency without further jeopardizing economic equality. We may conclude, therefore, that fully flexible prices that would reflect both scarcity and utility are likely to come slowly, if ever. The proviso for central control over prices in order to prevent inflation—the Soviet consumer's chief fear—and other maladies caused by market-formed prices is a critical one designed to ensure that the Soviet living standard will not be eaten up by increasing prices; it will not be quickly discarded. Yet, central control over prices is antithetical to flexible, rational pricing.

Second, the integration of commodity prices from the beginning of the production process to retail sale is an important and positive development. In market economies, this integration is a natural phenomenon. In the Soviet economy, a gap exists between the cost-plus prices used at the wholesale level and retail prices, which are designed to "clear the market" through application of either subsidies or a turnover tax. As a result, retail prices, reflecting neither scarcity nor consumer demand, necessarily distort economic behavior. An integration of wholesale and retail prices would close this gap and—depending on the impact of other reform measures—could send more accurate information to both producer and consumer.

Although the story on prices is yet to be played out, Gorbachev has probably gone as far as he can—or wants to—at this time. As a result, the most we can expect in this area in the near future is further debate on the

issue (with more radical elements calling for further liberalization) and some intermittent tinkering with prices and the pricing mechanism.

Financial and credit-granting mechanism. In order to facilitate the economic activities of enterprises, and to eliminate financial waste and pilfering, a radical restructuring of the financial and credit-granting mechanism is proposed. The Soviets consider this an integral part of the overall restructuring program, which makes sense given the new policy on the role and formation of prices, and the new economic activities of the enterprises. Their approach to issues of finance and credit indicates that they are aware that commodity-money relationships are a vital part of an efficiently operating economy.

The changes called for in this section are:

- making finance and credit one of the major instruments of the plan-based economic management and thereby increasing management efficiency;
- making five-year financial plans an integral part of the state plans for economic and social development;
- developing a fundamentally new financial policy for the USSR Ministry of Finance to be based on a combination of state and enterprise interests (This is to ensure, in part, control over the efficiency of management by using monetary levers.);
- making credit-granting institutions more interested partners in the economic activities of the enterprises;
- increasing the role of the USSR State Bank (Gosbank) as overall organizer and coordinator of all credit-granting arrangements;
- radically improving consumer insurance and savings bank services; and
- enhancing the financial and credit-granting mechanism in the sphere of foreign economic activity, including making the ruble convertible, first within the framework of the Council for Economic Mutual Assistance (CEMA), then (by implication) with other currencies.

The measures are somewhat vague and do not appear to represent a significant step toward rationalizing the role of finance and credit within the new Soviet economy. The first five measures listed aim at strengthening central financial control (*kontrol' rublyëm*) over economic performance and constraining the economic activities of enterprises and other entities. Such a development conflicts with the desire to integrate more fully the financial sector with the rest of the economy in a way that would enhance economic efficiency. Note, for example, that financial activity will be further centralized under the control of Gosbank. Thus, Gosbank is to become a "more active partner" in the economic activities of the

enterprises, with interest rates, repayment schedules, and credit qualification requirements still being centrally established. We should not, therefore, expect credit-granting institutions to compete with each other for business. Moreover, even if money-commodity relationships are "rationalized" and play a more integral role in microeconomic activity, institutional changes in the financial sector will tend to work in the opposite direction.

The improvement of insurance and consumer savings services addresses a longtime void in the consumer services sector and will no doubt be popular with Soviet citizens. The change to a convertible ruble will probably become a complex process, even within the CEMA, with the Soviets standing to lose in terms of purchasing power if a real exchange rate with other, non-socialist currencies were ever negotiated. Clearly, few Soviets would advocate losing control over their currency and subjecting it to the fluctuations of the world financial markets. In any case, there is minimal outside pressure on the Soviet Union to switch to a convertible currency. For example, there is very limited demand in the world markets for ruble claims against Soviet resources. As a consequence, the convertible ruble is, at least for the foreseeable future, probably a non-issue.

III. To Remake Organizational Patterns of Management.

Recognizing the unwieldy size of the current economic bureaucracy, this provision calls for a reform of the organizational structure of the Soviet economic system. It explicitly notes that, by involving themselves in the day-to-day operations of enterprises, the central economic bureaucracies have made enterprise performance "less and less efficient," and it addresses the following points concerning a new organizational structure:

- the new organizational structure should facilitate the economic activities of the more independent enterprises;
- ministries should be relieved of day-to-day management duties;
- the standing bodies of the USSR Council of Ministers should focus work on inter-sectoral scientific and technical problems and on strengthening the export capabilities of the economy;
- activity of the control apparatus should be reduced and regulated and the People's Control Committee of the USSR should become the single integrated system of control, allowing the consumer greater say in the direction of economic activity; and
- the system of official statistics should be revamped radically to include both a wider base of information on

matters of social development and selective surveys, and to eliminate padded reports and other statistical deception.

The significance of this provision has several dimensions: First, it explicitly states that the economic apparatus in general and the economic ministries specifically should be relieved of day-to-day management duties and focus instead on broader issues such as intersectoral cooperation, and ensurance of overall balance in economic activities. Second, the shift of control responsibilities to a restructured People's Control Committee is ostensibly designed to allow more room for consumer pressure on the enterprises. Third, it calls for improvement in the quantity and quality of economic and social statistics, which should provide both Soviet and Western specialists data better suited to more sophisticated analyses and accurate studies of the Soviet economy.

Most of the specifications of this provision are rather uncontroversial and appear to be logical components of the overall program. The measure stating that the economic bureaucracy will have to shift its focus from day-to-day management of the economy to broader strategic questions, however, will no doubt meet with a good deal of bureaucratic resistance since it stipulates that for such a switch to be effective, "streamlining" (i.e., staff reductions) of the state economic bureaucracy is necessary. Nonetheless, ministers will apparently retain responsibility for the performance of the enterprises under them, making it likely that they will continue to intervene in enterprise affairs when poor enterprise performance jeopardizes their success.

It is not clear what the impact of the "new" People's Control Committee will be. The provision specifies that this committee will be a highly centralized body whose decisions will apply to the entire country. It may be that one cumbersome bureaucracy is simply being replaced by another.

IV. To Ensure An Optimal Combination of Branch and Territorial Economic Management.

The main thrust of this provision is to enhance the role of territorial planning organizations. Accordingly, it specifies that long-term plans are to be territorial in focus, and are to take into consideration the activity of all enterprises in a given territory, regardless of the department to which they are responsible.

Furthermore, it charges the council of ministers of each union republic with heightened responsibility for solving economic and social development problems on a territorial basis. It also calls for the establishment of production-economic departments of executive com-

mittees of the soviets of peoples' deputies to be responsible for guiding economic organizations on the level of *kray* (territory) and *oblast* (province).

To ensure that economic plans and activities of the most strategically critical branches of the economy are balanced and cohesive, the provision assigns certain branches—such as heavy industry and geological survey—to all-Union bodies of management, while other industries are left to the responsibility of the republic and local government bodies.

Clearly, this provision forcefully establishes the importance of territorial planning under the conditions of the new economic mechanism. Moreover—in keeping with the structural reorganization of the economic apparatus—it sharply devolves responsibility for economic activity to more local institutions. It also appears to strengthen the role of municipal, provincial, and territorial economic plans.

One of the more interesting questions raised by this provision is what will be the impact of the reform on various territories in the Soviet Union. Inasmuch as some regions are blessed with greater supplies of economic resources (not to mention economic and entrepreneurial potential arguably inherent in particular cultures), we may see more rapid development in some republics than others.

It is worth mentioning that under this provision, two strategic elements of the economy will remain under the primary control of central authorities: heavy industry and geological survey (important for its role in the exploration of strategic resources such as oil and gas). Although this makes sense if we consider that some economic activities (such as coal mining) are more easily planned than others (such as consumer services), it will nonetheless sharply diminish the impact of decentralization since heavy industry produces a major share of total Soviet economic output.

V. To Enhance the Social Trend of Development.

This provision establishes the new conditions under which labor will work in the coming years. Stressing the human factor, it promises an increase in the level of the nation's prosperity.

Economically, this provision deals with the issue of wages. Stating that wages make effective incentives, it rejects the notion of wage leveling and, in fact, explicitly sets no limit to wage differentiation. Moreover, it establishes the collective contract as the primary basis for worker participation in the activity of the enterprise. This contract is to define working conditions, administrative rules, and the wage structure of the enterprise.

Politically, this provision is an attempt to assure the

Soviet populace that its leadership is aware of their fears about inflation and job insecurity and will take appropriate steps to ensure that these economic maladies do not threaten social welfare. It calls for the maintenance of a stable and growing supply of food and consumer goods. It also calls for the improvement of municipal services such as education, housing, health care, and physical culture. Interestingly, the provision addresses the phenomenon of labor force disruption that is bound to occur in the transition to and during the period of the new economic mechanism, and thereby tacitly acknowledges the inevitability of unemployment. It stresses the need for programs to organize, select, train and retrain, and place labor personnel who are released from other jobs, or who are unemployed but able-bodied. Finally, it addresses such sensitive issues as labor discipline.

The issues concerning the "human factor" in production have received the most attention from the Soviet leadership. Given that labor discipline has been terribly lax in recent years, the tightening of discipline has become a relatively inexpensive way of increasing productivity. How much productivity can be gained through this discipline campaign is unclear and in all probability systemic changes will have to be introduced for the effects of this discipline campaign to be substantial and enduring.

The issue of wage differentials has proven particularly controversial. The economic inequality resulting from increased wage differentials is an anathema to Soviet ideologists and threatens the stable and secure employment arrangement to which the Soviet labor force has become accustomed. Moreover, it still remains questionable whether wages will prove to be a very effective incentive in the Soviet Union. Shortages of consumer goods, and heavy subsidies on food, housing, education, medical care, and other basics have meant that Soviet citizens with low incomes did not fare much worse than those with high incomes. Unless other measures (such as price reform) effectively redress these issues, it is unlikely that wage differentiation will have the beneficial effect that the leadership anticipates.

VI. To Efficiently Organize the Restructuring of Economic Management.

Declaring that "it is impermissible that unreliable organizational assurances, tardiness, and lack of coordination should lead, as in the past, to delays and incomplete implementation of the radical reform of economic

management," this provision establishes an ambitious schedule for the implementation of the measures outlined in the other provisions. According to the schedule, by the end of 1987, the economic system is to be thoroughly prepared to start operating under the new "Law on State Enterprises," and by 1988–89, all enterprises should be actually operating under all the conditions of this law, including full cost-accounting and self-financing. In addition, the provision stipulates that the 13th Five-Year Plan (for 1991–96) is to be drawn up on the assumption that, by the end of 1990, the whole Soviet economy will be operating under the new economic mechanism.

The provision also states the need for upgrading the economic knowledge of personnel and increasing their ability to effectively employ economic methods of management. It calls for restructuring the system of training and retraining, for improving textbooks on economics for higher educational establishments, and for organizing business clubs where enterprise directors can discuss their experiences.

The importance of this provision lies in its instructions to the proper Soviet agencies to codify the provisions and measures outlined in the document, making them legally binding. Once these provisions are codified, they will make it difficult—though by no means impossible—for the opposition to drag its feet in implementing these reforms.

Conclusion

Even if the "Basic Provisions" document is effectively implemented, its impact on the structure and performance of the Soviet economy and on consumer welfare is likely to be limited. It does not redress the fundamental systemic obstacles to economic efficiency that plague the Soviet economy, and it leaves intact the central management of the economy (through planning, financial control, and personnel policies). We should remember, however, that dramatic and sweeping changes in the Soviet economic system are not possible overnight. Economic reform is too complicated and the political opposition to it too great. We should be careful, then, not to judge the success of the "Basic Provisions" in terms of whether the document creates a totally new, decentralized, and efficient economic system for the Soviets, but rather whether it is a step toward that goal. Examined in that light, the "Basic Provisions" seem a more positive step.

On *Perestroyka*: Gorbachev, Yazov, and the Military

Dale R. Herspring

THE SELECTION of Dmitriy Yazov to replace the aging Sergey Sokolov as USSR defense minister on May 30, 1987, though perhaps a surprise to Western observers, was probably no shock to those inside the Soviet military establishment. Not only did Yazov have an excellent military record, but also several years before Mikhail Gorbachev's accession to power, he had taken a public stance in favor of a number of the factors that were to become key elements in the General Secretary's policy of *perestroyka* (restructuring). Beginning in mid-1986, Yazov's support of *perestroyka* caused him to be singled out for special attention in the military press. Indeed, by January 1987, he was being held up as a model commander.

Yazov's selection came at a time when the military's stance was generally less than enthusiastic about *perestroyka*. No doubt, Gorbachev would have preferred to allow Yazov more time to "season," but the landing of a small private West German airplane in Red Square on May 28 of this year left Gorbachev with no alternative. The military had to be held accountable for its actions or shortcomings just like every other segment of Soviet society. The immediate impact of the Yazov appointment has been to intensify the restructuring process within the military. Over the long run, assuming Yazov is successful, *perestroyka* could produce a far more efficient and formidable Soviet military machine.

To understand the context of Yazov's appointment, it is essential to trace the emergence of Gorbachev's

proposals for *perestroyka*, their implications for the military, and the nature of the military's initial response to these demands.

Perestroyka—Initial Reactions

Gorbachev outlined the key elements of his policy of *perestroyka*, or *uskoreniye* (acceleration) as it was called at the time, in his speech to the Plenum of the Central Committee of the Communist Party of the Soviet Union (CPSU) in April 1985, shortly after becoming general secretary.¹ In this address, Gorbachev criticized the Soviet economic system—and especially the party-political apparatus—for failing to keep up with the demands of the times. He called for acceleration of social and economic progress "by making use of the achievements of the scientific-technological revolution and by making the forms of socialist economic management accord with contemporary conditions and demands"

His appeal focused on the need for more effective use of both human and material resources; a more creative approach to management; the acceleration of the tempo of work; and the revitalization of the party apparatus. He also stressed that ideological-political education should emphasize "acceleration of the country's socio-economic development." With regard to the human factor, Gorbachev spoke of the need to reinforce order and discipline, to hold workers responsible for their actions, and to develop a more creative leadership style:

Dale R. Herspring, a Foreign Service Officer with the US Department of State, is the author of numerous works on communist military affairs. He is currently working on a book to be entitled The Soviet Military: From Grechko to Yazov. The views expressed in this article are those of the author and do not necessarily represent the official position of the US Government.

¹"On Convening the Regular 27th CPSU Congress and Tasks Connected with Preparing and Holding It—Report of M.S. Gorbachev, General Secretary of the CPSU Central Committee," *Krasnaya Zvezda* (Moscow), Apr. 24, 1985. (Though the word *perestroyka* appears several times in this speech, primarily in connection with the need to improve management, the emphasis is on *uskoreniye*. *Perestroyka* figures more centrally in subsequent addresses, particularly those to the 27th Congress and to the January 1987 CC Plenum [see below].)