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**The Role of  
Market and State:  
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East-Central Europe**

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## WHAT COMES AFTER COMECON?

*Laszlo Csaba*

### I. Comecon in a Changing Eastern European Landscape

A process of historic transformation has been under way in Eastern Europe. Following the 15 years of seemingly stable political, institutional and economic conditions under Brezhnev, the bold reformatory policies of Gorbachev have brought the previously hidden ills of the Eastern European systems to the light. Coupled with popular pressure and with the growingly unsatisfactory economic performance, the ruling elite of the region face vital choices. Meanwhile institution of unpopular measures could not be evaded irrespective of the declared priorities of the individual leadership. Hopes for accelerated economic growth, as reflected in the five-year plans for 1986-90 have proved to be totally unfounded already after the first two years of the quinquennium. Contraction of overall economic activity, however, has not been followed either by a speedier adjustment of Eastern European economic structures to the external conditions, or by their improved competitiveness on the world markets. Thus the external as well as the internal equilibrium of the Eastern European state socialist systems have come under severe pressure, and they collapsed under the burden.<sup>1</sup>

By the 1990s, multiparty governments emerge on the place of the ossified structures of "real socialism". Even the Soviet Party renounced its pretense of being the single constitutional power in the USSR. German unity is within easy reach. Even the Soviet foreign policy plans its strate-

gy in terms of a united European economic region.<sup>3</sup> Thus practically nothing remained from among the factors which had historically conditioned the existence of Comecon, as a separated entity integrating the mandatorily planned economies. The foundations of a system functioning according to its peculiar own logic of trade and settlements, have been shaken by the historic earthquake. However, the economic intertwining among the CMEA economies has not disappeared. Moreover, conditions and factors constituting the market as a sophisticated instrument of coordination and communication<sup>4</sup> could, of course, not come into being merely by proclaiming the previously forbidden wish: we want the market. The January, 1990 Council Session demonstrated: it is easier to take stock of shortcomings and to declare new slogans than elaborate arrangements into workable new ones. Therefore it seems legitimate to overview in detail why after so many declarations of goodwill the first five Gorbachev years could not actually restructure CMEA.

Beyond doubt, the determinant external factor of the last few years for Eastern European developments has been that of *perestroika*. This truly historic process is characterized by a peculiar *duality in its development*. On the one hand, the radicalisation of analyses as well as of the political approach emerges as the dominant trend in the Soviet Union. On the other hand, the miners strikes (with the strike committees remaining on their place after the industrial dispute is over) as well as the perpetuation of the massive nationality movements signal widespread popular discontent with the actual economic outcomes of the recent politico-economic changes. There's a growing feeling: after five years of *perestroika*, the "years of stagnation" can't be blamed for the entirety of the present difficulties, esp, not for the deteriorating trends in supply (and in the monetary overhang). These unwelcome developments are in sharp contrast to the expectations induced by the initial Gorbachev program of accelerating growth and of providing major improvements by 1990; (as reflected in the quantitative targets of the current five-year-plan).

The duality of Soviet *perestroika* also bears its imprint on the restructuring of the CMEA. On the one hand, even official language has become blunt about the sorrowful state of affairs within the other European integration. Bold, radically sounding plans of creating a unified socialist market in place of the partial intertwining of planning hierarchies has been approved already by the 1988 Prague Session of the Council. Creating the free flow of factors, currency convertibility is on the agenda, and direct

interfirm cooperation should take the place of intergovernmental administration of the pettiest detail in intrablock trade. All this received very appreciative assessment even from some usually critical outside observers, with the UN having spent last year a special chapter in its world Economic Survey on Comecon reforms. The UN analysts qualified the decision on the unified market as "momentous". The respective political decision "has since produced a number of changes that in time may lead to a sharp mutation in integration" (including the developing members).<sup>5</sup> On the other hand, there is a growing skepticism even among traditionally conservative Soviet policy advisors against the feasibility of the forced march towards the unified market with 10 so differently endowed and inclined members. They even put forward the previously heretic idea of forming smaller subgroupings within the integration, that would be ready and able to move towards meaningful market relations.<sup>6</sup> In early 1989 the Hungarian Government has practically abandoned the multilateralist approach to the CEMA, and opted for a bilateral reform with those interested. The Hungarian proposal is to do away with the system of plan-coordination and to switch over to trade in convertible currency in the Hungarian-Soviet exchanges. Either will be Council be capable of reforming itself totally, or it will disappear<sup>7</sup> - noted the youthful Hungarian Premier speaking on the Sofia Session in January, 1990.

But how to reform, even "fundamentally"? In order to be able to deliver an answer, an overview of the attempts of the last five years is justified. Radicality of slogans was not among the shortage items, still the outcomes proved to be modest. Ways and means of actual restructuring might explain this discrepancy to a fairly large extent.

## II. Multilateral Restructuring: Objectives<sup>8</sup>

The initiative to do something sweeping with the multilateral arrangements of socialist integration a mere year after the Economic Summit of 1984, that had been originally meant to set the direction for the long run, has come from the Soviets. It had to do with their reassessment of their entire, domestic and international strategy. The first stage of the new policies included a sharp critique of the intra-Comecon state of affairs. Major organisational changes have been proposed, later calls have been made for the reform of the economic mechanism of cooperation including the free

ing of direct interfirm contacts, furthermore a special program for accelerating technological progress and self-reliance in the high-tech areas has also been adopted. Since several earlier papers have been devoted to discussing these projects, it is appropriate to summarize their outcomes, that proved to be in no relation with the ambitions.

As far as the working style of the *multilateral organs* is concerned, discussions have become more frank, the previously predominant self-appreciative tone gave way to a more realistic style. After heavy infights the number of standing organs has been decreased from 107 to 34.

All this, however was anything but a breakthrough. In most cases previously separately functioning organs have been merged into one, with their profile and competences basically unchanged. Both the Secretariat and the Standing Committees have undergone some slimming cure. However, the basic Hungarian deliberation to do away with all sectoral organs and focus the activities of the Secretariat exclusively on macroeconomic analyses, organisation of consultations on issues of overall economic policies as well as its delivering business services, could not get through. This is at down to two factors:

a) in countries where the reform of the traditional economic model of socialism is not even contemplated-as in Cuba and Romania<sup>9</sup> -the logic inherent in the domestic planning system requires maintenance of the traditional integrational arrangements. These countries advocate as many "concrete", "palpable" agreements and decisions as possible, since this is something which fits into the logic and needs of planning in kind. They also wish to expand the scope of long-term specialisation and cooperation agreements to enhance foresight and thus stability in planning;

b) The Law on the State Enterprise of July, 1987 and the following legislation have *expressis verbis* increased the role of the *sectoral organs* in Soviet macroeconomic management. The laws and decrees of the 1986-89 period, modifying foreign trade legislation have also devoluted competences to the *sectoral organs* rather than to the firms, thus enhancing the former's role in managing external economic relations. This trend and the Hungarian, GDR and Czechoslovak proposals to restrain the activities of Council organs to functional issues proved to be obviously incongruous. Therefore comes the compromise: cutting back the number of organs (to meet political expectations) without seriously curtailing their *competences*.

Among the various *convertibility proposals* two have gained practical significance in the 1980s. The first was the ageold polish proposal,<sup>11</sup>

represented this time by the Hungarians, in which initially 20-25 percent, later a growing share of the year-end balance in payments were to be cleared in convertible currency by the debtor, the Soviets. The second idea is that of using domestic currencies of the CMEA-memberstates for settling accounts. On the 1987 Council Session agreement has been reached in principle among 7 member-states (excluding the non-Europeans and Romania). Accordingly, in the direct interfirm relations domestic currencies may also be used for settling the accounts.

Given the inherently bilateral nature of all intra-CMEA affairs, it goes without saying that separate intergovernmental agreements are necessary to make the multilateral agreement operative. From among these the Polish-Soviet and the Czechoslovak-Soviet agreements are of most interest; some others-as the Czechoslovak-Bulgarian one-have not yet produced relevant outcomes.

The two countries adopted dissimilar approaches. In Poland the official view has always stressed the need for a forced march towards market integration, with convertibility of the domestic currency and direct interfirm deals playing a decisive role. In so doing they gave up theorising about the peculiar meaning and qualities of intra-Comecon relations and integrated these-at least the liberalised part-into the overall system of control. Thus Polish firms could have rouble accounts and were allowed to participate in the incipient Soviet wholesale trade operations. According to their experience, spending these sums encountered immediately difficulties.<sup>12</sup> The shortcomings of the use of national currencies under the present foreign trade regimes is well cognized by some Soviet analysts noting that the arbitrary, bureaucratic bilateral exchange rate, derived from the multilateral Karl-Marx-Stadt agreement of 1973 coupled with the underdeveloped state of internal markets as well as the inherent clearing nature of the bilateral arrangement put severe limits on this method, from the very outset of its application.<sup>13</sup>

Reflecting this realistic assessment as well as the previously very cautious Czechoslovak approach to systemic change, the latter country has instituted an *ob oyo* very restrictive regime of using the national currencies. The regulations<sup>14</sup> effective from March, 1988 underlined the supplementary nature of this area of cooperation. Therefore it could function only for intra-industry direct relations, for R + D cooperation and in occasional, one-time deals. Companies open special Soviet rouble/crown accounts, whose balance is *not* allowed to be transferred to the normal

interstate TR accounts, but counter-deliveries had to be found within the framework of the given arrangement. In other words, a *de facto* barter agreement was the most probable (nearly the only practicable) solution. Experiences above explain the rather restrained Hungarian attitude *vis-à-vis* this particular "convertibility" proposal, which is sometimes<sup>15</sup> seen as inconsistent with the country's long-standing pro-market stance in Comecon. As it is obvious from the above said, the point in these particular attempts was not bringing about the comprehensive set of preconditions to actual monetization of the national economies.

This state of affairs already foreshadowed the fate of *direct interfirm relations*. As it could be seen earlier,<sup>16</sup> the degrees of state control over this form of enterprise activity hasn't shown much sign of fading away. Given the lack of progress towards currency convertibility, companies continued to lack a good compass in their intra-CMEA economic decisions. According to Hungarian experience, the one-sided emphasis on the end-results of a Comecon reform (convertible currency and joint ventures), coupled with the neglect for the organic evolution of their underlying preconditions, have opened the way to one-sided export-expansion of certain large firms. Trying to overcome their severe liquidity troubles some of them formed Hungarian-Soviet "political joint ventures-like Medicor or AZIM-as a covert form of expanding their exports without importing, not to speak of covering the convertible currency input of their sales.<sup>17</sup>

All in all, the very modest outcomes have given ground for *the radicalised reform endeavours in the CMEA* since the 1985-86 concepts have not produced that quick breakthrough which has been expected from them. Following the increasingly radical Soviet initiatives the 1987 Session reached a political consensus on the need for a new integration strategy. This took the form of the Collective Concept of Socialist International Division of Labour for the Years 1992-2005, adopted at the Prague Session of 1988.

### III. The Collective Concept and the Small Countries

The Collective Concept must be seen similarly to its predecessors, the Comprehensive program of 1971 or the Long-Term Target Programmes of 1978-79-as a programmatic reflection of the *common denominator* of the member-states in a given period of time. Being a normative international document, it does not compel any country to institute any specific

measure, but is meant to provide some guidance and framework for conceptual and also practical work on improving socialist economic integration.

The Concept is reminiscent of its predecessors also in its *duality*. On the one hand, it contains six priority areas (those of the Target Programmes plus the non-productive spheres and services), with a *large number of sectoral and subsectoral specialisation and cooperation projects*. On the other hand it possesses also with a general part about the objectives and methods of cooperation, as well as about the need for increased competitiveness and reintegration into the world economy. Except for Romania, the member-states agreed that the long-term objective is a *common market, with free flow of factors and convertible currency*. They also agreed that all these require systemic changes *within* the constituent economies, that will be instituted in a gradual manner.

Given the fundamentally different international environment of today from the post-invasion period of 1989-1971, the Collective Concept-unlike the Comprehensive Programme of 1971-could not even aspire to become a landmark. That would imply closing conceptual debates for one period, while setting the rules of the game for a following stage. In other words, the inherent *instability of a transitory period*, mentioned in the introductory section, did set severe limits to any ambition wishing to mold consciously the state of affairs for a longer period. With the political earthquake of the last quarter of 1989 the meticulously equilibrated programmatic document has, of course, lost its residual relevance. The deepening recession, and the politico-economic reorientation of the European member-states rendered the Collective Concept obsolete by the time of its official take-off.

But what did the small countries look for? In short: obviously everyone is after something else. The East Germans-even nowadays-and the Romanians-traditionally-long primarily for stability to be provided by obligatory longterm interstate agreements, that could be built into the system of macroeconomic balances.<sup>18</sup> And conversely, talking about coordination of plans at the company (combine) level, GDR authors air their concern over the growing instability (implying also effects of decentralisation) that makes the mutual preliminary determination of effective demand extremely difficult for the period up until 1995.<sup>19</sup> Similarly, the Romanian premier called for signing as many detailed concrete programs for cooperation, implying long-term interstate agreements as possible. Moreover he disapproved attempts to orient the multilateral organs towards "abstract" (functional) problems, while he saw their job in preparing as

many tangible cooperation projects as possible.<sup>20</sup> A further commonality in the position of the two countries is their doubt in the use of direct interfirm relations in other forms than subordinate to the state-administrative methods.<sup>21</sup> The justification for this stance is different: while in the GDR there is a tendency to interpret direct relations as a long accomplished objective (implying the subservient role of combines to various forms of state trading), Romanians reject the idea as such in any form other than stipulated by their national legislation. As far as the latter is concerned, the Romanian regulations effective since the summer of 1988 severe the sanctions for deviating from the plan-contracts. Accordingly, if a foreign trade contract results in a loss, or the product is unsalable, or the contract deviates from the targets envisaged by the plan, it is considered to be a criminal act (and will be persecuted accordingly). Moreover, launching production for exports is allowed only after the foreign trade contract has been concluded. The latter arrangement precludes even those limited and tentative forms of doing business directly that have been allowed by the Soviet legislation since several years.

There is some difference in emphasis and style between the two countries over the issue of the unified socialist market and currency convertibility. While the Romanians until recently flatly rejected the very idea at the highest political level, and even after the revolution consider participation in it for themselves as premature the GDR has adopted a *more sophisticated approach* of saying no. They chose to support studying the preconditions for a common market, and only after each and every of these conditions have been met (suggesting explicitly a more or less complete saturation of each domestic market), would they support the implementation of the very target.<sup>22</sup>

In an early sign of the later thorough changes (and present governmental policies in East Berlin), the first article ever favouring convertibility has been published in spring 1989 in the GDR. In his professorially comprehensive and abstract article<sup>23</sup> Hans-Joachim Dubrowsky made three rather unconventional steps: a) he comes out unambiguously in favour of convertibility of the national currency of the GDR; b) he surpasses the conventional narrow approach of limiting discussion to terms of financial techniques and interprets the whole problem as a systemic issue; c) he advocates foreign economic opening as an institutional, qualitative change against the traditional planning model. As he formulated it, the use of convertible currency will enable direct interfirm relations to become the

dominant form of international economic intercourse, both with the East and with the West.

Up until very recently a somewhat similar duality seem to have characterised the *Czechoslovak approach*. The official line of the last Communist government was critical but extremely cautious. This co-existed with a sizable frank, competent and sometimes openly reformist scientific output, whose tone has long been among the most critical within the CMEA. This duality was explicable with the divided domestic political scene. One faction-as e.g. former Deputy Premier Obzina,<sup>24</sup>-saw Czechoslovak participation in the CMEA basically as a political issue, to which there's no alternative. They reiterated-without explicit reference-the position taken by dr. Gustáv Husák at the 1971 party Congress having declared that CMEA is the guarantor of the "class-political stability of our republic".<sup>25</sup> In this "good or bad, my integration" attitude the adverse effects are seen either as minor nuisances, or-as in a recent article-easy to overcome through systemic change. No matter, how badly it is functioning, the CMEA remains an irreplaceable source of fuel, energy and technology for the Czechoslovak economy-sounded their conclusion.<sup>26</sup>

This position, however, was far from being uncontested even under Milo Jakes. Influential analysts-now in the coalition government-advocated already in 1988-89 an opening to the world economy, economic reorientation; moreover they saw it as a precondition for any meaningful structural adjustment and reform program.<sup>27</sup> In this-today official-perspective the immanent shortcomings of the traditional model of intra-CMEA relations are anything but secondary. Reform-minded Czechoslovak economists pressed for radical systemic change within their country, also as a precondition for integrational success. Reality of prices depend not only on subsidies, but also on the economic actors freedom to choose: thus the way out is the use of directly negotiated prices set by companies, while eliminating interstate obligations-sounds one proposal.<sup>28</sup>

Others explain: for a common socialist market a fully-fledged domestic market is required, and then integration in production would emerge only if free interfirm deals actually dominated intra-CMEA deals.<sup>29</sup>

The *Bulgarian approach* is ambiguous due to the protracted domestic imbalance of forces even after the demotion of Zhivkov. On the one hand, the attempts to do away with mandatory planning and the related critical theorising is more than a decade old in Bulgaria. On the other hand, various elements of state administrative control continue to dominate manage-

ment practice. As one Bulgarian observer noted<sup>30</sup> all changes in the 1978-88 period were constrained to reorganising the upper management levels, whereas fundamental features of entrepreneurship, the quality of macroeconomic environment for companies remained unchanged.

On the other hand, Bulgarian changes lacked until 1990 not only the political (*glasnost*) elements of Soviet reforms, but also their radicalising tendency. While increasing the use of market-type instruments, various elements of state administrative control remain also in force and this state of affairs does not seem to have changed amidst the turbulent political scenes of 1989/90. This has an immediate bearing on the Bulgarian approach to Comecon.

For one, the previous Bulgarian premier<sup>31</sup> blamed the predominance of outdated administrative approach to integration problems for the very modest progress of Comecon reforms in practice (despite the agreement in principle, reached on the 1987 Session to adopt a promarket approach). He called for qualitatively new ways and forms to secure a continuous and more efficient coordination of various interests, whose conflicting nature has recently become conspicuous. On the other hand, his former deputy-and now successor, Lukanov-interpreted and evaluated the Collective Concept much in the same manner as the GDR and Romanian officials of the time. He believed that the list of concrete tasks and cooperation lines were the good thing in it, as these provided the backbone of a CMEA-wide coordinated structural policy.<sup>32</sup> True, he had also appraising words for market instruments of integration, and called for solving the price problem as part of a wider systemic change.

Favourable evaluation of the theorem of comparative advantages, rejection of their earlier course of self-reliance (favouring "comprehensive structures") is an important novelty of the Bulgarian development strategy. As part of the up-to-date approach, emphasis on the role of the tertiary sector as well as focusing on microeconomic rather than macroeconomic interpretation of structural change is a major novelty of the Bulgarian thinking.<sup>33</sup> This view is well complemented by the radical, clearly free-marketeer interpretation of the socialist common market, requiring a radical systemic change in the existing model of CMEA cooperation. The remarkably strong side of the twelve points program of Petkov<sup>34</sup> is its approaching marketising reforms as a package that can not be instituted in a step-by-step manner, or in fragments. "Conditions for the victory of socialism can hardly be in neglecting the objective laws of the economy".

concludes the Bulgarian analyst.

Turning to Poland two conditions should be mentioned before discussing integration policies proper. First, owing to the prolonged economic and political crisis, Poland's indebtedness *vis-à-vis* its Comecon partners continued to grow, despite her improved terms of trade in the post-1986 period. Therefore in 1988 Poland had to reschedule its debts of 2.4 billion \$(of which 1.4 billion is owed to the Soviet Union).<sup>35</sup> Second, in Poland it is a widely shared view that CMEA is primarily a political organ which is quite impotent in economic matters; on the top of it each country is much more concerned with its own headaches than with improving the multilateral fora.<sup>36</sup>

Polish authors<sup>37</sup> always had second thoughts whether the political breakthrough attained at the 1987 Council Session in favour of the socialist common market was a real one. Therefore they stressed the formal nature of novelties, including the use of national currencies, or of expanding direct interfirm relations in Polish-Soviet trade. Until a thorough and systematic liberalisation does not take place, the age-old hindrances to cooperation will remain effective sounded the consensus view.

It must be said, however, that contemporary intra-Polish systemic changes did not quite support this verbal radicalism. Many of the very radically sounding-or intended-measures have remained formal under Polish conditions, like the abolition of the system of material-technical supply, or even freeing prices.<sup>38</sup> The above quoted authors demonstrate: as money can't actually be spent on commodities, doing away with administrative rules imply only the further disintegration of market, not a healthy economic equilibrium.

One also wonders why Polish thinking on CMEA follows so traditional paths. As well documented by a relatively recent Polish-Soviet meeting the fight for maintaining the interindustry pattern of trade (implicitly the present level of Soviet fuel supplies), the quest for getting extra Soviet inputs to run idle Polish industrial capacities (the core idea of the reorientation strategy of 1982-83), the political approach to joint ventures seem to dominate, leading to the support of most Soviet initiatives at a very general level. This policy line seem to have prevailed during the 45th Council Session in January, 1990.

A peculiar paradox seems to be characteristic of the Polish attitude. On the one hand, the Mazowiecki Government has opted for a clear-cut reorientation strategy both in political and economic terms. As part and parcel



of this approach, the Balcerowicz Plan has already created the "internal convertibility" of the Zloty, and has gone cut of its way to dismantle the command planning system. On the other hand, there seems to be a certain disarray over what to do with trade with the East. Interestingly the Poles seem to have agreed to introduce a 10-15 percent share of their bilateral trade with the Soviets to be conducted in convertible currency. This is anything but a reform-step, as experiences of Hungary over the last 15 years have amply demonstrated. On the other hand, the elimination of the entire quota system in the Polish-Hungarian trade will be a small but relevant change inside the overall intrabloc trade.

#### IV. From the Theoretical Quest for the Market to Real Market-or Just Another Change in Terms of Trade?

The real sensation of the January, 1990 CMEA Session was that the Soviet Premier proclaimed this time in a fully official form<sup>39</sup> that the Soviet initiate a switchover to trade in convertible currencies with their CMEA partners from 1 January, 1991. The proposal *per se*, as well as its implications in any variant of interpretation certainly conclude a historic process and open a new one. The pillars of Comecon: isolation from the West, reliance on command planning as a basic method of organising international exchanges as well as the concomittant use of inconvertible clearing units, have ceased to exist. This completes the process of general rethinking at Soviet policies in the domestic, foreign, economic, military and ideological areas alike. The process of strategic reassessment has been going on for years, and as the convergence/culmination of politico-economic renewal this decision was only to be expected for some time.<sup>40</sup> In Fact, the idea to trade in hard currency has originated in March, 1989 from the Hungarian side, when this was officially proposed on a bilateral top-level meeting between the leaders of the two Communist Parties. But as it is common knowledge, if two state the same they rarely mean the same. This applies to our topic-an issue we shall discuss below.

First let's have a glimpse over the Hungarian stand, and let's try to look into the motives of this small country in initiating what conventional wisdom would interpret as a Soviet threat to her best economic interest.

In fact, the view on Comecon counts among the very few on which he enjoyably controversial Hungarian economist profession and even

officialdom reached a *de facto consensus* (some lonely outsiders and vested interest apart). This view has been expressed in numerous publications of this and other authors, the most concise version being the statement of the head of the Hungarian delegation, speaking on the 1988 Prague Session of the Council. Accordingly<sup>41</sup> the socialist community managed to find an appropriate answer to the military challenge of our age, not, however one for the economic and technological challenges. Accomplishing a radical change in the present model of cooperation is long overdue, otherwise *membership in the CMEA will become a hindrance rather than a help to overcoming the economic malaise in the constituent economies*. Though the requirement to modernise finances is two decades old, still stagnation has been the characteristic feature of this field. While grandiose statements are being made over the need to reform, in reality not even minor technical improvements are being accepted. Thus the ideas of a free trade zone, of customs and/or currency union have a set of preconditions which may emerge only in the very distant future. It must be understood that the market can't be declared by *fiat*, nor can it be substituted by instituting administrative measures. There is a inherent logic in how certain elements of a monetary and other elements of the management system constitute a market; these can't be escaped or partially implemented.

What is the wayout? Since for a small country there is no alternative to taking its external environment as it is, rather than moaning about unwelcome developments it is compelled to adjust to it by drawing the conclusion from this state of affairs. To put it in a nutshell, the pressure for overall consolidation in the Hungarian economy has grown so much, that the country surely has no time to wait untill the multilateral system of CMEA integration will become ready for a market-type reform. True, thereby Hungary foregoes abstract-but never realised-advantages of reintegrating into the world economy as part of a regional community, but meets the very pressing needs of her society, creditors and business partners.

"Going alone" implies three separate issues. First, Hungary obviously has to give up the very idea of *converging* her economic system to its CMEA partners in any conceivable form. Second, within the CMEA, a *case-by-case bilateral approach* to partners must take the place of the multilateralist approach of the last two decades. Third, if the CMEA region remains to be one of economic strains, further the systemic modernisation-in its practical outcomes and impacts-remains a limited one, a strategy of *reorientation* must become a centerpiece of the current reform policies.

Thus there's no coincidence that already the first draft of the current reform project<sup>42</sup> contained these three elements, laying special emphasis on the need to abolish the system of interstate obligations in trade with CMEA partners. With the time passing these elements have gained growing relevance for the entire reform-package's point of view.

It is beyond the subject of this paper to elaborate on the policy of re-orientation as well as on the most recent Hungarian reform projects. Therefore I shall constrain myself to the Hungarian concept of the way our *relations to Comecon partners could be reformed so that they fitted to the emerging fully fledged market economy*.

This comprehensive and far-reaching issue has been a subject of hested debates<sup>43</sup> in several working groups as well as in the economic press over the last year. Over and above the remaining numerous differences of various importance, the following points have been accepted:

a) Hungary can by no means afford taking art in the current round of plan-coordination for 1991-95 "as if nothing happened", since that would emasculate the radical marketising approach within the country before its inception;

b) the whole arsenal of interstate trading should be eliminated or cut back to a marginal role, with rewards and risks of "trading with the East" being devoluted to companies;

c) in such a radical change Hungary will incur sizable losses, still it has to be instituted no later than in 1991. Otherwise the opportunity would come first in 1996 which is much too late for a reform whose point is to contribute to the consolidation of the Hungarian economy during the years of its Western balance of payments crisis, in 1991-93. In case of postponing action the direct losses due to the sizable Hungarian surplus in TR in 1987-92 to the high convertible currency contents of Hungarian sales for TR, coupled with dynamic losses of a stagnant macroeconomic structure and its direct influence on Hungarian exports to the West, together would outweigh the undoubtedly high cost of transition to a non-state trading régime.

d) Introducing real market relations in both previously protected markets of the Hungarian producers will probably bring a dozen or so large and influential firms into the red. This cost must be partly born by the government, launching a program of modernisation and reorganisation of these, involving Western direct investment, the expertise of international consulting firms as well as of specific financial support of the IMF/IBRD.

What would the switchover to trade according to real market principle imply for Hungarian-Soviet trade? First and foremost the filtering out of elements or traditional overtrading thus the inevitable process of shrinking exchanges will integify. However, this would most probably occur also under traditional arrangements, given the markedly growing structural incongruity of mutual demand (already revealed during preliminary plan-coordinating talks). Second, the majority of interfirm relations would remain *de facto* barter deals. This might be inevitable under the growing shortage phenomena on the Soviet market, but I do not see any wrong with it. The point is to delegate risk to the companies thus decentralising the problem. According to several opinion polls<sup>45</sup> conducted among large exporting companies, introducing trade in convertible currency would not have a sweeping one-way "dragging out effect on all Hungarian firms from their Soviet market, but the impact would be differentiated. Most major exporters are confident in their ability in maintaining a significant chunk of their present sales, among others for lack of comparable competitive offers. Third, as on the macroeconomic level the Soviets would most probably win in the short run, this secures their overall favorable stance on the issue. Fourth, be that cash or barter, the Soviet supplier in this case has got an immediate stake in doing business with the Hungarian partner. Therefore the actual binding force of these interfirm deals is bound to be far superior to that of any interstate clearing operation (even if the latter is signed by top-level politicians). *Securing Soviet interest in exporting under deteriorating domestic market conditions and conformity with the overall domestic market order to be instituted soon in Hungary* are the two decisive strong points of this option.

This fundamentally systemic approach has resulted in the official Hungarian proposal<sup>46</sup> to form a "small integration grouping" among the radically reforming pluralist countries: Hungary, Poland and Czechoslovakia. The idea draws on the West-European initiatives at two-phased integration (*intégration à deux vitesses*) which emerged at the time of enlargement of the EC. It is thought that those willing and ready could form a closer community than the very diverse respective trade blocs.

It is worth noting that partly due to its political undertones this basically rational idea has not materialised in the EC either. Moreover in the Eastern European region parallel shortages and parallel overproduction as well as parallel factor endowments prevail. Therefore the scope for "small integration" as a third way (between East and West) is inherently limited.

Overplaying this idea the press might awake a false illusion and divert public attention from the inevitability and the fundamental nature of the need to adjust to Western markets.

In the course of bilateral consultations that followed the Sofia Session it has been cleared that the initiative is *not* meant to establish a new integrational organisation, a free trade zone or a customs union. The point is a more intensive and regular exchange of policy experiences among the reformist states. In fact, as it has turned out already at the January, 1990 Council Session the task of how to cope with a qualitatively unreformed main trading partner is a common policy puzzle for the three countries facing otherwise different<sup>47</sup> problem.

It is no secret that the government program of Premier Ryzhkhov for the years 1990-1995<sup>49</sup> contains a postponement of radical reform measures. In this logic, in the first phase of 1990-92 the prevailing shortages in the Soviet economy should be overcome, primarily *via* administrative measures. Only after having consolidated the domestic market, should in 1993-95 the really biting pieces of economic reform be introduced.

Whatever are the causes and motives, this option is bound to have an immediate bearing on Soviet foreign trade reforms. The "transitory measures" of 13, March, 1989, suspending most of the liberal December, 1988, foreign trade decree have been complemented with new restrictions.<sup>50</sup> In order to protect Soviet domestic consumers as well as to counterveil the flourishing speculation based on enormous arbitrage potential stemming from grossly distorted Soviet domestic prices, administrative and police controls have been strengthened over all those trading abroad. Therefore the stipulations of the 1987 Law on the State Enterprise and of the December 1988 decree on generously granted foreign trade rights to each Soviet company surely won't shape the Soviet foreign trade mechanism in the first half of the 1990s. The uniform exchange rate, rouble convertibility and the like remain basically subjects for theoretical elaboration.

Therefore the basic of the Ryzhkhov proposal to trade in convertible currency with Eastern Europe is obviously the wish to capitalise on the terms of trade gains resulting from the change in settlements. I do not see any wrong in it, as normally no deal is being struck unless your counterpart also has his gain. The trouble may arise, however if the tentatively formulated proposal implies merely a change from one type of clearing to the another. The latter interpretation may follow from the Soviet Premier's emphasis on the structurally determined Soviet demand *in kind*, with

special regard to agriculture, pharmaceuticals and industrial consumer goods.

It should be quite clear from the above said that the current real economic crisis situation is absolutely unfit for any form of trade that would be based on long-term interstate agreements of whatever sort. The point is precisely in getting rid of the *ex ante* fixing of deliveries and state-trading in general. This is the objective for which a marketising economy could and should pay the price of terms of trade losses. Looking from the Soviet perspective, it should certainly cause no problem from the point of macroeconomic control to group six countries from among the clearing relations to the hard currency area. On the other hand as it has been pointed out in due time<sup>51</sup> it is certainly unrealistic even to have postulated that the six small CMEA countries could extract an annual combined surplus of 10-12 billion dollars in 1991-93<sup>52</sup> just because for mildening Soviet domestic macroeconomic imbalances it might be just as well to dispose of these sums. Such an approach, which can't entirely be excluded, could best be taken as a conventional bargaining card of Gosplan in a usual intra-CMEA poker game rather than a serious business offer, or an attempt to "reform".

All in all, in the coming months and years a lot of expert-level talks as well as independent analyses will have to be conducted in elaborating the precise mechanism of introducing trade in convertible currency in the place of state-trading in the CMEA. Lots of tentative proposals and speculations float around. Pressing practical issues as the conversion rate of rouble surpluses into dollars are still to be elaborated. As it is no novelty whatsoever for Soviet economists as well in market economies the state administration normally has no prerogative to deal directly abroad, leave alone to settle the macroeconomic proportions of international exchanges. Therefore, whatever are the (very) short term Soviet commercial policy deliberations, CMEA as it had existed for four decades with its long-term obligatory delivery agreements signed at the level of a Premier is not any more among us. And what comes next? Trade, among geographically close, traditionally intertwined, differently endowed economies will probably still flourish, and at a smaller, economically sound level it will certainly survive the collapse of its previous ossified institutional arrangements.

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## STRATEGIC AND ECONOMIC ISSUES AND TRENDS IN EAST-WEST RELATIONS — A KOREAN PERSPECTIVE —

Whee Mok Roh\*

### I. Introduction — Threshold of a New Era

Periodic declarations of a new day of harmony between the East and the West have been an important theme of the postwar period. As the decade of the 1980s drew to a close, the United States and the Soviet Union appeared finally to have resolved their forty-year-old conflict. At the Malta summit between Presidents George Bush and Mikhail Gorbachev, they showed a convergence of American and Soviet positions on most agenda items. It seems that their bipolar competition will end and good relationships will develop with minimum tension, bringing a major peace dividend for both economies.

An epoch-making improvement in Soviet-American relations has already occurred, and even more dramatic improvement seems possible as the U.S. is losing its hegemony in the West and the Soviet Union is stagnating economically.

Gorbachev's capacity to play the game by the old rules has been crippled by the failure of the Soviet economy and the crumbling of communist rule in Eastern Europe. Hoping to overcome internal and external problems, he has launched the most ambitious, sweeping, and promising program of reform in the history of the Soviet Union. What is now occurring within the Soviet Union has opened the possibility of a new era in international relations.

\*Dr. Whee Mok Roh passed away in a tragic traffic accident in 1990.