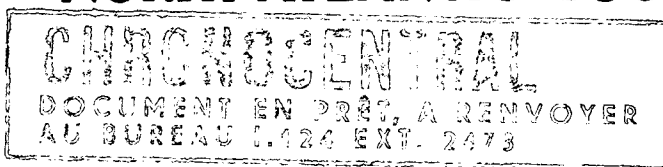


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RECENT ECONOMIC DEVELOPMENTS IN THE
GERMAN DEMOCRATIC REPUBLIC (1971-1972)

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Note by the Chairman of the Economic Committee

The Economic Committee examined the recent developments in the GDR on the basis of a report submitted by the German Delegation and with the participation of experts from capitals.

2. The attached short report, which summarizes the main findings of the Committee, is submitted for the information of the Council.

(Signed) Y. LAULAN

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RECENT ECONOMIC DEVELOPMENTS IN THE
GERMAN DEMOCRATIC REPUBLIC (1971-1972)

REPORT BY THE ECONOMIC COMMITTEE

SUMMARY

1. The German Democratic Republic is, economically, the most advanced of all the East European countries linked to the Soviet Union. Its population has a long tradition of general and specialized education, its industry and agriculture are well developed, its standard of living is the highest in the Communist world. The long term trend in the COMECON area is for the less developed countries gradually to catch up on the more developed, and East Germany, like Czechoslovakia which also started the post-war period with certain advantages in economic maturity and tradition, has lost some ground relative to countries now in process of industrialization. According to COMECON figures, which may slightly exaggerate overall advance, the percentage growth in the net material product over the decade 1960-70 was: DDR 52; Czechoslovakia 53; Hungary 70; Poland 80; USSR 98; Bulgaria 110; Romania 123. The ultimate effect of this trend would be that Poland would become the most important country of the Northern countries, Romania of the Southern. Understandably the East German leaders have sought to preserve as far as possible their country's industrial preeminence in the Communist world. It is perhaps partly because of this that they have shown particular care to co-operate with the USSR.

A. THE LABOUR PROBLEM

2. One of the chief problems facing the DDR has been the labour situation. Whereas the other COMECON countries have, at least until recently, had abundant labour to pursue their policies of industrialization, the DDR has been handicapped by a shortage of labour from the start.

3. Previous to 1961 there was a constant outflow of population from the DDR to the Federal Republic, particularly amongst the young. After the building of the Berlin Wall this loss of manpower was arrested, but the position was, at best, stabilized.

4. Over the period 1960-71 there was an actual decline in total population and the number of people of working age but owing to increased participation rates there was a very slight increase in the number of those actually employed.

	<u>1960</u>	<u>1965</u>	<u>1971</u>
Total population (thous.)	17 188	17 040	17 042
People of working age (")	10 542	9 916	9 870
Number actually employed (")	7 686	7 676	7 804

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5. This stabilization in the labour force has been entirely due to the increased participation of women in economic activity. Whereas the female element of the working age population declined gradually from over 54% in 1955 to 50.06% in 1971 the proportion of women actually employed has consistently risen: 44% in 1955, 45% in 1960, 46.7% in 1965, and 48.7% in 1971.

6. The tight labour situation should be taken into account when comparing economic performance in the DDR with other countries: practically all the not inconsiderable rise in output is due to increased productivity. The East German leaders admit that it will be almost impossible to increase the labour force either through increased participation or immigration and accept that growth will continue to depend on rising productivity.

B. INSTITUTIONAL PROBLEMS

7. Another major handicap to economic progress in the DDR, shared incidentally by the CSSR, has been the need to operate within an institutional framework similar to that of the USSR, which is particularly unsuitable to already developed countries. It is true that the process of full socialization was delayed in East Germany. In July 1963 the East German leaders introduced the "New Economic System", the first of a series of measures extending up to the present, by means of which they hoped to provide a degree of flexibility which would give scope to the initiative and disciplined imagination of the German worker while maintaining the necessary degree of ideological conformity.

(a) Planning and Control

8. The main idea was to streamline the system of central planning. The centre would retain overall control, but the VVBs, i.e. the "Vereinigungen Volkseigener Betriebe" were to get considerably increased powers and operate as links between the state planning authorities and the producing enterprises (VEBs). These latter were required to operate on business lines, but were subordinated to the VVBs. Economic criteria, and economic incentives were accepted, and a large measure of actual decision at the level of the VVBs was envisaged. However the recreation of a market mechanism was not aimed at and the VVBs operated simply as government-owned monopolies.

(b) Prices

9. An important aspect of the reform was the rationalization of the price system which was undertaken in several stages from 1964 to 1969. The first step was to increase the nominal value of capital assets by about 51%. Then the price of a large number of raw materials was raised, on the average by some 70%; the price of another range of material was increased on an average by 40% and

some equipment by 4%. Finally in 1969, the prices of some commodities were somewhat lowered.

10. Retail prices were not affected by these changes, the purpose of which was to make prices reflect more faithfully real costs. Most retail prices were high already owing to turnover tax. Services such as housing and some commodities are subsidized, and it would be rational to raise such prices. However, the experience of Poland in December 1970 shows that price readjustment in this area is dangerous.

11. By 1969 the VVBs were supposed to fix about two-thirds of all prices, the ministries the remainder. The idea of price flexibility was partially accepted, a small margin for negotiation was allowed in the case of VVB prices and there were a few prices which could be fixed by arrangement. In principle the reform implied that there would be gradual price changes according to circumstances.

(c) Banking

12. In January 1968 the banking system was modified. The Deutsche Notenbank was set up with the functions of a central bank, while the Industrie und Handelsbank was intended to provide investment finance and short term credits.

13. Although the producing enterprises, the VEBs, had little real independence, it was intended that they should be dependent for further investment capital on their own profits and on bank finance so that they would be induced to make the best use of resources. The influence of the banks was circumscribed in so far as, generally speaking, they could only grant credits in accordance with the Plan.

(d) Foreign Trade

14. Steps have been taken to interest enterprises in foreign trade. Whereas hitherto the foreign trade organizations operated only on behalf of the Foreign Trade Ministry, they now operate on the behalf of other ministries, VVBs and certain combines. The financial position of the enterprise is influenced by its export earnings at least indirectly, that is, after certain adjustments such as differential exchange rates, export or import subsidies, have been taken into account.

(e) The Ulbricht Initiative: ESS

15. A fresh impetus was given to the reform movement in 1967 when Ulbricht associated himself with what was called the Economic System of Socialism which was presented as the special contribution to Socialism by the DDR and as a model and guide to other COMECON

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countries, including the USSR. Ulbricht was critical of the performance so far achieved by the VVBs and he made himself the spokesman of the new scientific approach which was supposed to characterize the system introduced in mid 1968. Considerable stress was laid on the use of economic levers to control the economy and on the use of computers to feed back information to the centre on the basis of which economic decisions could be taken and prices altered. Great importance and priority in investment was given to certain industrial branches which were to determine the future structure of the economy and provide a channel through which advanced techniques would reach it.

(f) The Retreat to Orthodoxy

16. Towards the end of the decade the DDR ran into a series of economic difficulties which jeopardized the fulfilment of the 1966-70 plan and necessitated some painful adjustments in 1971. Between the Party Congresses in September 1970 and June 1971 there was, parallel to the gradual elimination of Ulbricht from the leadership some quite frank criticism of official policy and certain aspects of the reform. At the turn of the year a series of measures appeared which altered the reforms as follows:

- As against the concept of a plan consisting of a limited number of directives - the VVBs having the task to fill in the details, there was a return to the old system of planning, detailed instructions being handed down to enterprises month by month.
- As against the concept of control of the economy largely by means of economic levers (investment and price policy) there was a reversal to the system of direct central control.
- A price stop has been decreed for consumer goods and effectively applied elsewhere. Price fixing has been reassumed by the state and the idea of gradual adjustment disavowed.
- There was a retreat from Ulbricht's concept of the DDR enjoying a special place in COMECON, instead there was renewed emphasis on the need for DDR integration in the COMECON system.
- There was a retreat too from some of the "scientific" aims of Ulbricht. There is to be less reliance on computers and cybernetics, more on the Party.
- A new set of planning targets has been proposed, more realistic no doubt, to correct the disproportions that had emerged.

(g) Further Socialization

17. Possibly to stress the fact that the present East German leaders do not wish to emphasize their difference from the other socialist countries, there was in 1972 a socialization drive which resulted in the elimination of practically all the remaining private and semi-private firms in industry. The scope of this upheaval can be judged from the following figures:

DDR Industry 1971

	<u>Number of firms</u>	<u>Employees (thousand)</u>	<u>Output (Milliard marks)</u>
<u>Industrialized Enterprises</u>	11 253	2 825	159.3
- Socialized	2 619	2 410	114.8
- Other	8 634	415	17.5

In 1972 10 500 new VEBs were created - from the former private and semi-private firms and certain industrial co-operatives. Over 400 thousand people previously employed in these firms were absorbed into the state labour force.

C. ECONOMIC PERFORMANCE

18. Economic performance in the second half of the decade 1960-70 is claimed to have been decidedly better than in the first half, which was due partly to the plugging of the manpower gap and partly to the positive effects of the reforms. The figures below show percentage increases over the two periods.

Increases (%) over Five Year Periods

	<u>1961/65</u>	<u>1966/70</u>
Net material product	19	29
Industrial output	33	37
Investment(1)	40	52
Retail Trade	14	25

19. Despite the improvement relative to the earlier period it is admitted that results of the 1966/70 period were not entirely satisfactory. Particularly towards the end of the decade dangerous trends came to light which were frankly discussed at the Party Congress in autumn 1970, and again in June 1971 in a way which implied criticism of Ulbricht's policy.

(1) Percentage increase over the previous Five Year Period

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20. The most obvious mistake made had been to concentrate investment too much in the priority sectors, chemicals, electronics engineering, and to neglect raw materials, fuels and transport. The severe winters of 1968/69 and 1969/70 had shown up the grave consequences of this policy.

21. Much attention was given to the emergence of "disproportions" in the economy. This simply means that alongside good performance in certain sectors and in respect of certain products, materials or components, there is a shortfall in the production of other items perhaps equally important as regards overall performance. This is a fairly common feature of the Soviet system of planning and control, which it would seem that the reforms adopted in the DDR at this time did not succeed in eliminating.

22. Under the impact of this experience and no doubt influenced by the Polish unrest at the turn of the year 1970/71 the new 1971/75 plan as eventually accepted was rather modest.

Increases (%) planned for 1975 relative to 1970

Net material product	27
Industrial output	34
Productivity	35
Investment(1)	29
Retail Trade	22

23. There was a notable cut back in investments relative to the previous period and as in the Soviet new Five Year Plan great stress was laid on improving consumer standards.

24. The year 1971 was obviously envisaged as a period of consolidation. Decidedly modest targets were prescribed - particularly as regards investment. Performance in many sectors did not come up to expectation. Agricultural output was down owing to bad weather. Although the retail trade turnover was reported to have been higher than the target set, there were shortages of certain consumer goods.

25. After the pause in 1971, the economy recovered somewhat in 1972. The goals set remained moderate, but many of them were surpassed. This applied particularly to the material product and industrial output. Agriculture too was very satisfactory. It would be a mistake, however, to assume that the problem of "disproportion" has been overcome.

(1) Attention is called by the German Delegation to the fact that whereas normally the index numbers of growth given in the Plan represent output or performance envisaged in 1975 relative to 1970, in the case of investment it is the total for the period 1971/75 which is planned to be 29% greater than the total of the period 1966/70. Investment in 1975 would be only some 13% more than in 1970.

Plan and Performance in Recent Years
Annual Increases (%)

	1971/75 Plan	1971 Plan	1971 Result	1972 Plan	1972 Result	1973 Plan
Net material product	4.7-5.1	4.9	4.5	4.6	5.4	5.7
Industrial output	6.0-6.3	5.6	5.5	5.5	6.3	6.5
Productivity in Industry	6.2-6.5	5.4	5	5.7
Investment	5.1-5.4	-1.5	0.6	2.0	3.0	9.0
Retail Trade	3.9-4.2	2.4	3.9		6	
Foreign		8		12.5		14

26. Judging by the 1973 targets, the DDR authorities are quite optimistic about prospects this year. In particular an increase of 9% in investment has been envisaged. It would appear that given the atmosphere of détente, a big increase in imports is expected which temporarily might provide the extra resources for investment or consumption. The forging of relations with a large number of countries and international organizations naturally improves the prospects for foreign trade from which the DDR economy must on balance benefit and which might yield some positive initial advantages.

D. FOREIGN TRADE

27. In the immediate post war years a policy of near autarchy was pursued in Easy Germany, but since the early fifties increasing importance has been given to foreign trade, which is now recognized as a factor promoting economic growth, and the volume of which is rising at a faster rate than the national income. In 1960 trade turnover was 18.5 milliard valuta marks; this rose to 24 milliard marks in 1965 and 42.2 milliards in 1971. East Germany's share in world trade was about 1½% in 1970, a proportion comparable with Australia's. Its turnover was about 2/5 that of the USSR and 40% greater than that of Poland or Czechoslovakia. Expressed in terms of value per head of population, East Germany's trade was the most important in COMECON. Imports in \$ per head of population was: DDR \$284; CSSR \$255; Hungary \$238; Bulgaria \$211; Poland \$110; Romania \$97; USSR \$48.

(a) Geographical Pattern

28. The geographical pattern of East Germany's foreign trade has changed relatively little over the last decade; there has been a slight shift from trade with Socialist countries to that with the industrialized countries of the West.

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Geographical Distribution (%) of DDR Trade

	<u>1960</u>	<u>1965</u>	<u>1971</u>
Trade Turnover milliard VM	18.5	24.7	42.2
as percentage	100	100	100
<u>With Socialist countries</u>	75	74	72
USSR	43	41	38
Other COMECON countries	25	28	29
Other Socialist countries	7	6	5
<u>With non-Socialist countries</u>	25	26	28
Industrialized countries	21	22	24
Federal Republic	10	9	10
Other Western countries	11	13	14
Less developed countries	4	4	4

29. About two-thirds of East German trade continued to be with other COMECON countries. The role of the USSR though slightly less than formerly is still dominant. There is little prospect of any notable change of pattern, indeed it was written into the current Plan that priority is to be given to trade with COMECON countries especially the USSR, in accordance with the long term trade agreements already concluded and in line with the policy of division of labour and co-operation within COMECON in respect of science, technology and production. This policy was emphasized in the agreement on the COMECON Complex conducted at Budapest in July 1971.

30. The share of total trade going to the West is rather smaller in the case of the DDR than in that of most other COMECON countries but it is increasing. This trade is particularly important economically as it provides access to Western technology, and supplements planned production in the DDR and the bloc and helps to overcome bottlenecks in production.

31. Intra-German trade is the most important element of trade with the West. In volume and composition this trade is not particularly important to the Federal Republic; to East Germany however it provides a convenient and very flexible market which can absorb plan surpluses which help to buy commodities, especially materials which are scarce. Incidentally the share of machinery in this trade is relatively small, greater emphasis being put by East Germany on materials.

32. Trade with other Western countries has grown proportionately to overall trade expansion. There has been considerable fluctuation in the flow of trade with particular countries.

33. Trade with developing countries continues at a modest level about 4% of the total.

(b) The Trade Balance

34. By and large East Germany has a trade surplus with the COMECON neighbours, in the form of capital equipment. This represents partly loans to these countries, partly it is the counterpart for services used (e.g. the Polish railways). With Western countries there is a cumulative imbalance which is covered by credits.

35. The general pattern of trade balance with COMECON and Western countries can be seen from the table below.

East German Exports/Imports (Milliard VM)

	<u>Total</u>		<u>COMECON</u>		<u>West</u>	
	<u>Export</u>	<u>Import</u>	<u>Export</u>	<u>Import</u>	<u>Export</u>	<u>Import</u>
1967	14.5	13.8	10.2	9.4	2.9	3.2
1968	15.9	14.2	11.4	10.2	3.0	3.0
1969	17.4	17.3	11.9	12.0	3.9	4.1
1970	19.2	22.4	13.2	13.5	4.2	5.4
1971	21.3	20.8	14.8	13.6	4.5	5.7

(c) The Commodity Structure

36. The commodity composition of East German trade has changed considerably over the decade. From the table below it can be seen that the share of materials in the total has diminished while that of engineering products has increased.

Commodity structure of East German Trade

<u>Commodities (% of total)</u>	<u>IMPORTS</u>		<u>EXPORTS</u>	
	<u>1960</u>	<u>1971</u>	<u>1960</u>	<u>1971</u>
Agricultural and forestry products	15.4	9.4	-	-
Raw materials	41.8	33.2	30.5	20.6
Engineering and metal products	14.4	36.9	51.8	56.8
Products of the light and food industries	27.7	19.1	15.8	20.8
Other products	0.7	1.4	1.9	1.8

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E. LIVING STANDARDS

37. Despite the slower rate of growth in the DDR than in many other Communist countries it still remains true that the standard of living is higher in the DDR than in any other Communist country. Following the same line as Brezhnev in the USSR Honecker declared in 1971 that the improvement in the material and cultural standards of the people was the main task of the 1971/75 Plan. This does not imply any major shift in priorities, involving any change in institutions, but it does mean that great importance will be attached to the realization of the consumer goods targets. The removal last autumn of the Ministers for Light Industry and Domestic Trade is regarded as a proof of this. An indication of the relative abundance of goods in the DDR is the eagerness with which Polish and Czechoslovak tourists in 1972 used the occasion of visiting the DDR to buy up large quantities of goods. It is true that their facilities had to be limited towards the end of the year as supplies were not sufficient to meet the extra pressure.

F. OUTLOOK

38. More than any other COMECON country, the DDR is dependent on rising productivity to sustain economic growth. The success of the regime, the credibility of the leaders, is very much bound up with this issue, which depends on improved technology, good management and labour morale.

39. There is little doubt that many East German enterprises could absorb and make profitable use of a great deal of modern equipment, but the acquisition of this in sufficient quantity is not easy, given the fact that almost two-thirds of the country's trade is, for political reasons, directed to other Socialist countries, which artificially limits the possibilities of trade with countries which would supply modern technology.

40. There appears to be a fund of managerial talent in East German enterprises but the recent reversal to centralized control and planning must be a source of frustration to this element. Moreover, the recent socialization of the remaining private and semi-private firms cannot have helped. Although these firms represented only about 15% in the labour force and in the output of industry they played a significant role as sub-contractors and suppliers of special products. In view of the lack of flexibility in the official system their elimination seems bound to have negative effects.

41. It is difficult to assess the impact of recent events on the morale of the public. Obviously a continued increase in the availability of consumer goods as the result of increased output or imports would be encouraging and presumably if greater contacts with the Federal Republic and other Western countries were really permitted, this would also be a positive influence. It is not certain, however,

to what extent the regime will be able to achieve the first of these desiderata and to what extent it will be willing to permit the second. The retreat from Ulbricht's policy of giving the DDR a special role within COMECON and Honecker's ready acceptance of a more subordinate line can hardly be a matter of satisfaction even to the most ideologically committed.

42. Failing some new development, it would seem, therefore, that the East German economy is likely to go on much as before, with achievements and frustrations, the traditional advantages and potential being offset by adverse political requirements.