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Reflections on Perestroyka and the Foreign Economic Ties of the USSR

Bela Balassa

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The first prerequisite is the establishment of rational prices. This objective may be pursued by adopting world market prices for raw materials and fuels, having the exporters of manufactured goods receive the prices they obtain abroad, setting domestic prices of imports at world market prices plus the tariff, and establishing market clearing prices for manufactured goods that are produced and sold domestically.

Eventually, world market prices would be brought to bear on domestic prices in conjunction with the liberalization of imports, but this will be a long process since the pent-up demand for imports cannot be satisfied from available foreign exchange. At the same time, given the limitations of raising fuel and raw material exports, which presently dominate Soviet foreign trade, it would be necessary to increase the exports of manufactured goods, where quality provides a constraint. To upgrade quality, there is need for foreign machinery, the purchase of which would require external borrowing and joint ventures. It would further be necessary to decentralize decisionmaking on foreign trade in enlarging the scope of firms that can directly trade abroad.

The decentralization of decisionmaking in foreign trade should be accompanied by decentralization in the domestic economy, to be complemented by the introduction of the profit motive and competition. In fact, rational prices, decentralization, profit maximization, incentives to managers, and competition are interdependent, and they will have to be pursued simultaneously for efficient resource allocation.

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REFLECTIONS ON

PERESTROYKA AND THE FOREIGN ECONOMIC TIES OF THE USSR

Bela Balassa *

TABLE OF CONTENTS — Page No.

I.	Introduction	1
II.	Price Setting in the Context of Economic Reforms . . . . . . and Export Expansion	3
III.	Foreign Exchange Needs and Capital Inflow	6
IV.	The Prerequisites of Export Expansion	8
V.	Decentralization, Profit Incentives and Competition	12
VI.	Trade Relations with Other Countries	15
VII.	Conclusions	18

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REFLECTIONS ON

PERESTROYKA AND THE FOREIGN ECONOMIC TIES OF THE USSR

I. Introduction

In his "Perestroyka and the Foreign Economic Ties of the USSR," prepared for the Conference on "Prospects for and Implications of Greater East-West Cooperation," Dr. Popov has provided an extremely interesting discussion of the present situation in Soviet foreign trade and outlined a new foreign economic strategy for the Soviet Union. We will briefly summarize his conclusions, with which we are in general agreement. Next, we will examine the preconditions of the proposed changes in terms of domestic economic policy and the measures that may be used to promote exports. Finally, possible implications for CMEA trade and for trade with capitalist countries and, in particular, the United States will be considered.

Dr. Popov notes that the Soviet Union has not exploited its foreign trade potential. He adds that Soviet trade is still being carried out on the basis of "an archaic, outmoded and essentially 'colonial' trade structure" (p. 4), which has largely involved exchanging fuels and raw materials for machinery and industrial consumer goods. In reference to the general upgrading and advance of world trade, he notes that the "Soviet Union has so far remained outside these developing worldwide economic processes" (p. 8). Dr. Popov further criticizes the system of import controls, the lack of convertibility of the ruble, and the practice of multiple exchange rates in the Soviet economy.

In connection with perestroyka, Dr. Popov notes that improvements have been made in giving a number of organizations the right to trade directly abroad and providing possibilities for joint ventures. At the same time, he makes proposals for the further development of a new foreign economic strategy in the Soviet Union.

The proposed new foreign economic strategy would include making the ruble convertible while establishing a system of customs duties; easing the conditions of establishing joint ventures and setting up special economic zones; permitting Soviet enterprises to borrow abroad; and making balance-of-payments statistics freely available. The described changes aim to "make the Soviet economy more open, create a modern export potential, give Soviet producers entry onto foreign markets and attract foreign firms to participate in projects carried out in the USSR" (pp. 13-14).

These are worthy objectives and one can on the whole agree with the policies proposed to pursue them. At the same time, consideration needs to be given to domestic policy measures necessary to support the policies introduced in regard to foreign economic relationships. Also, policies to promote exports will have to be spelled out.

Domestic policies will need to change in order to ensure efficiency in foreign trade and to provide exports of high quality in the Soviet Union. For one thing, without domestic reforms increases in trade may give rise to welfare losses because prices do not reflect resource scarcities so that high-cost rather than low-cost commodities may be exported. For another thing, domestic reforms are needed to ensure the upgrading of the Soviet export structure.

II. Price Setting in the Context of Economic Reforms and Export Expansion

Prices in the Soviet Union do not reflect resource scarcities or conform to consumer demand. The prices paid by consumers are divorced from producer prices, with turnover taxes imposed at variable rates separating the two. Producer prices are based on average costs often of a long ago period as there is an aversion to raising prices. Average costs are calculated to include wages and capital costs, which tend to understate the cost of capital; they do not compensate for the use of natural resources.

At the same time, there is no linkage between domestic producer prices and world market prices. As Dr. Popov notes, this means that every product effectively has its own exchange rate. In fact, for many products there is more than one exchange rate since in CMEA trade products are often sold at different prices in trade with different countries.

But how to establish rational prices? Could one set centrally prices that reflect resource scarcities and conform to consumer demand? Some suggested that this could be accomplished by solving on a giant computer a system of equations that would incorporate producer and consumer relationships. 1/

This is a chimera. The Soviet Union today has a sophisticated economy with tens of thousands of products, when different prices would need to be set for different product varieties and, as far as consumer prices are concerned, for products sold at different distances from the factory. Furthermore, technology is changing so that past data on production

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1/ Cf. e.g. Oscar Lange, "The Computer and the Market," in Morris Bronstein, Comparative Economic Systems: Models and Cases, Homewood, Ill., Richard D. Irwin, 1985, ch. 11.

coefficients soon become outdated. Consumer tastes also change, giving rise to variations in demand.

And how about adopting world market prices? Such recommendations have been made for small socialist countries, such as Hungary, which can maximize welfare by adopting world market prices domestically. The Soviet Union has a large domestic market and it manufactures products (e.g. Lada automobiles) that are not produced elsewhere. But, standardized commodities (e.g. petroleum) have a single world market price, and it may be assumed that the Soviet Union cannot affect the prices of the products it imports (wheat provides an exception to this conclusion).

World market prices are, then, relevant to the Soviet Union as they indicate opportunities available internationally. The Soviet Union has long been isolated from the international markets, however, and a wholesale changeover to world market prices cannot be effected overnight. While for some commodities world market prices can be adopted at an early date, this is not the case for others. In the following, some suggestions are made as to pricing under present-day conditions.

The domestic prices of raw materials and fuels should be set on the basis of world market prices. In this connection, it may be noted that world market prices were used as a yardstick by Stalin in criticizing "the confusion that still reigns in the sphere of price-fixing policy":

> "Our business executives and planners submitted a proposal [which] suggested fixing the price of a ton of grain at practically the same level as a ton of cotton and, moreover, the price of a ton of grain was taken equivalent to that of a ton of baked bread. In reply to the remarks of members of the Central Committee [of the Communist Party] that the price of a ton of bread must be higher than that of a ton of grain, because of the additional expense of milling and baking, and that cotton was generally much dearer than grain, as was also borne out by their prices in

the world market, the authors of the proposal could find nothing coherent to say." 1/

As noted earlier, raw materials and fuels importantly enter into Soviet exports while other raw materials are imported. Adopting world market prices would permit ensuring specialization according to comparative advantage and economizing with raw materials and fuels.

World market prices should also be used for manufactured exports. This means that producers would receive the prices they obtain abroad times the exchange rate. This would contribute to the expansion of exports that are profitable from the point of view of the national economy and would give incentives to producers to seek better prices abroad. In turn, imports of manufactured goods would be sold at prices obtained by adding a tariff to the cif import price expressed in terms of domestic currency at the exchange rate.

Different considerations apply to manufactured goods produced at home and sold in domestic markets. These products should be sold at prices that equate domestic demand and supply. This would mean linking consumer prices to producer prices and permitting prices to adjust to demand and supply conditions.

Eventually, world market prices would be brought to bear on domestic prices in conjunction with the liberalization of imports. But this will be a long process since, after several decades of strict import limitations, there is a pent-up demand for imports which cannot be satisfied as the Soviet Union does not possess the foreign exchange necessary to pay for these imports.

1/ Economic Problems of Socialism in the USSR, Moscow, Foreign Languages Publishing House, 1952, pp. 24-25.

III. Foreign Exchange Needs and Capital Inflow

Increases in the value of Soviet exports after 1973 resulted in large part from the rise of petroleum prices that brought the export share of fuels from 16.2 percent in 1960 to 47.3 percent in 1986. With the recent fall in petroleum prices, Soviet foreign exchange earnings derived from fuels have declined. Correspondingly, as Table 1 in Dr. Popov's paper shows, the ratio of foreign trade to national income decreased in both 1986 and 1987, and exports fared more poorly than imports in both years. At the same time, Soviet manufactured goods are not of world quality that would permit replacing the lost fuel exports.

The Central Committee of the Communist Party of the USSR set out as a target for the quality of manufactured goods to reach 90 percent of the world market level by 1990 and 100 percent by 1993 (Financial Times, August 25, 1988). These targets appear unrealistic if we consider that, according to sources cited by Dr. Popov, on quality grounds 17-18 percent of Soviet manufacturing output is competitive on the world market under optimistic estimates and 7-8 percent under pessimistic estimates (p. 9).

At the same time, the targets point to the need for the increased importation of machinery to improve product quality. This conclusion is strengthened if we consider the need to replace outdated machinery; reportedly, the average age of machinery in the Soviet Union is 20 years, compared with 12 years in the United States and 10 years in West Germany and France (Financial Times, August 25, 1988).

In order to increase the importation of machinery under present-day conditions regarding exports, a capital inflow would be needed. As far as foreign borrowing goes, this should take the form of borrowing by the central authorities rather than by individual firms. Otherwise, there is the danger of excessive indebtedness as shown by the example of highly-indebted developing countries.

Joint ventures offer advantages over borrowing, however, for several reasons. First, in the case of joint ventures there are no interest payment obligations and transfers of dividends are made from the firm's profits. Second, joint ventures bring in new technology, thereby improving the technological level and the international competitiveness of Soviet enterprise. Third, joint ventures can export through the marketing channels established by the foreign partner.

In practice, some mixture of foreign borrowing and joint ventures may be envisaged. While the legal and the fiscal treatment of joint ventures may be improved further, [1/] and one may also endorse Dr. Popov's proposal that the 51 percent domestic ownership limitation be abolished (p. 20), the experience of other countries indicates that the establishment of joint ventures takes time. Nor can it be expected that foreign interests would supply more than a fraction of the requirements of the Soviet Union. Correspondingly, there is need for external borrowing to provide foreign exchange for the increased importation of machinery.

Nevertheless, over time, the bulk of the increment in foreign exchange availabilities would have to come from exports. In this connection,

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1/ Cf. A. M. Volkov, "New Trends in World Economic Development and East-West Relations," paper prepared for the Conference on "Prospects for and Implications of Greater East-West Cooperation," held at Middlebury College, Middlebury, Vermont on September 19-24, 1988, p. 6.

the question arises what are the commodities where the Soviet Union may increase its exports.

IV. The Prerequisites of Export Expansion

We have seen that fuels account for nearly one-half of Soviet exports. Increases cannot be foreseen in regard to fuel exports, in part because of domestic supply limitations and in part because higher Soviet export volume would create problems with OPEC as it would contribute to a further weakening of petroleum prices. Supply limitations are also appai in regard to the exports of raw materials.

Such being the case, the Soviet Union would have to increase the exportation of manufactured goods. In the short to medium run, the best possibilities appear to lie in increasingly exporting raw materials and fuels in a processed form. In such exportation, the availability of raw materials and fuels gives an advantage to the Soviet Union. At the same time, the technological processes of transforming raw materials and fuels are largely standardized and are either available in the Soviet Union or can be obtained from abroad.

First of all, the Soviet Union could develop the exports of petrochemicals, involving a partial shift from the exportation of petroleum. There are further possibilities for exporting basic chemicals and, eventually, chemical products. Also, nonferrous metals could be exported in a processed form.

The Soviet Union could not, an hould not, aim at the exportation of labor-intensive products, such as textiles, clothing, shoes, and various simple manufactures. Textiles and clothing are subject to the Multi-fiber Arrangement and all labor-intensive products can be exported by less developed countries and China. These countries have considerably lower wages than the Soviet Union.

With the upgrading of industry, there are further possibilities for Soviet exports. These lie in the middle range of manufacturing industries where the level of technological sophistication is moderately high. Examples are automobiles (but this would require considerable improvements in the Lada, which is presently exported in small quantities to the West) and relatively simple machinery and machine tools.

For substantially increasing manufactured exports, however, certain conditions have to be met. This requires, first of all, establishing a realistic exchange rate. The present exchange rate between the ruble and the dollar is an artificial creation that does not correspond to the purchasing power of the two currencies in international markets. Thus, while the official value of the ruble is greater than that of the dollar, the opposite is the case as far as the ruble and the dollar exchange rates of Hungary and Poland are concerned. In fact, one ruble was worth 27 Hungarian forints on June 5, 1987 while the dollar was worth 47.5 forints at the exchange rate of the Hungarian National Bank. This means an implicit exchange rate of 1.76 rubles for the dollar as against the official exchange rate of 1.55 dollars for the ruble. 1/

The exchange rate should be set to make marginal exports profitable. As in the Soviet Union marginal exports are manufactured goods,

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1/ V. Belov, "Socialist Economic Integration in Its Present Stage," paper prepared for the Conference on "Prospects for and Implications of Greater East-West Cooperation," held at Middlebury College, Middlebury, Vermont on September 19-24, 1988, p. 15.

this can be accomplished by calculating the domestic cost of foreign exchange for manufactured exports and setting the exchange rate on this basis.

Such a method of exchange rate determination was used in Hungary following the 1968 reforms, except that the average domestic cost of foreign exchange rather than its marginal cost was calculated. This procedure did not provide sufficient incentives for exports while necessitating subsidies for exports that produced foreign exchange at a domestic cost higher than the average.

Increasing the domestic price of exports will not suffice, however, under present day conditions because of pent-up domestic demand for manufactured products. Also, exporting involves considerable uncertainty so that the fulfilment of the production plan may be jeopardized if exports do not work out as expected. Finally, exports have high quality requirements that involves a considerable extra effort.

At the same time, foreign exchange has a scarcity value that exceeds the exchange rate under conditions of import control. Thus, in order to encourage export expansion, consideration may be given to enlarging the scope of the existing foreign exchange retention scheme for exports. This would involve increasing foreign exchange allotments to exporters and allocating part of the allotment to the producers of inputs for export manufacture.

The latter point is of particular importance, given the difficulties exporters encounter in obtaining inputs for export production in general and inputs of appropriate quality in particular. These difficulties may be obviated if the producers of inputs for export production (indirect exporters) receive a foreign exchange allotment.

One may set the foreign exchange allotment as a percentage of net foreign exchange earnings from exports. This involves deducting from fob export value the cif cost of imported inputs as well as the fob value of materials that would otherwise have been exported. The deduction of exports foregone (e.g. that of fuels used in producing petrochemicals for export) is necessary since otherwise the increment in foreign exchange availabilities due to manufactured exports would be overstated. Subsequently, the foreign exchange allotment can be divided between direct and indirect exporters on the basis of their contribution to net foreign exchange earnings.

Foreign exchange allotments could be used to import machinery as well as intermediate products. One may also envisage an auction market for foreign exchange since some firms may not utilize their entire foreign exchange allotment. This would permit easing the foreign exchange shortage under which Soviet firms operate.

It would further be desirable to increase the number of firms that can directly trade abroad. Dr. Popov noted that in 1987 22 ministries and departments, as well as 77 associations, enterprises, and organizations were given the right to carry out export-import operations directly in foreign markets, accounting for 12 percent of exports (p. 14). This proportion should be increased so as to ensure a direct contact between producers and foreign markets. In the absence of such contacts, it is difficult to ascertain the changing needs of markets abroad.

At the same time, replacing foreign trade enterprises by ministries and ministry departments in carrying out export trade will not suffice. It is the producing enterprises that should have foreign contacts rather than the supervisory organizations. Decentralization in the trade area, in turn, should be part and parcel of decentralization in the overall economic sphere.

V. Decentralization, Profit Incentives and Competition

The decentralization of decision making is necessary to ensure that supply responds to demand. This is relevant not only at the consumer level but also at different stages of fabrication. Centralized planning cannot ensure the equalization of demand and supply, in part because of the impossibility to collect information on all products at the center and in part because of continuous changes that occur in needs and availabilities.

At the same time, for producers to respond to users' needs, they should aim at maximizing profits that bring the firm's own interests into harmony with the society's interests in efficient resource allocation. Profit maximization involves minimizing costs and catering to demand. Setting production targets from above would interfere with the pursuit of these objectives.

In order to ensure that firms maximize profits, firm managers should be provided appropriate incentives. This involves basing the managers' bonuses on profits rather than on the subjective judgment of supervisory organizations.

For profit maximization to lead to efficient resource allocation, there is further need for competition among producers. Competition can be ensured in the Soviet Union whose large domestic market can support a number of efficient size producers in most industries. This contrasts with the case of small socialist countries, such as Hungary, where the domestic market can support only one or two efficient size producers in each industry.

In conclusion, emphasis should be given to the interdependence of rational prices, decentralization, profit maximization, incentives, and competition. For commodities produced domestically, the establishment of rational prices requires equating demand and supply. This, in turn, necessitates the decentralization of decision making and profit maximization by the firm. At the same time, managers have to be provided with appropriate incentives in order to ensure that firms maximize profits. Furthermore, there is need for competition to guarantee that profit maximization leads to the efficient allocation of resources. Expressed differently, under the conditions indicated, the working of the market system in a socialist economy simultaneously ensures efficient resource allocation and the establishment of rational prices.

The described provisions go beyond the measures included in the document approved by the Supreme Soviet on June 30, 1987. This document, entitled "Basic Provisions for Fundamentally Reorganizing Economic Management" represents a half-way house between central planning and market socialism. While it contains a modicum of decentralization, "the basic provisions stress that the economy will continue to be centrally planned and managed as 'a unified national economy complex' directed toward carrying out the party's economic policies." 1/ Also, the possibilities for competition would be limited "by accelerating the ongoing process of amalgamating enterprises into production and science-production associations and creating large new

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1/ Gertrude E. Schroeder, "Gorbachev's Economic Reforms" in Ronald D. Liebovitz ed., Gorbachev's New Thinking, Cambridge, Mass., Ballinger Publishing Company for the International Institute for Economic Advancement, 1988, p. 56.

groupings called 'state production associations,' which integrate entities engaged in all phases of the resea~ch-production-marketing claim." 1/

An additional consideration is that rational prices of products presuppose that there are also rational prices for the factors of production. This, in turn, requires establishing markets for these factors where prices equate demand and supply. Thus, markets are needed for capital, labor, and natural resources.

Also, for the rational pricing of productive factors, the existing excess demand for these factors will need to be eliminated. Excess demand originates in the desire of the firms to expand that is not checked by financial limitations on the expansion. Utilizing an expression introduced by Jånos Kornai, firms face a "soft" budget constraint in the sense that they can expect their losses to be financed from the government budget.

Hardening the budget constraint means making firms fully responsible for the consequences of their actions. Inappropriate actions may, then, lead to bankruptcy, if losses accumulate as a result. Thus, one needs the carrot as well as the stick of competition, with firms benefiting from making profits and suffering the consequences of losses.

The discussion so far pertained to industry. It has been recognized that agriculture also needs a farreaching transformation in order to fully utilize its production potential. The recent decision to lease land to individual farmers up to 50 years represents an important move towards introducing greater efficiency in farming (Washington Post, August 27,

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1/ Ibid, p. 58 -- For a detailed discussion of the Soviet reforms, see Edward A. Hewett, Reforming the Soviet Economy, Washington, D.C. The Brookings Institution, 1988.

1988). It would further be necessary to transform the huge cooperatives and state farms into smaller, profit-oriented units.

In this connection, reference may be made to the experience of Hungary where the operation of profit-oriented units in agriculture has led to a considerable expansion of production. But Hungary is also an example of the lack of success of half-way houses in industry where continued state intervention has not permitted the full-fledged development of market socialism, with adverse effects on production and exports.

VI. Trade Relations with Other Countries

The question arises what are the implications of policy changes in the Soviet Union for trade relations with other countries. This question will be considered in the following in regard to the Council for Mutual Economic Assistance (CMEA) and for trade with capitalist countries, among which the United States requires special attention.

Decentralization in the economic system of the Soviet Union also requires decentralizing trade with the CMEA countries. While at the end of 1987 only 500 of nearly 40,000 Soviet firms established direct links with firms in the CMEA countries, 1/ trade on the basis of intergovernmental contracts would have to be increasingly replaced by market relations among firms.

Also, in the manufacturing sector, trade may increasingly take the form of intra-industry specialization. This would ensure the exploitation of

1/ Ivan Ivanov, "Restructuring the Mechanism of Foreign Economic Relations in the USSR," Soviet Economy, 3:3, 1987, p. 207.

large scale economies associated with longer production runs and the use of specialized machinery as firms narrow their product composition.

There are further possibilities for joint ventures among the CMEA countries. As of November 1987, only four joint ventures were created with firms in CMEA countries and letters of intent were signed for eight others. 1/ Yet, there are considerable opportunities for joint ventures among firms that use different technologies.

In the past, trade and joint ventures among the CMEA countries were limited by the lack of a convertible currency. As the surplus in bilateral trade between two CMEA countries could not be used to finance a deficit with a third CMEA country, there was an incentive to retrench rather than to expand exports.

As a first step to remedy this situation, a clearing of bilateral balances in CMEA trade should be established. Next, the resulting multilateral balances should be paid for in convertible currencies. In the final step, the currencies of the CMEA countries should be made convertible.

At the same time, the requirements for convertibility should not be underestimated. In the absence of balanced trade, with allowance made for the inflow of foreign capital, and sufficient foreign exchange reserves, there is the danger that a run is created on the currency, precipitating a substantial decline in its value.

This danger is especially apparent under present conditions in the Soviet Union, where exports do not appreciably respond to changes in the value

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1/ Ibid, p. 209.

of the currency. Thus, domestic policy reforms providing for an elastic supply of exports is a precondition for currency convertibility.

Convertible currencies are used to settle balances in trade with the capitalist countries. But Soviet trade with these countries has been limited by the availability of exports that could compete in their markets. Thus, the first priority is to increase the scope of commodities that are competitive in the markets of capitalist countries.

Geographical proximity favors Soviet trade with the European Economic Community. Apart from product availabilities for export, in recent years this trade suffered from the relatively poor economic performance of the Common Market countries. With the completion of the internal market in the EC by 1992, a resurgence of growth is foreseen, however.

Geographical proximity also favors trade between the Eastern parts of the Soviet Union and Japan. The question is however if the Soviet Union can compete on the Japanese market in middle range manufactured products, where not only does Japan have a strong position but there is also competition by the East Asian newly industrializing countries.

It has been said that the Soviet Union has few possibilities to export to the United States because of distance. This statement applies to fuels and raw materials where the Common Market countries provide nearby markets. But transportation costs have limited importance for manufactured goods as indicated by the success of Japan and the newly industrializing countries in the U.S. market. Once the Soviet Union establishes a competitive export structure, it should be able to sell in the United States.

As noted earlier, establishing joint ventures would help the export promotion effort. In this connection, U.S. firms may play a particularly important role as they have considerable experience with joint ventures in Western Europe and in developing countries.

At the same time, Soviet exports to the United States are limited by the lack of application of the mfn clause. This should change with the greater openness of the Soviet economy, increased emigration, as well as agreements on reducing nuclear and conventional armaments.

VII. Conclusions

In this paper, attention has been given to the policy conditions of changes in Soviet foreign trade. The discussion has centered on price reform, foreign exchange needs, and capital inflow, the prerequisites of export expansion, the interdependence of the reform measures, and trade relations with other countries.

It has been suggested that domestic policies need to change in order to ensure efficiency in foreign trade and to provide exports of high quality. The first prerequisite is the establishment of rational prices. This objective may be pursued by adopting world market prices for raw materials and fuels, having the exporters of manufactured goods receive the prices they obtain abroad, setting the domestic prices of imports at world market prices plus a tariff, and establishing market clearing prices for manufactured products that are produced and sold domestically.

Eventually, world market prices would be brought to bear on domestic prices in conjunction with the liberalization of imports, but this will be a long process since the pent-up demand for imports cannot be satisfied from available foreign exchange. At the same time, given the limitations of raising fuel and raw material exports, it would be necessary to increase the exports of manufactured goods where quality provides a constraint. To upgrade quality, there is need for foreign machinery, the purchase of which would necessitate external borrowing and joint ventures. This would, then, help to expand exports that will have to provide the bulk of the increment in foreign exchange availability over time.

There are possibilities for exporting fuels and raw materials in processed form. The Soviet Union should also have possibilities in middle-range products, such as automobiles and relatively simple machinery and machine tools. It is at a disadvantage, however, in exporting labor-intensive manufactures.

Establishing a realistic exchange rate is a pre-condition for expanding the exports of manufactured goods. It would further be desirable to increase foreign exchange retention quotas and to allot these to direct and indirect exporters alike. Finally, the scope of firms that directly trade abroad would need to be substantially enlarged.

The decentralization of decision making in foreign trade should be accompanied by decentralization in the domestic economy, to be complemented by the introduction of the profit motive and competition. In fact, rational prices, decentralization, profit maximization, incentives to managers, and competition are interdependent and they will have to be pursued simultaneously for efficient resource allocation. At the same time, improvements would need to be made in the conditions under which agriculture operates.

Decentralization of the economic system also requires decentralizing trade with the CMEA countries. At the same time, the expansion and rationalization of this trade would require the clearing of bilateral balances and the settlement of multilateral balances in convertible currencies, with the currencies of the CMEA countries eventually also becoming convertible.

Geographical proximity favors Soviet trade with the Common Market countries. Nevertheless, once a competitive export structure is established, there will be possibilities for exporting manufactured goods to the U.S. market. In the meantime, joint ventures with American firms hold considerable promise.

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