

# SOCIALIST ECONOMIC REFORMS AND THE DEVELOPING COUNTRIES

By Dr. J. B. Kelegama

Dr. J. B. Kelegama who was Secretary, Ministry of Trade, Director of Commerce, Director of Economic Affairs of the Treasury, Central Banker, Professor of Economics, Kelaniya University, Minister of the Boards of Directors of People's Bank, Bank of Ceylon and Sri Lanka Insurance Corporation, Economic adviser of the Government of the Gambia is now U. N. Consultant to FAO, UNCTAD and ESCAP. Among his numerous articles are Economic Reforms in China and Economic Reforms in the Soviet Union appearing in the Sri Lanka Economic Journal.

The sweeping economic reforms that are taking place in Socialist countries range from the outright rejection of Marxism and centralized economic management and the substitution of a free market economy in countries such as Poland and Hungary to the replacement of centralized economic management by a regulated market economy combining the best features of central planning with the best features of the market in China and the Soviet Union. The Socialist countries which had achieved high growth rates, raised living standards and developed their economies rapidly in the post-war years, began to stagnate from the seventies with slow growth, low income, unemployment, low productivity, inferior quality goods, alienation of workers from the means of production and corruption. The economic reforms are designed to modernize the structure of production and the methods of management, raise productivity and quality of goods, increase living standards and achieve greater consumer satisfaction.

The major economic reforms in China and the Soviet Union may be summarised as follows:-

(a) Shift from rigid centralized economic management to more flexible forms involving

decentralization and the grant of decision-making powers to state enterprises;

(b) Establishment of efficient and commercially viable state and collective enterprises, operating on the basis of market forces and profits without being dependent on State subsidies;

(c) Rejection of egalitarianism and the adoption in principle of payment "to each according to his ability" or linking wages to productivity; acceptance of the need to end the practice of life long employment irrespective of the contribution of the worker and the viability of the enterprise;

(d) Recognition of the positive role of the market mechanism under social control in economic activity; partial deregulation of prices; acceptance of the need for prices to reflect costs; the approval of the pricing system in allocation of resources within limits;

(e) Approval of private enterprise and voluntary co-operative enterprise including individual farming, individual services, private plots and joint-stock companies in specified sectors to supplement but not supplant

the state and collective enterprises;

(f) Opening to the outside world by inviting foreign private capital and technology to upgrade the obsolete technology by the offer of generous incentives, joint ventures with leading transnational corporations and establishment of free trade zones;

(g) Gradual introduction of macro-economic policies in place of administrative commands to guide economic operations.

The new approach tempers orthodox Marxism with pragmatism, rejects the view that economic efficiency can be raised by larger doses of Socialism and moving to a higher stage of Socialism, and considers that capitalist techniques and methods and the market mechanism have a crucial role to play at the present stage of socialist development. China regards herself as in the primary stage of Socialism in which productive forces being undeveloped, need to be highly developed by adopting market oriented reforms. The Soviet Union, contrary to orthodoxy, considers the existing socialist relations of production (administrative-command economy) as obstructing the development of productive forces and alienating the workers from the means of production and considers it necessary to change the relations of production by the above mentioned reforms to create a democratic, human and efficient socialism. Both countries agree that there is no model of Socialism to be emulated by everyone; that the founders of Marxism-Leninism gave only a definition of the essen-

tial characteristics of Socialism but not a detailed picture of Socialism; that the concepts of Socialism keep on developing and that Marxist-Leninist works cannot be used to solve all present day problems; that Marxism is not "unalterable,

to use certain Marxist principles... our historic development will surely be hampered...."

The economic reforms, Gorbachev argues, are not to replace Socialism with Capitalism but to

ified in the leading socialist countries precisely because it failed to realize their economic and social objectives. It is also being rejected or modified in the developing socialist countries such as Vietnam, Laos, Yemen and Ethiopia which are moving to market oriented economies. The Socialist reforms also indicate that developing countries should avoid copying models of other countries which may have different economic and social conditions and political and cultural traditions. In concrete terms, developing countries have been shown the dangers of regimentation which stifles people's involvement in development, collectivization which reduces farmers from being "masters of their land into day labourers," egalitarianism which discourages workers' initiative and effort, closed economic policies which deny access to foreign capital and technology, and preoccupation with dogmatic theories and approaches which obfuscates realism and pragmatism.

The second lesson is that economic laws are the same under Capitalism and Socialism and much time and effort has been wasted in attempting to draw a distinction between Capitalist economics and Socialist

---

***The new approach tempers orthodox Marxism with pragmatism, rejects the view that economic efficiency can be raised by larger doses of socialism and moving to a higher stage of socialism, and considers that capitalist techniques and methods and the market mechanism have a crucial role to play at the present stage of socialist development.***

---

sacred or inviolable" and should be developed and adapted according to circumstances.

**Gorbachev argues:**

"Any attempts to turn the theory by which we are guided into an assortment of rigid schemes and formulas which would be valid everywhere and in all contingencies is most definitely contrary to the essence and spirit of Marxism-Leninism. Lenin wrote back in 1917 that Marx and Engels rightly ridiculed the mere memorising and repetition of 'formulas' that at best are capable only of marking out general tasks, which are necessarily modifiable by the concrete economic and political conditions of each particular period of the historical process."

The official government newspaper People's Daily in China pointed out on December 7, 1984:-

"Marx died 101 years ago. His works were written more than 100 years ago. There have been tremendous changes since his ideas were formed. Some of Marx's ideas are no longer suited to today's situations because Marx never experienced these times, nor did Engels or Lenin. And they never came across the problems we face today. So we cannot use Marxist and Leninist works to solve all our present day problems. In terms of Marxism, we cannot be dogmatic. Times are changing. If we continue

strengthen Socialism, but not the Stalinist model of Socialism that has hitherto prevailed in the Soviet Union, Gorbachev made this clear in the interview with the Time magazine of June 4, 1990 when he stated:

"The Stalinist model of Socialism should not be confused with true socialist theory. As we dismantle the Stalinist system we are not retreating from Socialism but are moving towards it."

He contends that it is not Socialism that has failed but the emasculated version of it which was canonized, idealized and turned into a dogma in the Soviet Union and other Socialist countries.

---

***The first lesson of economic reforms in Socialist countries is that the centralized management or administrative-command system can no longer be regarded as a suitable model for economic development of developing countries.***

---

**Lessons to Developing Countries**

The economic reforms in the Socialist countries have six important lessons for developing countries.

The first lesson of economic reforms in Socialist countries is that the centralized management or administrative-command system can no longer be regarded as a suitable model for economic development of developing countries. It has been rejected or mod-

economics. For example, if demand exceeds supply, there will be a tendency for prices to rise. shortages to occur and blackmarkets to appear; if producer prices are low there will be little inducement to increase production and vice versa; if there is equal remuneration for unequal work, incentive to increase efficiency tends to be reduced; if there is deficit financing, it will tend to fuel inflation; subsidizing inefficient industries is tantamount to encouraging ineffi-

cient management. These laws operate under both capitalism or socialism. In other words, developing countries cannot escape from the basic economic laws by creating a socialist system.

The third lesson is that if

---

***Developing countries should learn to live with transnational Corporations as they have to rely heavily on them for foreign capital and transfer of technology, however much they distrust them. The simple fact is that it is transnational Corporations which have the capital and technology needed by developing countries.***

---

developing countries are attracted by the system of Workers' Self-Management in Yugoslavia, as an alternative to Centralized Management, they are going to be disappointed. The fact is that Workers' Self-Management in Yugoslavia has been a failure. The workers have treated enterprises as their fiefdoms, given priority to their own interests over national interests, resisted management by professionals, ignored productivity and efficiency and increased wages in excess of productivity gains, thereby contributing to hyper-inflation. Thus inflation in Yugoslavia exceeds 1000 percent, the value of currency has fallen fiftyfold in just three years, unemployment is 16 percent, foreign debt is over \$21 billion and economic growth is negative. These adverse economic factors combined with inability to service her foreign debt and the widespread ethnic clashes have created an unprecedented economic and political crisis for Yugoslavia.

The fourth lesson is that developing countries should learn to live with transnational Corporations as they have to rely heavily on them for foreign capital and transfer of technology, however much they distrust them. The simple fact is that it is transnational Corporations which have the capital and technology needed by developing countries. The Socialist countries have had no hesitation in accepting their direct invest-

ments or in establishing large-scale joint ventures with the leading transnational Corporations such as Coca Cola, IBM, Chrysler Corporation, Xerox, Dow-Chemical, Warner-Lambert and Alstom in the case of China, and Pepsi Cola, Mc Donalds, Fiat, Daimler Benz -

Volkswagon, Siemens, Alcatel and Mitsui in the case of the Soviet Union. Transnational Corporations have played an important role in the rapid modernization of the economies of Singapore, the Republic of Korea, Taiwan, Thailand, Malaysia and some Latin American countries. For instance, transnational Corporation accounted for about 70 percent of the manufactured exports of Singapore, over 40 percent in Brazil, 30 percent in Mexico and Argentina, 28 percent in the Republic of Korea and 10 percent in Hong Kong in the early 1980s. A code of conduct for transnational Corporations has been worked out by the United Nations taking into account the concerns of developing countries, but it has not yet

---

***The framework of the Mixed Economy which has been utilized by most developing countries for over 40 years has emerged as perhaps the most suitable system for economic and social growth.***

---

been accepted by the developed countries. The developing countries may not be in a position to postpone their development until such a code is internationally accepted.

The fifth lesson is that the developing countries should continue to work closely with international financial and trade organizations such as IMF, World Bank and GATT. They have no choice, for the IMF and the World Bank provide them with development

funds and balance of payments assistance and their approval of domestic economic policies is an essential prerequisite to extension of aid by donor countries; GATT on the other hand is necessary to bring about discipline to international trade. No developing country can develop by its own resources - whether Capitalist or Socialist - and so long as that is accepted, there is no point in opposing international organizations of which developing countries are voluntary members, as imperialist institutions. Socialist countries such as China, Vietnam, Laos, Kampuchea, Hungary, Poland and Romania are already members of these organizations; the Soviet Union has secured observer status in GATT but is expected to accept membership of all these organizations in the near future. Many developing countries have expressed their dissatisfaction with the adjustment policies imposed on them by the IMF but this is a matter on which they have to fight, perhaps with the support of Socialist countries, within the IMF itself. It needs to be recognized that without these international institutions - whatever shortcomings they may have - there can be chaos in the world economy without international trade, fiscal and monetary discipline.

The sixth and the last important lesson is that the framework of the Mixed Economy which has been utilized by most developing countries for over 40 years has emerged as perhaps the most suitable system for economic and social growth. The hybrid where predominant social ownership of the means of production and distribution and central planning are combined with limited private enterprise and market operations, which is what China and the Soviet

Union are building, is in fact a mixed economy or regulated market economy. The adoption of this model by these two countries has vindicated the economic policies of developing countries which opposed both capitalism and socialism and adopted a middle path for using both systems to

to unemployment and to the wastage of savings potential, with the result that the pace of development and technical progress is retarded."

At the same time, developing countries rejected the regimented administrative - command

They are not rivals. We may gradually change the picture as time goes on. First of all you control the strategic points in your Plan. Once you control them, you do what you can on behalf of the State and allow others to do what you cannot or do not wish to do for the moment. There is no conflict about it. As far as I can see the two must be seen as a whole. The main thing is to increase wealth in the country and to increase it in such a way as to lead more and more to the type of economy that we are aiming at."

---

***The experience of India in particular, indicates that a developing country can achieve reasonably good economic growth with democracy, political stability and some degree of social equity under a mixed economy.***

---

overcome their economic and social backwardness within a democratic framework.

### **The Mixed Economy**

Many developing countries while recognizing its economic efficiency, have rejected the free market economy or full capitalism on moral as well as social and economic grounds. Jawaharlal Nehru for instance, stated "A system which is based purely on the acquisitive instinct of society is immoral". The economic and social arguments against a free market economy have been well summarised by the South Commission as follows:

"There has hardly been a historical case of sustained economic growth and development without the active participation of the state as a regulator and promoter. By their very nature, unregulated market systems pay little or no heed to such strategic areas as basic industries, health and education services, scientific and technological research and the preservation of the environment and natural resources. It is particularly unlikely that the free play of market forces would result in the growth with equity that a people-centred development strategy seeks to achieve. Excessive reliance on market forces can lead to concentration of economic power and wide disparities in income and wealth, to the underutilization of resources,

economy of the Marxist Socialist countries in favour of democratic forms of political and economic management. The resultant mixed economy attempts as far as possible, to incorporate positive and useful aspects of both the systems and to avoid their negative and harmful aspects. Thus market mechanism is combined with macro-central planning and social controls and the private sector is combined with the State sector. The roles of the State and the market vary from country to country according to the stage of development, experience, social institutions, capacity of the private sector and management capabilities of the State. The role of the State is certainly greater in those developing countries where the private sector is weak or where considerations of social equity are given priority.

The same view was echoed in Sri Lanka's Six - Year Development Programme of Investment 1954/55 to 1959/60 - perhaps the first Plan of the country - which stated. "The Government and the private sector are therefore like oarsmen in a boat. While they must row together, they must ensure that they also row in rhythm; for it is only in a spirit of co-operative endeavour that we can reach the promised land of contentment and prosperity - that will give us confidence in ourselves as a nation." The broad approach of most developing countries has been that the State or the private sector is incapable of achieving national economic and social objectives by itself and that both must play a complementary role; further each sector can countervail the other - the State can check

---

***The Socialist countries have shown that Socialism has no miraculous power to change a poor and underdeveloped country into a prosperous one.***

---

Perhaps the main characteristic of a mixed economy is the co-existence of public and private sectors. Nehru who was aiming to build a socialistic economy in India expounded this concept when introducing India's First Five Year Plan as follows:-

"The Plan is an integrated whole and in that both the public and private sectors must be integrated.

the abuses of the private sector while the private sector can goad the state sector to greater efficiency.

Apart from building both state and private sectors, developing countries have attempted in many instances to mitigate the unfavourable effects of the operation of market forces by such devices as price control, rationing, state trad-

Contd on page 28

Contd from page 6

ing and marketing, consumer subsidies, high taxation of income and wealth, state ownership of banking and insurance and promotion of co-operative enterprises. It is true that some of these measures have created consumer discontent, bred corruption and created inefficient

growth rate of 10.4 percent a year in 1980-87 under a regulated market economy with more limited private enterprise than India, which was even higher than the 8.6 percent growth of South Korea in the same period.

Philippines, Brazil and Argentina while China, where the private sector is restricted, secured a growth rate even higher than South Korea's. This appears to indicate that while the identification of the state with the private sector is a major factor in the success of the first group of countries, it is also necessary to take into account other favourable factors such as natural resources, political stability, political alignment, absence of labour unrest, traditions, skills, work ethics, forms of management and entrepot trade.

---

***Perhaps the most significant result of Socialist economic reforms is that the two economic and social systems are moving closer together.***

---

state monopolies but it is debatable whether things would have been better without them, particularly in the context of inadequacy of foreign exchange to meet consumer demand facing most developing countries and the profiteering instinct of petty traders. Restrictive measures have generally been imposed in difficult times and relaxed when conditions improved. They have been motivated mainly by considerations of social equity. The poor record of many a state enterprise, however, can be explained mainly by excessive political interference where the authorities have been more concerned with securing employment to their friends, relatives and party supporters in these enterprises than in operating them on commercial lines. The reforms in Socialist countries emphasize the need for independent state enterprises free from political control, managed by technocrats and operating on commercial lines.

The experience of India in particular, indicates that a developing country can achieve reasonably good economic growth with democracy, political stability and some degree of social equity under a mixed economy. She has achieved high agricultural and industrial self-sufficiency and a economic growth rate of 4.6 percent a year in the period 1980-87 which is higher than that of more open developing market economies such as Brazil 3.3 percent, Indonesia 3.6 percent and Argentina minus 0.3 percent in the same period. China achieved a very high

### **Newly Industrialised Developing Countries**

On the other hand, some of the Asian developing countries with much greater private enterprise and more open economies than India such as Singapore, South Korea, Taiwan Province of China, Hong Kong, Thailand and Malaysia have enjoyed more rapid industrialization and higher growth than India in recent years and virtually become models for other developing countries. It would be an oversimplification however to assume that their dramatic growth is the result of the free play of market forces alone; for the State played an active role in identifying itself with the private sector by guiding, directing, encouraging and supporting it at every turn through protection, industrial finance, labour market control and promotion and control of foreign investment and transfer of technology. Further not all of those countries enjoyed democratic freedoms and workers rights. Thus a good part

### **The Future**

The Socialist countries have shown that Socialism has no miraculous power to change a poor and underdeveloped country into a prosperous one. They have further shown that Socialism as hitherto practised should in fact be avoided by the developing countries. The experience of China, Soviet Union, Vietnam, Ethiopia and other serves to demonstrate the validity of a prophetic statement made by Paul Baran, Professor of Economics at Stanford and one of the greatest Marxian economists of our times, in 1956, soon after Krushchev's denunciation of Stalin:

"Socialism in backward and underdeveloped countries has a powerful tendency to become a backward and underdeveloped Socialism."

This is corroborated by Gor-

---

***The developing countries can note with satisfaction that the regulated market economy that is taking shape in China and the Soviet Union is closer to their mixed economy than the Capitalism.***

---

of the credit for their economic success should actually go to their governments. It is also significant that some developing countries which have adopted market oriented policies like those of the above mentioned countries have failed to realize such high growth rates, for example, Indonesia,

bachev when he says that although Socialism has contributed to economic and social progress and has attracted millions of supporters, "Nowhere however has the socialist idea been adequately put into practice." It is precisely to put the Socialist idea into practice that Gorbachev has rejected the

Stalinist framework of regimentation and is building in its place an efficient, democratic and human socialism on the basis of a mixed economy or regulated market economy which synthesises the positive features of both Socialism and Capitalism.

Perhaps the most significant result of Socialist economic reforms is that the two economic and social systems are moving closer together. When Milovan Djilas, the Communist World's longest surviving dissident was questioned by the Newsweek: "You once stated that the two systems would come closer together, that Capitalism will be socialized and the Socialism will be capitalized. Do you still believe that?", replied in October 1989 as follows:-

"Yes, there has been such a movement to come closer together. But now it is more Communism that is getting closer to capitalism than the reverse, Western capitalism is no longer the classical capitalism in the Marxist concept; it is in this respect more socialized. But it is communism that is adopting to Western capitalism and liberalism both in economic and political terms. The result of this is a move to Western values. This is a historic event."

That the two systems will continue to move closer together is also the view of the distinguished American economist, J. K. Galbraith and the noted Soviet economist Stanislav Menshikov. When questioned by Menshikov "What will the world look like in a hundred years? Will it be capitalist, will be socialist? Will it be a kind of mixture of both as it is now, with the two systems co existing? Will it be one society that has coalesced as a result of the movement of the systems towards each other or will it be two societies that have become even more different from each other?" Galbraith replied:

"I would guess that we would have a mixture. There will be a movement to the market in what is now the Socialist world along the lines we have previously discussed. There will be a commitment in the capitalist world to greater social concern. And a hundred years from now there will be countries that are still emerging into this more mature combination of Socialism and Capitalism. Do I make that clear?"

The Menshikov answered: "Yes... I generally agree with you that the future will be a mixture of the existing forms, with perhaps some new forms putting in an appearance..."

The developing countries can

note with satisfaction that the regulated market economy that is taking shape in China and the Soviet Union is closer to their mixed economy than to Capitalism. The mixed economy as an economic model has often been ridiculed by ardent supporters of Socialism as well as the enthusiastic advocates of Capitalism and some Third World economists too have been rather apologetic in their defence of the system. Thus the mixed economy concept failed to receive the attention it deserved. It is often forgotten that the mixed economy has worked without major problems for about forty years and it has succeeded in accommodating both right wing and left wing views and forging pragmatic solutions to problems facing developing countries. The fact that it has survived despite the inducements of the two rival systems and despite their critical economic and social problems alone is adequate testimony to its relevance to developing countries. Now that it has been accepted by the two major socialist countries and become respectable, developing countries should have greater faith and confidence in their centrist and pragmatic approach to development and make every effort to devise ways and means of improving the mixed economy's techniques and efficiency to develop their resources rapidly and achieve high growth in combination democracy and social equity. ■