CURRENT ACCOUNT

Triangulation

Politics, economics, ethics: three dimensions of human existence, three sets of social values and objectives—often in conflict; only rarely, if ever, congruent. Such were my thoughts some weeks ago as I sat through a conference in Berkeley, California, sponsored by the academic journal *International Organization*, on the subject of the foreign economic strategies of European Communist states. The specific focus of the meeting was the period since 1980, when East Europe went through a debt crisis not unlike that experienced almost simultaneously in Latin America and some other Third World areas. How East European governments and their foreign bankers reacted to the crisis says much about the difficulty of effectively triangulating politics, economics, and ethics.

East Europe's accumulation of debt began with the coming of détente in the early 1970s. Western banks were happy to lend to the Soviet Union and its regional allies—Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, and Rumania—as well as to neutral Yugoslavia. At a time of intense competition and excess liquidity in financial markets, the region appeared to offer particularly attractive opportunities for new loan growth. All these nations had good records for low debt and punctual repayments. Most important, their central planning systems seemed to guarantee uninterrupted debt service in the future. In a command economy, presumably, the governmental authorities could always act to cut imports or promote exports as needed to assure availability of the requisite foreign exchange. Their methods might be inefficient, of course, or even repressive, but it is not for us to judge, the bankers insisted. Lending thus looked like a good bet. By the end of the 1970s, the region's foreign debt had grown tenfold, to $85 billion.

The East Europeans, for their part, were happy to borrow. Their domestic growth rates had been faltering for some years, owing to a variety of increasingly evident inadequacies in their mechanisms for formulating and implementing economic policy. The *dirigiste* planning methods of the 1950s, which depended foremost on centralized resource allocation, physical targeting, and administered pricing, had proved economically counterproductive in the 1960s; and except in Hungary and Yugoslavia, market-oriented reforms had been either resisted or vitiated by conservative Communist party bureaucracies. By the end of the 1960s it was clear that a shift of emphasis was needed, toward a more technology-intensive scheme of development, if greater efficiency and improved performace were to be achieved. It was also clear that the needed technology could only be obtained in the capitalist West. Export prospects to the West, however, were not favorable, especially with the poor quality of the region's manufactured output. Western credits, therefore, seemed to offer a convenient means by which to finance sought-after capital-goods imports. In effect, the savings of the outside world would be used to underwrite the objectives of domestic investment. Debts would be serviced out of the proceeds of enhanced production in the future.

Unfortunately, matters did not quite work out that way, particularly in Poland, which by 1977 had already gained the dubious distinction of holding the largest foreign debt in the region. Despite very high investment levels, the Polish economy began to falter as bottlenecks developed, productivity fell, and wages were permitted to outrun the availability of consumer goods. Soon debt service was eating up well over half of export revenues—clearly, an unsustainable situation. By 1981, with tensions mounting daily between Party leaders and the new Solidarity trade union movement, Warsaw seemed to be hovering on the brink of default.

The reaction of Western banks, unsurprisingly, was not at all encouraging to Solidarity. Bankers felt no responsibility to the Polish people, only to their balance sheets. What good was liberalization of Poland's political system if it threatened to disrupt debt-service payments? By 1980 all new lending to Poland had ceased. And by 1981, in a classic example of self-destructive herd behavior in financial markets, banks began to withdraw from other East European countries as well—not just from the poorly managed like Rumania, but even from the comparatively well run like Hungary—thereby precipitating the very debt crisis they would have preferred to avoid. Even neutral Yugoslavia got caught up by the raging regional "contagion."

Most revealing is what has happened since 1981 as each of the East European nations has struggled to come to grips with its external financial difficulties. Bankers, in effect, have encouraged renewed *dirigisme* in the short term, regardless of what this might mean over the longer haul for either living standards or the political environment of the region. Poland's suppression of Solidarity at the end of 1981 was greeted with audible sighs of relief in banking circles. Said one prominent investment analyst: "If the Polish Government is successful in gaining better control, it will be unfortunate for the Polish people, but the loans will be paid off." So much for the ethics of the situation. Similarly, brutal austerity measures have been welcomed everywhere from the Baltic to the Balkans because they appear to ensure that debt obligations will be paid. In the last year-and-a-half bankers once again have been cautiously reentering the region, but on a far more selective basis than before, favoring most those countries that have manifested the tightest grip over their economies and citizens.

There are two ironies in all this, one economic, one political. At the economic level, it is clear that current policy strategies in the region, however successful they may be in the short term, are only storing up serious problems for the future. There is no question that central planning systems can react faster and more effectively to a crisis. But they also hold out less promise of efficient performance in the long term. Stabilization today is purchased at the expense of growth tomorrow. At the political level, the irony is that, by encouraging austerity rather than reform, and reduced imports rather than expanded trade, the capitalist banks of the West are pushing the region's governments into even greater dependence on the Soviet Union.

And ethics? That seems to be lost altogether as East European governments and their foreign bankers close ranks. For the governments, perpetuation of power is the immediate goal; for the banks, perpetuation of profit. The interests of both come together in a stress on financial solvency. Theirs is the real "solidarity" in Europe today.

BENJAMIN J. COHEN