The Shock of the Global

THE 1970s IN PERSPECTIVE

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CHAPTER 4

The Kiss of Debt

The East Bloc Goes Borrowing

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WHAT TOOK PLACE in the East bloc in the 1970s was scarcely appreciated at the time, but it proved to be momentous. Edward Gierek, the Communist Party boss in Poland, and Walter Ulbricht, the East German Communist leader, each hit upon a bold new development strategy: borrow from the West in convertible currency in order to effect a great economic leap. The ostensible goal was to use the money to buy technology and expand industry in order to export goods to . . . pay back the loans. But the regimes also felt a deep need to mollify their populations by importing Western consumer goods. The immediate upshot was that the production of goods such as cars and television sets grew appreciably, while foodstuffs, clothing, and other daily items became more readily available. In the early 1970s, at least, economic times were good in Eastern Europe.[1]

Before the decade was out, however, the borrowing gamble turned into a bust. Both Poland and East Germany found themselves stuck with huge loans in currencies other than their own that they could not readily pay: the increased hard currency revenues from exports never materialized. A major part of the problem was the 1973 oil shock, or the pan-Arab refusal to sell oil to the West against the background of the Arab-Israeli War. The price of crude spiked 400 percent in a matter of months, and energy costs shot up substantially for East European industry. But the deeper problem was the fact that communism locked in low productivity while also doling out living standard subsidies. The dangers of the failed borrowing strategy were remarked in internal discussions. Yet the regimes lacked the political legitimacy to take the necessary hard measures of a structural adjustment,

such as cutting off subsidies (that is, raising prices) and throwing people out of work in the worst-performing sectors. The bloc was not merely on the verge of economic bankruptcy; more consequentially, it was politically bankrupt.

The capitalist West, meanwhile, in many ways had the exact opposite experience in the 1970s. The crippling oil shock sparked the formation by 1975 of the Group of Six, or G-6, a forum consisting of the United States, Japan, West Germany, Great Britain, Italy, and France (Canada would be added the next year), in an attempt to coordinate policy. All these countries underwent stock market swoons, grueling recessions, rises in unemployment, and declines in living standards. Times were tough in the first half of the 1970s. Still, the longer-term consequence of the oil shock and the market-induced structural adjustment in the leading capitalist countries was more robust economies. The postwar capitalist world in the 1950s and 1960s was extraordinarily different from its interwar incarnation: no more Great Depression and fascist militarism, but instead democracy and consumer boom. Furthermore, despite the economic difficulties of the early 1970s, and another recession in the 1980s, capitalism would manage renewed high performance. This was game changing for socialism. Either socialism was the antidote to capitalism, or it had no reason to exist.

The Polish Disease

Consider the crucial case of East Germany. In building socialism, the Soviets had radically suppressed consumption, but that was back when the capitalist world had been mired in 1930s mass unemployment. In the 1950s West Germany's growth rates were *in the double digits*, yearly. In July 1960 Ulbricht wrote to Soviet leader Nikita Khrushchev: "You can be sure that we are doing everything in our powers. But West Germany has turned out to be economically powerful." The upshot: the German Democratic Republic was being subverted by "hostile-negative forces," that is, by Western daily life. "In the final analysis, we cannot choose against whom we would like to compete," concluded Ulbricht, the son of a tailor. "We are simply forced to square off against West Germany. However, the GDR does not have enough economic power to do this alone." Ulbricht begged for more hard currency. Moscow said no. In January 1961 Ulbricht wrote again: "The booming economy in West Germany, which is visible to every citizen of the GDR, is the main reason that over ten years about two million people have left our republic."[2] Those runaways included entrepreneurs and skilled professionals (one day the entire mathematics department of the University of Leipzig defected). Small wonder Moscow consented later that year to Ulbricht's requests to wall in East Germans. But the living standard differential could not be walled out.[3]

Under Ulbricht, supplication before the Soviets never ceased, but he also turned to the enemy. In 1970, the year before his ouster, he told the chairman of the USSR Council of Ministers that because the Soviets would not underwrite the GDR to the extent necessary, the GDR would have to borrow from the capitalist West. "We know the plan will be upset by it," Ulbricht admitted.[4] But the GDR needed hard currency to make an industrial leap and, in theory, pay the debt back with a range of new manufactured goods. This, however, presupposed Western demand for GDR goods—as well as no competition from other low-price exporters. It also required expensive imports of components and raw materials, on top of the consumer imports necessary to placate a populace aware of West German lifestyles. And unless the GDR's export earnings kept ahead of these import expenditures, the country would suffer a trade imbalance and be unable to pay back the hard currency loans. Brezhnev and the comrades in Moscow suspected that in turning westward for loans, Ulbricht was signaling his readiness to sell out the Soviet Union in a deal to resolve the German question. Ulbricht, though, remained a dreamer. The same year he told the Soviets about his need to go cap in hand to the imperialists, he assured his chief planner that within five years the GDR would be selling computers to the West.

Erich Honecker elbowed Ulbricht aside and redoubled the efforts to build up a socially oriented consumer society under the banner of socialist orthodoxy. As late as 1971 the GDR's semiprivate and private sectors still employed nearly half a million people and accounted for 11.3 percent of output, but Honecker nationalized these mostly small, flexible private enterprises, whose profits were deemed politically anathema. Ironically, they had manufactured specialty machines and other goods for Western export (one GDR efficiency expert had dubbed them the country's "secret weapon").[5] Reducing revenues, Honecker also ratcheted up outlays for consumer and housing subsidies, which leapt nearly sevenfold between the onset of his rule and 1989. "The people need cheap bread, a dry flat and a job," the former roofer remarked. "If these three things are in order, nothing can happen to socialism."[6] The subsidies, however, came on top of pensions, hospitals, schools; the GDR regime could not raise productivity to pay for the lifestyle that it promised and the populace had come to expect. The almighty rulers walked on eggshells for fear of triggering a repeat of the June 1953 Uprising, when only Soviet military assistance had prevented a regime collapse. Communism's locked-in low productivity also derived from the inherent nature of planning, which through the unlimited demand for labor gave workers the power to shirk (even in an emigration-depleted GDR). East Germany's supposed ace in the hole was the big bet on high technology, which Honecker increased—right when the limits of the GDR's Fordist production model were being felt globally, thanks to rising energy costs. In the international political economy, socialist East Germany was not capitalist East Asia, as would soon be poignantly demonstrated when East Asian goods produced by market discipline economies trounced East German goods on global export markets.

The Kremlin, which had egged Honecker on in his palace coup against Ulbricht and in his total eradication of private enterprise, balked at underwriting his rule. Not long after the first oil shock hit in 1973, the Soviets announced price rises for their oil, and the GDR found itself needing to export 20 percent more goods to the West just to stay even in hard currency. GDR economic growth began to taper off (either from more than 7 percent on average to around 4 percent, or from around 4 percent to not much more than 1 percent, depending on how one assesses East European data). Honecker had also been re-exporting some of the cheap Soviet oil (at world prices), but in August 1981 Brezhnev informed his pal that after three consecutive poor harvests in the Soviet Union, Moscow would have to shrink oil deliveries to the GDR. State Planning Chairman Gerhard Schürer implored his Soviet counterpart, Nikolai Baibakov: "I assume that a healthy, stable, socialist GDR plays an important role in the strategic thinking of the USSR. Imperialism stands right at the door of our house with its hate on three television channels." In addition, said Schürer, complaining of the independent trade union Solidarity, "now we have counterrevolution in Poland at our backs." He begged for 3.1 million tons more fuel. "Should I cut back on oil to Poland?" Baibakov asked rhetorically. "Vietnam is starving . . . should we just give away South East Asia? Angola, Mozambique, Ethiopia, Yemen . . . we carry them all. And our standard of living is extraordinarily low."[7] (This was in 1981: so much for the oil-fueled uplift experienced by the Soviets in the 1970s.)

And so Honecker, too, found himself going to the imperialists, worker's cap in hand. He had blasted Ulbricht for running up the foreign debt, then he himself ballooned it beyond anything previously seen. The GDR's increasing dependency on the imperialists, especially West Germany, struck a psychological blow among the leadership. It was embarrassing enough that GDR schoolbooks taught that the goods of the West—which the regime doled out as rewards, and for which the GDR was sinking into debt—were produced by exploitation. But Honecker forbade even internal debate about the debt issue. When in November 1973 the regime's chief finance expert had warned the party chief that by 1980 the GDR's foreign debt would soar by a factor of ten, from DM 2 billion to DM 20 billion, Honecker instructed him to cease making the calculations. (The debt in 1980 turned out to be DM 25 billion.) Schürer, the chief planner, strove again and again to put across the dangerousness of the situation, but he was told to avoid taking any actions, lest they magnify the troubles. By 1989 GDR foreign debt had reached DM 46 billion, or $26.5 billion. The cost of servicing those obligations was $4.5 billion, nearly 60 percent of export earnings. And there was no end in sight to more hard currency borrowing. Finally, in October 1989, Schürer disclosed the extent of the debt to the rest of the GDR leadership. By then there was no way out, except for Western debt forgiveness. Living well beyond its means, the GDR had essentially lost its sovereignty.[8]

The Polish case—though extremely different in many ways—nonetheless bears some striking similarities to that of East Germany. Gierek, a former miner, had been in charge of a heavily industrialized coal mining region, Silesia, prided himself on being a manager, and, unusually, had lived abroad (in Belgium) and spoke French. Upon taking power as supreme party boss in 1970, he installed his "Silesian mafia" in Warsaw and broke up the country's seventeen voivodeships (the largest administrative units) into forty-nine smaller ones, eliminating any chance that someone could accumulate the power to challenge the authority of the first secretary (the way he had done as an overlord in Silesia). Besides centralizing power as well as expanding party membership—which rose from 2 million to 3 million over the decade of the 1970s—Gierek implemented the same strategy as Ulbricht: borrowing hard currency from the West to fatten consumption in Poland and turbocharge the economy. Poland's GDP grew at a stunning annual clip of nearly 10 percent during the first half of the decade, and salaries leapt accordingly.

Whereas in 1970 there had been 450,000 private cars in Poland, by the end of the decade, thanks to local production of the "small Fiat" from 1974, more than 2 million private cars were on the roads. But Polish production mostly failed to find buyers in the West, and the hard currency loans were eaten up; by 1979 up to one half of the raw materials and basic inputs necessary to keep production going in Polish factories had to be imported for hard currency. Foreign debt, nearly $4 billion in 1974, doubled the next year and reached $20 billion by decade's end. Gierek had loosened the autarky, exposing the system far more than ever before to the world economy.[9] Gierek also entered into long-term agreements linking Poland to Soviet-sponsored projects through Comecon. This guaranteed better access to cheap Soviet raw materials, particularly oil and natural gas, but in the second half of the 1970s Poland experienced shortages of capital goods (such as locomotives) because Comecon obligations required exports of such products out of Poland.

Above all, though, the 1973 oil shock, on top of the inherent wastefulness and nonmarket rigidity of planning, bludgeoned the borrowing strategy, leading Gierek again to try to lower the costly subsidies for food. In June 1976 price hikes—69 percent for meat and fish, 100 percent for sugar, 60 percent for butter—provoked strikes at 130 factories. (The atmosphere had been inflamed the preceding year by attempts to insert the "leading role" of the party as well as the "special friendship" with the USSR into the country's constitution.) The workers humiliated the establishment; an ashen prime minister went on television and revoked the "price adjustment" for meat products *one day* after having introduced them and belatedly promised consultations with unspecified "representatives of society." Imagine a state with monopoly control over everything—economy, education, the media, cultural institutions, unions, police, the military, entertainment—which could not raise the price of sausage without risking mass social protests.

By the late 1970s Gierek's consumption-led "boom" strategy had stalled in "growth fatigue," and Poland's current accounts balance had sunk to $25 billion in the red. The price for the compensatory foreign loans, moreover, was not just economic dependence on the West but, as would become evident, a certain independence of maneuver for Poland's opposition. It was now that in combination with workers' strikes, some members of a self-styled opposition formed KOR, or the Committee for Workers' Defense, offering recourse to beaten and incarcerated workers and their families—efforts that were supported by Poland's strengthened post-1968 political emigration. Suddenly every provincial party secretary had to reckon with the likelihood that if anything untoward happened to a member of the opposition, this fact would be publicized on Radio Free Europe and might affect Poland's standing with Western creditors.

Western banks, meanwhile, had the money to lend because of the selfsame oil shock: they recycled gushing Middle East petrodollars that had been placed on deposit with them to the bloc (as well as to Latin America). Although it was Tito's Yugoslavia that had first opened to Western funding, receiving around $2.7 billion between 1951 and 1960 from the United States alone (nominally in exchange for good behavior vis-à-vis Greece and Italy), East bloc borrowing became known as the "Polish disease." It could also have been called the East German disease. But even Ceauşescu's Romania, which had long prided itself on its near self-sufficiency, eventually succumbed to the temptation of Western borrowing.

Loss of Élan

In the late 1940s across Eastern Europe the Communist establishments were small minorities, yet their members seemed completely assured. They had resisted and defeated fascism; they were part of the movement of history; therefore their theories and actions were right, even if majorities of their compatriots did not immediately appreciate it; so they could lie at will. By the 1980s these Communist establishments had become enormous and possessed massive force, well-developed censorship mechanisms, and tight border controls. But the much bigger Communist establishments of the 1980s displayed the opposite sense of what the minuscule Communist establishments had known in 1948, namely that history was moving in the wrong direction; that defections could not be ignored, that the pervasive lying was sapping the will of the system's own functionaries. "All it will take," remarked one anxious Soviet general in the world's biggest armed force, "to bring the entire house down is just one spark."[10] In other words, sometime between the late 1940s and the 1980s the establishment suffered a psychological blow, a loss of its arrogance. That shift occurred not primarily because of the Hungarian events of 1956 or the Czechoslovak events of 1968, as important as those episodes were, but because the bloc's economic performance fell short against the backdrop of extraordinary Western capitalist successes.

Eastern European elites who had come to power with Communist systems viewed the latter as an instrument to force a modernization leap (of a particular nonmarket kind) on their "backward" countries. That is precisely what happened, with great violence, but all the same this had failed to close the gap with the West.[11] Between 1913 and 1950 per capita GDP growth in Eastern Europe had been an anemic 1 percent annually, slower than world averages, but from 1950 to 1973 it jumped to 3.9 percent annually, above world averages. For those twenty years, Eastern Europe's growth per capita was even slightly above Asia's (3.7 percent). To put the matter another way, having been entirely within the Axis wartime orbit, which culminated in vast destruction, Eastern Europe underwent an impressive postwar recovery led by heavy industry. But then the Communist tree ceased leafing. For example, Hungary's annual average growth rate of around 6 percent dropped to 1.6 in 1979, and to zero in 1980. The precipitating cause, again, was the 1973 oil shock. The Soviet Union, a major oil exporter, was buoyed by rising revenues. But despite some initial Soviet energy cushioning of the East European satellites, the oil shock worsened intrasocialist terms of trade. In 1974 the Soviets accepted eight hundred units of Hungary's Ikarus bus in exchange for 1 million tons of oil, but by 1981 that same quantity of oil required 2,300 buses, and by the mid-1980s 4,000 buses.[12]

Soviet-style economies mostly grew not by gains in productivity but by ever greater inputs of capital and labor (so-called extensive growth) and had notorious problems innovating. They could not even manage to assimilate the innovations their spy agencies succeeded in stealing from abroad. Most fundamentally, the systems invested in but misused (and abused) their human capital. Shortages (and queues) were endemic to the planned economy's normal operation, while the mania for heavy industry, the collectivization of agriculture (in most cases), and the suppression of the service sector (as capitalist) combined to ensure that even during the high growth spurt, rises in consumption lagged. True, after Stalin's death the regimes made concessions to the consumer across the bloc. But that only compounded the challenge: subsidies for housing, food, clothing, and other consumer items became ever more costly to maintain, while the least price hikes (when tried) sparked revolts that sometimes shook the regimes to their foundations. East European economies could not grow fast enough to meet the living standards challenge, on top of outsized expenses for military security and elite perquisites (which violated the ethos of social justice the regimes promoted). And yet the costly daily life subsidies seemed ever more necessary, because unlike the Soviet Union in the 1930s, the Eastern European satellites faced a capitalist world—in many cases right across the border—that had undergone its greatest-ever consumer boom in the 1950s and 1960s.

And nearly everyone knew it. They learned from the media—foreign but also official—and, partly thanks to détente, increasingly from direct contacts with visiting foreign tourists, and sometimes even from their own travels. Despite massive security police apparatuses, and despite monopolies on property and the public sphere, the East bloc establishments turned out to be paralyzed. None had much political capital. On the contrary, the regimes doled out the subsidies, and yet they still labored to burnish their legitimacy. They could not—again, unlike the Soviet Union—draw on a World War II victory to compensate for their relative failings. So predictably they fell back on cultivating nationalism. With some irony, Communist regimes promoted national feeling partly on the basis of anti-Russian sentiment. Be that as it may, whatever the straining of credulity on carrying the nationalist banner, each bloc country's "national communism" was linked to promises of economic and technical modernization, perhaps the core of the regimes' claims to legitimacy. And that was the killer: after all the exertions, violence, and sacrifice, far from outdueling the West, the East had fallen into dependency on it.

The East Europeans used the Soviet Union as a dumping ground for the inferior goods that they simply could not sell in hard currency export markets (low-quality, outdated clothes, footwear, fabrics, leather goods, furniture). But even Eastern Europe's supposedly Western-export-grade goods left a lot to be desired. And then came a market surprise. When Gierek, the Polish party chief, exhorted, "Build a Second Poland!" he meant doubling GDP in a decade. Such a great leap forward proved an utter fantasy—except in the capitalist world, especially East Asia. Japan's export-led boom inspired, and funded, the "tigers" of South Korea, Taiwan, Hong Kong, and Singapore. In the 1980s East Asian manufacturers blindsided the East Europeans. Lower-cost exports turned out to be a game others in the global economy could play, and better, with far cheaper labor and higher quality.

The East European borrowing strategy also depended on affordable interest rates and on foreign bankers' willingness to roll over the loans—something that the bankers began to rethink around 1979, the time of the second oil shock. By then Poland's convertible currency debt had reached around $20 billion; servicing that debt ate up 80 percent of the country's export earnings. (The neglect of agriculture, meanwhile, meant that food accounted for nearly a quarter of Polish imports in 1978, costing valuable hard currency.) Hungary's convertible currency debt ballooned from around $1 billion in 1972 to $9 billion by 1979, a burden that could be serviced only by taking on more debt. By 1989 Hungary's debt hit $18 billion, meaning that the country needed a surplus in hard currency from exports of more than $1 billion annually *just to pay the interest*. (The corresponding figure for Poland was $2 billion.) Across the bloc, total hard currency debt shot up from $6 billion in 1970 to $21 billion by 1975, $56 billion by 1980, and $90 billion by 1989, with no end of escalation in sight.[13]

To paraphrase Lenin, the capitalists had sold the bloc the rope with which to hang itself. Perhaps East European regimes could have united to default simultaneously, seeking to deal a blow to the global financial system that held them in a vise, or at least to gain leverage in a write-down. But they were Communists, not global casino players. Anyway they now needed continued access to Western capital markets (to say nothing of Western consumer goods) for their survival. Only Ceauşescu's dictatorship in Romania imposed a brutal austerity program (from 1982), demonstrating the ruinous cost of paying off the debt: blackouts, freezing interiors, severe rationing of food. This was a price the East German and Polish establishments could not pay. Staring at Romania's debt-reduction despair on one side and, on the other, at West Germany's relentless cornucopia, East Germany and Poland, as well as Hungary, took out ever more foreign currency loans to pay back their old foreign currency loans. "Most of Eastern Europe's economies had plunged head-first into the swimming pool of Western capitalism," two scholars have written, "and instead of emerging refreshed and revitalized had surfaced gasping for air and saddled with unsustainable debt."[14] The bloc had become a Ponzi scheme.

Geopolitics and Ideology

The profound structural changes after World War II, and especially during the 1970s, radically altered the global geopolitical context for Eastern Europe and demanded a response from its establishments. Over the years the responses generally boiled down to two opposed versions of trying to make socialism better. One involved the old reformers' dream—socialism with a human face—which, however, had shown itself to be not a renewal of socialism but its unwitting liquidation. Party conservatives were properly wary of Gorbachev's revival of socialism with a human face in the 1980s. But their alternative, conservative modernization—meaning a further tightening of "discipline" as well as profligate investment in technological panaceas—also failed to reenergize the systems, seemingly leaving them only with trying to muddle through by borrowing. Muddling through (albeit on capitalist money) held a certain appeal. After all, the system had raised up the members of establishments, and most hoped that if necessary, the system would somehow save them, especially if capitalism finally descended into the second Great Depression that Communists had long predicted for it. But someone forgot to tell the post–World War II capitalist world to go into a death spiral.

The compromises with capitalism made by the East bloc in the 1970s forced a severe reckoning in the following decade. Borrowing from the West had amounted, consciously or not, to a substitute for conceding the establishment's monopoly on power. But the bill came due. Predictably the bloc's establishments upped their pleas to the Soviets, but the Soviets could not bear the extra burden. From the 1970s—after having long paid below world market prices for imports from East Europe while extracting higher prices for Soviet exports—Moscow found itself needing to provide its satellites with raw materials at below world prices, while importing shoddy goods in return.[15] Then, after the world price of oil tumbled precipitously in 1985–86, thanks partly to deliberate Saudi overproduction, the Soviet Union—which could not implore *itself* for more money—eventually also became contaminated with the "Polish disease," borrowing from the capitalists to satisfy the consumer desires in a socialist country.

Meanwhile, Moscow fumed that the satellites were living better than their Soviet "friends," yet these "shameless" peoples were not even satisfied. Rank-and-file East European dissatisfaction, however, could not be directed at abstractions such as "the market" or "globalization"; the regimes themselves were held responsible. Many members of the Communist establishments voiced outrage at the "petty-bourgeois" hankering for dachas and cars, washing machines and refrigerators (as did many dissidents, including Vaclav Havel). Of course the elites, with their wives and children, enjoyed the best access to Western goods and services. In any case, those who decried "refrigerator socialism" were spitting into the wind. That said, even the dimwitted comprehended the depth of the trap.

If socialism was merely aiming to placate consumers just like capitalism, only not as well, was socialism's existence even justified? To put the matter in its starkest terms, how long could muddling through and borrowing continue if Western bankers refused to roll over the loans?

What to do?[16] Communist rulers in China—who endure as of this writing—discovered a solution for the party: a police state market economy. On June 4, 1989, when the multicandidate elections took place in Poland that would culminate in the formation of a Solidarity government, the tanks rolled into China's Tiananmen Square, cracking down on the demonstrators. It was a coincidence, but an extraordinary one. One Communist establishment found itself, unexpectedly, in a process of capitulation and went along; the other stood firm. But in bloodying its people who were demonstrating against corruption and for socialism to open up politically (and live up to its promises), the Chinese leadership also deepened the country's turn toward economic openness. Who would have guessed it would be the Chinese Communists, rather than the East Europeans, who would embrace the market? The East Europeans (Albania excepted) had not railed against the USSR for being in bed with imperialism (in détente) and abandoning world revolution.[17] Unlike Mao and his homicidal Cultural Revolution of 1966–1976 (which, unintentionally, destroyed China's economic planning capacities), the East European establishments had ceased to be militant. Rather, they turned out to be conservative, which derived from their long terms in power, and which had seemed vindicated by events in Prague in 1968; indeed 1968 helped formalize their conservative identities across the bloc as the resolute "healthy forces." They branded their nemeses—reformers—as counterrevolutionaries even though the latter also fought *to defend socialism*. In other words, members of the establishments of Eastern Europe, whether conservative or reformist, remained largely bound by ideology, especially in the economy, unlike the Leninist-type copycat single party in Taiwan or the post-Mao recovering Communist Party in mainland China.[18]

For the East European systems, the reformers such as those of the Prague Spring were the more immediately dangerous, since reform of the system invariably amounted to unintentional self-liquidation. But the conservatives bear the greater responsibility for the happy circumstance of the implosion. The mundane fact about the Communist establishments in Eastern Europe was that they were full of . . . Communists. And the single most important fact about the formerly secret Communist archives is this:

behind closed doors the Communists spoke with the same vocabulary and worldview that they used in public. Although the idea of permitting some market mechanisms had come under discussion early in the revolutionary regimes, it was always only as a way to have profit-and-loss calculations assist administrative methods, not as a displacement of planning. Even Hungary's János Kádár, considered one of the more flexible leaders on economic experimentation, pointedly remarked during a visit to a large factory in 1986: "It must be understood that the foundation of Hungary's people's economy is socialist, that the means of production are 96–97 percent in social property and that our future will be decided in the socialist factories. Everything else can be a useful supplement to this, but nothing else."[19]

The June 1989 crackdown in Tiananmen Square resounded throughout the bloc that summer and into the fall, but the incipient market success of the Chinese Communists mostly escaped the East Europeans. Károly Grósz—the fifty-seven-year-old who had emerged as Kádár's prime minister in 1987 on a platform of a "reform dictatorship" and then shunted Kádár aside as party chief in 1988—supported many long-contemplated economic reforms (capitalist-style banking, majority foreign private ownership). Grósz also showed intransigence over the party's monopoly (and explored the possibility of martial law). This desperate, crisis-ridden groping appears to have been inspired not by Communist China's example, however, but by the high-growth authoritarianism of 1980s South Korea. Be that as it may, in October 1989 Grósz was definitively eclipsed by Hungary's Communist Party political reformers, who sought survival in a Western-style multiparty system.[20] The possible exception of Grósz aside—the evidence is ambiguous and the time period short—the East European ruling circles that were insistent on retaining one-party rule ruled out embrace of the market. For them it was tantamount to treason.

For East Germany—which faced a hugely successful market economy Germany right across the barbed wire—"capitulation" to the market appeared to mean the end of the country. Would the East German establishment risk suicide? Would the Soviets accept the "loss" of East Germany, paid for with 27 million Soviet lives? Here ideology meshed with geopolitics. A reversion to capitalism under Communist rule—something like China's market Leninism—seemed out of the question. Socialism had been a promise to transcend all problems, but the accumulated entrenched interests of socialism, its establishments, would not countenance

an attempted transcendence of socialism's problems, only "more socialism." The Soviets, in other words, were not alone in keeping Eastern Europe locked on its fatal trajectory, in the teeth of the radically altered world circumstances of the postwar era. But the Soviets upset the apple cart even further with Gorbachev's repeal of the Brezhnev Doctrine of using force to retain socialism in Eastern Europe, and with his socialism-with-a-human-face insistence that the bloc regimes themselves not use force to try to hold on.

51. Paul Volcker, "The Political Economy of the Dollar," *Federal Reserve Bank of New York Quarterly Review* 3 (Winter 1978–79): 1–12.
52. Brent Scowcroft to Ford, "Call from Prime Minister Callaghan," September 29, 1976, GFPL, NSA Files, International Economic Affairs Staff, Box 3, United Kingdom; "Note of Meeting Held at 11 Downing St.," December 6, 1976, http://www.bankofengland.co.uk/publications/foi/disc060519.htm/.
53. Brzezinski and Frank Moore to Carter, "Administration Strategy on Human Rights Amendments," April 16, 1977, JCPL, Staff Secretary, Handwriting File, Box 18; and Brzezinski to Carter, "State Department Report Concerning Human Rights Policy and the IFIs," March 27, 1978, JCPL, WHCF, HU [Human Rights], Box 1.
54. Susan Strange, "The Persistent Myth of Lost Hegemony," *International Organization* 41 (1987): 551–574.
55. Paul Kennedy, *The Rise and Fall of the Great Powers* (New York, 1987). Also Michael Cox, "Whatever Happened to American Decline? International Relations and the New United States Hegemony," *New Political Economy* 6 (2001): 311–340.
56. Maier, *Among Empires*.

3. The Great Transformation

1. There is, of course, already a *Nixon in China* opera and at least one recent account (by Margaret Macmillan) of the event that presents it in the grand opera style.
2. I have been working with Chen Jian of Cornell University on a project provisionally titled "The Great Transformation: China's Road from Revolution to Reform." This chapter is a think piece that has been fed by long conversations between the two of us; while I am grateful to Chen Jian for his insights, he is of course not responsible for the preliminary conclusions I draw here.
3. This overview is based on interviews with former political leaders in the South and with former factory managers, military officers, and local CCP cadres. Some of the more general conclusions are supported by the recent scholarly literature in Chinese; see for instance Chen Yongjun, *Cong jihua dao shichang: Zhogguo jingji tizhi gaige de xuanze* [From Plan to Market: Choices in the Reform of China's Economic System] (Fuzhou, 1999); Han Guangfu and Hu Yongxiang, *Gaige niandai: Deng Xiaoping de gaige suiyue* [The Reform Decade: Deng Xiaoping's Reform Period] (Shenyang, 2004); and Zhonggong zhongyang dangshi yanjiushi disan yanjiubu, comp., *Deng Xiaoping yu gaige kaifang de qibu* [Deng Xiaoping and the Rise of the Reform and Open Door Policy] (Beijing, 2005). For valuable reminiscences of early reform in the South, see Li Junxiao, *Bi lu lan lu xian xing yi bu: Guangdong gaige kaifang chuqi lishi janjiu* [Arduous First Steps: Historical Research on the Initial Period of Reform and Opening in Guangdong] (Guangzhou, 2008).

4. Two good recent overviews of party politics in this crucial period are Shi Yun and Li Danhui, "Nanyi jixu de 'jixu geming'—cong pi Lin dao pi Deng 1972–1976" [Difficult Continuation of the "Continuous Revolution"—from Criticizing Lin to Criticizing Deng, 1972–1976]; and Xiao Donglian, "Lishi de liangui: Cong boluan fanzheng dao gaige kaifang" [The Changing Paths of History: From Bringing Order Out of Chaos to Reform and Open Door], both 2008 working papers from the Chinese University of Hong Kong's Contemporary China Research Center. In English, see Frederick C. Teiwes and Warren Sun, *The End of the Maoist Era* (Armonk, N.Y., 2007), esp. pp. 110–186.

4. The Kiss of Debt

1. This chapter is adapted from *Uncivil Society: 1989 and the Implosion of the Communist Establishment* (New York, 2009), by Stephen Kotkin, with a contribution by Jan T. Gross.
2. As cited in Jeffrey Kopstein, *The Politics of Economic Decline in East Germany, 1945–1989* (Chapel Hill, 1997), pp. 43–44. Between 1949 and 1990 approximately 2.7 million people permanently crossed from East Germany to West Germany, almost all of them before 1961; about 200,000 people crossed in the other direction.
3. In 1963, on a visit to Moscow, Ulbricht remarked that "even after the closing of the state borders, the high living standards [in West Germany] strongly affect the population of the GDR and its political attitudes." Kopstein, *Politics of Economic Decline*, p. 48.
4. Ibid., pp. 68–69.
5. Ibid., p. 80.
6. André Steiner, *Von Plan zu Plan: Eine Wirtschaftsgeschichte der DDR* (Munich, 2004), p. 190.
7. Kopstein, *Politics of Economic Decline*, pp. 93–94.
8. Schürer blamed the Eighth Party Congress of 1971, when Honecker had taken over, for deciding that the GDR must underwrite a consumer society and welfare state. Charles S. Maier, *Dissolution: The Crisis of Communism and the End of East Germany* (Princeton, 1997), p. 60.
9. Kazimierz Z. Poznański, *Poland's Protracted Transition: Institutional Change and Economic Growth, 1970–1994* (New York, 1996), pp. 3–4. See also Włodzimierz Brus, "Economics and Politics: The Fatal Link," in *Po-*

land: Genesis of a Revolution, ed. Abraham Brumberg (New York, 1983), pp. 26–41; and Alex Pravda, "Poland 1980: From 'Premature Consumerism' to Labour Solidarity," *Soviet Studies* 34, no. 3 (1982): 167–199.

10. Quoted in Zdeněk Mlynář, *Nightfrost in Prague: The End of Humane Socialism* (New York, 1980), p. 143.
11. Much of the scholarly literature blames the relative "backwardness" of East Europe on Soviet backwardness. By contrast, Iván Berend has argued that in the twentieth century, the Eastern European countries mounted two revolts against the West out of humiliation: an antiliberal right-wing rebellion in the interwar years and an antiliberal left-wing rebellion in the postwar years, both motivated by "economic backwardness and the increasing gap which separated them from the advanced Western core." Iván T. Berend, *Central and Eastern Europe, 1944–1993: Detour from the Periphery to the Periphery* (New York, 1996), p. x.
12. Charles Gati, *The Bloc That Failed: Soviet–East European Relations in Transition* (Bloomington, Ind., 1990), p. 119. When it came to higher oil prices, the Soviets felt that they could not stick the satellites with the entire bill because of possible political fallout, so Moscow tried to adjust prices moderately, absorbing some of the economic costs, but enduring the fallout anyway. Paul Marer, "Has Eastern Europe Become a Liability to the Soviet Union: (III) The Economic Aspect," in *The International Politics of Eastern Europe*, ed. Charles Gati (New York, 1976), pp. 59–81 (quotation p. 70). Romania imported oil from the USSR but not at subsidized prices.
13. Hajna Istvanffy Lorinc, "Foreign Debt, Debt Management Policy, and Implications for Hungary's Development," *Soviet Studies* 44, no. 6 (1992): 997–1013; Jan Vaňous, "East European Economic Slowdown," *Problems of Communism* 31, no. 4 (1982): 1–19; Gati, *Bloc*, pp. 108–9; Katherine Verdery, "What Was Socialism, and Why Did It Fail?" in *The Revolutions of 1989*, ed. Vladimir Tismăneanu (New York, 1999), pp. 63–85 (quotation p. 81).
14. Derek H. Aldcroft and Steven Morewood, *Economic Change in Eastern Europe since 1918* (Aldershot, 1995), p. 170; Valerie Bunce, "The Empire Strikes Back: The Evolution of the Eastern Bloc from a Soviet Asset to a Soviet Liability," *International Organization* 39, no. 1 (1985): 1–46 (quotation p. 39).
15. Aldcroft and Morewood, *Economic Change in Eastern Europe*, p. 137. For a high-end estimate ($87 billion) of Soviet trade subsidies to Eastern Europe between 1960 and 1980, see Michael Marrese and Jan Vaňous, *Soviet Subsidization of Trade with Eastern Europe* (Berkeley, 1983).
16. Retrospectively, Valerie Bunce has suggested that the choice had narrowed to two unpalatable options: liberalize and thereby destroy the system, or put off reforms and purchase short-term stability but long-term doom.

Jeffrey Kopstein has written that "leaders throughout the bloc faced two alternatives, either retreat to a conservative immobilism or proceed down the road of gradual capitalist restoration." Valerie Bunce, *Subversive Institutions: The Design and Destruction of Socialism and the State* (New York, 1999), p. 37; Kopstein, *The Politics of Economic Decline*, p. 46.

17. In 1966 a pro-Chinese "Polish Communist Party" in exile was proclaimed by Kazimierz Mijal in Albania, advocating for a return to orthodoxy (Stalinism) at home and a more revolutionary policy abroad, against Gomułka's "revisionism" and alleged "renunciation of socialist conquests." See http://files.osa.ceu.hu/holdings/300/8/3/text/44-5-8.shtml.
18. Bruce J. Dickson, *Democratization in China and Taiwan: The Adaptability of Leninist Parties* (Oxford, 1998).
19. Jason McDonald, "Transition to Utopia: A Reinterpretation of Economics, Ideas, and Politics in Hungary, 1984 to 1990," *East European Politics and Societies* 7, no. 2 (1993): 203–239 (Kádár quoted p. 214).
20. Elemér Hankiss, *East European Alternatives* (Oxford, 1990), p. 203; McDonald, "Transition to Utopia," pp. 217–228; Rudolf L. Tőkés, *Hungary's Negotiated Revolution: Economic Reform, Social Change, and Political Succession, 1957–1990* (New York, 1996), pp. 297–298; Paul Lendvai, "The Many Faces of Károly Grósz," in *Hungary: The Art of Survival* (London, 1988), pp. 127–155.

5. The Global 1970s and the Echo of the Great Depression

1. Karl Polanyi, *The Great Transformation* (New York, 1944).
2. Hyman P. Minsky, "The Financial Instability Hypothesis," Jerome Levy Economics Institute Working Paper no. 74 (May 1992).
3. On trends in financial globalization, see Maurice Obstfeld and Alan M. Taylor, *Global Capital Markets: Integration, Crisis, and Growth* (New York, 2004). On the evolution of international financial policies, see Rawi Abdelal, *Capital Rules: The Construction of Global Finance* (Cambridge, Mass., 2007).
4. On various interpretations of the limited role of developing countries in GATT prior to the Uruguay Round, see Rorden Wilkinson and James Scott, "Developing Country Participation in the GATT: A Reassessment," *World Trade Review* 7, no. 3 (June 2008): 473–510.
5. Carlos Díaz-Alejandro, "Latin America in the 1930s," in *Latin America in the 1930s: The Role of the Periphery in World Crisis*, ed. Rosemary Thorp (London, 1984), pp. 17–49; Deepak Lal, *The Poverty of "Development Economics"* (Cambridge, Mass., 1986); Peter Temin, *Lessons from the Great Depression* (Cambridge, Mass., 1989).
6. Theoretical treatments of policy persistence include, inter alia, Gordon