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DEVELOPMENTS IN EASTERN EUROPE AND THE THIRD WORLD - ECONOMIC IMPLICATIONS*

Introduction

Events have moved so fast in East European countries over the past several months engendering so complex and unpredictable ramifications that the whole international system has been jolted and faces drastic adjustments and realignments. It is not possible at this stage to say much with any degree of certainty regarding the evolving socio-politico-economic structures and their consequences. This paper makes tentative observations regarding the changes with particular reference to their economic implications for the Third World.

Section 2 discusses emerging major structural changes in the world economy to enable us to review the changes in Eastern Europe in a broader context; section 3 discusses the implications of the East European changes for the Third World, and section 4 contains concluding remarks.

The World Economy Context

The East European changes came on the scene as the international economic system has been increasingly becoming characterized by

*Paper presented at the Seminar on **"Changes in Eastern Europe : Regional and Global Impact,"** organized by Bangladesh Institute of International and Strategic Studies (BIISS), Dhaka, 11 March 1990.

efforts devoted to the management of instability and crises which have been brewing over the past two decades (1970s and 1980s) following the relative stability of the 1950s and the 1960s. But underlying the crises ridden system, certain trends and tendencies have been strongly emerging. These include increasing globalization of economic activities, multipolarity of economic power, and regionalism in economic interest and approach.

Globalization and multipolarity, which are intimately related, have been gaining ground, particularly since the mid-1970s, as countries such as Japan, newly industrializing economies (South Korea, Taiwan, Singapore, Hongkong, Mexico), and West Germany and country groups such as European Community (EC) and Association of South East Asian Nations (ASEAN) have been fast increasing their capital resources, technological stocks and levels, production, and trade both in absolute and relative terms. The pre-eminence of the USA in terms of power and influence in the international economic decision making has consequently been declining.

The world trade has been growing at faster pace than world output in recent decades–about 50 per cent faster during 1971-88. But the USA runs a current account deficit of US $ 150 to 170 billion. The persistent surplus of Japan is about US $ 80–90 billion, while West Germany runs a surplus of a similar order. The USA is now the world's largest net debtor country, which was not so long ago the world's largest net creditor country. Although some of the EC countries suffer net current account deficits, the EC as a whole has been emerging as a strong competitor in the world economy and had a net current surplus of US $ 3 billion in 1987. The completion of the process of political and economic integration of the EC economies in 1992 will make the bloc a very powerful force in the world economic system.

The USA, as it tries to put its own house in order, faces strong competition from Japan and EC in particular. As the severity of the competition may further increase in a multipolar system, all these countries may increasingly become inward looking and involved in intense economic battles among themselves. The EC will have an additional problem of introducing and managing economic restructuring within the bloc itself, which will be needed in the wake of its complete integration. This may consume most of the bloc's attention and resources, and it may not therefore be able to give much attention to the Third World. As a result, its contribution to Third World development may become much more limited in the 1990s than has hitherto been the case. While Japan seems to show increasing interest to provide aid to the poorer countries, there are question marks regarding the size and duration of Japanese surplus because of demographic changes in Japan and the impact of attempts to reduce the US trade deficits. Moreover, the Japanese surpluses are held largely by the private sector and may not be available for ODA. However, it is likely that Japan will continue to be a surplus country in the 1990s and perhaps beyond and can therefore play a useful role in the developmental efforts of the Third World countries. But Japanese conditionality is usually very restrictive and Japanese financing is often tied to the World Bank and Asian Development Bank funding.

The Third World countries have, on the other hand, been rapidly accumulating debt; and their debt servicing payments have also been increasing rapidly. Three things need be noted here. First, there has been in the 1990s a reverse resource transfer to the developed countries from developing countries. Thus, while there was a net inflow into the developing countries of US $ 41.7 billion in 1980, a net outflow of US $ 32.5 billion from these countries was registered in 1988-89–a reversal of US$ 74.2 billion. An alarming development. The external debt of the developing countries has soared to US $ 1,218 billion by 1987 from US$ 633 billion in 1980. Also while in money terms ODA to developing countries has been increasing to some extent during the 1980s the real ODA has fluctuated around a declining trend during the decade and steadily declined during 1985-87.

The world economy is thus characterized by a two-track growth. While the USA, EC, Japan and NIEs and other up-coming economies such as those belonging to the ASEAN, experienced high incomes and/or high economic growth, the low income developing countries of Asia and Africa in particular have registered slow or decelerated growth, or stagnated, or experienced negative growth. The 42 least developed countries have mostly experienced stagnation and some outright retrogression in the 1980s. These countries as a group achieved an average economic growth of 2.3 per cent per annum against an average population growth rate of 2.6 per cent during 1980-87. Poverty deepened and widened, and unemployment and underemployment soared in most of these countries during the period. The World Bank and IMF sponsored stabilization and restructuring policies which many least developed and other developing countries followed in the 1980s often caused decline in investments, which affected all sectors, in particular social sectors, such as, education and health. As a result not only that these countries suffered immediate low economic growth but their future growth prospects were also adversely affected.

Given the prevailing socio-economic conditions, savings rates in most of the least developing countries are very low so that the need for foreign aid is very high both for replacement and expansion of capital stocks. For example in Bangladesh the average domestic savings ratio (proportion of the GDP saved) and the average national savings ratio (domestic savings plus foreign remittances) were respectively 1.7 per cent and 4.5 per cent per annum during 1980-87. But the investment was about 12 per cent of the GDP per annum during the period so that foreign aid accounted for about two-thirds of the investment.

In certain developing countries however savings rates are relatively high but they still need foreign aid for expanding their developmental base and modernizing their economies. For example, in India, the domestic savings ratio was 21 per cent in 1986, but India still needed foreign aid for some of its developmental activities.

An important feature of the world economy in recent times has been the protectionism resorted to by the industrially advanced countries against exports from developing countries, especially manufactured exports. This has immediately hit the concerned developing countries ; but in the long run such a policy is damaging to the growth of the world economy as it will adversely affect output growth in the developing countries, which will in turn adversely affect their imports from other countries including developed ones, which in turn will adversely affect output growth in the latter countries. As a result a dynamism in the world economy that could have originated from the expansion of such trade is stymied. Consequently, all the countries, developed and developing, will ultimately lose.

Another important feature of the world economy that should be taken note of is the growth of the international capital market which mobilizes surpluses from the surplus countries. This capital market is likely to become more important than ODA in terms of the size of funds to be channelled to developing countries. But it will be more expensive and difficult for the developing countries to raise funds from this market as these funds will surely be more security oriented and not concessional. Hence, these countries are likely to face harder times as ODA and other concessional aid may be less forthcoming. The situation of the weaker developing countries will become particularly vulnerable as their ability to raise funds from the capital market will be extremely limited.

These have been some of the major trends and developments in the world system producing a configuration of economic powers, which is more diffused than before but, nonetheless, heavily stacked against the developing countries, particularly the weaker and least developed ones.

Economic Implications of Changes in Eastern Europe for the Third World.

A broad sweep of the major characteristics and emerging structural changes in the world economy has been provided above. Keeping these in view, some of the implications that the changes in Eastern Europe may have for the Third World may be explored. While economic implications are our main focus of attention, the discussion cannot but be placed in broader socio-political context.

First of all, nobody could have expected such fast and far-reaching changes in Eastern Europe and the whole international system was, therefore, caught unawares. As it is, the international economic order (consisting of bilateral relations, Bretton woods institutions of the World Bank and the IMF and other international agencies and institutions), which was developed with the metropolitan powers, particularly the USA, at the centre stage and calling the tunes, has been found unsuited and wanting for formulation of policy and institutional responses to deal effectively and equitably with the major structural changes taking place in the world economy such as those noted earlier and foster international cooperation for development.

Hence, the need for a new international economic order (NIEO) was felt, which was discussed a lot in international fora some years ago. Strong voices were raised around the world in its favour and proposals were prepared by various international commissions (e.g, Brandt Commission) and country groups (e.g., Group of 77) and institutions (e.g. UNCTAD). But precious little has been achieved in concrete terms, mainly because the vested interest powers (advanced countries) are not interested in and have shown monumental insensitivity for changing the system. Even the subject of NIEO has in recent years been relegated to relative unimportance in the international fora.

But, it is urgently needed for the benefit of all countries, developed and developing, East and West, that the international economic system is restructured thoroughly, in accordance with the new and emerging realities and increasing interdependence in the world economy.

The countries of Eastern Europe in which unprecedented political changes swept away the rulling order is a matter of only a few months starting in August 1989 are: Poland, Hungary, East Germany, Czechoslovakia, Bulgaria and Romania. The ignition key of the whole process was the policy of *perestroika* (restructuring and *glasnost* (openness) initiated by Mikhail Gorbachev in the Soviet Union. It became clear that the Soviet Union would not oppose political changes in Eastern Europe if the people of those countries so desired and pushed for. The rather long drawn out countries so desired and pushed for. The rather long drawn out Polish experience was a case in point. Change in Poland at later stages came through negotiations and expression of peoples will through ballot. Once the grip of communism was broken in Poland, people at large in other East European countries desirous of similar changes mounted widespread, large-scale and passionate movements against the communist rule and succeeded in ousting them. Except for Romania, army did not take part directly in any other country. It is the common people who spearheaded the movements. It appears that, as the communist rule in these countries were imposed from outside, the people did not accept it and in fact became disenchanted with the way the communist leaders were running the countries. Hence the very first time when it appeared that the Soviet Union would not intervene, the people in different East European countries rose against the ruling order, moved fast and got rid of it. The political changes now underway in these countries encompass taking of power by anticommunist government, multi-party system, western style social democratic political development, and sharing of power by communists and opposition parties. In USSR also, the Soviet Communist Party's monopoly on power has been abandoned, and the stage is set for a multi-party system to emerge. A strong presidential form of government is also in the proeess of being established.

On the economic front, the changes being introduced in East European countries include decentralization of economic decision making and activities, emphasis on market forces and the establishment of private sector, which are among the basic ingredients of a western style capitalist economy.

The above noted directions along which political and economic changes are seen to have been moving in the countries concerned are surely tentative, and the situation in each of the countries is still so volatile that how the political and economic processes and coalitions that may last will eventually shape up cannot be predicted at this stage with any degree of certainty. But it would seem that the kind of communist rule that these countries experienced over the decades since the World War II is now a matter of the past. I would expect, however, that the people of these countries should be aware of the basic socialist principle of equitable access to opportunities, income and resources, which the communist leadership of their countries failed to deliver or flouted and that, therefore, they will be vocal and establish countervailing forces against the differentiating impacts of the market mechanism and the trap of dependent capitalism that entails subjugation of national interests to outside influences. If not, then I am afraid they may face different but formidable sets of problems in not too distant a future.

It would appear that because of huge deficits faced by the USA and the likely increasing inward looking posture of the EC after 1992 and the strict conditionalities usually imposed by Japan, the aid climate facing the Third World in the coming years may be rather subdued. (I shall later take up the question of possible resource availability as a result of reduced East-West tensions and increased detente consequent upon the East European changes).

Since the changes in Eastern Europe, which have virtually ditched communism, are desirable from the point of the Western countries and the international economic system they have developed, one would expect the changes to be and actually are being supported by the West. It has been quite common over the past few months to hear statements emanating from various Western countries and international institutions in support of the changes in Eastern Europe and pledging economic assistance to help the countries sustain the processes and proceed with socioeconomic restructuring and progress. In addition to the offers of assistance extended by individual countries, the rich Western countries have also started coordinating aid programmes for East European countries. Very recently (on 16 February 1990), 24 leading industrial democracies including the EC, the USA and Japan meeting in Brussels gave a strong hint that they would soon give aid to East European countries seeking Western money. They in fact expressed their readiness to coordinate assistance for the East European countries according to the need and situation of each country provided these countries are committed to political and economic reforms (such as market orientation, multi-party system and free election). The EC also recently announced cuts in its export guararantee programme for 66 developing countries–apparently to divert the funds to Eastern Europe. The EC has also asked its 12 member countries to join hands with the World Bank in providing a billion dollar medium term loan it pioneered to help Hungary's structural adjustment. Poland's Western government creditors have agreed to reschedule (a postponement for 14 years) a record 9.4 billion dollars of debt repayment. Emergency medical and food aid are already being provided, which have benefited Romania in particular. All the countries will receive economic aid according to their needs. Fact finding missions will visit the countries for the purpose. Britain and West Germany have also offered to help with management training and access to a know-how funds to facilitate the switch to a market oriented system.

The East European countries together have a current population of about 140 million (135.4 million in 1987), and per capita income of three of the countries for which data are available, viz. Poland, Hungary and Yugoslavia, is over US$ 2000 (US$2, 007, US$2,020 and US$2,300 respectively in 1987). These countries are therefore upper middle income countries and many times better off than all the least developed countries (42 in number with a population of about 400 million) and many lower middle income countries, which are crucially dependent on aid. However, the Third World countries have been receiving aid for decades without much success in improving their socio-economic conditions. There is, therefore, a monotonic repetition of reviewing failures and giving more aid in expectation that things will improve. Now here is a group of countries which were for over 40 years behind iron curtain and ideological opponents, but now they have broken out from behind the curtain and are moving ahead with reforms towards integration with the Western system. This is a big attraction and opportunity for the West. Moreover, these countries offer new situations for the aid givers to operate in; and, given their levels of development and education, these countries may achieve much better results if aided.

Hence, not only that likely massive aid flows to Eastern Europe in the coming years may adversely affect availability of funds for providing aid to the Third world countries but also the donors are likely to be more interested from the point of view of the utilization of aid to provide aid to the East European countries in preference to many Third World countries. Moreover, the USSR is also reportedly keen to attract western capital. All these are likely to make the aid climate facing the Third world rather bleak in the 1990s, given that the overall aid climate, as noted earlier, will itself be rather tepid. However, given strategic importance and pro-western policies and satisfactory aid utilization, particular countries may succeed in attracting substantial aid. but the influence of the donors on domestic policy making in such countries may further increase because they will need to meet more stringent conditionalities in order to secure aid.

The integration of East and West Germany may take place soon. In that case, tremendous infusion of capital into East Germany will be needed to prop up the East German economy so that it moves towards a level comparable to that of West Germany in some years timet–he length of the time to be planned for the process will depend on what the people will be willing to accept. And West Germany will naturally devote lot of its resources to East Germany, which may constrain West German involvement in Third world development.

Also moves are afoot for the whole of Europe to come closer politically and economically. As noted earlier, a single market EC is going to be established by 1992, democracy is emerging in Eastern Europe and German reunification is very much on the cards. Further, there are moves to create an European space with 12 EC and 6 EFTA (European Free Trade Association) countries participating. One school, members of which are known as deepeners, wants to keep EC as the central group of coutries allowing EFTA countries access to the single market but not full membership or decision making powers and granting trade advantages and aid to Eastern Europe. There is another view that seeks to establish a community that encompasses all European countries including Northern and Eastern European countries as well. The proponents of this view have come to be known as wideners. All this indicates that a close-knit Europe and hence a strong Euro-centricism may emerge perhaps in not too distant a future, whatever be the shape, coverage and nature of the association and working relationships. A consequence may be that Europe will be primarily concerned with Europe and its OECD partners, and the Third world countries may be relegated to further back seats in so far as European assistance for these countries is concerned.

While many Third world countries, particularly least developed ones, have failed to attract foreign private capital although they have been trying for it by offering concessions of various types and extents, already there seems to be a rush to move funds to East European countries, particularly by US, British and German investors. These funds have been dubbed 'perestroika funds'. One estimate shows that several firms have alreaby lined up over US$1 billion (Table 1) for the purpose. These investors see opportunities of making profits from markets opening up in East European countries and increased East-West trade. Hence, they are moving in with technical and managerial expertise to support and promote industries and businesses such as modernizing telecommunications, light bulb making, personal and commercial sewing machines, irrigation projects and whatever else appears prospective. Japanese private investors are also known to be exploring possibilities of investing in

Table 1

Funds Lined up by Western Firms for Investment in East European Countries

Firm	Fund	Amount (Million US)
Deutsche Bank	New Germany	421
Alliance Capital	Austria	90
bean, Stearns	First Hungary	80
Tyndall Holdings	Emerging Eastern Europe	250
Scudder, Stevens	Scudder New Europe	186
Total		1,027

Source: *Newsweek*, 5 March 1990, p. 32.

Eastern Europe. The already poor prospects of attracting foreign private investment faced by the poor developing countries are further dented by the onrush of private western investments to Eastern Europe.

Some of the Third World countries used to barter some of their commodities against products needed by them and supplied by East European countries. But now that the international trade of the East European countries will be carried on under market mechanism, the Third World countries may lose these markets in the face of competition from stronger and aggressive trading countries. And it may be even more difficult to secure alternative markets in a competitive world trade regime.

The intense antagonism and confrontation, covert and overt, that characterized the relationship between the two superpowers, with each spending huge amounts of money and other resources in arms race and military preparedness over the past several decades suddenly entered into an altogether new detente phase. *Perestroika* and *glasnost* in the USSR and political changes in Eastern Europe have removed much of the *raison detre* of the East–West confrontation, cold war and tension. It has been estimated that the annual US NATO-related expenditure has been running at a level of about US$ 150 billion, about half of the US total military budget; and that about half of the US arms production capacity (out of about US$ 120 billion) amounting to about US$ 60 billion has been NATO-related. The European NATO members also spend substantial resources for NATO. Now the disarmament option is availabe, and if it is grasped the US and its European Allies can save big sums of monies, which can be diverted to other purposes. The USSR also will save money by cutting down expenditure on armaments industry and military. While the USSR can use the savings to build its own economy which is in serious difficulties, the savings of the US will improve its current account situation and perhaps even lead to a modest surplus.

The consequent reduction of US import demand would reduce demand for world's exports if compensatory demand from elsewhere does not come forth. However, recycling the surplus of such countries as Japan and West Germany to developing and socialist countries will be a counter to the deflationary effect of the reduction of US deficit. The financial capacity of the US and other countries, which will reduce their military expenditure, to provide assistance to poorer countries should increase. Hence, it is agrued by some that the flow of funds to the East European countries need not adversely affect the availability of funds to be provided as aid to the Third World countries. But, as noted earlier, the surpluses are essentially held by the private sector, and it may be difficult for the governments of the countries concerned to increase tax burdens on the people and/or raise allocation for providing aid to Third World countries substantially. Hence, it seems to me that it is unlikely that there will automatically be increased funds available in the donor countries for providing aid to the Third World countries.

I also find it quite difficult to accept the view that the NATO establishment will be cut back in a big way quickly, let alone its dismantling, although one hears that allied governments are contemplating sharp cuts, and that USSR has been expressing its willingness to reduce its arms capability substantially and has, in fact, started withdrawing its military involvement from the East European countries.

First of all, even if there are no major backlashes or setbacks, it may still take some years before reasonably settled and predictable international political configurations can be established in which the power blocs which have so long been so bitter antagonists can confidently work together in a spirit of cooperation and coexistence for peacc, progress and security for all. In the meantime, there will surely be talks, contemplations and even plans on both sides for substantially reducing arms and military capability, but not much may actually be done to that end. A cautious approach has been strongly advocated by, for example, NATO military chief, General John R. Galvin arguing that "... there are problems and turbulence, instability and unpredictability along the road", He suggests that, under the circumstances, "NATO still has a job to do, perhaps a more essential one than ever". (See *Newsweek*, 26 February 1990). I don't think this is either an isolated or only a military view. I believe a cautious and slow approach will be followed by both sides in reducing arms and military capability. And that is, on the assumption that the processes of changes that have begun will continue without serious setbacks and reversals. Otherwise, it may all be back to square one.

I would, therefore, argue that because of donor interests in the Eastern Europe, aid climate facing the Third World as a whole will be adversely affected. However, if the international community can fully grasp the reality of the interdependence among all the countries of the world and that the poorer countries cannot be left behind in the interest of an orderly progress of the global society takes steps to reform the international economic policy and institutional framework and create new ones if necessary in such a way as can adequately respond to the needs and circumstances of the poorer countries, then the prospects of the Third World will improve and the advanced countries will also benefit in the long run via trade and an international system which is more stable and subject to less tension.

Concluding Remarks

A tremendous elation has been reverberating through the West at the dismantling of communism in Eastern Europe and its progressive backsliding in the USSR. Is the process irreversible? Or in other words, will the process of socio economic transformation that has begun in East European countries lead to their full integration into the Western system? That it should is very much desired by the West; and, hence, the vigorous Western push to support and help consolidate and expedite the process is understandable. No doubt, at the root of this Western attitude is the head-on ideological opposition between the two systems.

Now, as the West goes ahead with its East European thrust, can it afford to neglect or assign lower importance to the Third World? While the opportunities available in Eastern Europe may not be neglected the needs of the Third World cannot be ignored because there are compelling reasons for a one-world approach. A neglected and retrograding Third World may give rise to tensions and conflicts in different parts of the world which may, reverberating through the two camps, destabilize the on-going East-West detente building process. Also, for a healthy world system, solution to such problems as the Third World poverty and debt, racism, terrorism, drug trade, environmental degradation, and, above all world economic management system should be sought and found. And the Third World has a crucial role to play in all these. Moreover, because of the size and growth of population, the Third World has the potential for market expansion in future, the extent of which will also depend on the economic growth that these countries will achieve; and the future prospects of the now advanced countries will importantly depend on market expansion in the Third World countries. A serious limitation to the expansion of markets in the advanced countries is the stabilization and even likely future declines in their populations. On their part, the Third World countries will need assistance from the advanced countries for their development. This mutuality of interest is an important dimension of interdependence in the world economy.

But it is essential that the world economic system is appropriately restructured, taking into account the emerging trends and realities, some of which were briefly discussed earlier, and reflecting the importance of the poorer countries so that all countries, rich and poor, benefit equitably from it. The present iniquitous international system has divided the world into segments in terms of economic, political and military power. And indeed within national boundaries, there are huge gaps between the rich and the poor, the employed and the unemployed, those who have access to power (economic, military, social, political) and those who are educated and in command of know-how and those who are not. Just as the gross iniquity in the world system is not acceptable, such iniquity within the nation states cannot also be accepted.

Can the world community at all levels–international, regional, national and local–rise to the occasion and find adequate, effective and equitable responses to the persistent and pressing problems facing the world to-day as it passes through the last decade before the advent of a new century and a new millennium?

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