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## ► To cite this version:

Etienne Peyrat, Kristy Ironside. The Communist World of Public Debt (1917–1991): The Failure of a Countermodel?. Nicolas Barreyre; Nicolas Delalande. A World of Public Debts: A Political History, Palgrave Macmillan, p.317-345, 2020, Palgrave Studies in the History of Finance (PSHF), 978-3-030-48794-2. 10.1007/978-3-030-48794-2\_13 . hal-02971296

**HAL Id: hal-02971296**

**<https://hal.science/hal-02971296>**

Submitted on 28 Dec 2020

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## The Communist World of Public Debt (1917–1991): The Failure of a Countermodel?

*Étienne Forestier-Peyrat and Kristy Ironside*

Communists were among public debt's most vehement critics. Under capitalism, public debt purportedly offered opportunities for profit and necessitated increasing taxes for the poorest categories of the population in order for “bourgeois” states to repay it, while external debt was an instrument of exploitation in the hands of imperial powers.<sup>1</sup> Engels’ prediction that the state would “wither away” also called into question what precisely qualified as state debt: should it be redefined to take into account an expanded public sphere that was not limited to the state per se, but could encompass state-run companies, social organizations, trade unions,

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and other institutions that blurred the boundary between public and private debts? In January 1918, the Bolsheviks repudiated the Tsar's debts—a seemingly new and audacious but, in fact, not unprecedented measure that became known as the doctrine of “odious debt,” or the argument that debts incurred by a fallen regime should not be transferred to a subsequent regime if the debt did not benefit nor was authorized by the population.<sup>2</sup> Public debt, it would seem, had no place in the communist world.

Over the course of the twentieth century, however, communist regimes proceeded to accumulate substantial debts, both foreign and domestic. Shortly after the repudiation, the Bolsheviks began aggressively pursuing foreign credit. When this was not forthcoming, they turned inward and, by the Stalin era, had devised a highly coercive system of domestic borrowing, accumulating billions of rubles in debt to the population on state loans with returns so questionable that the contemporary American economist and Sovietologist Franklyn D. Holzman labeled them a “hoax.”<sup>3</sup> Other communist governments, notably China and Yugoslavia, implemented similarly aggressive domestic bond programs. After the Second World War, the Soviet Union became a foreign creditor itself, lending billions of rubles in money and in-kind to the so-called People's Democracies of Central and Eastern Europe who, in turn, joined it in becoming creditors to budding socialist countries in the postcolonial world. External debts helped build an interdependent communist economic bloc, but also bound together a shaky alliance dominated by Soviet interests.

Foreign and domestic debts, furthermore, proved to be important causes of communist regimes' undoing in the late twentieth century. Though many countries, notably the Soviet Union, were considered creditworthy by foreign lenders until the 1980s, declining economic growth, coupled with unsustainable promises of rising living standards, led them to go on borrowing sprees and develop massive unsustainable debts in the last two decades of their existence. Growing public awareness of long top-secret debts in the late 1980s, along with painful austerity measures, undermined the already tenuous legitimacy of these regimes, many of which had been installed and stayed in power through rigged elections and the repression of their opponents. Their gamble that borrowing from the West to pay for technological improvements would spur production and ultimately raise living standards was a bust; instead, they found themselves stuck with massive loans in currencies other than their own that they could not pay, and the increased hard-currency revenues that were

expected from exports never materialized. As Stephen Kotkin writes, “the capitalists had sold the bloc the rope with which to hang itself.”<sup>4</sup>

Addressing the relationship between communism and public debt in the twentieth century, as this chapter aims to do, allows for a mutual reassessment. Though early communists were deeply critical of the international-capitalist order of public debt and, by the postwar period, claimed to have created an alternative system of self-sacrificing domestic financing and brotherly “mutual assistance,” they made relatively conventional use of public debts to further their political and economic agendas. Moreover, although they would repeatedly disappoint domestic creditors, another radical repudiation of their foreign debts, as had occurred in 1918, did not take place. Mature communist regimes proved unwilling to reject the international order of public debt when they ran into economic trouble, accepting technical solutions to their financial woes and avoiding confrontations with Western lenders. As the anthropologist Katherine Verdery observed, far from teaming up to collectively default in the late 1980s, their willingness to repay their debts revealed “how vital a thing was capitalists’ monopoly on the definition of social reality.”<sup>5</sup>

### PUBLIC DEBT BETWEEN POLITICAL CONTROL AND WAR MOBILIZATION

In the immediate wake of the Russian Revolution, public debt seemed as if it would go the way of other relics of capitalism including profit, private property, and money, but the new authorities quickly sensed its value as a bargaining chip with the former Tsarist regime’s creditors; furthermore, the new socialist regime was broke. During the Russian Civil War, foreign lenders did not abandon hope of getting at least some of their money back, as demonstrated by the relative optimism of the markets: in 1920, 1906 bonds were traded with a 20 percent yield to maturity.<sup>6</sup> Though they were in default, Tsarist bonds were not entirely worthless. In September 1921, Georgy Chicherin, the Commissar of Foreign Affairs, pushed the Politburo to tie resumption of payments to a political settlement with the Allies. An expert commission was created to develop concrete proposals on the debt issue. At the Genoa conference in April–May 1922, Soviet delegates proposed to resume paying some of the Tsar’s debts, but also demanded an immediate large loan in exchange. France insisted that the Bolsheviks assume responsibility for Russia’s debts. As negotiations broke

down, Chicherin and his German counterpart, Walter Rathenau, signed a treaty at Rapallo canceling all financial claims against one another. For the remainder of the interwar period, the Bolsheviks continued to offer partial debt repayment in exchange for new credit and, in the context of the Great Depression, boasted of being a credible debtor at a time when many other countries were defaulting on their foreign debt.<sup>7</sup> They held out hope that they might receive funds from the United States into the 1930s.<sup>8</sup> These efforts proved unsuccessful: no one had forgotten about the repudiation, nor did they trust the communists.

This forced the Soviet Union to turn inward. During the New Economic Policy, the government floated several internal lottery loans which it promoted as a means of protecting the value of money against the problem of hyperinflation, which they inherited from the Tsar and exacerbated through continued excessive currency printing.<sup>9</sup> In 1926, at the dawn of the industrialization drive, citizens' incomes and savings were targeted as internal resources to be better exploited.<sup>10</sup> In 1927, the Soviet government successfully experimented with selling its State Internal 10 percent lottery bond directly to workers in Soviet workplaces, and the so-called "mass subscription bond" was born. Unlike so-called "market" or "free-circulating" bonds—lottery bonds which continued to be sold under socialism primarily to wealthier elites on a voluntary basis and which were fully liquid—mass subscription bonds were subject to strict quotas, participation was virtually compulsory, and cashing them in was virtually impossible. Ideally, workers subscribed for at least 100 percent of one month's average wage to be deducted in ten installments with a short reprieve before the next year's campaign began. Collective farmers, by contrast, were expected to contribute minimum lump sums based on their expected cash earnings from private agricultural production.

Removing bond sales from the marketplace allowed the government to exert considerable "moral pressure" upon subscribers.<sup>11</sup> Unlike Nazi Germany, a famous example of the use of "silent financing," as Middendorf's contribution in this volume (Chap. 12) discusses, the Soviet Union resorted to more explicitly coercive strategies to ensure citizens' compliance. Activists embedded in the workplace, known as the Commissions for Contributions to State Credit and Savings (*Komissiiia sodeistviia goskreditu i sberegatel'nomu delu*, better known as *komsody*) lectured their peers on the bonds' vital contributions to socialist construction, and often threatened a subscriber with social and economic retaliation when he or she offered less than what was expected or less than everyone

else. Although the bonds' purchase was never officially portrayed as anything but voluntary, secret police reports paid close attention to expressions of discontent related to their purchase, aware that many citizens were less than thrilled to subscribe.<sup>12</sup> The coercion involved in meeting subscription quotas, coupled with the bonds' low returns and repeated conversions in 1930, 1936, 1938, and 1947 that extended their terms and reduced interest rates, led the economist Holzman to conclude that they were taxes in all but name.<sup>13</sup>

During the Second World War, the tradition of mass mobilization prevented a collapse of the economy in its first months.<sup>14</sup> The Soviet government turned to war bonds as a source of war financing, as many other belligerents did, at this time. War bonds were sold on the existing mass-subscription model, and the Soviet press expatiated on the enormous sums workers and peasants contributed to defend the Motherland.<sup>15</sup> Issues rose to unprecedented levels: 10.3 billion rubles in 1942, 13.5 billion in 1943, 25.12 billion in 1944, and 25 billion in 1945. The war marked a culmination of the coercive social dynamics driving the mass-subscription campaigns: with the exception of the last, each bond was oversubscribed within about a week of its announcement. While before 1942, subscriptions among workers never reached the ideal sum of the average monthly wage, usually not surpassing two-thirds, in 1945, subscriptions reached 120 percent and even peasants met steep subscription expectations. Between 1940 and the end of 1944, state debt to the population on the bonds more than doubled, from over 39 billion to over 94 billion rubles.<sup>16</sup>

The Second World War also saw the Soviet Union engage more directly with foreign states in the field of public debt. On the eve of the war, in March 1938, the USSR financed the Guomindang's war against Japan with a substantial dollar loan.<sup>17</sup> During the war, the Soviet government finally received foreign loans in the form of credit in-kind from the United States through the Lend-Lease program.<sup>18</sup> After the war, Soviet diplomats were instructed to obtain more credit from the Americans. In a letter to State Secretary Byrnes on 15 March 1946, the *chargé d'affaires* Nikolai Novikov explained that the Soviet government was eager to receive long-term credit to finance reconstruction and suggested tying it to the conclusion of a trade agreement.<sup>19</sup> That the United States and their allies should provide loans to the Soviet Union was perceived by Soviet leaders as part of a moral compact acknowledging the wartime sacrifices of the Soviet people. Similar arguments were made by the Central European countries that soon fell into the Soviet sphere of influence when they asked for credit

from the Bretton Woods institutions. Poland, Yugoslavia, and Czechoslovakia were among the first members of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD) to express such claims. The reluctance of these institutions to provide the amounts demanded by Central European countries merely accelerated the rift between East and West in the burgeoning Cold War.

### A COMMUNIST WORLD OF PUBLIC DEBT?

As communist regimes sprang up across Europe and Asia in the late 1940s, a new communist world of public debt began to take shape. Accepting, rather than repudiating, the previous regimes' debts was one way the new Soviet-backed authorities in Central and Eastern Europe positioned themselves as legitimate heirs to the national state tradition immediately after the war. These debts, both internal and external, were largely contracted for the needs of state-building and some as early as the nineteenth century.<sup>20</sup> At the same time, these states resorted to conversions and monetary reforms designed, in part, to reduce domestic debts. For example, the 1947 currency reform in the USSR reduced state debt on mass subscription bonds from 158.8 billion to 58.8 billion rubles with additional billions in debt *de facto* canceled because the paper bonds were not turned in for conversion by the deadline.<sup>21</sup> Across Eastern Europe, communist regimes sought to renegotiate their foreign debts and, after 1948, became more assertive and antagonistic toward the West. After the Prague coup in February 1948, financial negotiations between communist Czechoslovakia and the United Kingdom were suspended but resumed a few months later as Czechoslovak leaders conceded a debt settlement in exchange for a trade agreement.<sup>22</sup>

Postwar communist regimes' emulation of the Soviet model of public debt is reflected in their aggressive use of domestic loans to finance reconstruction.<sup>23</sup> The Soviet government floated several "reconstruction and development" bonds and by 1951 a record-sized issue of 30 billion rubles was launched. Within just four years, the Soviet Union's domestic debt had risen to 146 billion rubles, up from 28.7 billion rubles in the wake of the currency reform.<sup>24</sup> After the communist victory in China, the financial mastermind of the regime, Chen Yun, initiated a similar mass loan that called upon citizens' patriotism and emphasized the bonds' stabilizing effect on the economy in an effort to gain support from economic elites

on the coast.<sup>25</sup> In Yugoslavia, slogans for its 1948 loan ranged from “Subscribing to the loan is the best patriotic act of every individual” to “Subscription to the national loan is the best way to invest your savings, since it pays 10 percent interest a year and lasts only four years.”<sup>26</sup> A second National Loan followed in August–September 1950 with an intensified propaganda campaign and increased canvassing in the countryside. However, popular “enthusiasm” for the bonds proved elusive; the population complained about arrears on the first loan and about the economic difficulties their purchase entailed.

The consolidation of communist regimes in the late 1940s generated increasing tensions between them and international financial institutions (IFIs). In 1947, the political imbroglio surrounding the Polish and Czechoslovak Soviet-influenced rejection of the Marshall Plan revealed strong disagreements between communist politicians and other coalition members. The two states repeatedly complained of unfair treatment from IMF and the IBRD, despite being founding members of both institutions. Poland walked out of negotiations in March 1950 and Czechoslovakia refused to pay its share of capital, which led to its eventual expulsion in 1954.<sup>27</sup> The only exception to this was Yugoslavia. After the Tito-Stalin split in the spring of 1948, Western countries and IFIs took it upon themselves to “keep Tito afloat.”<sup>28</sup> Yugoslav leaders pressured American diplomats for loans, which were necessary for the country’s survival; at the same time, they tried to keep a low profile as they knew the Cominform would undoubtedly hold these loans against them.<sup>29</sup> The Yugoslav Politburo also never abandoned its distrust toward Western lenders, who sought to obtain political influence incommensurate with the relatively small amounts of credit they were ready to provide.<sup>30</sup> Yugoslav financial stakes with the West nonetheless contrasted with the communist bloc’s drift toward an alternative communist community of credit.

Although the Soviet Union, in many respects, behaved like an “imperial scavenger” in Central Europe, it also became a major lender to other communist countries after the war.<sup>31</sup> Having forced its allies to refuse Marshall Plan aid, providing credit to rebuild their economies was necessary to bolster its legitimacy within the emerging Eastern bloc. Much of this debt was offered and expected to be repaid in-kind, in equipment, and in consumer goods. In January 1948, the USSR gave Poland 450 million rubles in credit in industrial equipment in order to create the steel complex of Nowa Huta, for example.<sup>32</sup> Simultaneously, Central European financial systems were refashioned along Soviet lines, and experts were sent to

Moscow to be trained by the State Bank and Ministry of Finance.<sup>33</sup> The People's Democracies were eager to exchange views and experience in dealing with debt issues with the West, as exemplified by Bulgarian solicitations to Yugoslavia, Hungary, Romania, and Poland to coordinate their behavior against Western creditors. Credit was also needed to prevent the natural trend toward autarky, a consequence of imitating the Soviet economic model. As a result, foreign debt to the Soviet Union grew rapidly between January 1951 and January 1956, by around 11.9 billion rubles, the vast majority of which constituted money loans and credit to the Peoples' Democracies in Central Europe. Poland alone owed 528 million rubles to the Soviet Union by 1955.<sup>34</sup>

Communist leaders and theoreticians emphasized that their practice of public debt fundamentally differed from Western conceptions of public debt, constituting fraternal "aid" and "mutual assistance." The absence of "surplus capital" in socialist economies supposedly changed the meaning of foreign credit.<sup>35</sup> Concrete differences between capitalist and socialist credits revolved more around technical details, however, such as lower interest rates and longer terms.<sup>36</sup> Advantageous conditions were particularly useful when courting Third World countries the Soviet government hoped would go communist, such as Sukarno's Indonesia, which obtained particularly low interest rates in the late 1950s.<sup>37</sup> Smaller, economically weaker countries in the Eastern bloc often emphasized their "backwardness" when attempting to reduce their debt burdens; for example, Albania and Mongolia regularly petitioned to reschedule or cancel outright their trade-related debt. At the end of 1957, the German Democratic Republic (GDR) conceded to the Albanian request to cancel the 61 million rubles in debt the republic had accumulated by 1955, but downplayed it publicly, as the write-off occurred simultaneously as it was asking East Germans to make great material sacrifices in the name of socialism. When the Albanian newspaper *Zeri i Popullit* published a letter of thanks to the GDR government, East German diplomats were embarrassed and tried to cover it up.<sup>38</sup> Similarly, Gomulka expressed his impatience with frequent demands by Mongolia to write off its debt during Comecon meetings, viewing it as a matter-of-fact necessity to honor one's debts.<sup>39</sup>

The solidarity supposedly underwriting communist mutual assistance within the Comecon was tested by the Hungarian revolt in the fall of 1956. Sizable deficits in its balance of payments had made Hungary dependent on Western credit by the 1950s; Imre Nagy and Mátyás Rákosi wanted to reduce this dependence through Soviet loans.<sup>40</sup> After the

“counterrevolution” was crushed, the new Hungarian leadership asked all “friendly countries” for economic help through state and commercial credits in goods and currencies to the tune of 455 million dollars.<sup>41</sup> All communist countries offered help in the form of credit, as their contribution to the fight against counterrevolutionary forces. Zhou Enlai, who was on a tour of Central European countries in early 1956, made grandiose announcements about the Chinese government’s support for Kádár’s government in an effort to prop up his own country’s importance within the bloc.<sup>42</sup> However, this channeling of socialist aid to Hungary also revealed its deepening rifts.

### THE PROBLEM WITH WESTERN LOANS

The increasing use of foreign loans in communist countries was directly linked to their attempts to reform socialist economic systems and correct imbalances through market mechanisms in the 1960s. An alarming decline in growth rates in 1960–1962 prompted communist leaders to pay more attention to the limits of the Stalinist model of industrialization and collectivization. Reform programs were articulated in several countries. International institutions such as the UN’s Economic Commission for Europe and the Bank for International Settlements (BIS) also played important roles in East-West policy and intellectual transfers.<sup>43</sup> These reform programs shifted economies toward external sources of growth. Foreign credit was sought in an attempt to secure much-needed technologies and licenses from the West. Under Khrushchev, the development of new sectors, such as chemical and car industries, was boosted by foreign inputs, financed in part by borrowing.<sup>44</sup> Foreign borrowing was particularly important in countries like Bulgaria and Romania, who wanted to overcome economic “backwardness” and develop full-fledged modern industries. Furthermore, the failure of economic integration within the Comecon and increasing assertion of “national sovereignty” made the pursuit of Western credit particularly important, a fact emphasized by the Romanian leadership in its famous declaration of independence in April 1964 when it refused to become the Comecon’s agricultural base.<sup>45</sup> Lack of integration led to the replication of productive capacities throughout the bloc, accelerating indebtedness in the mid-1960s.

Acquiring foreign debt was seen as a painless process that would repay itself thanks to exports generated by industrial investments and licenses. It appeared to be a miracle solution for communist regimes trying to achieve

stabilization and fight growing social unrest caused, in part, by their populations' mounting economic grievances. While the USSR could finance a more generous social welfare policy with revenues from oil and raw commodity exports until the mid-1970s, other countries developed dependence upon foreign lenders to finance their welfare agendas. This was not yet seen as worrying. Economic planners often saw foreign trade and financial obligations as a beneficial form of external discipline imposed on domestic actors, recreating a lacking market constraint. In Czechoslovakia, the reforms of the late 1960s emphasized the need to relaunch industrial competitiveness thanks to the external constraint of trade with the West.<sup>46</sup> External debt was perceived across the bloc as a way to defuse tensions and engineer a new wave of industrialization without requiring material deprivation and sacrifices on the part of their citizens.

Yugoslavia enjoyed rapid growth based on IBRD and IMF credit due to its closeness with the West and, unlike in other communist societies, where borrowing practices were concealed from the public and figures strictly classified, foreign credit was openly discussed there. Concerns about financial transfers and inequality between Yugoslavia's constituent units were mediated by discussions of foreign loans. In the summer of 1969, a major crisis emerged between the federal government and Slovenia over loans the IBRD had postponed, an action the Slovenes attributed to federal maneuvering. This crisis, known as the "road affair" because the funds were originally earmarked for the construction of two highways, sparked demonstrations in Slovenia and attacks on the federal government by Slovene authorities.<sup>47</sup> This debt-induced crisis was a landmark event in Yugoslav history, for it resulted in a constitutional revision which considerably extended the prerogatives of the republics and self-managing organizations.<sup>48</sup> This, in turn, facilitated a significant rise in public debt, disseminating it across a vast array of public and semi-public organizations. Until then, it was the federal government and Central Bank that had contracted the overwhelming majority of foreign loans; from 1968 to 1981, the share of federally endorsed external debt fell from 95.1 percent to 34.1 percent.<sup>49</sup>

Post-1969 Yugoslavia was an example, albeit an extreme one, of the manner in which external credit hunger was fueled by internal structural transformations, whereby the communist state's traditional monopoly on foreign trade and external financial relations was weakened. While inter-governmental or government-backed trade credits had made up the bulk of communist external debt in the 1960s, private debt contracted with

European, American, and Japanese banks went up in the 1970s. Foreign trade banks expanded their competency against central banks, as well as other investment, industrial, and agricultural banks, and an ever wider array of foreign trade actors.<sup>50</sup> This multiplication of actors coincided with intensified contacts in financial marketplaces and Eastern European countries' growing presence in the emerging Euromarkets. The international networks established by Soviet-controlled banks such as the Moscow Narodny Bank and the Eurobank illustrate the increasing integration which facilitated financing in Western currencies.<sup>51</sup> The status of external debt was therefore progressively changed in nature. It was contracted by actors who were often only remotely controlled by central-state decision makers. If this debt could be considered public, it partially defied the notion of central planning and ratification at the highest level, a situation some criticized as dangerous.

Foreign debt became a key issue for communist regimes during the period 1969–1972. By then, taking out foreign credit was a well-established practice, but Soviet leaders, in particular, were discomfited by how quickly their debts were rising. On 27 April 1971, the East German general secretary Walter Ulbricht was dismissed by the SED Politburo and the new leadership committed itself to reestablishing the primacy of economic relations with the Eastern bloc, disavowing Ulbricht's strong dependence upon Western credit and technology.<sup>52</sup> Debt was the recurring subject of top-secret central reports. In an August 1973 report to the Politburo, Konstantin Katushev, secretary of the Soviet Central Committee for relations with communist countries, emphasized the burden of foreign debts for all Central European countries. Anatoly Chernyaev remarked in his diary: "Everywhere the economy is going down. All these countries hold a considerable debt in Western currencies (in particular Bulgaria and Romania)."<sup>53</sup> This concern was expressed in private meetings with Central European leaders as early as 1970, and Brezhnev routinely emphasized the Soviet Union's inability to come to the rescue of failing debtors due to the burden it had already taken upon itself in the name of socialism.<sup>54</sup>

Attempts were made to rejuvenate the Comecon and, in turn, foster greater bloc integration.<sup>55</sup> Two banks were created to facilitate trade and international investments, but they failed to prevent further financial dependence upon the West. The most illustrative example was the Romanian decision to seek financial support in the Bretton Woods institutions that seemed to provide cheaper means for development. Interest in the IBRD and IMF grew in all communist countries at the end of the

1960s, with the creation of the Special Drawing Rights (SDRs) in 1969 but also with the renewed credit activism of the World Bank group. Reports were produced within the Comecon and in national institutions about them, and the temptation to use them as new sources to resolve balance of payment problems and finance investment grew. In January 1970, a report by the Romanian Bank for Foreign Trade emphasized the advantages of the SDRs and suspected that the USSR, Hungary, and Poland might be interested by joining the IMF.<sup>56</sup> Communist countries indeed seemed caught between different imperatives. On the one hand, Comecon reports criticized the IMF and the IBRD as “tools of imperialism” and tried to create their own financial institutions. On the other hand, several states were tempted to branch out on their own. In late 1971 and October 1972, Romania blocked attempts by Comecon organs to adopt a joint position toward the Bretton Woods organs as they were in the midst of negotiations with them.<sup>57</sup> Although Romania made its project known to other Comecon countries in May 1972, its adhesion to both organs in December 1972 came as a thunderbolt.<sup>58</sup>

### SILENT FINANCING AND ITS DISCONTENTS

While some Communist leaders began to worry about the growth of foreign loans, domestic debt was also becoming a cause for concern. Following Stalin’s death in March 1953, the quasi-compulsory mass subscription bonds came under increased scrutiny as contradicting the new emphasis on raising living standards. Expected subscription amounts for low-earning citizens were scaled down and republic authorities were informed during the 1955 campaign that “observance of the voluntary principle” was now expected of them—in other words, to reduce the emphasis on coercive mobilizational tactics that helped to ratchet up subscriptions and the state’s debt on the bonds.<sup>59</sup> The Ministry of Finance also began to warn that payments on the bonds for interest and prizes could not continue at current levels due to the burden on state finances and the inflationary risks associated with introducing billions of rubles into circulation in the form of interest, prizes, and redemption payments, money that could not be matched by consumer supply. In 1956, Minister of Finance Arseny Zverev predicted that, by 1960, state payments would reach 37.7 billion rubles, up from 30.2 rubles in 1955, or a rise of 25 percent. The government, by then, owed 228 billion on the bonds. By the end of the sixth Five-Year Plan, that would rise to an estimated 350 billion

and, by 1960, the Soviet government would have to make 21.5 billion rubles in payments, he emphasized. Bondholders were poised to “recapture a real nest egg, possibly worth two or three times what [they] had paid for it,” in the words of long-time critic of the bonds, Franklyn D. Holzman.<sup>60</sup>

In March 1957, the presidium of the Party Central Committee decided to abolish the bonds, leaving them “in the hands of the bondholders (as a symbol of their investment in the common project of building socialism).”<sup>61</sup> That April, in meetings with workers and peasants in Gorkii, Khrushchev came clean about the size of the state’s debt—by then, around 260 billion rubles.<sup>62</sup> Though they had played a crucial role in financing socialist development, Khrushchev explained, the mass bonds had become a drain on state finances. The government was stuck in a “vicious cycle” because payments rose with each passing year: he estimated that in 1957, around 16–17 billion rubles would be spent on prizes and redemption payments, while in 1958, the government would pay 18 billion rubles and, by 1967, 25 billion rubles—almost the entire sum that would be obtained from planned proceeds of the bonds in 1957.<sup>63</sup> As a result, the government planned to halt all future issues as of 1 January, 1958 and freeze payments on existing bonds for 20 years. A “light bond” of 12 billion rubles was issued in 1957 instead of the planned bond of 26 billion. Despite the massive unpopularity of the move and accusations that the Soviet government had stolen “our only savings,” a recurring line in letters of complaint, the last mass subscription bond was significantly oversubscribed.

The abolition of mass domestic loan programs was progressively implemented by all communist regimes. The aforementioned rise of external debt as the major source of economic and technological investment reduced the importance of such domestic borrowing, and socio-political stabilization diminished the need for and advantages of Stalinist mobilization methods. This paralleled a broader shift ongoing elsewhere, as illustrated by Matthieu Rey in his chapter on Iraq and Syria (Chap. 14), which increasingly turned to international organizations like the IBRD for loans to finance their development. The only country that continued to rely upon domestic mass-mobilization methods was China, now in open conflict with the Soviet Union. Mao emphasized the need for domestic debt to ensure popular support for the Great Leap Forward and because “the Soviets wanted their money back,” a slogan that played upon popular rhetoric about usurers.<sup>64</sup> The end of these mass loans did not mean the

end of domestic debt in communist countries, but a turn toward forms of silent financing, at a time when other non-communist nations did the same thing.<sup>65</sup> The phrase is particularly apt as all countries featured high levels of secrecy and dissimulation in official publications about the economy and the size of their public debts.<sup>66</sup> Financial experts in communist countries generally denied the existence of macroeconomic imbalances that justified deficits in capitalist economies. The existence of a budget deficit was never officially recognized by communist governments; instead, deficits were financed by direct transfers from the State banks and savings banks.<sup>67</sup> Savings steadily increased in these countries: in the USSR, they rose from 10 billion rubles in 1959 to 131 billion rubles in 1978.<sup>68</sup> This system was far from uncommon in post-1945 Western Europe, but was progressively abandoned in the 1970s, at a time when communist regimes increasingly relied upon it.

Internally, communist central bankers voiced criticism not dissimilar to what led to major reforms in Western countries. In the Soviet Union, the State Bank complained in November 1966 about the “insincerity” of the state budget for 1967, which featured an official deficit of 2.9 billion rubles, “whereas the actual budget deficit would be much higher,” due to the manipulation of financial data. The short-term resources of the State Bank were used to finance long-term state investment, a policy opposed by the State Bank, to no avail.<sup>69</sup> A similar case was made by Nikola Lazarov, head of the research unit at the National Bank of Bulgaria, in July 1969. He reminded the government that the state budget had been replenished for several years by resources coming from the two main savings banks of the country, the DSK and the DZI. The state owed 1.1 billion levas to the DSK alone, since the DSK had transferred between 1954 and 1966 61 percent of all new savings to finance the hidden deficit of the state. The problem, Lazarov insisted, was that the Ministry of Finance did not intend in the least to pay this money back and only paid interest to the savings banks.<sup>70</sup>

This form of “silent financing,” not dissimilar from the methods implemented in Nazi Germany, was facilitated by direct state control over intermediary financial institutions, such as savings banks and insurers. The major difference, however, lay in the absence of a context of mass mobilization through war, since silent financing was here a direct result of the transformations communist regimes had undergone since the 1950s: the rhetoric of material sacrifice inherent to domestic borrowing campaigns became incompatible with the promise of rising living standards and the

population's savings had to be dealt with more carefully in order to avoid exacerbating inflationary pressures and depressing consumption.<sup>71</sup> The government had to accept the creation of a secondary market for state bonds in order to satisfy popular requests, although savings banks enjoyed advantageous conditions for buying back the bonds.<sup>72</sup> In the wake of the 1957 *de facto* default, the Soviet government enthusiastically promoted investing in "market bonds," that is, the 3 percent lottery bonds that were fully voluntary and liquid. A new 3 percent lottery bond was launched in 1966, converting the 1947 issue and reducing interest and prize payments; that issue was, in turn, converted in 1982. Repeatedly converting the bonds was unpopular: older citizens, in particular, lamented perpetually postponed repayment, complaining about low living standards and criticizing the younger generation for lacking their political consciousness when it came to making investments in socialism.<sup>73</sup> The Ministry of Finance diligently answered their letters, but held onto their investments, for now. The mass subscription bonds were not repaid until the mid-1970s, at which point inflation had undermined their value and many older bondholders had died without seeing the state's debt repaid.

### TENSIONS AND DIVISIONS IN THE BLOC

The mounting contradictions of communist economies became obvious as Poland, Romania, Yugoslavia, and the GDR found themselves trapped in severe debt predicaments in the early 1980s. It is worth recalling, however, that the unity of the communist bloc was first tested in the mid-1970s. In September 1974, North Korea was the first communist country to suspend service on its debt, which was estimated at 400–700 million dollars, taking aback its creditors in the West and Asia.<sup>74</sup> They expected other communist countries to help the failing state, but no such solution was offered, since both China and the Soviet Union had grown impatient with the quirks of the North Korean regime by then. Western bankers who had lent money to North Korea were surprised by the lack of solidarity between communist countries, in contradiction with the basic assumption they had made until then. This forgotten debt crisis had the short-term effect of turning North Korea once again into a political and economic "Hermit Kingdom" after a decade of expanding contacts with the non-communist world.

North Korea may have been odd enough a country to be discarded as an exception by Western financiers, but its default coincided with a

growing awareness that foreign debt in the communist world was reaching perilous levels. Leading economists and planners in several countries criticized the debt accumulation that had made possible generous social programs, or the “unity of social and economic policies,” as proclaimed by Erich Honecker and Edward Gierek.<sup>75</sup> In 1976, the heads of two East German research institutes submitted a report outlining the perils of a continued increase in external debt for the regime.<sup>76</sup> The Planning Commission was a stronghold for opponents to external indebtedness and its chairman, Gerhard Schürer, convinced the Central Committee secretary for economic affairs, Günter Mittag, to sign in March 1977 a joint letter to Honecker, pointing out the already tense situation on foreign currencies, exports, and debt.<sup>77</sup> The Kremlin had also become concerned regarding these countries’ debt accumulation and the social instability it could create. Events such as the June 1976 unrest in Poland led Soviet leaders to discuss the issue with a reluctant Polish government, further increasing Moscow’s qualms.<sup>78</sup> Some national leaders also realized that they could leverage this situation to their advantage with Moscow. Debt was routinely mentioned as a reason for Moscow not to reduce subsidies on oil and raw materials. Moscow had to save its allies from falling into the hands of Western capitalists, claimed the Bulgarian Communist Party leader Todor Zhivkov in April 1978 when he came asking for more aid.<sup>79</sup>

Moscow did provide some help, but remained in a situation significantly different from its allies—despite being forced to import food, for the time being, it maintained a relatively low level of foreign debt and the rising price on oil products replenished its coffers.<sup>80</sup> Its foreign debt nevertheless rose over the course of the 1970s. Estimates vary on the exact level of Soviet foreign debt, with the US Directorate of Intelligence putting it at 1.8 billion dollars in 1970 and 17.8 in 1980.<sup>81</sup> By the mid-1970s, the Soviet government was still considered a first-class borrower because of its centralized control over export revenue and commodities-based currency flows and, as a result, Western lenders were eager to give them seemingly “riskless” loans; however, they were unaware of the exact extent of its external debt due to statistical manipulations, the peculiarities of Soviet accounting practices, and price distortions.<sup>82</sup> Meanwhile, the Central and Eastern European countries plunged into unprecedented levels of indebtedness in Western currencies, in part due to the oil crisis and declining export revenues. Yugoslavia’s debt jumped from 3.4 billion dollars to 20.6 billion during the 1970s and the reduction of remittances from Western Europe only sharpened the crisis.<sup>83</sup> In 1981, the overall debt of

communist countries stood at around 90 billion dollars. The Soviet Union was also largely responsible for the debt crisis that erupted after its invasion of Afghanistan because of the restrictions on credit imposed by the Reagan administration in retaliation.

The debt crisis that unfolded was remarkable for the relative passiveness that characterized communist states' responses. Outright attacks on foreign debt as tools of global imperialism were largely absent from the discussion. The first reason for this silence was internal divisions within the bloc. Faced with financial difficulties, each country tried to defend its own case with little concern for others. If anything, they wanted to assure Western creditors that they were not just another communist country in trouble. In March 1980, the managers of the East German Bank for Foreign Trade met with their Czechoslovak counterparts, who informed them that they were trying to obtain credit from the West and insisted that they were far less indebted than other communist countries and were "first-class borrowers."<sup>84</sup> For GDR leaders who felt the pinch of the credit crunch, such an attitude was anything but cooperative. They used their own connections to get an exclusive loan from the Federal Republic of Germany (FRG) in the summer of 1983, the infamous *Milliardenkredit* negotiated by Bavarian politician Franz-Joseph Strauss. Romania soon followed a course of isolation and attempted to mobilize political allies in a rhetoric that avoided any reference to communism whatsoever. Asking for French support in their dealings with the banks and the IMF, the Minister of Foreign Affairs, Ștefan Andrei, suggested to Mitterrand that he could become a new Napoleon III and save Romania from the lenders, preventing it from falling back into the arms of the Soviets who had purportedly offered several billion dollars in loans.<sup>85</sup> The allusion to French help in creating Romania in the twentieth century was well in line with the new rhetoric of Ceaușescu's regime but not with the rhetoric of communist solidarity.

Western lenders and IFIs contributed to this division by adopting a conciliatory position. The IMF played a facilitating role in the negotiations pursued by the Club of Paris and the Club of London. The first rescheduling agreement was signed between the Club of Paris and Poland in April 1981 for 2.2 billion dollars.<sup>86</sup> The IMF expressed its support for a rescheduling of Romanian debt in 1981–1982 and maintained communication channels with the Romanian leadership amid rising distrust toward other lenders. The Reagan administration encouraged a policy of "differentiation" between communist countries and, although they criticized this

policy, their leaderships were quite conscious that Western partners were ready to make concessions and no one was tempted to follow a confrontational course.<sup>87</sup>

A second reason for the absence of joint struggle was that the debt crisis could serve the interests of political actors engaged in power struggles. Although the Soviet Union provided some financial help to Poland at the peak of the crisis, observers speculated that Soviet leaders might find in the debt crisis a convenient way to bring the Poles back into the communist fold. Media coverage of debt problems became a vehicle for indictments of former rulers in several countries.<sup>88</sup> More figures were disclosed to IFIs and lenders and popular support was sought after to give credibility to structural reforms. In Yugoslavia, a new group of politicians embraced reform plans prepared with the IMF in an attempt to evict the old guard. Federal Prime Minister Milka Planinc shielded her actions behind the demands of the IMF and pushed through several new laws in July 1983. In East Germany, Günter Mittag and Erich Honecker strengthened their political control through managing external debt but their compromises with the West infuriated the "Moscow fraction," whose members secured the dismissal of Pro-West figures in the 1980s and sent incendiary reports to Moscow.<sup>89</sup>

A third reason had to do with the fact that several communist states saw themselves not only as debtors but also as lenders to the Third World.<sup>90</sup> By November 1979, the Soviet government had adopted stricter guidelines for credit to Third World countries and had taken measures to reduce its exposure to various risks of credit. This explains the difficulty involved in canceling the debt of underdeveloped countries: indeed, Fidel Castro and his associates found it difficult to mobilize communist leaders beyond private statements of solidarity. Outright criticism of the order of debt was limited to those communist countries that leaned toward the non-aligned movement. Yugoslavia and Romania shared sympathy for the group of 77 pursuing their objective of new economic relations with developed countries.<sup>91</sup> But even these countries had contradictory interests. As it pleaded for a comprehensive remaking of the international financial system and a debt write-off for Third World countries, the Romanian leadership reminded the same countries that "Romania, being still a developing country itself, needed all external resources and could not accept a cancellation or reduction of debts."<sup>92</sup> Similarly, the Soviet Union refused to side openly with Latin American countries in their struggle against Western creditors and the American Treasury.<sup>93</sup> At Fidel Castro's request, the

Soviet Central Committee created an ad hoc commission that concluded in June–July 1985 that developing countries owed 26 billion dollars to the USSR and should repay this debt.<sup>94</sup> However, after 1984, Castro was left alone in the Cartagena Process group, convoking a Latin American conference to denounce debt.<sup>95</sup>

Policies implemented in response to mounting debt in the 1980s diverged in significant ways across the bloc. A majority of Central European countries adopted austerity measures. While they varied in their severity, one common feature was the erosion of political legitimacy they caused. Jonathan R. Zatlin has convincingly demonstrated that East German leaders undermined their own legitimacy by multiplying concessions to the capitalist system in the 1980s. Mittag's policy to cut costs and increase exports demonstrated the failure of socialist ideology and practice: "The political imperative of staving off insolvency deepened the very reversal of means and ends the socialist ideology promised to rectify."<sup>96</sup> While Mittag condoned clandestine operations to obtain Western currencies through the infamous *Kommerzielle Koordinierung*, and diluted the unity of state action by creating parallel accounting systems, Hungary could sell itself as a "Swiss-style banking center" to investors.<sup>97</sup> Communist regimes did not manage either to use debt repayment as a way to improve their domestic legitimacy or to increase accountability. While their financial creditworthiness was progressively repaired by the mid-1980s, internal tensions increased. In Romania, the endeavor to pay back the entire external debt at an accelerated rhythm led to considerable suffering among the population, but also discontent among high-ranking officials and technocrats who criticized the very economic legitimacy of a move they blamed upon Ceaușescu's wounded pride.<sup>98</sup>

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On 12 April 1989, Ceaușescu triumphantly declared to the Central Committee that Romania had repaid its external debt in full: "For the first time in her long history, Romania has no more external debt, pays tribute to nobody and is truly independent, economically and politically!"<sup>99</sup> This delirious expression of national pride illustrated the wide gap that had emerged between him and the Romanian people, who had by then hardened against him because of the painful material sacrifices this had required, but also the equally puzzling situation of a Communist leader who had been squarely focused on repaying foreign capitalist lenders for a decade.

Far from trying to remake or challenge the rules, Communist leaders of the 1980s had fully accepted the capitalist order of public debt. This undoubtedly factored into the demise of these regimes at the turn of the decade.

By the early 1990s, the countries of Central and Eastern Europe had come full circle on the issue of public debt, confronted once more with the question of who should inherit the burden of the previous regimes' debts. Here too, their responses are telling. The argument that "odious debts" need not be repaid was not seriously revisited—although communist states' questionable popular mandates to contract such massive debts could have made for a legitimate argument. Managing their debts figured prominently in the new regimes' capitalist transition agendas. Debt write-offs were also offered as an incentive to avoid the temptation to fall back upon socialist planning habits and fully transition to capitalism by Western governments, especially to heavily indebted countries such as Poland.

Ironically, perhaps no post-communist country's response was as diametrically opposed to debt repudiation as that of Russia. As the successor state to the Soviet Union, the Russian government assumed much of its estimated 85 billion dollars debt, and viewed repaying it as an important strategy for regaining Russia's geopolitical status. Russia became a member of the Club of Paris in 1997, repaying its debts to the group 14 years ahead of schedule in 2006. Of late, Russia has once again positioned itself as a benevolent creditor to its economically weaker allies. Vladimir Putin has used debt cancellations as a political tool, and official sources put these as high as 140 billion dollars over the last 15 years. For example, in early 2016, Russia allowed Mongolia to write off 97 percent of its debt to Russia acquired during the Soviet period, which, as of 2010, totaled 174.2 million dollars.<sup>100</sup> On the domestic debt front, the results are more mixed. While most of the former Soviet republics defaulted on their domestic debts upon breaking away from the Union, Yeltsin promised to repay "lost Soviet savings" to the Russian people, a process that has repeatedly stalled.<sup>101</sup>

The financial crisis of 2008, which resulted in a violent economic downturn and a massive withdrawal of capital in much of Central and Eastern Europe, saw some countries looking for lessons for how to deal with external debt in the communist past. In Bulgaria, the "secret bankrupts of communism" were associated with the corruption and incompetence of contemporary political elites.<sup>102</sup> In Romania, journalists revisited Ceaușescu's claim to have fully liquidated external debt. In Poland, these

discussions were tightly linked with controversial memories of communism, and the announcement in 2012 that “Gierek’s debt” to the Club of London had been liquidated renewed debates about the dismantling of welfare benefits that was supposed to pay for it. This lasting fascination with communist-era debt can, perhaps, be linked to the secrecy that long surrounded it. The truth is, however, that the fall of communism did not reveal any major discrepancies between official and “real” figures, contrary to what some expected.<sup>103</sup> The mystery of public debt, in a sense, became a metaphor for regimes that made secrecy a fact of life to the point that it became detrimental to their own interests.

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