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THE LIBERMAN PROPOSAL FOR MANAGING SOVIET INDUSTRY

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THE LIBERMAN PROPOSAL FOR MANAGING SOVIET INDUSTRY

A proposal for a revision of the present Soviet system for controlling industrial enterprises 1/ recently has been receiving widespread attention in the Soviet press. This proposal, originated in March 1961 by an obscure Soviet economist, Ye. G. Liberman of the Economic-Engineering Institute at Khar'kov, seeks to simplify planning and control and to eliminate the conflict of interest between the individual enterprise and the central planners. 2/ To accomplish these objectives, Liberman proposes that detailed central regulation of individual industrial enterprises be reduced and that central control be exercised by imposing on enterprises a single success criterion -- "profitability" -- on which all bonus awards would be based. To provide sufficient incentive for enterprises to maximize profitability, which is defined as total profits divided by total (fixed plus working) capital, the size of bonuses would be increased, and bonuses would be determined in proportion to profitability, depending on the size of the enterprise.

Under the Liberman proposal, major production targets would continue to be determined centrally. Although the assortment of goods and delivery schedules would still be determined centrally, direct contracting between suppliers and consumers apparently would become more significant. The meeting of these three obligations would continue to be a prerequisite for the receipt of any bonus award. Other targets -- cost reduction, investment, labor productivity, introduction of new technology, and consumption norms for material inputs -- would be determined by the individual enterprises. Liberman contends that under the single incentive to maximize profitability, enterprises would improve on their present performance in respect to these targets and that, therefore, the present detailed central control would be unnecessary.

Liberman recognizes that present industrial prices must be modified in order to avoid discouraging enterprises from producing some products simply because errors in price setting by the central planners make their production unprofitable. He suggests that prices be raised in such instances or that bonus schedules be adjusted in the absence of price changes. He does not envisage, however, that changes in prices will be used by the central planners as a major means for influencing what is produced in industry nor of reallocating resources among enterprises, and he in no way is suggesting that individual enterprises be given increased control over the prices of their products.

Innovations of the Proposal

The Liberman proposal contains four novel features. First, the proposal would permit enterprises to plan many of their own targets, thus reducing the inefficient "petty tutelage" over individual enterprises now exercised by the central planners. Under the proposal the role of the central planners would be to determine the production, assortment, and delivery targets for each enterprise, to determine "large-scale" investment, to coordinate detailed plans initiated by individual enterprises, and to revise prices periodically to avoid discouraging production of products needed in the economy.

Second, the proposal implicitly introduces a return on invested capital by linking bonuses to profits as a percent of capital of the enterprise. This feature, which would encourage enterprises to make more intensive use of their plant and equipment and to minimize their holdings of stocks of new materials and semifinished goods, has not been the subject of much discussion in the literature but, to judge from its favorable reception, satisfies a recognized need. Without this feature the new success indicator in principle would be very similar to the present cost reduction criterion that is now used in some industries.

Third, the proposal would base awards on the excellence of enterprise performance both in relation to its own past performance and to the performance of other enterprises. The present principle of awarding bonuses on the basis of fulfillment or overfulfillment of planned targets has been criticized frequently because it rewards enterprises for making improvements over their past performance but takes no account of their levels of performance in relation to other similar enterprises. Under the proposal, enterprises would receive bonus awards based on the levels of profitability which they maintain as well as on improvements which they may make in these levels.

Fourth, the proposal would reduce the incentive for enterprises to "underplan." Under the present system, which rewards overfulfillment heavily and penalizes underfulfillment of targets, it is to the interest of the enterprise to obtain as low a target as possible. Recognizing this tendency, the central planners endeavor to force targets as high as possible, with the result that the final levels set for each target are essentially negotiated compromises rather than feasible maximums. The Liberman proposal seeks to eliminate this conflict of interest between the enterprise and the central planners. Under the proposal the bonus award for the attainment of a given level of profitability is greater if it results in fulfillment or slight underfulfillment of a high profitability plan than if it results in overfulfillment of a lower profitability plan. Although Liberman contends that enterprises would no longer seek low production targets under his proposal, it is likely that enterprises might still strive for low production targets because no profitability bonus would be paid unless the production targets were met.

Prospects for Adoption

Prospects appear poor for early adoption of the proposal, at least in the form proposed by Liberman. Comments on the proposal by high-level Soviet economists have ranged from wholehearted support by Academician V.S. Nemchinov 3/ to sweeping denunciation by former Minister of Finance A.G. Zverev. 4/ The bulk of the comment, however, is typified by that of the editors of the Ekonomicheskaya gazeta (Economic Gazette), organ of the Central Committee of the Communist Party, 5/ who display considerable skepticism toward using a single, universal criterion of success and recommend that the proposal be subjected to careful testing.

The principle of using profitability as a success indicator and the method of relating bonus awards to profitability, however, have themselves received relatively little public criticism and eventually may be adopted in some industries either in conjunction with other success indicators or possibly alone. Public criticism has centered on the use of profitability as the sole criterion for all industries and on the reduction by the central planners in the amount of detailed regulation of the performance of individual enterprises. Although many of the critics also are opposed to "petty tutelage" over the activity of individual enterprises, they are skeptical that the use of the profitability criterion alone will insure satisfactory performance in all enterprises on such targets as volume of production or increased labor productivity.

In view of the cautious reaction to the proposal by most critics, it appears doubtful that the principal parts of the proposal will be seriously considered for adoption until after additional discussion and considerable testing. Liberman has announced that the proposal is to be tested soon in a number of enterprises in Khar'kov and elsewhere. 6/ Because successful operation of the revision may depend in part on a modification of present prices -- a requirement that cannot be simulated readily under conditions of limited testing -- the significance of the outcome of these tests is in doubt.

Evaluation

The Liberman proposal appears to bear little resemblance to "market socialism" as envisaged by the Polish economist Oskar Lange or as practiced in Yugoslavia. If adopted in its present form, its incentive features should result in some improvement in efficiency in industry, the extent depending on the degree of decentralization of decision-making actually put into practice and on the degree of incentive provided by the particular bonus schedules used. The precise effects of the proposal, however, cannot be evaluated at present because of its vagueness on these two points and on other critical points (such as pricing policy) and because of uncertainty as to the ultimate form in which it may be adopted.

Analyst:

Sources:

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2. Nepreryvnost' v planirovanii i pokazateli gosudarstvennogo plana (Continuity in Planning Indicators of the State Plan), Moscow, 1962, p. 383. U.
3. Pravda, 21 Sep 62. U.
4. Ekonomicheskaya gazeta, 13 Oct 62. U.
5. Ibid.
6. New York Times, 20 Oct 62. U.