

# RADIO FREE EUROPE *Research*

## COMMUNIST AREA

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### SITNIN ON THE WHOLESALE PRICE REFORM

V. Sitnin, the Chairman of the State Prices Committee, has explained in a long article in Kommunist (No. 14, 1966) the broad principles of the reform of wholesale prices which is to take place next year.

For years past the coal-mining industry, iron ore and manganese ore mining, the production of sulphuric acid and numerous other raw materials and fuels have been making planned annual losses because the present prices are too low. As a consequence of the unduly low prices for coal and ore, many metal prices have also been underestimated.

In 1964 the coal-mining industry made a loss of 16%, whereas instrument manufacture showed a profit of 50% on the basis of its production funds. There are other branches where profitability ranges between 100 and 200% p.a., and the wide range, according to Sitnin, makes it impossible to use profit to judge the progress of a given factory, as is required by the September Plenum of 1965.

### The Energy Sector

Wholesale prices for coal are to be raised by 75% next year, which should enable the industry to return a profit of 7.5% on its production funds.

An even more drastic increase is to take place in the price of crude oil, which is to go up by "more than 100%," with the net profit being paid out largely as rent. Nevertheless petrol and diesel oil prices are not expected to

rise appreciably, in order to avoid slowing down the mechanization of agriculture and the increasing motorization of the economy as a whole.

The major changes reflect the overall energy shortage, particularly reflected in electricity and hard coal, which affects the European parts of the USSR. Three-quarters of Soviet fuel resources are in the eastern areas, but the major demand is in the industrialized west. In the first half of 1965, Soviet fuel output grew by 7%, whereas the growth of industrial production was 9.3% (Pravda, 31 July 1965).

The 7-year plan (1959-65) was supposed to see the introduction of new coal-mines with a capacity of 217 million tons a year. But in practice pits with only about 130 million tons of new capacity were completed (Pravda, 29 August 1965), leaving a major gap which could not be filled even by the rapid expansion of the oil and gas industries. As the Financial Times (17 August 1965) put it:

.... Excessive reliance was placed on oil as the supplier of expanding demands for fuel. The recent development of the output of fertilizers and of artificial fibres will have created a competing demand for oil, with resulting difficulties.

Another reflection of the energy deficit problem is that, according to Sitnin, the coal-mining industry is to pay only 3% p.a. in interest on its capital, whereas industry as a whole is to pay 6%.

#### Profit Margins

In most industries, including ferrous metals, non-ferrous metals, oil, gas and engineering the profit index is to range between 8-15% of production funds. In the chemical industry it is to be reduced from 20% to 15%, presumably to encourage market growth, while in forestry it is to rise from 8% to 20%. This ratio of profit to production funds is to be the basic index of profitability.

Sitnin rejects the views of those economists who have been arguing in favor of a uniform rate of profit per ruble of production funds. He says that if this were approved, it would be impossible to stimulate production by the use of prices or to use prices to redistribute investments.

### Quality

The new price lists, especially in the engineering industry, are to contain a whole system of increments for high quality and of discounts for poor workmanship. Higher quality will therefore mean higher profitability provided that demand for the goods concerned is also high.

### Retail Prices

Sitnin repeats the slogan of the 23rd Congress concerning an overall reduction of retail prices, and argues that because of this it is not possible to raise wholesale prices so much that losses would result in the consumer industries. He criticizes one school of economists, which has argued for a sharper increase in wholesale prices on the theory that after the reform there should be only one price level for both group "A" and "B". Sitnin finds this view unrealistic, because in group "B" there are whole industries which are unprofitable (such as meat, milk and fishing) coexisting with highly profitable industries such as wines, spirits and tobacco.

In heavy industry the highly profitable oil and gas industries coexist, with coal-mining and iron ore extraction among the big losers. Sitnin claims that to overcome all these differences would need a 40-45% increase in heavy industry prices, which is too big a leap for the immediate future.

### Planned Loss Factories

Some economists have been proposing that in order to eliminate all subsidies, prices should be based not on average industry-wide costs but on the costs of factories with higher costs which are included in the plan. Sitnin finds this unacceptable because if coal were priced at the level needed for the worst pits, it would involve much higher prices for the whole of heavy industry. In turn that would involve losses in agricultural machinery production, automobile manufacture and the service trades. Sitnin therefore concludes that the way to eliminate plants making planned losses is by improving their work and by cutting costs. Even so there will still be some of them after the reform has been implemented, though the number of plants needing subsidies will be considerably reduced.

### Average Price Rise 11%

Wholesale prices for heavy industry products are to be raised by about 11-12% on average, giving a normal



profitability rate of 15% on production funds employed. This should result in no change in the present distribution of national income as between consumption and accumulation. Sitnin does not support the theory that all expansion should be paid for by an industry's own internal resources. He argues that if such a rule had been made the rapid expansion of the chemical industry would have been stunted by the need to charge unnecessarily high prices.

Even after the reform, the meat industry and some mineral fertilizer production will still be unprofitable, the milk and fishing industries will be showing only a small profit, and the textile industry will still be highly profitable. Thus change will be slow, rather than drastic, and many of the disadvantages of the present situation will continue for the next five years at least.

For most branches of light industry, Sitnin is aiming at a profitability rate of 30-35% on production funds, and about 6-8% on current manufacturing costs. For electric power production the profitability margin is to be 10% on funds and about 50% on the basis of current costs. (This maximal profit margin for electricity is also presumably a reflection of the present tensions in energy supply).

#### Freight Changes

In general, rail freights will remain at the present price levels, but they will be increased for short distances and reduced for long hauls. This change will make truck transport more profitable over the shorter distances.

#### Effective July 1st 1967

The new wholesale prices for both heavy industry and group "B" will take effect on 1st July 1967. As from the beginning of 1967 new prices will be introduced in the light and food industries in order to make the transfer to the reformed system of management feasible.

#### Another Change Before 1971

Sitnin reports that another major overhaul of wholesale prices can be expected when the 1971-75 plan begins. He therefore appreciates that the present changes are only an interim solution, and he also argues that the current amortization rates must also be revised during 1966-70 to make a quicker write-off of machinery possible. In 1970 the basic funds of industry are to be revalued, in order to provide a more "correct value" basis for the next five-year plan.

Conclusion

Sitnin ends his article by rejecting free price formation as an "idealized practice of the first years of the N.E.P." But he immediately qualifies this dogmatic statement on behalf of his own Committee's administrative rule by saying that:

"in future we should more widely introduce the practice of fixing calculation norms which allow the factories themselves to form prices on the basis of these norms, and should introduce limit prices. The time has come to increase the role and expand the rights of the factory in price formation." Evidently in the next year or two we shall gradually have to accumulate experience in this field, to perfect the mechanism of price formation, on the essential condition of a single state price policy and of the guiding role of the state in price formation."

Hence the principle of floating prices fixed by the factories within approved limits and of limit prices to guide those drawing up direct contracts has apparently been accepted. Sitnin will be watching Hungarian and Czechoslovak experience in these fields during 1967 and 1968, and towards the end of the present five-year plan yet another short but important step forward is likely to be taken towards rational instead of arbitrary prices.

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