Chapter VI

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Rapid economic growth was possible in the Russian/Soviet situation only through a strategy of synchronized investment over a wide range of technically related industries. Extensive co-ordination of investment decisions was the only effective way to sustain investment. In other words, as we have argued elsewhere in this work, what the Russian/Soviet situation needed was a Nurkse/Rosenstein-Rodan type of balanced growth process. However, in an economy such as the Russian/Soviet one, which had lagged far behind in development a mere balanced pattern was not enough to make investment profitable. With the advanced world progressing towards ever larger scales of production, it was necessary to have large indivisible plants in all industries.

The organizational methods appropriate for the task of synchronization of investment over a wide range of technically related large-scale industries included, among other things, massive centralization of decisions, as also accumulation in sudden large-scale bursts rather than by slow acceleration. Successful accumulation of this nature in its turn called for highly centralized decision-making. Whereas in the backward countries of the nineteenth century such synchronization of investment and accumulation were sought to be promoted by large decision-making units like industrial banks and cartels (with the State playing a major role in some cases), in Russia they were undertaken by the State itself, which was the largest
decision-making unit in the economy even before the Revolution of 1917.

In thus performing its role as the largest decision-making unit in the economy the State in Russia/the Soviet Union evolved and deployed a battery of institutional devices to sustain a high rate of economic development. These devices included communal holding of land/collectivization of agriculture, public enterprises, co-ordination of investment through the Ministry of Finance or centralized planning, and a system of administrative controls and pressures combined with incentives. We have already discussed the communal holding on land/collectivization of agriculture in the previous chapter. We shall, therefore, concentrate here on other institutions.

**Public Ownership**

The concept of the State as the general proprietor has existed since long in Russia. The State was the preponderant land-holder until the Bolshevik nationalization of land in 1917-18. It also owned a significant number of manufacturing and mining enterprises. The purchase of railroads in the 1890s and after led to a high degree of State ownership in an enterprise that employed nearly half the non-agricultural workers of the country in 1914. Public ownership, however, was by no means limited to the Imperial Government. It also extended to *zemstvos* and municipalities.

After the Revolution in 1917, public ownership was swiftly extended and became almost universal. Most productive property in industry, transport, trade, and finance was nationalized during the period of War Communism (1917-21). Of course, during the period of the New Economic Policy (NEP, 1921-28) most retail and wholesale trade and small enterprises were returned to private control, but with the inauguration of the First Five-Year Plan, they returned to public ownership.

An interesting feature of the ownership pattern in Russia, particularly in the Soviet Union, was that it was through expropriation of property from individuals that public ownership was established, whereas in several other countries as, for instance, in Britain and the United States the same method was used to strengthen private ownership. This difference in the patterns of ownership can perhaps be explained by the differences in the development patterns of the countries concerned. In countries like the United Kingdom and the United States the development process was largely initiated and dominated by private individuals and corporations, whereas in Russia/the Soviet Union the state was always the dominating factor.

The key factor in determining the extent of public ownership was the need to synchronize investment decisions and to achieve massive accumulation within the shortest possible time. So long as ownership of property was in private hands, there was the danger of diffusion of effort and dispersal of scarce resources over many different lines of activity leading
to loss of dynamic momentum in the economy. There was also the danger of such a dispersal of investment over a large variety of consumer-goods industries being carried to excess. Besides, individual decisions of producers and consumers, not being properly co-ordinated, were sure to obstruct the Government policy of establishing a pattern of mutually supporting investments over a range of industries wide enough to overcome the frustration of isolated advance. On the other hand, control of the "commanding heights" of the economic life of the country enabled the State to use scarce resources exclusively to forge growth-inducing, "decisive links."

Centralized planning rested on nationalization. Nationalization enabled the Government to determine the division of national product between investment and consumption as well as the basic composition of each of these categories. It was only after provision had been made for investment that resources were made available for the production of consumer-goods and for services. Nationalization also permitted centralization of decisions regarding price policy.

Nationalization of property also helped the State achieve accumulation on a dramatic scale. The State siphoned off the

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2 Oskar Lange points out that centralized planning "is made possible by the existence in the economy of a large socialist sector, which controls ... 'the commanding heights' of economic life." Oskar Lange, "Role of Planning in a Socialist Economy," in his Problems of Political Economy of Socialism (New Delhi, 1962), p. 16.

resources that would otherwise have gone for conspicuous consumption and utilized them to promote productive reinvestment. Profits from State enterprises were channelized largely for developmental investment.

Centralized Planning as a Device of Synchronization

Soviet economic institutions such as centralized planning cannot be understood merely in political or ideological terms. Centralized planning was not just an instrument of political control over the economy. Nor was it merely a means by which to combat the anarchy of the market. It was basically an institutional device to achieve the much-needed synchronization of investment over a range of technically related industries and to maximize the rate of growth through realization of economies of scale.

Much before the Revolution of 1917 Sergei Witte saw the need for planning, albeit vaguely, to ensure the success of the Government economic policy in achieving its primary goal of promoting rapid industrialization. Perhaps recognizing the interdependent nature of the modern industrial structure, he argued: "Every measure of the Government in regard to trade and industry affects almost the entire economic organism and influences the course of its further development.... [Hence] this policy [should] be carried out according to a definite plan,

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with strict system and continuity...." In fact, under Witte, the Ministry of Finance became something of a Ministry of National Development extending its influence into every sphere of national life. The Ministry's activities were so enormous as to make Izvolsky describe it as a State within a State.

After the Revolution, the Government evolved the device of centralized planning to maximize the national product through co-ordination and concentration of investment. The need for centralized planning arose because of the following reasons:

In a free market economy the foresight of the investors can hardly be perfect. The investor maximizes private, not the social, net marginal product. External economies are not fully exploited. Complementarities of industries are so great as to call for simultaneous inducement. Modern industry, being indivisible in character, entails large changes rather than small ones. The price mechanism, however, works well only on the assumption of small changes. More importantly, the automatic responses of a free economy cannot ensure an equilibrium between aggregate demand and aggregate supply. Without such an equilibrium, however, the price mechanism breaks down. It is only by means of a deliberate policy that equilibrium between


demand and supply can be ensured.

Successful industrialization in the Soviet Union, therefore, required an entirely new institutional framework that could provide the perspective of interrelated growth of a number of industries and their economic viability — a framework that would enable the computation of both the volume and the cost of production on the basis of the anticipated future. It was especially necessary to evolve an overarching institution that could plan and create the whole of the industry as one huge firm or trust. It was the only way to internalize external economies. Centralized planning bade fair to perform these tasks in the Soviet Economy.

The main aim of centralized planning in the Soviet Union was thus to assure the country of the maximum national income through time by maximizing the amount and by optimizing the composition of investment. The means employed were, of course, direct. It was designed to take into account the "short- and long-run trends, notably of intersectoral demands resulting from complimentarity of industries (revealed by a periodically revised input-output table) and of indirect effects of investment on future demand of domestic, imported or so far exported


Planning Mechanism

The Soviet planning system consists essentially in a centrally operated macro-economic balancing of demand and supply for industrial products in physical terms through the "material balances." The central planning authority draws up a budget for each commodity made up of estimates of production, stocks at the beginning of the plan period, and imports. It compares these estimates with estimates relating to consumption ascertained by applying technical coefficients and by adding exports and stocks at the end of the period. The whole exercise is intended to match total availabilities with total needs. At the first stage, the planned output of, say, Sector I is distributed to the other industries which use that particular commodity. These industries, given their inputs, proceed to frame their output plans. The estimated outputs are in their turn distributed to other consuming industries. The problem of consistency of the plan is resolved by successive iterations.

The system does not start with the final demand. It usually begins with the setting of targets for some "leading links," or priority sectors, functioning as determinants of the outputs which follow from technical necessity. This enables planners to arrive at quantities of goods that are consistent with each other.

9 Rosenstejn-Rodan, n. 7, p. 418.
Flexibility is built into the physical plan in a number of ways. Pressure may be put on some enterprises to force them to economize on the input side. This, in official phraseology, is "mobilization of internal resources." Allocations to non-priority sectors may be cut down; substitution between materials may be encouraged wherever feasible; or imports may be stepped up; or exports may be slashed.

The physical plan was reinforced by the financial plan. A system of "control by rouble" was adopted to force individual enterprises to conform to the plan. The financial system was so designed as not only to establish equilibrium between the volume of consumer goods produced and the purchasing power of households but also to prevent all possible dissipation of resources. Individual enterprises were prevented from purchasing more than the allocated share of resources. They were allowed only a small profit above costs. The budget of the national Government played the key role in the distribution of the national product. All major macro-economic decisions such as the division of current output between investment and consumption were embodied in the budget. The national budget also fulfilled

an important allocative function with regard to investment flows — between industry and agriculture, among industries, etc.

Decisions regarding price fixation were centralized in the hands of the Government. The State used prices to ensure that the enterprises complied with the plans. Although resource allocation was administratively determined, prices were used to influence the allocation of resources and thereby the pattern of production in various ways. Since it was impossible to specify in detail the inputs and outputs of each enterprise in the plans, the managers of the enterprises had a limited range of choices regarding both inputs and outputs. The relative prices of inputs and outputs were manipulated to influence the decisions of the managers in this regard. Wage differentials were also used in a big way to secure distribution of labour. Of course, the relative pricing of substitutes must have also had some influence on the choice of technological coefficients.

Through centralized planning a great deal of pressure was exerted on the economy. This pressure was twofold. There was first the pressure on the productive capacity of the basic enterprises in order to increase output:

11 George Garvey, "Finance and Banking in the USSR," in Bornstein and Fusfeld, n. 10, p. 139.
This pressure for more output per unit of input, this search for reserves of productivity was ubiquitous, and it was supported by a multitude of economic, social and political incentives: the monetary rewards for surpassing production targets, the red banners for victory in interplant competitions, the political promotion (or demotions) for production successes (or failures). It imparted to all the producing units in the economy a constant and omnipresent conditions of excessive effective demand. (13)

And then there was the pressure on the living standards of the people which manifested itself in the rising rate of investment out of GNP and the falling rate of consumption over long periods. The gap between growth of output and growth of consumption was stupendous.

Centralized planning in the Soviet Union succeeded in achieving very high levels of capital accumulation. More importantly it succeeded in achieving the necessary concentration of resources integrally and sequentially according to priorities. This proved decisive in breaking the Nurksian "vicious circle."

