

## THE ROAD TO NOWHERE

The cause of the Party's defectiveness must be found. All our principles were right, but our results were wrong. This is a diseased century. We diagnosed the disease and its causes with microscopic exactness, but wherever we applied the healing knife a new sore appeared. Our will was hard and pure, we should have been loved by the people. But they hate us. Why are we so odious and detested? We brought you truth, and in our mouth it sounded a lie. We brought the living life, and where our voice is heard the trees wither and there is the rustling of dry leaves. We brought you the promise of the future, but our tongue stammered and barked . . .

Arthur Koestler<sup>1</sup>

### INTRODUCTION

During the 1990 May Day celebrations Mikhail Gorbachev was jeered by the crowd. Some of the signs of protest read: 'Workers of the World We're Sorry,' 'Freedom instead of Socialism,' and chants of 'Resign' and 'Shame' were heard from the crowd directed at Gorbachev. Perhaps the most telling banner simply read: 'Seventy-Two Years on the Road to Nowhere.'<sup>2</sup>

On 7 November 1990 the celebration of the seventy-third anniversary of the Russian Revolution proved to be a similar experience for the Soviet leader. Gavriil Popov, the mayor of Moscow, had suggested that the celebration be suspended. But Gorbachev insisted that the historic choice of the October Revolution was the correct one and that the spirit of October still remained a great inspiration for his people and the world. So a celebration proceeded

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The seventy-third anniversary parade, however, met with jeering crowds and even a lone gunman who fired two shots but did not harm anyone. The more peaceful demonstrators conveyed their frustrations with the Soviet regime with banners and slogans calling for the resignation of the Communist government. But Anna Pecheikina stole the show by displaying a sickly plucked chicken high above the crowd on a stick. One woman pointed to the bony chicken and said: 'That is what Gorbachev got the Nobel Prize for.' Another man simply hoped he could find the chicken's little brother to eat. The burden of mundane economic survival – characterized by long lines and poor products in the official sector – grew more severe and unbearable under Gorbachev's regime.<sup>3</sup>

At the same time, the historical awakening that represented one of the cornerstones of Gorbachev's policy of *glasnost* increasingly questioned whether the Revolution should be a cause for political celebration at all. Rather, a public mourning would be more appropriate. The movement to erect a monument to political victims of the Stalin era in Moscow by the Memorial Society represented the beginning of a necessary historical cleansing.<sup>4</sup>

Much of the history written by Soviet scholars in the age of *glasnost* does not support the research of the 'respected' voices in Western scholarship on the history of socialism. In fact, Western scholars such as Robert Conquest and G. Warren Nutter, who were dismissed by some as reactionaries because they recorded the political horrors of Stalinism or challenged the economic claims of socialist planning, were continually vindicated,<sup>5</sup> whereas the historical research of many respected Western scholars of the Soviet system became continually suspect. The work of political historians such as Roy Medvedev and Alexander Tsipko during the age of *glasnost* confirmed the scholarly findings of Conquest, and economic writers such as Vasily Selyunin and Nikolai Shmelev agreed with Nutter that the growth rates of the Soviet economy were systematically overstated.<sup>6</sup> The regime had lost its battle to retain the historical lie of achievement born of great sacrifice. The sacrifice was real, but what achievement could this system possibly claim for its people?

7 November 1991 came and went without any official celebration.<sup>7</sup> The Revolution Day holiday was suspended by the ruling government. The attempted coup of August 1991 had destroyed any legitimacy the communist government had retained during the Gorbachev era. Gorbachev's message on his return from house arrest that the Communist Party could still be democratically restructured,

and that the socialist choice of 1917 was still the historically correct one, fell on deaf ears and sealed his political fate. He, like the Communist Party he represented, was simply a dying dinosaur. On Christmas day 1991, Mikhail Gorbachev formally resigned and the Soviet Union ceased to exist as a political entity.<sup>8</sup> Thus ended one of the most closely watched and studied peacetime political eras of the twentieth century.

The Gorbachev period captured the attention of the world. 'Gorbymania' characterized most of the Western press coverage of the unfolding events. All our previous preconceptions of the world were challenged. As the socialist system collapsed, the Cold War was brought to a glorious end. As the iron curtain fell, the horrible economic and social realities could no longer be ignored or apologized for. Reports of economic, environmental and social deprivation were no longer limited to émigré interviews beyond the control of state censors, and Western anti-communist scholars and intellectuals. Soviet bloc officials themselves admitted the failures of the existing system. The socialist reality could be viewed on Western television and Western newspapers carried reports almost daily about some fallen icon of the socialist age or some new historical revelation about the imperfections of the Soviet past.

Unfortunately, the intellectual prejudices of the twentieth century had poorly prepared Western scholars and intellectuals for the task of understanding and interpreting the events of the late 1980s. These prejudices distorted their basic understanding of history, politics and economics, and as result, fundamental questions of social organization lay outside of their grasp. Theorists in both the East and West were at a loss in offering sound analysis of the system that collapsed before their eyes. While the world was swamped with journalistic coverage of the events, there was a lack of deep reflection on the nature of the problem confronting these societies. One reason for this was simply that the speed of the changes from 1989 on were so fast as to not afford such reflection. Another reason, though, was the persistence of certain false prejudices which prevented commentators from understanding.

All historical interpretation is guided by intellectual prejudices for good or bad. The advantage of the bridge to the past provided by the passage of time, in fact, is that it affords scholars and intellectuals a great opportunity in the assessment of which prejudices mislead and which enable interpretation. Obviously, in attempting to understand the unfolding of the Gorbachev and the post-Gorbachev era we do not have the benefit of temporal distance that we do with say the

American, French or even the Russian revolution. But, understanding the reason for the Gorbachev reforms in the first place provides the key to establishing a criteria from which to assess the problems with the Gorbachev reforms and offer advice on how to move forward in a more positive direction in the post-Gorbachev era. But in order to understand the reforms it is necessary to understand the Soviet system and its historical operation. In order to accomplish this task, we must view the grand story of Soviet history through the right pair of theoretical lenses. 'Our understanding of the past,' Douglas North tells us, 'is no better than the theory we use and that theory has been woefully deficient.'<sup>9</sup>

### THE POOR PREPARATION FOR UNDERSTANDING

Our ability to understand the Soviet experience has been distorted greatly by the intellectual trends of the twentieth century. The dominant theories in both politics and economics conspired to warp historical interpretations of capitalistic processes and socialist practice. In addition, as the century progressed interest groups developed which served as the guardian of these misunderstandings. Ideas came both to create, and then to serve, the purposes of vested interests which would not allow dissenting opinion to challenge the establishment.

This is not meant to imply that no debate was allowed. Certainly there was debate, but the parameters of the debate were firmly established and unquestioned. For much of the twentieth century the basic consensus on either side of the dispute concerning the grand questions of social organization was that capitalism had failed in providing equity and humane social conditions which progressive legislation must correct.<sup>10</sup> Moreover, the Great Depression of the 1930s supposedly demonstrated that capitalism was not only unjust, but also unstable as an economic system. Capitalism, if it was to survive at all, must be subject to democratic forces of control to tame its operations and protect the populace from unscrupulous business and irresponsible speculation. Socialism, in fact, was viewed as a great threat to those who favored capitalism precisely because it was perceived as offering a viable alternative.<sup>11</sup>

This general intellectual climate was reinforced by the theoretical developments in economics. As academic economic theory became more technically sophisticated and rarified in its presentation of its basic theorems, an appreciative or intuitive understanding of the

nature of market institutions and their operation became scientifically suspect.<sup>12</sup> The flip-side of the development of the idea of perfect competition, and the strict conditions established for its attainment, was the development of the theory of market failure. Market failures were said to exist whenever capitalist reality did not meet the conditions of the frictionless textbook model of perfect competition.<sup>13</sup> The concepts of externalities, public goods, monopoly and imperfect competition and macroeconomic instability were developed and used by professional economists to explain why markets may fail to allocate resources in a socially desirable manner. Real existing competitive capitalism generated negative externalities in the form of pollution and other undesirable third-party effects, possessed an inherent tendency toward monopolization and waste, could not provide many basic services such as roads and education and suffered from recurring business cycles. That was the theoretical picture of competitive capitalism that dominated the intellectual landscape for most of the twentieth century.

Obviously, this theoretical perspective colored historical interpretation. The rise of industrial capitalism in the late nineteenth-century United States was viewed as simply a process by which the 'Robber Barons' acquired monopoly power. The banking panics of 1893 and 1907 were viewed as the result of the inherent instability of capitalist industrial processes. The solution to these problems, if one was conservative, was to bring capitalism under the control of democratic forces (preferably dominated by leaders of industry themselves). To eliminate monopoly, the Sherman (1890), Clayton (1914) and Federal Trade Commission (1914) Acts were passed. To eliminate bank panics and regulate business cycles, the Federal Reserve System (1913) was established. Radicals, on the other hand, argued that such reformist measures would not rid society of the ills of capitalism – which possessed inherent contradictions – and that only a transition to a socialist society would accomplish that goal.

The Great Depression shook an entire generation's faith in the efficacy of capitalist markets. Rational planning of the economy came to be viewed not only as the most viable alternative, but the only alternative. The parameters of the debate had shifted drastically by the 1930s. *Laissez-faire* was no longer considered as any kind of option in the economic policy debate. Classical liberal economic policy simply reflected the beliefs of the naive and simple minded. The modern world had become too complex for an eighteenth-century idea to offer anything of value.

John Maynard Keynes went so far as to argue that the great social experiments of the time in Germany (fascism) and Russia (communism) would point the way to the future of economic policy. Country after country had abandoned the old presuppositions of classical political economy. Russia, Italy and Germany had moved towards establishing a new political economy, Keynes argued, and their experience must be watched closely. No one could tell which of the new systems would prove itself best, but they nevertheless successfully persuaded thinking men and women in Great Britain and the United States to strive after a new economic plan of their own. Some may still cling to the old ideas of *laissez-faire* capitalism, 'but in no country of the world to-day can they be reckoned as a serious force.'<sup>14</sup>

Keynes considered himself, and was viewed by others, as a realist in the classical liberal tradition. The Keynesian idea was for government officials to intervene rationally in order to improve the workings and outcomes of the market economy. Keynes's proposal was to combine the socialization of the capital market with the nineteenth-century political traditions of Great Britain. While he saw that the socialization of investment was the only way of securing an approximation of full employment, this change did not require a break with the general traditions of bourgeois society. Moreover, Keynes merely conceived of his theory as an extension of classical political economy and classical liberalism, not a rejection of those systems of thought. Keynes's advocacy of a greater role of government in planning the economy was, in his mind, a practical attempt to save individualism and avoid the destruction of the existing economic system.<sup>15</sup> Keynes's attitude toward *laissez-faire* reflected the general consensus of the times among intellectuals, scholars and politicians.

The spirit of the age led even someone usually recognized as an intellectual leader of classical liberalism, Frank Knight, publicly to declare the virtues of communism.<sup>16</sup> It seemed as if everyone advocated some form of government control and planning of the economy to ensure stability and equity. Paul Homan provided a contemporary overview of the literature on economic planning in 1932 in the *Quarterly Journal of Economics*, and while he criticized various proposals for lacking details, he did not voice any criticism of planning in principle. Contemporary proposals for planning may be faulty, he argued, especially since many disregard the important insights of price theory, but they nevertheless represented the first 'pamphlet' stage of addressing the problems of stability and full employment. Homan pointed out that modern industrial complexity

could curiously be employed both as a reason of why we *must* plan the economy, and why we *cannot*. But the idea that industrial relations are too complex to be brought under direct control, though shared by some economists, was the view of an intelligent businessman. Businessmen, however, did not understand the essential characteristics of the problem of economic instability. Their education, according to Homan, was defective with respect to the economics of financial markets, and the fields of money, credit and investment. This businessman's perspective was colored by the American tradition of private enterprise and non-governmental interference. The responsible question of the day was simply which was the best way forward for economic planning, not whether or not the government should engage in planning the economy. The profitable cultivation of the ideas of economic planning will lead to more coherent and comprehensive proposals to solve the problems of stability and equity.<sup>17</sup>

The July 1932 issue of the prestigious *Annals of the American Academy of Political and Social Science* was entirely devoted to national and world economic planning. Not a single criticism of economic planning was voiced in that volume. Instead, planning was lauded as the method by which 'individual and corporate economic activity' could be molded into group-defined spheres of action which are rationally mapped out and fitted, as parts of a mosaic, into a coordinated whole, for the purpose of achieving certain rationally conceived and socially comprehensive goals.<sup>18</sup>

*Laissez-faire* as a policy was held in disrepute by scholars, intellectuals and politicians. Franklin D. Roosevelt even chose to attack classical economists in his third fireside chat on 24 July 1933. 'I have no sympathy,' he stated, 'for the professional economists who insist that things must run their course and that human agencies can have no influence on economic ills.' On 19 December 1936, Roosevelt expressed his complete agnosticism with regard to the truth of any tenet of political economy in a letter to Joseph Schumpeter. He had studied economics for thirty-six years, Schumpeter was informed, but Roosevelt was 'compelled to admit - or boast - whichever way you care to put, that I know nothing of economics and that nobody else does either!'<sup>19</sup>

In a 1934 book by Rexford Tugwell (a professor of economics at Columbia University and the assistant secretary of the Treasury under Franklin D. Roosevelt) and Howard Hill, the argument against

*laissez-faire* was carried further, and included a direct discussion of the Soviet experience. They argued that

the challenge of Russia to America does not lie in the merits of the Soviet system, although they may prove to be considerable. The challenge lies rather in the idea of planning, of purposeful, intelligent control over economic affairs. This, it seems, we must accept as a guide to our economic life to replace the decadent notions of a *laissez-faire* philosophy.<sup>20</sup>

Julian Huxley, the noted scientist, argued that the Soviet five-year planning system was simply the 'spirit of science introduced into politics and industry.'<sup>21</sup>

The intellectual *gestalt* of the time could neither appreciate nor tolerate the challenge to economic planning offered by its critics, namely Ludwig von Mises and F. A. Hayek. But without an understanding of even the potential difficulties that economic planning may confront in practice, it would be impossible to make sense out of any real world experiment with economic planning. It should not be a surprise that within such a climate of opinion that Soviet practice could not be properly understood. It was not just a matter of communist apologetics - though, of course, there was some of that - the real problem of interpreting Soviet practice was a simple blind spot on the part of scholars and intellectuals.<sup>22</sup> It just could not be that economic planning would not work as envisaged. It seemed so rational, so scientific, and it had the great potential of providing economic stability and guaranteeing a more equitable distribution of the social pie.

Not only did this intellectual bias fail to appreciate the *economic* problems of planning, it failed miserably to grasp the *political* problems inherent with planning. In the West, this was due to an utterly naive view of the operation of democracy that dominated political science by the early twentieth century.<sup>23</sup> The textbook model of democracy portrayed the political system as one in which individual citizens could effectively determine the rules by which they would live. The vote process unambiguously conveyed the necessary information concerning the array of public goods and services demanded and the level of taxes that must be paid. Democracy was an ideal model of self-rule. Faced with market failure, democratic governments could easily set the matter straight. If government action failed, it was not due to any structural weakness in the

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democratic system – political actors would just have to gather more information and try harder next time.

Such a view of democratic processes, however, was woefully deficient. And, it possessed a deleterious affect on interpretations of the institutions of socialist policy. The political problems of Stalinism, which were recognized by many early on, were not attributed to the nature of planning per se, but rather to the lack of a democratic tradition in Russian history. Planning, as such, was not seen to possess any threat to political freedom whatsoever. Economic planning, under democracy, would not face any of the problems associated with Stalinism. Keynes, for example, in reacting to Hayek's *The Road to Serfdom*, wrote that

I should say that what we want is not no planning, or even less planning, indeed I should say that we almost certainly want more. But planning should take place in a community in which as many people as possible, both leaders and followers, wholly share your own moral position. Moderate planning will be safe if those carrying it out are rightly oriented in their own minds and hearts to the moral issues.<sup>24</sup>

So as long as 'good' people were in charge, nothing was objectionable with economic planning. In fact, economic planning was desirable.

Herman Finer was not as kind to Hayek as Keynes. Finer accused Hayek's *The Road to Serfdom* of being 'the most sinister offensive against democracy to emerge from a democratic country for many decades.'<sup>25</sup> The true alternative to dictatorship, Finer assured his audience, was not economic individualism and competition, but a democratic government fully responsible to the people. Hayek's world, according to Finer, would leave individuals under the control of aristocrats or the moneyed bourgeoisie. But, free people can govern themselves without such masters. Economic planning was simply democracy in action, and it proved itself every time there was a successful government action.

The level of Finer's misunderstanding of Hayek's basic argument was astonishing viewed from our vantage point today, but at the time it was not. The Mises-Hayek analytical criticism of socialist planning was hardly understood by any professional economist and in many respects has not been fully appreciated even to this day.<sup>26</sup> Moreover, the naive view of democracy that Finer defended in his book only came to be seriously challenged as the theory of public choice developed in the post-Second World War era. The mainstream of

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thought simply did not appreciate, let alone incorporate, the important insights concerning information and incentives in economic and political processes that only became evident with the further development of modern political economy.

Why should it be surprising, therefore, that Sovietologists were ill-prepared to understand their subject matter? They possessed neither a sound economic or political theory from which to interpret the unique Soviet facts. The intellectual spirit of the age applauded what the Soviet Union was attempting even if there existed normative disagreements about how it was going about it. Economic failures of the Soviet system were attributed to its backwardness, just as the political problems of the system were attributed to the lack of democratic traditions. What was essentially missing from Sovietology was a thorough examination of the *structural* weakness of socialist institutions.

## THE MALPRACTICE OF ECONOMIC MEASUREMENT

The degree of poor preparation was not just limited to a failure to recognize that the problems that plagued the Soviet system were not *in* the system, but rather *were* the system. Several other developments also conspired that prevented many from even recognizing that there were problems at all. The emerging hegemony of macroeconomics in the economic profession and in the public mind was perhaps the most fateful turn of intellectual events in blinding observers of the Soviet economy to the reality of the systemic failure of socialism.

The development of techniques in aggregate economics in the wake of the Keynesian victory in economic thought drew economists' attention away from the structural make-up of a system and instead focused their attention on aggregate figures such as gross national product (GNP). Beside the conceptual problem of how one aggregates the data in a world where prices are meaningless, the approach was a fundamentally flawed one for understanding the industrial structure of any society. Aggregate concepts, such as price level, national product, savings rate and levels of public investment, do not allow the economist to examine how complex production plans in an industrial economy are continually adjusted to match with consumer demands through time. But the mutual adjustment of intertemporal decisions by economic actors to coordinate the plans of producers with

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consumption preferences of buyers makes up the unique capital structure of any industrial economy. It is the mutual accommodation of suppliers and demanders through a process of competitive bids and offers that economics must explain, and the techniques of aggregate economics simply drew economists' attention away from this task. As aggregate economics came to dominate the profession in the 1940s, 1950s and 1960s, the problem became even more acute. Not only did economists not pay much professional attention to the dynamics of capitalist processes of production, they ignored them completely.<sup>27</sup>

An example may illustrate the fundamental problem of aggregate economics in assessing economic systems. Consider the case of a fat man and a muscular man. They may both weigh 225lbs, but the composition of each of their bodies is radically different. One is flabby, the other is fit. To understand the health of either individual it does not much matter what the aggregate weight is, the important point is to examine the *structural composition*.

The Soviet economy was similar to the fat man in my story above. Aggregate growth statistics concealed the flabby and faulty capital structure that was born in Stalin's industrialization. But economists preoccupied with such figures did not appreciate the distinction between sustainable development and non-sustainable development of an economy. Western Sovietologists knew of the dangers associated with working with the falsified official statistics on the Soviet economy. But the techniques the United States Central Intelligence Agency (CIA) developed still focused on gaining some aggregate or macroeconomic measure of performance, rather than encouraging detailed microeconomic analysis of the industrial structure of the Soviet Union.

Not only did the CIA develop techniques which were misleading even in the abstract, but they tended systematically to overstate the capability of the Soviet economy on their own grounds. A comparison of alternative measures of Soviet economic growth is found in Table 2.1, and shows that in the late 1970s and 1980s the CIA overstated the growth of the Soviet economy as compared to the estimates of Vasily Selyunin and Grigory Khanin.

But the CIA's performance was actually much worse than these figures would suggest. Whereas the official TsSU figure for the average annual rate of growth of national income in the Soviet economy from 1928 to 1985 was 8.8 per cent, the CIA's estimate was 4.3 per cent, and Khanin's estimate was 3.33 per cent. But this conceals the Soviet decline of the 1970s and beyond. In the 1970s,

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Table 2.1 Alternative measure of Soviet economic growth (average annual growth in %)

	Official Soviet statistics (%)	Selyunin-Khanin estimates (%)	CIA estimates (%)
1951-60	10.3	7.2	5.1
1961-65	6.5	4.4	4.8
1966-70	7.8	4.1	5.0
1971-75	5.7	3.2	3.1
1976-80	4.3	1.0	2.2
1981-85	3.6	0.6	1.8

Source: *Revisiting Soviet Economic Performance under Glasnost: Implications for CIA Estimates* (Washington, DC: SOV 88-10068, 1988): 11.

Selyunin and Khanin estimate that Soviet GNP grew at about 2 per cent annual rate of growth, whereas the CIA estimate was 3.7 per cent. For the eleventh five-year plan (1981-5), Selyunin and Khanin estimate a growth rate of 0.59 per cent, whereas the CIA estimates 2 per cent average annual growth of Soviet GNP.<sup>28</sup>

Moreover, Selyunin and Khanin date the negative decline of the Soviet economy not to the mid-1970s, but rather fifteen years earlier to the beginning of the 1960s. Even if alternative calculations of the Soviet economy may show significant growth, they do not examine the meaning of that growth in terms of the industrial structure created and the employment of scarce resources. As Selyunin and Khanin pointed out, Soviet growth was achieved through

inordinate resource expenditures. In almost all periods of our history, the use of material resources and fixed assets grew more rapidly than did national income. From 1928 through 1985, material-intensiveness increased by 60% and return on assets fell 30%.

Labor productivity grew only modestly throughout this period. The Soviet method of economic management, they argued, was made possible only because of the abundance of resources at the regime's disposal. 'But the price was high: living standards fell for decades.'<sup>29</sup>

This point, however, does not square well with CIA estimates that Soviet per capita GNP converted at US purchasing power equivalents amounted to \$8,370 in 1986 or about 49 per cent of the US.<sup>30</sup> More

recent alternative estimates of Soviet per capita GNP challenge the CIA figures significantly by placing the Soviet economy at somewhere around 25 per cent of the US.<sup>31</sup> If the CIA figures were accurate the Soviet economy would have been a maturing industrialized economy, but the reality was that the former Soviet economy provided a standard of living equivalent to a well-developed Third World economy at best. Moreover, if the CIA statistics were correct, then there would not have been any need for a radical economic reform and Gorbachev's rhetoric would have been incomprehensible and unfounded.

Even with revised data international comparisons of per capita GNP systematically overstate the well-being of Soviet citizens. One reason for this bias was that the low quality of Soviet products was not considered. Another reason was that the persistent shortages of goods and the corresponding queuing for even those goods that were available was not reflected in the statistics. And, finally, the per capita GNP statistics do not reveal the low percentage of GNP that went to household consumption in the former Soviet Union. Only about 50 per cent of GNP in the former Soviet Union went to household production.<sup>32</sup> Soviet consumers were far worse off than even revised estimates indicated.

One significant consequence of these mismeasurement problems was that the military capabilities of the Soviet Union were grossly distorted. If the national income of the former Soviet Union was actually less than a third of the US, the military burden of the empire was much greater than ever estimated by Western Sovietologists. Correcting for these alternative calculations of Soviet GNP, and incorporating information from the glasnost era, it is estimated that the military burden represented about 25 per cent of GNP in the former Soviet Union.<sup>33</sup> As a result, most Western estimates of Soviet military strength were seriously mistaken because the military burden (in terms of the explicit and implicit tax on the population) was understated at the same time that the long-term viability of the Soviet economy was overstated. Correcting the figures challenges previous perceptions concerning the capability of the former Soviet system to engage in a sustained military conflict with the West.<sup>34</sup>

These distortions, though, were not simply the product of poor information and inadequate measurement techniques. The distortions served a very important ideological and interest group function. On the one hand, conservative anti-communists supported the bias toward overestimating Soviet economic and military strength because

it reinforced their fears of the impending encroachment of communism throughout the world. The statistics justified large military expenditures to fight the advent of global communism. If the Soviet economy was structurally weak, then the threat of communism would have been rather shallow and would not have justified the military conflict of the Cold War. Only a developing industrial power could supply the economic base and technological innovations that would pose a sustainable threat to Western powers. On the other hand, radical intellectuals, even if they despised the Soviet regime, believed in the basic ability of the system of centralized economic planning to promote development. If Soviet economic planning was a failure, then socialism may have been a questionable policy goal to advocate even in more democratic situations. Scholars, intellectuals and politicians of both 'left' and 'right' persuasion, therefore, possessed an ideological stake in the ability of the Soviet economy to develop and prosper.

These ideas about the efficacy of Soviet economic planning also created an extremely powerful interest group, namely the military-industrial establishment in the West. The military-industrial establishment benefited directly from the overestimation of Soviet capabilities.<sup>35</sup> Right-wing and left-wing beliefs about the developing Soviet economy provided the needed justification for large appropriations toward armament productions and military research and development.<sup>36</sup> Thus, an iron-triangle was forged of ideas and interests that simply could not, and would not, allow analysis that seriously challenged the Soviet myth of economic success. But, as we have seen, the Soviet system was far from an economic success. More to the point, the Soviet economy may well be the ultimate political economy tragedy of this century.

### A SHORT HISTORY OF SOVIET ECONOMIC FAILURE

Lenin came to power in Russia promising the emancipation of man from the domination of other men and nature. His utopian vision was inspiring and his will to power was resolute. Lenin and the Bolsheviks possessed a concrete vision of the path to a better future. Their plan of social construction after the revolution was not a by-product of improvisation, they knew what they wanted to accomplish and how they were supposed to accomplish that goal. Of course, the civil war influenced the way that policies were implemented, but war had little

or nothing to do with the motivation behind the policies. If anything, the Russian Revolution of 1917 was an ideological revolution.

Between 1917 and 1921 the Bolsheviks tried to substitute a unified economic plan for the 'anarchy' of the market. Production for exchange, which characterized the commodity mode of production, would be replaced by production for direct use. The irrationality of the capitalist mode of production would be overcome in strict accordance to Marxian principles.

In economic life the Marxian project entailed eliminating the constant struggle between competing autonomous private interests on the economic scene by bringing economic life under conscious public control. It was this process of bringing all of economic life under conscious control that pre-occupied the Bolsheviks upon coming to power in 1917.

At Lenin's first appearance before the Party after the October revolution in 1917, he gripped 'the edge of the reading stand, letting his little winking eyes travel over the crowd as he stood there waiting, apparently oblivious to the long-rolling ovation, which lasted several minutes. When it finished, he said simply, "We shall now proceed to construct the Socialist order!"<sup>38</sup>

And proceed they did. Between 1917 and 1921 the Bolsheviks attempted to bring all economic activity under the conscious direction of the Supreme Economic Council. The attempt to abolish money relations and monetary calculation was pursued with a passion. This was quite natural given their ideological program.

The Bolshevik project of rationalization and emancipation was spelled out in the program adopted at the Eighth Congress in March 1919. In the realm of economic affairs, the Party program called for expropriating the expropriators, increasing the productive forces of society by eliminating the contradictions of capitalism, mobilizing labor, organizing the trade unions, educating the workers and, basically, securing 'the maximum solidarisation of the whole economic apparatus.'<sup>39</sup> In order to accomplish this goal the Bolsheviks established the Supreme Economic Council to bring economic existence under rational control, i.e., substitute production for direct use for the chaotic system of production for exchange that characterized the commodity mode of production, and seized the banks and merged them into a single state bank. The bank would become an apparatus of unified book-keeping for society. The bank was to become, to use Lenin's terminology, 'the nodal point of public accounting.'<sup>40</sup> Following Lenin, the Party program of the Eighth

Congress stated that 'Upon the basis of the nationalisation of banking, the Russian Communist Party endeavours to promote a series of measures favouring a moneyless system of account keeping, and paving the way for the abolition of money.'<sup>41</sup>

The rationalization of economic life under communism would eliminate the waste of capitalist production and lead to increased productivity. This burst of productivity would free individuals from the 'chains imposed upon them by nature.' The utopian promise of the project was that 'concurrently with the disappearance of man's tyranny over man, the tyranny of nature over man will likewise vanish. Men and women will for the first time be able to lead a life worthy of thinking beings instead of a life worthy of brute beasts.'<sup>42</sup>

The utopian aspiration, however, resulted in a nightmare by early spring of 1921. In all areas economic output fell far below pre-war levels. In 1921 the Soviet Union, as Stephen Cohen has pointed out, lay

in ruins, its national income one-third of the 1913 level, industrial production a fifth (output in some branches being virtually zero), its transportation system shattered, and agricultural production so meager that a majority of the population barely subsisted and millions of others failed even that.<sup>43</sup>

The Bolsheviks were forced to retreat from their attempt to implement Marx's utopia and instead re-introduced market relations of exchange and production with the New Economic Policy (NEP) in the Spring of 1921. 'In attempting to go over straight to communism,' Lenin wrote on 17 October 1921,

we, in the spring of 1921, sustained a more serious defeat on the economic front than any defeat inflicted upon us by Kolchak, Deniken or Pilsudski. This defeat was much more serious, significant and dangerous. It was expressed in the isolation of the higher administrators of our economic policy from the lower and their failure to produce that development of the productive forces which the Programme of our Party regards as vital and urgent.<sup>44</sup>

While the NEP saw a modicum of the rule of law restored within the Soviet Union this period was not without ambiguities.<sup>45</sup> At the same time that Lenin re-introduced market mechanisms he outlawed all political factions within Soviet politics, including factions within the



Party. While denationalizing the majority of industries the Bolsheviks maintained control over the 'commanding heights', e.g., major manufacturing and banking. At the height of the NEP, for example, while only about 8 per cent of industrial enterprises remained state owned, that 8 per cent employed about 85 per cent of the industrial labor force.

The NEP saw a great recovery from the cataclysm of the communist experiment with economic planning, but the system itself was a massive interventionist system possessing its own dynamic. The NEP had its own unintended and undesirable consequences. As Lenin would write of the NEP system in the spring of 1922:

The machine refused to obey the hand that guided it. It was like a car that was going not in the direction the driver desired, but in the direction someone else desired; as if it were being driven by some mysterious, lawless hand, God knows whose, perhaps of a profiteer, or of a private capitalist, or of both. Be that as it may, the car is not going quite in the direction that the man at the wheel imagines, and often it goes in an altogether different direction.<sup>46</sup>

Not only did the NEP fail to produce the results the Bolsheviks had intended, but the system evolved into a bureaucratic embarrassment. No structural changes were introduced to the economic institutions that were the legacy of war communism. The tasks of economic institutions were re-arranged but they were not dismantled. The problem of bureaucracy in the Soviet Union led Lenin to declare that the 'state apparatus [had become] so deplorable, not to say wretched.'<sup>47</sup> But with Lenin's health failing throughout 1922 and his final stroke on 10 March 1923, which ended his political activity for good, the Soviet regime was left without a leader.

On 21 January 1924 V. I. Lenin died and with him so did the public ideology of Bolshevism. The resulting ambiguity and despair toward socialist construction was the legacy of Lenin. Lenin had criticized political bureaucracy, yet he established a political monopoly for the Party. He argued for concessions to capitalism, but his legitimating ideology demanded an assault on any hint of emerging capitalist relations. Lenin ended his life staring at a stark contradiction. Socialism rather than emancipating man by rationalizing social existence delivered man into a new serfdom characterized by political and economic irrationality.

The revolutionary cadre was caught in despair. 'Lenin had led his

followers into the wilderness only to die before he could lead them out.<sup>48</sup> Despair and confusion plagued the Old Bolsheviks from the time of the NEP until their demise at the hands of Stalin in the purges of the 1930s. The Old Bolsheviks thought they had diagnosed the disease that plagued capitalist society, but wherever they applied the healing knife of socialist policy a new sore appeared. They believed that they had brought the truth to the Russian people and the world, but in their mouth it sounded a lie. They promised to bring the living life to the masses, and where their voice was heard the trees withered and died. By the late 1930s, the entire ruling cadre of the Old Bolsheviks - Lenin, Bukharin, Trotsky, Zinoviev, Kamenev, Rykov, etc. - had been eliminated from the political scene by either fate or Stalin's political maneuvering.<sup>49</sup> It was already by this time questionable whether the revolution was worth the suffering it wrought.

In addition to the ideological confusion that permeated the NEP period, the economy was plagued by recurring crises as a result of the government's economic policies. Arbitrary government intervention destroyed the economic incentive to invest and produce in the official market sector. Because of the government's agricultural policy at the end of the NEP, peasants no longer had any incentive to market their grain surplus leading to the 'Grain Crisis' in the winter 1927/28. Net marketings of grain in 1926 and 1927 were only 50 and 57 per cent of the pre-war level although grain output at that time was almost equivalent to the pre-war level. The grain procurement crisis provided the final justification for Stalin to begin his military assault on the Soviet economy. It was the 'Grain Crisis' that gave rise to the rhetorical justification for the 'de-kulakization' drive that brought an end to the NEP.

The poor economic results and the uncomfortable ideology of the NEP, along with fear of foreign intervention, led to Stalin's revolution from above. Stalin with political power firmly in hand by 1927/28 began his military siege of economic life.

Soviet style socialism came to maturity under Stalin. It is important, however, to keep in mind that even at the height of collectivization Stalin never again tried to abolish post-haste and completely commodity relations of production and monetary calculation as the Bolsheviks had sought to do from 1917 to 1921.<sup>50</sup> Marxism became under Stalin merely a mobilizing ideology for power and not a utopian aspiration for man's emancipation. What emerged out of the late 1920s was a *nomenklatura* system whose beneficiaries received

ideological justification from Marxism.<sup>51</sup> This has been the case ever since.

The Western textbook image of a rational, hierarchical, planned economy, that was able to achieve tremendous growth (despite its terrible costs) and transform the Soviet Union from a backward peasant economy into a military and industrial power is an illusion. The five-year planning system instituted during Stalin's reign, as Eugene Zaleski points out, could only be referred to as 'planning' with the greatest reserve, and it certainly was not rational.<sup>52</sup>

The Soviet system merely gave the appearance of a centrally planned system, when in reality the system depended crucially upon decentralized decision-making processes to achieve any degree of coordination.<sup>53</sup> There is no doubt that the historical operation of the Soviet system was characterized by strong central power, but that did not affect its fundamental organizational form – at base the Soviet system remained a commodity production economy. The capital structure of the Soviet economy was fundamentally affected by central decisions, particularly those of Stalin, on the direction of industrial development. But, influencing the path of development is not the same as organizing society in strict accordance to a central plan. The US government could decide tomorrow to ban the production of steel and this would radically change the structure of the American economy, but it would not abolish the decentralized processes of market coordination.

The capital market under conditions of public ownership was simply replaced by another decentralized system, one that was more clumsy and less efficient. The 'plan' was built up from the competing requests of the various enterprises and ministries. The political competition among rival pressure groups characterized the 'supreme' economic decisions. The primary function of the planning bureaucracy was to serve as a supply agent and avoid the practice of free price formation and monetary rationing. Capital resources, however, are scarce and, therefore, must be rationed.

If a decree eliminates price competition as the rationing device to coordinate economic decisions, then alternative methods will be relied on to allocate scarce resources. A rent control, for example, which fixes the legal price below the market clearing price will not only lead to shortages of apartments, but also increase the use of non-price competition to allocate scarce apartments. The price control produces costs to the buyer, such as waiting in queues, and so forth, that are not simultaneously benefits to the seller. If the seller possesses any power

to transform the deadweight loss into a benefit for themselves they will do so. Problems of discrimination, poor upkeep of apartments, bribing of the landlord, etc., are all common phenomena in areas with rent control. In the Soviet context, both in the consumer and producer sectors, bribing officials, illicit market transactions and special privilege to political elites, emerged as predominant rationing devices.

In addition, despite legal decrees to the contrary, private property in the economic sense was never abolished. Those who exercised control and decision-making power over existing resources were *de facto* private owners, e.g., managers of the factory, etc., even if the claim was made that they acted in the interest of society. These *de facto* private ownership rights of public property, in fact, were the primary source of private benefit from the Stalinist regime to those who 'own' them.<sup>54</sup>

The above only concerns how the official 'planned' sector operates. If we include the unofficial use of the market by planners, then the image of a central, unified and rational plan becomes even more questionable. First, Soviet planners carefully study world markets to aid them in their planning decisions. Thus, as Soviet economic journalist Vasily Selyunin writes, the Soviet planners believe the idea that they can regulate economic life in strict accordance to the plan 'when they carefully study world trends, which are determined by market forces, in order to plan what we should produce.' In doing so 'they tacitly admit that there is a better means than ours for the regulation, or rather self-regulation, of the economy.'<sup>55</sup> Second, the black market is pervasive in the Soviet economy and the coordination of production and exchange activity even within the planned sector, let alone the consumer sector, depends crucially upon its existence.<sup>56</sup>

The Soviet economy never conformed to the ideal picture of a rationally planned communist economy that would abolish completely commodity production because that system is a hopeless and unachievable utopia, as Mises demonstrated in theory in 1920 and Soviet performance demonstrated in practice in 1921. The only attempt to achieve that utopia (1917–21) ended in what William Chamberlin described as 'one of the greatest and most overwhelming failures in history.'<sup>57</sup>

The mature Soviet system evolved into a vast military bureaucratic apparatus that yielded profits to those in positions of power.<sup>58</sup> The root of the Stalinist bureaucracy that plagued the Soviet economy, however, lay in the original Marxian aspiration to plan the economic

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system rationally even if the original goal was unattainable. Stalinism was, whether intended or not, the logical consequence of Marxist-Leninism. The economic consequences of the Stalinist system were to produce an entirely distorted industrial structure that notoriously disregarded the consumption demands of the populace. In a very important sense, the mature Soviet economy was, and continues to be, a giant mal-invested capital structure where the preponderance of the population goes to work in the wrong place to do the wrong job to produce the wrong goods. Such is the legacy of Stalinist industrial policy.

It is important to understand the history and nature of the system in order to grasp the meaning and task of the reforms under Gorbachev. As Leonid Abalkin, one of Gorbachev's leading advisors, wrote: 'No small number of difficulties arise in the theory and practice of restructuring the economic and management system due to the lack of thoroughly substantiated evaluations of many stages in our economic construction.' Abalkin continued by arguing that at a time when the Soviet government was breaking with existing 'forms, methods, and structures,' they must clearly understand the legacy they were renouncing. It would be 'impossible to assimilate the lessons of the past and to determine the rational avenues of socioeconomic development without substantial reform in economic theory, without the formation of a new type of economic thinking that is radically different from the past.'<sup>59</sup>

Perestroika, it must be understood, did not represent a move away from Marxian central planning - that move was made by Lenin in 1921. Rather, perestroika at best represented a supposed improvement of the bureaucratic system of economic management. But understood at even that level, Gorbachev's reforms did not address the challenge that lay before him from 1985 to 1991.

## GORBACHEV'S CHALLENGE

Production and distribution are inexorably connected. Though classical political economists treated production and distribution as analytically distinct that was a serious flaw in their analysis.<sup>60</sup> Market processes of production determine the income and functional distribution of productive factors, such as labor. Within a free-market process there is no distributional process separate from the processes of exchange and production. Factors are paid according to the service they render, or are perceived to render, to others in the market. But in

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a system, like the former Soviet Union, where the state takes on the role of distribution, wealth is transferred from one class to another based on political rationales. The ability of the state to transfer wealth depends upon its ability to extract economic rents from the productive system without destroying completely the incentive to produce.

The history of the Soviet Union is filled with various 'inventions' by the ruling elite to extract rents from the populace; from the forced grain requisitioning during war communism and the tax-in-kind during the NEP to the collectivization and labor armies under Stalin. The various attempts over the years to reform the Soviet system - Khrushchev's 1957 *sovmarkhoz* reforms; the Brezhnev-Kosygin reforms of 1965; the 1973 industrial reorganization; and the 1979 reforms - were all attempts to improve economic efficiency, expand the productive capability of the economy and enhance the well-being of the *apparatchiks*. Perestroika should be viewed as a further attempt in this Soviet tradition of political economy.

The political distribution of wealth, which necessarily lives off productive output of economic activity in a parasite-host relationship, can be relied upon only to a point.<sup>61</sup> The tax state has its origins in the private property order of the market system. Taxation is derived from the revenues appropriated from the wealth created in the market. Beyond a certain point economic productivity will begin to decline in response to overburdensome taxation, and at that point the economic system enters a crisis. It is probably no exaggeration to say that the most important factor determining economic productivity throughout the world is the system of rules governing the economy. An economy lacking natural resources can flourish if the set of rules governing social intercourse cultivates economic productivity, while an economy rich in natural resources will decline under an unfavorable set of rules.

The peculiar art of Soviet economic policy was to balance an ideological hatred of market relations, which justified the Party's privileged position in society, with the reality of allowing enough market production and exchange so that the Party's ability to extract rents was not threatened. Soviet leaders were chosen for their ability to uphold the fiction that the fictional reality of communism was not fictitious. 'The principle that capitalism (meaning reality) has to be destroyed,' the French Sovietologist Alain Besancon states,

is therefore capped by another principle - enough capitalism (meaning reality) must be preserved so that the power is not threatened in its material and political base. The whole econ-

omic art of the Soviet government consists in combining these two principles so that the socialist design of destroying capitalism is achieved while the strength and vitality of the Party-State on which depends the achievement of this task are preserved.<sup>62</sup>

Besancon concludes that Lenin was the master of this unique Bolshevik art of economic policy. Gorbachev's reforms were consistently in-line with this Bolshevik practice. It was this peculiar Soviet economic tight-rope act that Gorbachev was attempting to master with his zigs and zags between 1985 and 1991.

Gorbachev inherited an economic mess when he rose to power in 1985. 'The problems in the country's development,' Gorbachev stated in his *Political Report of the CPSU Central Committee to the Twenty-Seventh Congress of the Communist Party of the Soviet Union* on 25 February 1986, 'grew more rapidly than they were being solved. The inertness and rigidity of the forms and methods of management, the decline of dynamism in our work, and increased bureaucracy - all this was doing no small damage. Signs of stagnation had begun to surface in the life of society. . . .' Gorbachev insisted that the top priority must be to 'overcome the negative factors in society's socio-economic development as rapidly as possible, to accelerate it and impart to it an essential dynamism, to learn from the lessons of the past to a maximum extent,' so that the decisions the party adopted for the future would be absolutely clear and provide a resolute course of action to remedy Soviet society's ills.<sup>63</sup>

In his book, *Perestroika*, Gorbachev stated that the radical restructuring of the economy was 'an urgent necessity.' Any delay in introducing perestroika, he argued, could lead 'to an exacerbated internal situation in the near future, which, to put it bluntly, would have been fraught with serious social, economic and political crises.'<sup>64</sup> In other words, Gorbachev needed to move to introduce enough economic reality (meaning capitalism) to eliminate the threat to the power base that had developed during the pre-Gorbachev era.

Gorbachev found himself in charge of an economy in decline. The Novosibirsk Report by Tatyana Zaslavskaya, which was originally presented in April 1983 at a closed seminar organized by the economics department of Communist Party Central Committee, the USSR Academy of Sciences and Gosplan, argued that the 'social mechanism of economic development as it functions at present in the USSR does not ensure satisfactory results.' Poor labor habits and

backward technology, she argued, were a 'result of the degeneration of the social mechanism of economic development' which was structured 'not to stimulate, but to thwart the population's useful economic activity.'<sup>65</sup> The solution to the problem, however, was not to be found in decentralization of economic activity. Rather the solution was to be sought in perfecting the social mechanism of development, i.e., improving the institution of planning to accelerate economic growth.

Abel Aganbegyan, Gorbachev's chief economic advisor in the early years of perestroika, argued that the whole purpose of the new economic strategy was to reverse the declining trend in the rate of growth of basic social and economic conditions in the past fifteen years.<sup>66</sup> By the end of the 1960s, Aganbegyan argued in another essay, measures of economic growth and social conditions in the health and housing sectors had deteriorated far below acceptable levels.<sup>67</sup>

After over 70 years in power the Soviet system had produced for its people a standard of living significantly less than all the major countries of Western Europe, the United States and Japan. As mentioned above, the Soviet economy delivered a consumer bundle to its citizens more appropriate to a Third World country than to a world superpower. Consider, for example, data on motor vehicles per capita. In the United States the number of passenger cars per 1,000 people in 1983 was 540, while in the Soviet Union that figure was 36. Perhaps more importantly, the figure in other Soviet bloc nations during the same year was better than that in the Soviet Union. For example, passenger cars per 1,000 people in Hungary was 118 and Poland 87 in 1983, and 1985 data show that in East Germany that number was 180 and in Czechoslovakia 163. The data on telephones per capita also provides evidence of the failing Soviet economy. In 1984, telephone units per 100 population was 76 in the United States, but only 9.8 in the Soviet Union. At the same time, in East Germany there were 21.1 telephone units per 100 population and 22.6 units in Czechoslovakia. Also consider the evidence on infant mortality. Deaths in the first year per 1,000 births for 1985 were 25.1 in the Soviet Union, 17.5 in Poland, 15.3 in Czechoslovakia, 10.4 in the United States and 9.2 in East Germany.<sup>68</sup>

Even consumption of certain basic food items in the Soviet Union was lower than its Eastern Bloc neighbors. For example, in 1984, as Gertrude Schroeder pointed out, 'per capita consumption of meat in the USSR' was 60kg. compared with 75 in Bulgaria, 78 in Hungary, 94 in the GDR, 84 in Czechoslovakia, and 64 in Poland.<sup>69</sup> Clearly the

Soviet economy that Mikhail Gorbachev inherited was, at best, struggling and, at worst, teetering on the edge of an abyss.

The former Soviet system simply failed to provide for its citizens. There was no systemic connection between production and consumption in the economy. The Soviet consumer simply did not matter. Decent medical care or housing, or even the basic nutritional necessities of life, simply could not be had by the average Soviet citizen through official channels.<sup>70</sup> Data on health and human services in the former Soviet Union document this point in gruesome detail. Since 1964, life expectancy had fallen from 67 to 62 for men and from 76 to 73 for women.<sup>71</sup> Lack of available birth control led to a situation where it was estimated that each woman would have between 8 and 14 abortions in her lifetime.<sup>72</sup>

The housing situation also grew acute. In 1981, 20 per cent of Moscow's population still lived in communal apartments.<sup>73</sup> The housing shortage was a direct legacy of Lenin, who had declared that housing space should be allotted at 9 square meters per head. In 1979 *Pravda* reported that there was 12.1 square meters per person including kitchen and bathroom, one-third the corresponding figure in the West.<sup>74</sup> The system failed at both a microeconomic and macroeconomic level.

It was within this economic context that Gorbachev announced his plans for the radical restructuring of the Soviet economy. The social and political context, in addition, was one of a growing cynicism as the corruption of the Brezhnev era was too blatant to be ignored. The economic stagnation and the social cynicism combined to produce a corrupt situation which, as Konstantin Simis described, infected 'the ruling apparatus of the Soviet Union from top to bottom' and had spread through out the whole society 'to all spheres of life.'<sup>75</sup>

This is why Gorbachev argued that he had 'no time to lose.' Speed was of the essence, he stated, 'to overcome the lag, to get out of the quagmire of conservatism, and to break the inertia of stagnation.'<sup>76</sup> The bureaucracy would resist change, but this obstacle must be overcome if there was to be any chance of real restructuring of the Soviet economy. Perestroika, Gorbachev argued, 'means a resolute and radical elimination of obstacles hindering social and economic development, of outdated methods of managing the economy and of dogmatic stereotype mentality.' He understood that perestroika would affect the interests of many people, in fact, the whole society. And, as he put it, 'demolition provokes conflicts and sometimes fierce clashes between the old and the new.'<sup>77</sup>

Selyunin summed up the problem confronting perestroika nicely. 'The existing bureaucratic machine,' he argued, 'cannot be incorporated in restructuring. It can be broken up and eliminated, but not restructured.' Succumbing to the conservative pressure from the bureaucrats and the ordinary people who 'fear independence' and 'harsh economic realities' and, therefore, argue for gradualism, will 'undermine and discredit the whole reform package. 'Losing time,' Selyunin argued, 'means losing everything.' It would be 'useless to gradually introduce new rules into the existing system' since the old system possesses tremendous inertia and will reject all challenges to the established order. The only thing that could be accomplished with gradualism was a discrediting of reforms. "You see, years have been wasted on talk, and one can't see any changes." History will not forgive us if we miss our chance. An abyss must be crossed in a single leap - you can't make it in two.'<sup>78</sup>

This was Gorbachev's challenge. How does one reform a political economy with such entrenched special interest groups? The planning bureaucrats did not wish to resign their posts voluntarily. But, as Nikolai Shmelev stated, either the Soviet Union would move forward with real reforms and break with the past method of economic administration or the system would 'turn into a backward, stagnant state that [would] be an example to the entire world of how not to organize economic life.'<sup>79</sup> The choice that faced Gorbachev and the Soviet people was clear, Selyunin stated, 'either the feeble but absolute power of administrators and the inevitable collapse of the economy, or restructuring with good chances for salvation.'<sup>80</sup>

Besides fighting a bureaucracy that produced for itself - the economic legacy of the Soviet regime - Gorbachev had to fight against the cultural legacy of the regime.<sup>81</sup> The cultural legacy of Soviet rule was perceived as one of the biggest impediments to real restructuring.<sup>82</sup> Complaints ranged from concern about higher prices and lack of economic security to envy over profit making and income inequality.<sup>83</sup> This should not have been surprising. The Gorbachev reforms, if they had represented a sincere effort at 'marketization,' would have brought with them, at least temporarily, the so-called three worse sins of capitalism: *higher prices* as the market adjusted to years of artificially suppressed prices, *unemployment* as some of the previously subsidized firms were forced out of business and *income inequality* as entrepreneurs earned profits by satisfying consumer demand.

Perestroika, therefore, confronted both an economic legacy of a

distorted industrial structure with entrenched special interests, and a cultural legacy which resisted change. This is the essence of the challenge Gorbachev confronted. He tried to enlist the Soviet intellectuals through glasnost to aid him in the endeavor. But the ambiguity and paradoxes within perestroika eventually undermined the alliance with liberal intellectuals through glasnost. The paradox in perestroika, as Gorbachev perceived the reforms, was that he needed strong central control to accomplish a great decentralization of economic decision-making. If he was successful he would lose centralized control to forces that could threaten his political authority. Gorbachev was certainly aware of the risks of his strategy and, therefore, must have believed that either he could withstand the pressure or he did not really intend systematic reform.<sup>84</sup> If no systematic reform was forthcoming, though, then he ran the risk of alienating his strongest supporters – Soviet intellectuals who enjoyed the fruits of glasnost.

Gorbachev's challenge was real. We know from the study of public choice that policy formation within democratic regimes tends to produce policies that possess a bias toward short-term and easily identifiable benefits at the expense of long-term and largely hidden costs. What Gorbachev's professed perestroika promised – if it was to be a sincere effort at marketization – was short-term and easily identifiable costs and long-term and largely hidden benefits. Within a democratic regime, despite the economic logic of such a program, that would mean political suicide. Perhaps an examination of the reform package Gorbachev introduced will give us an indication of how he intended to confront that logic and why his approach ended in failure.

### THE GORBACHEV REFORM PACKAGE

The system Gorbachev inherited was economically and politically bankrupt. Both internal and external debt were enormous, persistent shortages and poor quality products characterized economic life, a tremendous technological gap existed between the Soviet Union and the West and the promise of an integrated European Economic Community in 1992 would highlight the Soviet economic failure. Gorbachev's strategy, decidedly different from the reform path chosen in China, was to institute political, cultural and economic reform. *Perestroika* (restructuring), *glasnost* (public frankness), *Noyoe Myshleniye* (new thinking) and *uskorenie* (acceleration) became the 'buzz-words' of the Gorbachev era. Beginning with the

'Principles of Restructuring: Revolutionary Nature of Thinking and Acting,' *Pravda* (5 April 1988) the Gorbachev era was defined, at least in rhetoric if not always in practice, by radical reform in the political economy of Soviet socialism.

There was, though, a fundamental ambiguity within the reforms from the beginning. The ambiguity was apparent within Gorbachev's words and deeds. Gorbachev's first policies for renewal were an anti-alcohol campaign, and industrial and agricultural centralization with super-ministries. Not exactly an auspicious start for a liberal reformer. Decentralization efforts in economic reform really only emerged in 1987.

Moreover, Gorbachev wanting to reduce the Soviet burden had *de facto* repudiated the Brezhnev doctrine. In fact, he applauded the reforms in Eastern Europe of 1989. At the same time, however, he acted with hesitation and trepidation toward the independence movement in the Baltic nations.<sup>85</sup>

In addition, while the rhetoric of perestroika from 1987 to 1991 moved beyond calls for worker discipline and industrial intensification, and instead demanded the freeing of economic life to stimulate private initiative, Gorbachev continually postponed fundamental economic reform claiming that the people would not tolerate economic change.<sup>86</sup> This constant shifting of policy cost Gorbachev his credibility. For all the talk about renewal and restructuring, Gorbachev had nothing to show on the economic front.

The program of perestroika was filled with ambiguities and inconsistencies and on several levels never did get at the real problems confronting the Soviet economy. Alice Gorlin upon examining the original Gorbachev strategy concluded that his efforts would have only a marginal impact because they did not address the real problems within the system.<sup>87</sup> The basic economic institutions would remain intact. The system would remain much too bureaucratic to expect any significant change. Second, even though new individuals have replaced the previous ministers and bureaucrats, they have as much a vested interest in preserving the current system from which they benefit as did their predecessors.

The Gorbachev reforms, as represented in some of the crucial documents and reforms – specifically, the Law on State Enterprises and the Price Reforms – reveal no coherent strategy for economic renewal. For example, the Law on State Enterprises, which as Gorbachev stated, was of 'primary importance' to the economic reform, was instituted on 1 January 1988.<sup>88</sup> The law was supposed to

grant financial autonomy to enterprises. Firms that could not cover their expenses were no longer to receive subsidization from the state. The intent of the law was to transform firms into fully self-accounting, self-financing and self-managed entities. But enterprises were still subject to state control both in their pricing and output policy. Despite the rhetoric and promise of enterprise autonomy the Law on State Enterprises did not go nearly far enough to meet the objectives of real economic reform.

An even bigger ambiguity within the Gorbachev reform process was probably in the area of price reform. Initially, price reform was to come in 1989, then 1990, and finally it was postponed with the disclaimer that the Soviet people would rather wait on line than pay higher prices.<sup>89</sup> Every time Gorbachev debated freeing up prices there was a run on the state run stores. This just exacerbated the shortage problem already plaguing the Soviet system. Shortages of everything at the state stores became the common condition.<sup>90</sup> So Gorbachev promised to bring relief through subsidized basic products and the whole process of reform was stalled.

Moreover, what was meant by price reform under Gorbachev was never very clear. Aganbegyan, for example, stated that under perestroika a 'radical and total reform of price formation is envisaged' but this did not include the wholesale adoption of free pricing. Prices instead of established

in a voluntaristic fashion . . . will be based on social costs and will take into consideration the cost effectiveness of production and the level of world prices shaped by the relations between supply and demand. The prices will be reviewed at least once every five years and will be closely tied to the indicators of five-year plans . . . The state will set up a certain method for calculating prices, and the Prices Committee is being invested with the task of assessing the rationale for contractual and free prices. In particular, speculative price increases aimed at excessive profit will not be permitted.<sup>91</sup>

In other words, perestroika did not include a proposal to allow freely fluctuating prices to guide exchange and production in a complex economy, but rather it included a call for a better administration of prices. Such a system of price administration should not have been expected to produce any significant desirable results in terms of restructuring the Soviet economy.

These ambiguities were reflected in the economic policy debates

and the speed with which different positions seemed on the rise only to be defeated the following week.<sup>92</sup> In October and November 1989, for example, it appeared as if Leonid Abalkin would push through a radical reform package, including the full adoption of private property and free market prices.<sup>93</sup> Abalkin's program, however, was defeated in December 1989 by the more cautious program of Nikolai Ryzhkov.<sup>94</sup> Then again in March 1990 it seemed that Ryzhkov would be removed from power and that radical economic reforms would be instituted at the urging of Abalkin and Gorbachev's personal economic advisor Nikolai Petrakov.<sup>95</sup> Even in early April 1990 Soviet officials were arguing that there was a good chance they would institute radical economic reforms similar to the program instituted in Poland as of 1 January 1990.<sup>96</sup> But by the end of April 1990 market reforms were postponed indefinitely.<sup>97</sup> And, then, in August and September 1990, it was reported that Gorbachev had finally decided decisively for radical market reforms with the adoption of the Shatalin '500-Day' plan. However, as with all the other reform packages the 500-day plan was rejected in favor of a Gorbachev compromise program with the old Soviet institutions of economic management which basically amounted to no reform at all.

This inconsistency, coupled with the incoherent reform package, resulted in lackluster economic results. The economic performance of the official sector under perestroika was less than desirable. As Aganbegyan admitted in his book, *Inside Perestroika*, from 1985 to 1988 policy-makers had not been able to reduce the problem of shortages and pent up consumer demand.<sup>98</sup> Moreover, the 1990 plan admitted that 'of the 178 highly important types of output that are under state statistical monitoring, the production of 62 was lower in the first eight months of this year than during the same period of last year.'<sup>99</sup> Such basic items as petroleum, coal, gasoline and diesel fuel, fertilizers, chemical fibers, sawtimber, pulp, cardboard, hosiery, sugar and flour were all in short supply. The Soviet economy by 1989 was in even worse shape than it was in 1985. The living standards of the people had not improved. There were shortages of almost everything in the official market, even in Moscow. The collapse of the official market continued throughout the history of perestroika. By the summer of 1990, most products were acquired outside the official state retail distribution system. It was estimated that 42 per cent of meat products, 55 per cent of vegetables, 20 per cent of milk, 75 per cent of potatoes and 44 per cent of eggs were sold outside the state distribution system.<sup>100</sup>

Gorbachev's own hesitation and inconsistency contributed to the problems of reform – which would be difficult enough under even the best of conditions.<sup>101</sup> Gorbachev and his advisors were prisoners of a mode of thinking which could not grasp the basic functions of capitalist markets, nor could they appreciate the institutional preconditions necessary for the successful functioning of markets. This inability resulted in conceptual weaknesses in the reform package which undermined perestroika.<sup>102</sup>

The reforms introduced during the Gorbachev era did not represent a radical restructuring of the Soviet economic system. More accurately they represented a radical realignment of special interest groups from those who benefited under Brezhnev to those who would benefit under Gorbachev.<sup>103</sup> One must infer from his efforts that Gorbachev's intent was simply 'a revitalization of the old regime.'<sup>104</sup> Nothing in the reform package would have been able to overcome the basic structural problems facing the Soviet system. As Marjorie Brady, deputy director of the Russian Research Foundation in London, pointed out, Gorbachev neither rejected the socialist system of planning nor embraced the idea of a free market. Gorbachev envisaged, instead, a 'law-governed economy'; a 'corporatist ideal' if you will. Gorbachev, she stated, was 'bent on creating economic structures of a kind that would scarcely find favor with the Austrian or Chicago schools of economic thought.'<sup>105</sup> In this assessment she was quite correct. And, unfortunately for the peoples of the former Soviet Union, not only did the reforms fail to restructure the system, they actually accelerated the decline of their standard of living as officially measured.<sup>106</sup>

### DOES ECONOMICS HAVE A USEFUL PAST?

One of the most common complaints heard concerning the transition of the economies in East and Central Europe and the former Soviet Union, is that there does not exist a transitional model. But this overlooks the several experiences in history in which strong central governments have been turned back and market economies have flourished.

Yuri Maltsev argues that the models of Spain, Taiwan and Korea are suggestive.<sup>107</sup> Post-Second World War reconstruction also offers several historical models of transformation. The West German 'economic miracle' of Ludwig Erhard speaks well of the positive effect of immediate abolition of price controls.<sup>108</sup> The Hong Kong 'miracle'

is also suggestive. Alvin Rabushka contrasts the economic development of the three Chinas – mainland China, Taiwan and Hong Kong – in the post-Second World War era. By analyzing three jurisdictions with a common cultural heritage, Rabushka demonstrates that prosperity depends far more upon economic institutions than cultural traits or natural resources.<sup>109</sup> The institutional rules that govern economic activity either promote or discourage economic prosperity. The economic benefits of a free market require the underlying institutions that sustain the system: free entry and private property protected by a rule of law. These are indispensable insights for drawing up a workable economic and political constitution for the post-communist world.

Another suggestive approach to the problem of the transition from strong central government to greater economic freedom that has direct relevance to the economies in Eastern Europe and the Soviet Union is Hernando DeSoto's *The Other Path*.<sup>110</sup> DeSoto documents the vast underground economy in operation in Peru. Peru's economic problem is not the people's lack of initiative nor any cultural resistance to capitalism but an over-regulated economic environment. Productive activity flees to the underground to escape the regulatory and taxing power of a bloated bureaucracy. The underground economy was also a staple part of the Soviet type economy as well, representing in some estimates up to 30 per cent of GNP and employing over 20 million in the Soviet Union.<sup>111</sup> Would-be reformers must provide the incentives to economic actors to bring the vast energies devoted to the underground economy to the legitimate economy. In order to do that, firm rights to private property have to be established, consumer and producer subsidies must be eliminated, prices must be completely deregulated and taxation must be limited.

The characterization of the situation in the East as one of trying to make an aquarium out of fish soup is not as apt as it is literary. Economic life was not destroyed in the former Eastern Bloc, just channelled in a different direction. The reform task is one of redirecting the economic energy of the population toward productive activity that has something to do with the satisfaction of consumer demand.

### CONCLUSION

If the disease that plagued the former Soviet economy was misdiagnosed, then that was because the basic anatomy of the Soviet



system was little understood by the doctors of Sovietology. Gorbachev's policy of glasnost eliminated the ability to attribute the failure of the Soviet system to the historical backwardness of the country. Life under the Czars certainly was not very good, but in many respects, life under the communist system was even worse. Throughout its history much of the Soviet population lived in a state of constant fear brought on by the reality of arbitrary political terror.

On the economic front, Soviet citizens did not fare much better. It is a mistaken argument to suggest that Soviet citizens traded-off Western style consumerism for Soviet style security. Sure enough, the society enacted a cradle to the grave security blanket. But that blanket did not provide much comfort. Soviet consumers were forced to wait in long queues in order to acquire products of poor quality. Pride in one's work and the psychological benefits of self-fulfillment were suppressed by an institutional structure which discouraged an ethic of workmanship. The social compact in the former Soviet Union was 'we pretend to work and you pretend to pay us.'

The labor situation in the distorted industrial structure of the Soviet economy represented an implicit welfare system. Workers received no incentive to work in jobs at state run enterprises that could not survive a market test. Pavel Bunich, a reform economist in the former Soviet Union, has remarked that the Soviet Union had the highest unemployment in the world. Unfortunately, he added, the unemployed all get salaries.<sup>112</sup> The structural incentives for enterprise managers rewarded conformity with the gross output targets as opposed to cost minimization. As a result, the Soviet labor market was characterized by an excess demand for labor. Overmanning resulted, but simultaneously so did underemployment of workers as they produced goods which were not valuable to consumers. With a near guarantee of employment, and the low official pay differentials that existed between employment grades, Soviet workers simply had no incentive to exert much effort in their official state jobs.

The official low prices on Soviet products did not offset the low salaries the state employees received. Low prices for goods that cannot be bought at that price are economically meaningless. The failings of the official system to provide goods and services to Soviet consumers forced everyone to rely on the illicit market to purchase basic necessities and augment their paltry official work income. 'Criminal' economic behavior in the black market was both a normal way of life and an albatross around the average citizen's neck. This

economic situation simply reinforced the Kafkaesque environment within which the Soviet people found themselves.

Gorbachev promised to change both the political and economic landscape of Soviet life. To a large extent he did through glasnost. But his success was also his failure. The Soviet system was simply not reformable. The political and economic irrationality that Soviet citizens had to cope with was inherent in the institutional structure of the system.

The establishment of civil society and the unleashing of the productive capacity of the population required a complete break with the old regime. Such a complete break, however, was not a task which the Gorbachev government was up to, and as a result, the situation merely grew more acute from 1985 through 1991. Any claim to legitimacy eroded from the official sector in both politics and economics. The situation of 'dual power' between the official state and the underground society that had always existed implicitly throughout Soviet history emerged explicitly in the late 1980s as dissident intellectuals and politicians vied for intellectual and political power and a new breed of entrepreneurs sought their millions in the embryonic private market economy. This explicit challenge to the ruling order was a necessary condition for the resurrection of a society that had followed the 'road to nowhere' for over seventy years.

During the Gorbachev era, it seemed that the old order withstood the challenge. But it turned out that the ruling *nomenklatura* had won several small battles only to lose the war as the Communist Party was replaced in December 1991 by Yeltsin's democratic Russia. It is not yet clear whether the Yeltsin government will succeed in its endeavors. Moreover, we still do not have a clear picture of the drama of the Gorbachev years. The two 'plays,' however, are connected. We must understand the moral of the story of the one, before we can begin even to construct the tale of the other.

- (Bellevue, WA: Free Enterprise Press, 1990). Piyasheva created a polemical stir in the market debate in the Soviet Union when she published her short paper, 'Where are the Pigs Meating?' (*Novy Mir*, no. 5 (1987)), translated in Anthony Jones and William Moskoff (eds) *Perestroika and the Economy* (New York: M. E. Sharpe, 1989), pp. 99-103. See also her, 'Why is the plan incompatible with the market?', *Annals* (January 1990): 80-90.
- 6 The idea of Gorbachev as a benevolent liberal reformer became the dominant Western perspective after the events of 1989. See, for example, the discussion of Gorbachev in Joshua Muravchik, 'Gorbachev's intellectual odyssey,' *New Republic* (5 March 1990): 20-5. Muravchik argued that Gorbachev 'may yet complete his odyssey by sailing the Soviet ship of state safely beyond the grotesque clutches of Leninism and Marxism to the friendly port of democracy and freedom.' For the events of 1989, Gorbachev was awarded Man of the Decade by *Time* and won the Nobel Peace Prize.
- 7 See *New York Times* (1 January 1989): A1.
- 8 See the discussion of the economics of German unification in Leslie Lipschitz and Donogh McDonald (eds) *German Unification: Economic Issues* (Washington, DC: International Monetary Fund, 1990). On the importance of the collapse of the East German model for Soviet reformers see Marshall Goldman, *What Went Wrong With Perestroika* (New York: Norton, 1991), pp. 56-7.
- 9 Aggregate measurements of well-being, such as per capita GNP, place the former Soviet Union at about 25 per cent of the corresponding figure in the US economy. See *PlanEcon Report*, 6 (52) (28 December 1990): 17. However, since many goods are not available in the state stores at the official price, such calculations do not measure the per capita income of citizens in a shortage economy.
- 10 See George Orwell, *Animal Farm* (New York: Harcourt Brace Jovanovich, 1946). Orwell's book was a parable of the corruption of the Soviet revolution by Stalin and the consequences of collectivization and industrialization. The ideological dictum that all animals were equal gave way to the reality that though all animals were equal some animals were more equal than others. In the end, one could not tell the difference between the pigs (the leaders of the animals) and the humans outside of the farm - the pigs had become just like their previous oppressors.
- 11 See David Levy, 'The bias in centrally planned prices,' *Public Choice*, 67 (1990): 213-26. Also see Konstantin Simis, *USSR: The Corrupt Society* (New York: Simon and Schuster, 1982), and Olimpiad Ioffe, *Gorbachev's Economic Dilemma* (St Paul: Merrill/Magnus Publishing, 1989) for a discussion of the monopolistic and rent-seeking behavior of individuals within the Soviet economy.
- 12 See the pioneering studies on non-market decision-making under non-democratic regimes by Gordon Tullock, *The Social Dilemma* (Blacksburg, VA: Center for Study of Public Choice, 1974) and *Autocracy* (Boston: Kluwer, 1987).
- 13 See Mancur Olson, *Rise and Decline of Nations* (New Haven: Yale University Press, 1983).

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- 1 Arthur Koestler, *Darkness at Noon* (New York: Macmillan, 1941), p. 18.
- 2 See the reports in *The New York Times* (2 May 1990): A1, *The Financial Times* (2 May 1990): 1 and the report by Quentin Peel, 'Revolt against Moscow gathers pace across Union,' *The Financial Times* (3 May 1990): 2.
- 3 See the reports of the Revolution Day Parade in *The New York Times* (8 November 1990): A1 and A12, and *Wall Street Journal* (8 November, 1990): A21.
- 4 See Robert Kaiser, *Why Gorbachev Happened?* (New York: Simon & Schuster, 1991), p. 247, and Hedrick Smith, *The New Russians* (New York: Random House, 1990), p. 132.
- 5 See Robert Conquest, *The Great Terror: A Reassessment* (New York: Oxford University Press, 1990) and *The Harvest of Sorrow* (New York: Oxford University Press, 1986), and G. Warren Nutter, *The Growth of Industrial Production in the Soviet Union* (Princeton: Princeton University Press, 1962) and *Political Economy and Freedom* (Indianapolis: Liberty Press, 1983). Also see Gary Becker's discussion of Nutter in 'Capitalism vs. communism: why it's still no contest,' *Business Week* (2 May 1988): 20. For a discussion of Conquest see Tatyana Tolstaya, 'In cannibalistic times,' *New York Review of Books* (11 April 1991): 3-6. As she points out, when Conquest's *The Great Terror* was published in the Russian journal *Neva* in 1990 many readers exclaimed that they knew all this already. But where had they learned it? From Conquest. When the *Great Terror* was first published in English twenty years ago, Tolstaya informs us, it quickly became an underground classic in the Soviet Union with which all thinking people were acquainted. For an interpretative essay on the rise of historical conscience under Gorbachev see David Remnick, 'Dead souls,' *New York Review of Books* (19 December 1991): 72-81. Also see Thomas Sherlock, 'Politics and history under Gorbachev,' *Problems of Communism* (May-August 1988): 16-42.
- 6 See Roy Medvedev, *Let History Judge*, revised edition (New York: Columbia University Press, 1989), Alexander Tsipko, *Is Stalinism Really Dead?* (New York: Harper Collins, 1990); and Nikolai Shmelev and Vladimir Popov, *The Turning Point: Revitalizing the Soviet Economy* (New York: Doubleday, 1989). Shmelev created a stir with his article, 'Advances and debts,' *Novy Mir*, no. 6 (1987), as did Vasily Selyunin with 'Sources,' *Novy Mir*, no. 5 (1988); both articles fundamentally challenged Soviet claims to economic success.
- 7 *Pravda* (9 November 1991): 1, translated in *The Current Digest of the Soviet Press*, 43 (45) (11 December 1991): 1-2. Though no official government parade occurred, two demonstrations did take place. At one demonstration, in fact, several pro-communists set flowers at the foot of the Lenin monument and carried signs denouncing Gorbachev and Yeltsin. In the other demonstration at Lubyanka (formerly Dzerzhinsky Square), pro-democracy groups held signs that included one that read: 'Lenin - the national disgrace of Russia! Forgive us, Russia, for this

disgrace that we suffered from 1917 until Aug. 19, 1991.' Another read: 'November 7 1917 - a day of national tragedy.'

- 8 See Serge Schmemmann, 'A Russian is swept aside by forces he unleashed,' *The New York Times* (15 December 1991): 1, 12-13, for a report of Gorbachev's rise and fall from power. On Gorbachev's resignation see *The New York Times* (26 December 1991): A1; *The Wall Street Journal* (26 December 1991): A3. See *The Current Digest of the Soviet Press*, 43 (52) (29 January 1992): 1-6 for domestic reports on Gorbachev's resignation. Also see Robert Tucker, 'The last Leninist,' *The New York Times* (29 December 1991): 9.
- 9 Douglas North, *Structure and Change in Economic History* (New York: Norton, 1981), p. x.
- 10 See Mary O. Furner, 'Knowing capitalism: public investigation and the labor question in the long progressive era,' in Mary O. Furner and Barry Supple (eds) *The State and Economic Knowledge* (New York: Cambridge University Press, 1990), p. 241-86. Furner argues that with industrial maturity, economic gains in productivity and wealth were offset by rising social conflict, economic waste in terms of manpower and uncertainty due to business cycles. The private contractual relationships mediated on the market gave way to market failure, collective action and class conflict. *Laissez-faire* policy necessarily ended and was replaced by a multifaceted corporate liberalism, social activism and egalitarian democratic collectivism, which marked the boundaries of modern liberal discourse from the Progressive Era to the New Deal and beyond.
- 11 The drastic change in the climate of opinion during the end of the nineteenth and beginning of the twentieth centuries put a 'fear of socialism' in the hearts and minds of businessmen. Woodrow Wilson challenged leading businessmen, in an address to the Economic Club in New York on 23 May 1912, to develop an alternative vision of the future:

What is the alternative, gentlemen? You have heard the rising tide of socialism . . . Socialism is not growing in influence in this country as a programme . . . If it becomes a programme, then we shall have to be very careful how we propose a competing programme . . . If you want to oust socialism you have got to propose something better. It is a case, if you will allow me to fall into the language of the vulgar, of 'put up or shut up.' . . . It is by constructive purpose that you are going to govern and save the United States . . . Very well, then, let us get together and form a constructive programme [that posterity will say that after America had passed through a simple age] . . . when the forces of society had come into hot contact . . . there were men of serene enough intelligence . . . of will and purpose to stand up once again . . . [and who found out] how to translate power into freedom, how to make men glad that they were rich, how to take envy out of men's hearts that others were rich and they for a little while poor, by opening the gates of opportunity to every man . . .

As quoted in Martin Sklar, 'Woodrow Wilson and the political economy

of modern United States liberalism,' in Ronald Randosh and Murray Rothbard (eds) *A New History of Leviathan* (New York: E. P. Dutton 1972), pp. 66-7, fn. 84.

- The alternative program put forward by the leading businessmen of the day was government regulation of the economy. This drive to regulate their own industry expressed the desire to 'help shape the right kind of regulation before the wrong kind [was] forced upon [them]'. See the letter from Ralph Easley to George Perkins, 9 June 1909, as quoted in James Weinstein, *The Corporate Ideal in the Liberal State* (Boston: Beacon Press, 1968), p. 33. Perkins, who was a partner in the banking house J. P. Morgan and Co., argued that a business court was needed. Ruthless competition led to waste, the sweatshop, child labor and panic and failure. A court comprised of leading businessmen of honorable reputation would ensure the control of competition and promote cooperation between business, labor and government. Thus, such a program would correct the flaws of capitalism without rejecting the system as a whole. Perkins, 'Wanted - a national business court,' *The Independent* (30 November 1911): 1173-7. Gabriel Kolko, *The Triumph of Conservatism* (New York: Free Press, 1963), presents the classic discussion of the rise of political capitalism between the end of the nineteenth century and the First World War.
- 12 On the effect that this has had on modern economic education see Arjo Klamer and David Colander, *The Making of an Economist* (Boulder: Westview Press, 1990). Also see Don Lavoie, 'The present status of interpretation in economics,' Center for the Study of Market Processes, George Mason University, unpublished paper, 1986.
- 13 The metaphor of a frictionless machine was borrowed from physics. On the nature of 'physics envy' in economics see Philip Mirowski, *More Heat than Light* (New York: Cambridge University Press, 1989). One of the most fundamental problems with the friction metaphor in economics is that as it is usually employed it overlooks the fundamental fact that market institutions to a large degree operate only because of frictions. Just like the friction between the sole of our shoes and the road enables us to walk (on a perfectly smooth surface we could find no grip and therefore would not be able to walk), the existence of frictions in the market are the spur for entrepreneurial discovery in competitive capitalism. Israel Kirzner has persistently stressed this point in his work on the theoretical nature of competitive markets. See Kirzner, *Competition and Entrepreneurship* (Chicago: University of Chicago Press, 1973), *Perception, Opportunity and Profit* (Chicago: University of Chicago Press, 1979) and *Discovery and the Capitalist Process* (Chicago: University of Chicago Press, 1985). Also see the interview with Kirzner by Stephan Boehm, 'Austrian economics and the theory of entrepreneurship,' *Review of Political Economy*, 4 (1) (1992): 95-110.
- 14 John Maynard Keynes, 'National self-sufficiency,' *The Yale Review* (1933): 761-2. In 1926, Keynes had argued 'that if Communism achieves a certain success, it will achieve it, not as an improved economic technique, but as a religion.' Keynes argued that the main problem with the conventional critique of communism was that 'We hate Communism

- so much, regarded as a religion, that we exaggerate its economic inefficiency; and we are so much impressed by its economic inefficiency that we underestimate it as a religion. A sound critique of communism, therefore, required the critic to neither exaggerate its economic inefficiency nor underestimate its power as a religion. Keynes, *Laissez-Faire and Communism* (New York: New Republic, 1926), pp. 129-30.
- 15 Keynes, *The General Theory of Employment, Interest and Money* (New York: Harcourt Brace Jovanovich, 1936(1964)), pp. 378-81.
  - 16 See Frank Knight, 'The case for communism: from the standpoint of an ex-liberal' (1932), *Research in the History of Economic Thought and Methodology: Archival Supplement 2* (1991): 57-108. Also see Warren Samuels, 'Introduction,' to Knight's article, 49-55. Knight was a deeply pessimistic person 'incapable of summoning up much enthusiasm for any human institution' and his concern at the time of writing 'The case for communism,' was that liberal society had failed to provide social order. If that was the case, Knight reasoned, then communism may regrettably provide the social order so desperately needed. Knight also argued that the problems of collectivism were not economic problems, but political problems, and as such, the economic theorist had little or nothing to say about the efficacy of collectivism. See Knight, 'The place of marginal economics in a collectivist system,' *American Economic Review*, 26 (1) (March 1936): 255-66. However, also see Knight, 'Socialism: the nature of the problem' (1940) in *Freedom and Reform: Essays in Economics and Social Philosophy* (Indianapolis: Liberty Classics, 1982), pp. 154-93, where he argued that the fundamental economic problem of socialism arises due to the dynamic nature of economic life which demands adjustment and adaptation on the part of economic decision-makers in response to ever-changing conditions.
  - 17 See Paul Homan, 'Economic planning: proposals and the literature,' *Quarterly Journal of Economics*, 47 (1) (November 1932): 102-22.
  - 18 William Loucks, 'Public works planning and economic control: federal, state, and municipal,' *Annals* (July 1932): 114.
  - 19 See William J. Barber, 'Government as a laboratory for economic learning in the years of the Democrat Roosevelt,' in Mary O. Furner and Barry Supple (eds) *The State and Economic Knowledge* (New York: Cambridge University Press, 1990), pp. 103-37.
  - 20 Rexford Tugwell and Howard Hill, *Our Economic Society and Its Problems* (New York: Harcourt, Brace and World, 1934), p. 527. Tugwell in numerous writings stressed the theme that laissez-faire was a bankrupt idea out of touch with the modern world. Tugwell's formula for solving the economic problems of the day was 'concentration and control' of the industrial sector. See, for example, Tugwell, 'The principle of planning and the institution of laissez-faire,' *American Economic Review* (March 1932): 75-92.
  - 21 Julian Huxley, *A Scientist Among the Soviets* (New York: Harper & Brothers, 1932), p. 60.
  - 22 A classic case of an apologist was the correspondent for *The New York Times*, Will Duranty.
  - 23 The founding fathers, however, did not possess such a naive view of

- democracy. Much of the analysis of modern public choice economics derives inspiration from the work of the founders on constitutional design. See, in particular, James Buchanan and Gordon Tullock, *The Calculus of Consent* (Ann Arbor: University of Michigan Press, 1962). One possible explanation of the loss of the basic wisdom of the founders may be due to changes in the intellectual landscape with the 'death of God' in the nineteenth century. Whereas before man was viewed as a fallen angel in need of constraint, now he was viewed as a risen ape capable of great accomplishments. Rather than constrained, this vision of man sought to unleash man's unlimited potential. See Peter Boettke, 'Constitutional erosion caused capitalist decay,' *The World and I* (November 1991): 540-2. Unleashing the powers of democracy was one method to tap into that potential. For an examination of the alternative perspectives on social theory that derive from a constrained versus unconstrained vision of man see Thomas Sowell, *A Conflict of Visions* (New York: William Morrow, 1987).
- 24 Letter from Keynes to F. A. Hayek dated 28 June 1944 in John Maynard Keynes, *Collected Works*, vol. 27 (New York: Cambridge University Press, 1980), p. 387.
  - 25 Herman Finer, *Road to Reaction* (Chicago: Quadrangle Books, 1945), p. v. For a more even headed criticism of Hayek see, Barbara Wootton, *Freedom under Planning* (Chapel Hill: University of North Carolina Press, 1945).
  - 26 See Peter Boettke, 'Analysis and vision in economic discourse,' *Journal of the History of Economic Thought*, 14 (Spring 1992): 84-95.
  - 27 As Hayek wrote, 'The consequences of this is that in the statistical study of social phenomena the structures with which the theoretical social sciences are concerned actually disappear. Statistics may supply us with very interesting and important information about what is the raw material from which we have to reproduce these structures, but it can tell us nothing about these structures themselves. In some fields this is immediately obvious as soon as it is stated. That the statistics of words can tell us nothing about the structure of a language will hardly be denied. But although the contrary is sometimes suggested, the same holds no less true of other systematically connected wholes such as, for example, the price system.' See *The Counter-Revolution of Science* (Indianapolis: Liberty Classics, 1979(1952)), pp. 108-9.
  - 28 See Richard Ericson, 'The Soviet statistical debate,' in Henry Rowen and Charles Wolf (eds) *The Impoverished Superpower* (San Francisco: ICS Press, 1990), p. 77.
  - 29 Grigory Khanin and Vasily Selyunin, 'The elusive figure,' *Novy Mir*, no. 2 (February 1987), translated in *The Current Digest of the Soviet Press*, 39 (25) (1987): 10-12.
  - 30 *CIA: Handbook of Economic Statistics, 1987* (Washington, DC: GPO, 1987): 24-5.
  - 31 Soviet per capita GNP in 1990 was estimated to be \$5,060 as compared to \$21,000 for the US. See *PlanEcon Report*, 6 (52) (28 December 1990): 17. Even this figure overstates Soviet GNP because of the unavailability of many goods at official prices. Also see Andres Aslund,

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- 'How small is Soviet national income?,' in Rowen and Wolf (eds) *The Impoverished Superpower* (see Note 28), pp. 13-61.
- 32 See Merton Peck and Thomas Richardson (eds), *What Is To Be Done?* (New Haven: Yale University Press, 1991), p. 4.
- 33 See Rowen and Wolf, 'Introduction,' *The Impoverished Superpower* (see Note 28), p. 7.
- 34 This is not meant to suggest that the former Soviet Union posed no threat to world peace. Clearly, the stock pile of nuclear weapons amassed by the Soviet government could destroy the world several times over, as could those collected in the West. But, two questions immediately emerge concerning Soviet military power when confronted with the revised data. How could the Soviet Union have accomplished its military build-up with such a backward economy, and could these military developments be sustained over time? To answer these questions, we must recognize the fundamental distinction between a technological problem - where there is only one unified end considered by decision-makers - and an economic problem - where there are multiple ends being pursued within society. By turning all economic problems into technological problems a social system eliminates the problem of competing ends for which scarce means must be allocated among alternative uses. However, the technological approach to social policy does not allow the experimentation, and the social learning of trial and error that generates the innovations and industrial progress that are vital for economic development. Without sustainable economic development, moreover, military power erodes. On the difference between a society which provides for the reconciliation of many ends and one in which only one end may be pursued see F. A. Hayek, *Law, Legislation and Liberty*, vol. 2 (Chicago: University of Chicago Press, 1978), pp. 107-32. Also see James Buchanan, 'Markets, states, and the extent of morals,' in *What Should Economists Do?* (Indianapolis: Liberty Press, 1979), pp. 219-29. On the relationship between economics and military power see Tyler Cowen, 'Economic effects of a conflict-prone world order,' *Public Choice*, 64 (February 1990): 121-34.
- 35 See Seymour Melman, *The Permanent War Economy* (New York: Simon and Schuster, 1974) and *Profits without Production* (New York: Alfred Knopf, 1983) for a critical discussion of the military economy.
- 36 Even if left-wing intellectuals opposed increased military expenditures, their arguments concerning the desirability of socialism as an economic system simply reinforced right-wing fears about the threat of communism.
- 37 As pointed out by V. Sirotkin,

It has become a copybook maxim to assert that the policy of 'War Communism' was imposed on the Bolsheviks by the Civil War and the foreign intervention. This is completely untrue, if only for the reason that the first decrees on introducing the 'socialist ideal' exactly 'according to Marx' in Soviet Russia were issued long before the beginning of the Civil War (the decrees of Jan. 26 and Feb. 14, 1918, on the nationalization of the merchant fleet and of all banks),

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- while the last decree on the socialization of all small handicraftsmen and artisans was issued on Nov. 29, 1920, i.e., after the end of the Civil War in European Russia. Of course, the Civil War and the intervention left an imprint. But the main thing was something else - the immediate implementation of theory in strict accordance with Marx (from 'Critique of the Gotha Program') and Engels (from 'Anti-During').
- See Sirotkin, 'Lessons of NEP,' *Izvestia* (9 March 1989), translated in *The Current Digest of the Soviet Press*, 41 (10) (5 April 1989): 6.
- 38 John Reed, *Ten Days that Shook the World* (New York: Penguin Books, 1985(1919)): 129. Also see Leon Trotsky, *The History of the Russian Revolution*, vol. 3 (London: Pathfinder, 1980(1932)), pp. 323-4.
- 39 'Program of the Communist Party of Soviet Russia,' in Nikolai Bukharin and E. A. Preobrazhensky, *The ABC of Communism* (Ann Arbor: University of Michigan Press, 1966(1919)), p. 390.
- 40 V. I. Lenin, *The Immediate Tasks of the Soviet Government* (1918), in *Collected Works*, vol. 27 (Moscow: Progress Publishing, 1977), p. 352.
- 41 *Program of the Communist Party of Soviet Russia*, 397. Also see the discussion of money and banking in Lenin's *Draft Programme of the RCP(B)* (1919), in *Collected Works*, vol. 29, p. 115 (see Note 40).
- 42 Bukharin and Preobrazhensky, *The ABC of Communism* (see Note 39), p. 77.
- 43 Stephen Cohen, *Bukharin and the Bolshevik Revolution* (New York: Oxford University Press, 1980(1973)), p. 123.
- 44 V. I. Lenin, *The New Economic Policy and the Tasks of the Political Education Departments* (1921), in *Collected Works*, vol. 33, pp. 63-4 (see Note 40).
- 45 The importance of the NEP is not limited to historical understanding, but is intimately connected to the Gorbachev reforms. Gorbachev described perestroika as a return to the NEP. As Theodore Draper wrote, 'This return to an NEP-type reform is particularly characteristic of the unfolding Gorbachev period; Gorbachev himself has invoked the precedent of the NEP, as if it gave him a license to do what he wants to do. Thus, we are not straying too far from the present in paying special attention to the NEP period. Nep-thinking is imbedded in the present.' Draper, 'Soviet reformers: from Lenin to Gorbachev,' *Dissent* (Summer 1987): 287.
- 46 V. I. Lenin, *Political Report of the Central Committee of the RCP(B)* (1922), in *Collected Works*, vol. 33, p. 289 (see Note 40).
- 47 V. I. Lenin, *Better Fewer, But Better* [1923], in *Collected Works*, vol. 33, p. 487 (see note 40).
- 48 Richard Day, *Leon Trotsky and the Economics of Isolation* (New York: Cambridge University Press, 1973), p. 69.
- 49 By 1938, Stalin had out-manipulated all of the original Bolshevik leaders. Of the original central committee of the Bolshevik Party in 1917, by 1938 only Stalin remained. See the dramatic picture detailing the fate of the Old Bolsheviks in *Spartacist*, 41-2 (Winter 1987-8): 38.
- 50 See, for example, Joseph Stalin, *Economic Problems of Socialism in the USSR*, 2nd edn (Moscow: Foreign Languages Publishing, 1953), pp. 104-

- 5, where he argued that the fact that since a considerable proportion of the collective farm output goes into the market and perpetuates the system of commodity circulation prevented the elevation of collective farm property to the level of public property.' The goal of socialist policy, Stalin argued, must be to eliminate commodity production and institute a system of production for direct use. 'Such a system would require an immense increase in the goods allocated by the town to the country, and it would therefore have to be introduced without any particular hurry, and only as the products of the town multiply. But it must be introduced unswervingly and unhesitatingly, step by step contracting the sphere of operation of commodity circulation and widening the sphere of operation of products-exchange.'
- 51 See Michael Voslensky, *Nomenklatura* (New York: Doubleday, 1984), pp. 14-67.
- 52 Eugene Zaleski, *Stalinist Planning for Economic Growth, 1933-1952* (Chapel Hill: University of North Carolina Press, 1980), p. 484.
- 53 See Paul Craig Roberts, *Alienation and the Soviet Economy* (New York: Holmes and Meier, 1990(1971)), pp. 48-88, for the pioneering analytical study of the polycentric nature of the Soviet economy. Roberts derived and developed his ideas from the suggestive work of Michael Polanyi. See, in particular, Polanyi, *The Logic of Liberty* (Chicago: University of Chicago Press, 1980(1951)), pp. 111-37.
- 54 See Aleksander Bajt, 'Property in capital and in the means of production in socialist economies,' *Journal of Law and Economics*, 11 (April 1968): 1-4. Also see Svetozar Pejovich, *The Economics of Property Rights* (Boston: Kluwer, 1990), pp. 97-103, 115-20. In addition, see Jack Wiseman, 'Property Rights and Post-Soviet Liberalization,' *The Financial Times* (3 April 1990).
- 55 Selyunin, 'Sources,' *Novy Mir*, no. 5 (May 1988), translated in *The Current Digest of the Soviet Press*, 40 (40) (1988).
- 56 See Gregory Grossman, 'The "second economy" of the USSR,' *Problems of Communism* (1977), reprinted in Morris Bornstein (ed.) *The Soviet Economy: Continuity and Change* (Boulder, CO: Westview Press, 1981). Also see Grossman, 'Roots of Gorbachev's problems: private income and outlay in the late 1970s,' *Gorbachev's Economics Plans*, vol. 1 (Washington, DC: GPO, 1987), pp. 213-29. In addition, see F. J. M. Feldbrugge, 'The Soviet second economy in political and legal perspective,' in Edgar Feige (ed.) *The Underground Economies* (New York: Cambridge University Press, 1989) and G. Belikova and A. Shokhin, 'The black market: people, things and facts,' *Ogonek* (September 1987), translated in *Soviet Review*, 30 (3) (May-June 1989): 26-39.
- 57 W. H. Chamberlin, *The Russian Revolution*, vol. 2 (Princeton: Princeton University Press, 1987(1935)), p. 105.
- 58 See Gary Anderson, 'Profits from power: the Soviet economy as a mercantilist state,' *The Freeman*, 38 (12) (December 1988): 483-92.
- 59 Leonid Abalkin, 'Relying on the lessons of the past,' *Kommunist*, 16 (1987), translated in *Problems of Economics* (June 1988): 7, 11, 15.
- 60 See the classic discussion of the distinction in John Stuart Mill, *Principles of Political Economy* (New York: Augustus M. Kelley, 1848(1976)),

- pp. 199ff. Mill argued that while the laws of production are governed by nature, the laws of distribution are solely a matter of human institutions.
- 61 See the analysis of Joseph Schumpeter, 'The crisis of the tax state,' in Richard Swedberg (ed.) *The Economics and Sociology of Capitalism* (Princeton: Princeton University Press, 1990(1918)), pp. 99-140. Also see David Prychitko, 'The welfare state: what is left?,' *Critical Review*, 4 (4) (Fall 1990): 623-5.
- 62 Alain Besancon, 'Anatomy of a spectre,' *Survey*, 25 (4) (Autumn 1980): 156-8.
- 63 Mikhail Gorbachev, *Political Report of the CPSU Central Committee to the 27th Party Congress* (Moscow: Novosti Press Agency, 1986), p. 6.
- 64 Mikhail Gorbachev, *Perestroika* (New York: Harper & Row, 1987), p. 17.
- 65 See Tatyana Zaslavskaya, 'The Novosibirsk Report,' *Survey*, 28 (1) (Spring 1984): 106.
- 66 See Abel Aganbegyan, *The Economic Challenge of Perestroika* (Bloomington: Indiana University Press, 1988), pp. 1-44.
- 67 See Abel Aganbegyan, 'Acceleration and perestroika,' in Aganbegyan and Timofeyev, *The New Stage of Perestroika* (New York: Institute for East-West Security Studies, 1988), p. 26.
- 68 See Zbigniew Brzezinski, *The Grand Failure* (New York: Simon & Schuster, 1988), pp. 263ff.
- 69 Gertrude Schroeder, *The System Versus Progress* (London: Centre for Research into Communist Economies, 1986), p. 75.
- 70 See Paul Craig Roberts and Karen LaFollet, *Meltdown: Inside the Soviet Economy* (Washington, DC: CATO Institute, 1990), pp. 39-74, for a discussion of the plight of Soviet consumers.
- 71 Nick Eberstadt, *The Poverty of Communism* (New Brunswick: Transaction Publishers, 1988), p. 50.
- 72 Francine du Plessix Gray, *Soviet Women: Walking the Tightrope* (New York: Doubleday, 1989), pp. 13-27.
- 73 Marshall Goldman, *USSR in Crisis* (New York: Norton, 1983), p. 99.
- 74 David Willis, *Klass: How Russians Really Live* (New York: Avon Books, 1985), p. 59.
- 75 Konstantin Simis, *The Corrupt Society* (New York: Simon & Schuster, 1982), p. 299.
- 76 Gorbachev, *Perestroika*, p. 51 (see Note 64).
- 77 Gorbachev, *Perestroika*, pp. 51-2 (see Note 64).
- 78 Selyunin, 'Sources,' p. 17 (see Note 55).
- 79 Nikolai Shmelev, 'Economics and common sense,' *Znamia* (July 1988), translated in *Problems of Economics* (March 1989): 58.
- 80 Vasily Selyunin, 'A profound reform or the revenge of the bureaucracy?,' *Znamia* (July 1988), translated in *Problems of Economics* (March 1989): 31.
- 81 For a 'conservative' defense of the Soviet regime see Nina Andreyeva, 'Polemics: I cannot waive principles,' in Isaac Tarasulo (ed.) *Gorbachev and Glasnost* (Wilmington: Scholarly Resources, 1989), pp. 277-90. Andreyeva's letter generated much controversy when it was published in *Sovetskaya Rossiya* on 13 March 1988 and solicited responses from

- Gorbachev and his supporters in the pages of *Pravda* on 5 April 1988. In addition, in a poll conducted in the Soviet Union in November of 1989 40 per cent of those polled stated that they wished to see a return of a 'strong hand' and to the old system of economic management. See *The New York Times* (5 November 1989). However, there have been some important questions raised concerning the validity of the poll. See Aleksandras Shtromas, 'Russia on the road to political and economic freedom,' in Richard Ebeling (ed.) *Austrian Economics: Perspectives on the Past and Prospects for the Future* (Hillsdale: Hillsdale College Press, 1991), p. 236.
- 82 'Perhaps the most painful legacy of all,' Gertrude Schroeder argued, 'rests in the inherited values, attitudes, and habits of the work force. For decades, people have been taught that private property means exploitation and that socialism means a welfare state, an egalitarian distribution of income, permanent job security, and low prices for the basic necessities of life. In other words, people have learned to let the government take care of them. But successful perestroika requires a virtual renunciation of such attitudes and values; it requires "new thinking" and a "new psychology" as Gorbachev often puts it.' See Gertrude Schroeder, 'The Soviet economy: is perestroika possible?', *The World and I* (November 1989): 55.
- 83 See Marshall Goldman, *What Went Wrong with Perestroika* (New York: Norton, 1991), p. 116, for a discussion of the 'envy' effect toward private farmers during the Gorbachev regime. Goldman, however, argues that the hostility toward private trade is not solely a legacy of communist indoctrination, but is deeply rooted in the Russian culture. While undoubtedly certain factors underlie some of the main propositions that will emerge from my argument in this book is that institutional rules are a much greater force in determining economic performance than either the endowment of natural resources or the cultural heritage of a country.
- 84 See Mikhail Gorbachev's interview in *Komsomolskaya Pravda* (24 December 1991), translated in *The Current Digest of the Soviet Press*, 43 (51) (22 January 1992): 7-8.
- 85 See Mikhail Gorbachev's formal response to the ethnic unrest in response to the fiftieth anniversary of the Stalin-Hitler Pact in *The Current Digest of the Soviet Press*, 41 (34): 1-9, (38): 5-10. Also consider the 'Tbilisi crackdown' on 8 April 1989 where Soviet troops were sent in using sharpened shovels and lethal gas to restore order and ended up killing 20 and poisoning 1,000 people. See Peter Reddaway, 'The threat to Gorbachev,' *New York Review of Books* (17 August 1989): 21. Also the events following the Lithuania declaration of independence in March 1990 demonstrated the ambiguity within Gorbachev's domestic political policy.
- 86 See, for example, the report by Bill Keller in *The New York Times* (25 April 1990): A7, on the decision by the Gorbachev regime not to follow Poland's example of 'shock therapy' and to postpone fundamental economic reform. Also see *The Financial Times* (23 May 1990): 2, 4.

- 87 Alice Gorlin, 'The Soviet economy,' *Current History*, 85 (October 1986): 325-8, 343-5.
- 88 Gorbachev, *Perestroika*, p. 86 (see Note 64). The complete text of the Law on the State Enterprises was published in *Pravda* (1 July 1987) and translated in *The Current Digest of the Soviet Press*, 39 (30) (1987): 8-13, 24, and 39 (31) (1989): 10-27, 28. Also see the analysis of the law by Richard Ericson, 'The New Enterprise Law,' *The Harriman Institute Forum*, 1 (2) (February 1988).
- 89 See the report by John Lloyd in *The Financial Times* (25 April 1990) that Nikolai Petrakov, Gorbachev's personal economic advisor at that time, blamed communism for the decision to delay market reforms.
- 90 See David Lascelles, 'After the great lie, the ghastly truth,' *The Financial Times* (9 March 1990): 19, for a description of economic life inside the Soviet Union five years after the rise of Gorbachev.
- 91 Aganbegyan, *The Economic Challenge of Perestroika*, pp. 133-5 (see Note 66).
- 92 Anders Aslund, *Gorbachev's Struggle for Economic Reform* (Ithaca: Cornell University Press, 1989), p. 185, argues that it would be inappropriate to refer to the reforms as Gorbachev's reforms because all reform laws emerge as a compromise package. 'The overall conclusion,' Aslund states, 'is that Gorbachev pushes energetically for reform, but does not control its design. The Soviet Union is actually governed by a truly collective leadership. Therefore it is not very accurate to talk about "Gorbachev's economic reforms."'
- 93 See Abalkin, 'The radical economic reform: top priority, tasks and long-term measures,' *Ekonomicheskaya Gazeta*, 43 (October 1989), translated in *The Current Digest of the Soviet Press*, 41 (46) (13 December 1989): 10-11, 39-40.
- 94 Earlier Ryzhkov had proposed a program which would have slashed state ownership from 85 per cent to 30 per cent. See *The New York Times* (17 November 1989): A16. But on Wednesday 13 December 1989, Prime Minister Ryzhkov delivered a speech, that represented the official position on perestroika, which undermined the earlier movement toward a market economy and was seen as a clear victory for GOSPLAN. See Ryzhkov, 'Efficiency, consolidation, and reform are the path to a healthy economy,' *Pravda* (14 December 1989), translated in *The Current Digest of the Soviet Press*, 41 (51) (17 January 1990): 1-9. Also see *The Financial Times* (15 December 1989): 18.
- 95 See *The Financial Times* (20 March 1990): 18 and Ed Hewett, 'Prognosis for Soviet economy is grave, but improving,' *New York Times* (25 March 1990) for a discussion of the promise of radical market reforms.
- 96 See the *Investor's Daily* (2 April 1990): 10, for a report of Vyacheslav Senchagov, chief of the State Price Committee, speech to the deputies of the Supreme Soviet. He suggested that the Soviet Union would follow Poland's 'shock therapy' approach, but added that such a plan may be blocked by angry consumers. Therefore, while a radical approach would be preferred, a more moderate approach may be pursued during the transition to maintain the population's confidence.

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- 97 See Ed Hewett and Richard Hornik, 'Hurry, doctor,' *Time* (7 May 1990): 81-2, for a criticism of Gorbachev's decision to back off from radical reform in the spring of 1990.
- 98 Abel Aganbegyan, *Inside Perestroika* (New York: Harper & Row, 1989).
- 99 See *The Current Digest of the Soviet Press*, 41 (40) (1 November 1989).
- 100 See Alfred Kahn and Merton Peck, 'Price deregulation, corporatization, competition,' in Merton Peck and Thomas Richardson (eds) *What Is To Be Done?*, p. 43 (see Note 32).
- 101 See Goldman, *What Went Wrong with Perestroika*, p. 110 (see Note 83). The adverse reputational effect of Gorbachev's indecision and inconsistency will be discussed at length in Chapter 6.
- 102 See Padma Desai, *Perestroika in Perspective* (Princeton: Princeton University Press, 1989), p. 53.
- 103 This argument is more fully developed in Gary Anderson and Peter Boettke, 'Perestroika and public choice: the economics of autocratic succession in a rent-seeking society,' *Public Choice* (1992), forthcoming.
- 104 See William Odom, 'How far can economic and social change go in the Soviet Union?,' in Ronald Liebowitz (ed.) *Gorbachev's New Thinking* (Cambridge, MA: Ballinger Publishing, 1988), p. 86.
- 105 See Marjorie Brady, 'The Fascist element in perestroika,' *The Wall Street Journal* (31 October 1989).
- 106 *Izvestia* (17 October 1990), for example, reported that with an official poverty line set at 78 roubles/month, 40 million lived in poverty. If the poverty line was raised to 100 roubles/month, it estimated that the figure would be 70.9 million.
- 107 Yuri Maitsev, foreword, in Peter Boettke, *The Political Economy of Soviet Socialism: The Formative Years, 1918-1928* (Boston: Kluwer, 1990).
- 108 See F. A. Lutz, 'The German currency reform and the revival of the German economy,' *Economica*, 16 (May 1949): 122-42; Henry Wallich, *Mainsprings of the German Revival* (New Haven, CT: Yale University Press, 1955) and Egon Sohmen, 'Competition and growth: the lesson of West Germany,' *American Economic Review* (1959): 986-1003. An interesting note, however, is that the majority of the economics profession viewed the Erhard reforms with great caution. See, for example, Horst Mendershausen, 'Prices, money and the distribution of goods in postwar Germany,' *American Economic Review*, 39 (June 1949): 646-72, and Walter Heller, 'The role of fiscal-monetary policy in German economic recovery,' *American Economic Review*, 40 (May 1950): 531-47. Also see the discussion in T. W. Hutchison, *The Politics and Philosophy of Economics* (New York: New York University Press, 1981): 155-75.
- 109 Alvin Rabushka, *The New China* (Boulder, CO: Westview Press, 1987).
- 110 Hernando DeSoto, *The Other Path* (New York: Harper & Row, 1989).
- 111 See Walter Laqueur, *The Long Road to Freedom* (New York: Charles Scribner's, 1989), p. 203.
- 112 As quoted in Hedrick Smith, *The New Russians* (New York: Random House, 1990), p. 185.

## NOTES

## 3 THE THEORETICAL PROBLEMS OF SOCIALISM

- 1 Alexander Tsipko, *Is Stalinism Really Dead?* (New York: Harper Collins 1990), p. 12.
- 2 Ludwig von Mises, *Socialism* (Indianapolis: Liberty Classics, 1981(1922)) p. 41.
- 3 Mikhail Gorbachev, for example, has even recently reiterated the standard socialist and Western Marxist argument that the Soviet collapse had nothing to do with socialist ideas, but rather represented the collapse of Stalinism. See Gorbachev, 'No time for stereotypes,' *New York Times* (24 February 1992): A19. On the intellectual staying power of Marxism in the face of recent events see Henry F. Myers, 'Das Kapital, his statues topple, his shadow persists: Marx can't be ignored,' *The Wall Street Journal* (25 November 1991): A1 and A4.
- 4 Tsipko, *Is Stalinism Really Dead?*, p. 12 (see Note 1).
- 5 For an extensive history of Marxism see Leszek Zolakowski, *Main Currents of Marxism*, 3 vols (New York: Oxford University Press, 1985(1978)). On Marx's project see Andrzej Walicki, 'Karl Marx as philosopher of freedom,' *Critical Review*, 2 (4) (Fall 1988): 10-58.
- 6 See Don Lavoie, *Rivalry and Central Planning* (New York: Cambridge University Press, 1985), pp. 29-30.
- 7 Karl Marx, *Capital* (New York: Modern Library, 1906(1867)), p. 92.
- 8 Alan Ryan, 'Socialism for the nineties,' *Dissent* (Fall 1990): 441-2, (emphasis added).
- 9 David L. Prychitko has argued that the organizational logic of even the most decentralized and democratic socialism leads to centralization during the process of resolving the conflict of alternative requests for resource use. See Prychitko, 'Marxism and decentralized socialism,' *Critical Review*, 2 (4) (Fall 1988). Also see Prychitko, *Marxism and Workers' Self-Management: the Essential Tension* (Westport, CT: Greenwood Press, 1991), pp. 83-100.
- 10 For this reason it has been forcefully argued that the Lange-Lerner theoretical system did not provide an answer to Mises's critique of socialism. See Paul Craig Roberts, 'Oskar Lange's theory of socialist planning,' *Journal of Political Economy*, 79 (3) (May/June 1971): 562-77; Karen Vaughn, 'Economic calculation under socialism: the Austrian contribution,' *Economic Inquiry*, 18 (1980): 535-54; Peter Murrell, 'Did the theory of market socialism answer the challenge of Ludwig von Mises?,' *History of Political Economy*, 15 (1) (Spring 1983): 92-105; and Lavoie, *Rivalry and Central Planning*. Also see Larissa Popkova-Pijasheva, 'Why is the Plan incompatible with the market?,' *Annals*, 507 (January 1990): 80-90, and Anthony deJasay, *Market Socialism* (London: IEA, 1990), for criticisms of the logical coherence of market socialism.
- 11 Kornai, *The Road to a Free Economy* (New York: Norton, 1990), p. 58.
- 12 Adam Smith did possess a germ of the argument when he stated that:

What is species of domestic industry which his capital can employ, and of which the produce is likely to be of the greatest value, every individual, it is evident can, in his local situation, judge much better