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The Privatization of Soviet Socialism

According to Richard Ericson, many Soviet citizens have lost faith in Socialism, but they have not abandoned a number of the values that the socialist system was founded upon. *Perestroika* has so far failed to rescue the system from crisis, yet it continues to offend deeply-seated beliefs of the average Soviet citizen. Ericson, professor of economics at Columbia University and the Harriman Institute, addressed these issues at a special interdisciplinary seminar November 30, 1988.

Perestroika's radicalism not only challenges social values such as egalitarianism, the primacy of social obligation over private interest, and collective ownership. It also attacks the system's key institutions — the command economy and the idea of reward according to service rather than result — which had enshrined these values. This challenge is “nowhere clearer than in the evolution of *perestroika's* economic program and its increasingly merciless attack on the traditional socialist system and its shortcomings and tragic costs.” Legitimizing *perestroika* has meant, in the eyes of many, “denigrating the achievements of socialism.” In this vein, contemporary economists Nikolai Shmelev and Vasilii Seliunin “argue that existing Socialism is responsible for only waste and suffering.”

Stages of Reform

Professor Ericson outlined three stages of economic reform under Gorbachev: the first (1985-6) featured traditional measures such as tightening discipline and shifting investment. The second stage, inaugurated in early 1987, attempted to reform the state economic sector and to create a socialist market economy. Professor Ericson dubbed the third stage of economic reform, which began in early 1988, “the privatization of Soviet socialism.” Intended to “revivify a stagnating economy,” the reforms of this stage include the Law on Cooperatives, implementation of long-term leasing to private operators (especially in agriculture), and the earlier Law on Individual Labor Activity. This period of change has spawned active debate on the reform of property relations. From these debates “it has become

clear to economic reformers that for market socialism to work, a number of ideologically, socially and morally ‘alien’ market institutions need to arise.”

Up until now, the structure of production in the Soviet Union discouraged competition and hence prevented implementation of true state sector reform. Industry has remained monopolized and rigid. Managers know virtually nothing about the operation of markets and continue to rely on their superiors for information and advice, and “bureaucratic superiors are only too glad to oblige and provide supervision.” As a result, competition has been nonexistent and the Soviet consumer has remained miserable. The third, ‘privatizing’ stage of reform is an attempt to rectify the shortcomings of the earlier stages. It aims to “rescue *perestroika* for the Soviet consumer.” This would be achieved by laying a basis for institutions that would create and sustain real competition, eliminating the need for central economic coordination.

Ericson emphasized that markets cannot function without money as a universal equivalent and indiscriminating commercial banking and credit. Markets also require flexible prices which respond to economic, not social and/or political pressures. Middlemen, who are still forbidden in the Soviet Union, must be allowed to compete for profits. Soviet Socialism has always branded these forces suspect and dangerous; Ericson deems them indispensable to economic improvement. Moreover, “they cannot work properly without real, effective competition, based on an economic struggle for wealth and property.”

Legislation enacted in the third stage of economic reform has “vastly expanded the scope of legal private organization and initiative in production activity.” The effort goes both too far and not far enough. No steps have been taken to legalize middlemen, so effective economic reform remains a pipe-dream. Yet the reforms glorify the pursuit of profit and individual wealth, which most Soviet citizens find “vicious and uncivilized.”

Ericson asserted that the private cooperatives must “become large and important enough to compete with the state.” While this competition may some day solve



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consumers' problems, the solution comes at the cost of sharpening social tensions, and perhaps even of undermining the bases of Party and state authority.

A Distorted Private Sector

Legal, bureaucratic and social obstacles to cooperatives and individual activity have rendered the private sector in the USSR counterproductive. Individual labor activity is subject to severe restrictions, and taxes on profits are heavily punitive. Ericson suggested that these measures "give teeth to" feelings of deep hostility and envy borne by many average Soviets toward the few who are striving for economic success and wealth.

Private economic activity is expanding rapidly despite these hindrances, but it has produced a distorted private sector. This sector centers on consumer services, construction, consulting, and agriculture. But since there are no middlemen, "who are crucial to sustaining the balance of a market economy," there is little feedback and competition. In the absence of real competition, private producers can get away with selling shoddy goods at "obscene prices." According to Ericson, many private outfits are fly-by-night operations which "do not strive to improve quality." They serve purely their own interests; their reward is unrelated to social service. Outraged Soviet consumers consider them "parasites," but have no economic recourse or protection from their abuses.

Although the distorted private sector provokes hostility in the Soviet population, measures to correct the distortions would only "further affront Soviet values." These developments would include arbitrage, the accumulation of private capital, and an expanded share for the private sector. An ominous ramification is that state interests could "become to some extent derivative of private interests." A "crisis of power" could arise as private economic interests seek political expression and gain the resources to achieve it.

The Party's Future

Soviet leaders seem in a quandary over how to bring about economic revival. "The Party needs to withdraw from the economy for even the socialist markets of *perestroika* to work." Yet privatization could jeopardize the Communist Party's role in Soviet society. Without an explicit economic function, the Party would lose some of its claim to legitimacy.

Ericson believes that major progress can occur only as an outcome of the Party sharing economic power with successful private producers, but "this is a truly alien idea for most Soviets, including the leadership." He found it ironic that *perestroika*, which was intended to respond to the crisis of values and power in the USSR, is now attacking values and institutions that most Soviet citizens hold dear.

Reported by Rachel Denber

Note to Instructors:

The following back issues of *The Harriman Institute Forum* are available, at no charge, for classroom distribution and use:

The Foreign Economic Factor in Perestroika by Ed A. Hewett

Legal Reform in the Soviet Union by William E. Butler

If interested, contact Publications Officer Paul Lerner

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