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# Venezuela and New Socialism

In 1989 Paul Cockshot and Allin Cottrell wrote a book on socialism which was published three years later in English as *Towards a New Socialism*. This book was addressed at an audience in the USSR and East European countries because it dealt with the problems that socialism was then facing in these countries. It had been the intention to have it translated and published in Russian. The book presented a model of how to run a socialist economy based on clear economic and moral principles and re-asserted the basic values of socialism against the pro-capitalist measures being introduced under Gorbachov. Events moved so fast to allow the book to come out in Russian before the USSR fell, but since then what it says has been recognised to be sufficiently important that publishers in Sweden, Germany, Czechoslovakia and Venezuela have published translations under a variety of national titles.

In June 2007 at a workshop in Venezuela to launch the Spanish translation entitled *Hacia el socialismo del siglo XXI*, Paul was asked how the principles in the book could be applied to the process of establishing socialism in that country. This report tries to answer that question.

Clearly an economic model designed to answer the problems of a mature socialist industrial economy like the USSR can not be applied immediately to Venezuela. What it can do, is give people some idea where the process of socialist transformation may end up. It can warn them about avoiding some economic mistakes that were made in the USSR and Eastern Europe: for those who do not learn from history are doomed to repeat it.

When a society undergoes a transition to socialism there are decisions that have to be made, forks in the road that have to be chosen. If the wrong set of turnings are chosen, you can end up going in a circle. Starting off going towards socialism, you can end up on a path that eventually leads back to capitalism. We all know that this happened in several 20th century attempts to go towards socialism. The worst thing is that the implications of decisions are not immediately obvious at the time they are made. This means that, almost up until the last moment, people can think that they are still on the right course.

This is not the place to repeat what was said in the book *Towards a New Socialism*, but let us summarise the 3 key features of the mature socialism that it describes:

The economy is based on the deliberate and conscious application of the labour theory of value as developed by Adam Smith and Karl Marx. It is a model in which consumer goods are priced in terms of the hours and minutes of labour it took to make them, and in which each worker is paid labour credits for each hour worked. The consistent application of this principle eliminates economic exploitation.

Industry is publicly owned, run according to a plan and not for profit. State retail enterprises for example, work on a break even rather than profit making basis.

Decisions are taken democratically, both at a local and a national basis. This applies in particular to decisions about the level of taxation and state expenditure. Such democratic decision making is vital to prevent the replacement of private exploitation with exploitation by the state.

When we compare this with Venezuela today, we see that all three key features still need to be built. On some features the progress towards socialism has not yet started, on others it has started but the country has only taken a few steps along the path.

Let us look at these points one at a time.

## Still a money economy

The Venezuelan economy is still based on money. In his great book *Capital*, Karl Marx showed how money was at the root of the evils of capitalism. The essence of capitalism is to start out with a sum of money at the beginning of the year and end up with a larger sum at the end. Marx denoted this by  $M \rightarrow M'$ , where  $M$  might be \$1,000,000 for example and  $M'$  might be \$2,000,000.

Because capitalists have more money than working people, they can use this money to hire workers to work for wages. These wages are much much less than the value which workers create during the working week. Since the capitalist can sell the product for more value than they paid out in wages, the capitalists become richer and richer whilst workers stay as poor as ever.

This process is still going on in Venezuela. It is the root cause of the difference between rich and poor, between the oligarchy and the masses.

On top of this there is a secondary form of exploitation that allows capitalists to increase their money: lending money at interest. This process allows the money-lender to get richer year by year by doing absolutely nothing. This again, still occurs in Venezuela.

## Still an unplanned economy

In Venezuela, unlike for example the USSR, the supply of most goods and services is regulated by the market. Whilst this is not entirely a bad thing, since it does, to a limited extent allow supply to be adjusted to peoples wants, the drawback is that the provision of goods and services is systematically biased towards the wishes and desires of the rich. Venezuela currently lacks the mechanisms by which the structure of the economy as a whole can regulated by a concious social plan both to achieve development and to equitably meet the needs of all citizens.

Towards a New Socialism, assumed public ownership of the economy. Most of the economy in Venezuela, is still privately owned, although this may be changing now.

## Democratic revolution not yet complete

Whilst Venezuela has made great strides towards local participative democracy, it has yet to introduce participative democracy on key questions of national economic control. Issues relating to the raising of state revenue and the allocation of this revenue between major budget headings : defence, social care, infrastructure investment etc, are taken centrally rather than allowing the people as a whole to vote on them. If this is not addressed, it will in the long run, as the state comes to dominate more and more of the economy, be a serious danger. You could end up with a situation as occurred in the USSR where the state, and the bureaucracy of the state could be seen as being rather like a new exploiting class.

When we think of what happened in the USSR just before it collapsed, the desire of state bureaucrats to go from being like an exploiting class, to become outright capitalists like today's Russian oligarchs, must be counted as a key factor in the collapse.

## How to effect the transformation

The great economist Keynes remarked that practical political men, whether they be cautious or bold, fond themselves unconsciously repeating the ideas of long dead economists. Politicians who advance neo-liberalism, whether they know it or not, are repeating the ideas of the reactionary Austrian economists Ludwig von Mises and von Hayek. The policies that we suggest below counter those ideas by drawing on the insights of others particularly the Scottish philosopher Adam Smith, the German economist Karl Marx, the Polish socialist economist Oscar Lange and the Englishman Maynard Keynes.

As economists and social scientists we can only sketch out possible courses of action and some of their likely consequences of these actions. Decisions on what course to take are essentially political and political community, the leaders and the citizens of the country concerned are responsible for their own destiny. What intellectuals can do is to suggest possibilities which influence the terms of debate.

In the last section we looked at key objectives in the socialist transformation of an economy and the extent to which they have been met in Venezuelan experience. We will now shift the focus to specific policy measures, which we will present one by one and whilst explaining how each of these helps to achieve the broader objectives we have described.

## Currency stabilisation

There is, by world standards, a considerable degree of inflation in the Venezuelan economy. This is masked by administrative measures to stabilise prices of certain essentials of life but it is nonetheless real. Of itself, inflation is not necessarily against the interests of the poor and working classes, provided that wages keep up with prices. The people who are hit hardest by inflation are the rentier class whose holdings of money and interest bearing assets depreciate. Since these people are opponents of socialism anyway, a socialist government need not worry about any financial loss they suffer were it not for the other social effects of inflation.

Uncertainty about future prices can lead to a social psychology of instability leading to a loss of confidence in the government. We explain in an annexe how this sort of inflation played a role in the collapse of the USSR. For this reason alone, it will eventually be necessary for the Venezuelan government to take measures to regulate inflation.

However, if ones objectives are to establish a socialist economy based on the equivalent payment of labour, then currency reform can be a step towards this goal. What we suggest is that, following the introduction of the new strong Bolivar, the state place a legal obligation on the central bank to maintain a stable value of the currency in terms of labour<sup>1</sup>. A prototype for this could be the successful monetary policy of the British Labour Government after 1996. At that time the government placed monetary policy under a committee of expert economists ( The Monetary Policy Committee) rather than politicians and gave them a clear legal obligation to achieve a particular target rate of inflation. One might have expected this

policy to be severely deflationary, but it has actually been very successful, because committee are legally obliged to avoid both deflation and inflation in their policy.

Where our proposal differs from British policy is in the goal it sets – we advocate fixing the value of the Bolivar in terms of labour not in terms of the cost of living index. The reasons for this goal are twofold:

As labour productivity rises, a Bolivar fixed in terms of hours of labour, will be able to buy more each year, cheapening the cost of living.

Once the value of the Bolivar has been stabilised in terms of labour, then the labour value of Bolivar notes should be printed on them in hours and minutes. This step would be an act of revolutionary pedagogy. It would reveal clearly to the oppressed just how the existing system cheats them. Suppose a worker puts in a working week of 45 hours and gets back Bolivars and sees that the hours printed on them amount to only 15 hours, then she will become aware that she is being cheated out of 30 hours each week. This will act to raise the socialist consciousness of the people, and create favourable public opinion for other socialist measures.

Instead of just having a committee of economists charged with regulating the value of the Bolivar, the principle of participative democracy implies that the Value Policy Committee should be made up both of economists and delegates from the trades unions and consumers associations. The Value Policy Committee would have to commission surveys of how much work was being done in different industries, and how much monetary value added there was in these industries, in order to guide its stabilisation policy.

Reform of accounting and pressure for fair prices

All firms have currently to prepare money accounts, The government should make it a condition of their accounts being approved for auditing, that they also produce labour time accounts. and that they mark on all products that they sell their labour content.

Initially firms need not be legally obligated to sell their commodities at their true values. They could attempt to sell them for a price that is higher or lower than the true value. But since the consumer can now see when they are being overcharged, consumers will tend to avoid companies that sell goods at above their true value. This will put psychological and consumer pressure on companies that are overcharging. This too will be an act of socialist mass pedagogy to raise consciousness.

In the first few months, before all goods have their labour values printed on their price tags, firms will have to impute labour values to the goods they purchase using the printed exchange rate between Bolivars and labour hours. They will add to the labour value of their inputs, the number of hours of work that are performed by their employees to get a labour value for the final product.

We mentioned earlier the need to establish labour accounting in industry for pedagogic purposes. The government should also move towards having a dual system of national

accounts, labour accounts alongside money accounts because, at the level of national economic policy, there are many issues on which labour accounts would be more informative than money accounts. Money accounts hide the fact that what government economic policy really does is re-allocate society's labour. Money is the veil behind which real labour allocation occurs.

Enshrine the rights of labour in law

Scientific evidence shows that in the capitalist world the money value of goods is overwhelmingly determined by their labour contents. Studies find that for most economies the correlation between labour values and prices are 95% or above. So Adam Smith's scientific hypothesis that labour was the source of value has now been statistically verified.

This scientific fact should be incorporated in law.

The law should recognise that labour is the sole source of value and that in consequence, workers, or their Unions will have a claim in law against their employers if they are paid less than the full value of their labour.

If we consider the previous measures and the revolutionary pedagogy that would follow from them, it should be relatively easy to pass a referendum on such a law.

Following such a law being passed, there would be a huge wave of worker activism as workers and their unions sought to end the cheating and deceit to which they and their ancestors had been subjected. It would also bring about a very large increase in real wages, cementing support for the socialist government.

The employing class, on the other hand would see sharp fall in their unearned incomes. Employers who were active factory managers would of course still be legally entitled to be paid for the hours that they put in managing the firm, just like any other employee.

The cumulative effect of the three measures outlined so far would be to substantially abolish capitalist exploitation in the workplace – at least in the short term. There will be long term difficulties if other measures are not taken, and we shall examine these later.

## Eliminating other forms of exploitation

In addition to the exploitation of employees by employers, there are other forms of unearned incomes, the most economically important of which are interest and rent.

### Usury

Interest, the getting of money from money itself, was regarded for thousands of years as being sinful. Philosophers like Aristotle condemned it. Papal encyclicals banned it. Islamic

law still forbids it in Muslim countries. But in capitalist countries, such was the social power of the banks and other money lenders that this moral objections came to be forgotten.

In capitalist countries which were undergoing very rapid industrialisation, for instance, Japan in the 1950s or 1960s, lending money at interest did serve a necessary economic purpose, since it allowed peoples savings to be channelled, via the banks, to fund industrialisation. But once a country has industrialised, firms finance most of their investment from internal profits. Indeed they normally have more profit than they know how to invest. Instead of borrowing from the banks, industrial firms run a financial surplus, and they themselves lend to the banks. The banks now channel the financial surplus of firms into loans to the third world, or to Northern governments and consumers. Lending at interest loses the temporary progressive function that it had during industrialisation and reverts to being what morality and religion originally condemned : usury.

Socialism abolishes interest as a form of income. It has no class of rentiers – people who do no work but just live off the interest on their money. So it is clear that at some point, that a government seriously intent upon socialism has to pass a legislation banning the lending of money at interest. It could specify, for instance, that interest on debt could not be enforced in the civil courts. It could impose severe criminal penalties on those who used threats of harm to extort interest.

Before moving to a step such as this, a socialist government needs to put in place replacements for the economic functions still served by lending, and charging interest.

## Investment

It will still be necessary to fund new investments. This could be done by interest free loans from the state bank. But if this is not done with care, the resulting expansion of the money stock will lead to the type of suppressed inflation which occurred in the USSR.

Investment on credit is based on the illusion that you can push the cost of investment into the future. Whilst this can be true for an individual borrower, for society as a whole, today's investment has to be made using today's labour. We can not get future generations to travel back in time in order to do work for us. Socialist economies should thus rely mainly on tax revenue to fund investment.

## Regulating price levels

Capitalist central banks try to control inflation by adjusting the interest rate. If inflation is too high, they raise interest rates. The effect is to choke off investment, reduce demand, and so reduce inflationary pressures. If interest is banned, how is the price level to be regulated ? –

or, in the light of what we said earlier – how would the Venezuelan Value Policy Committee ensure that the value of the Bolivar in terms of labour was held steady?

An alternative control mechanism would be to adjust the term on which loans are made. The state bank could set maximum durations for loans. For example, if the Value Policy Committee thought the value of the currency was in danger of falling it could shorten the period for which loans could be had. If loan periods were reduced from 10 year to 5 years, then monthly repayments rise, just as happens with interest rate rises today.

Another means of regulating prices is tax policy. Paper money, like the Bolivar, is inherently worthless – just printed paper. It has value imputed to it, from the fact that the government will accept its own currency for tax debts. The fact that people need money to pay their taxes, forces them to value it. If governments tax less than they spend, the money stock will rise leading to inflation. The second way to regulate prices is thus to fine tune tax levels.

## Rent

Rent is another type of exploitation. Socialists regard it as immoral since the owner of land enriches himself, not by his own labour, but by the labour of others combined with the bounty of nature. Rent is however an inevitable phenomenon in a commodity producing society. If there is some product, be it crude oil, or corn, the efficiency whose production depends on the land being used, then rent incomes will arise.

Suppose the price of a ton of corn is \$200, then any land on which the corn's cost of production is less than \$200 will be worth cultivating. By the cost of production we mean the ultimate labour cost translated into money – including the cost of fertilizers. If land will yield corn at a cost of production of only \$50 – say because of its great fertility – then its owner can rent it out to farmers for \$150 and they can still break even selling corn at \$200. The same applies to oil production. If on the marginal oil field – say the tar sands of Athabasca in Canada, oil can be produced for \$50 a barrel, then a productive oilfield like the Venezuelan where costs are much lower, say \$15, will yield its owner (the state in this case) a rent of \$35 a barrel.

In a socialist economy all rent income should accrue to the state and be used for the good of the community in general. Socialist states have usually nationalised land, but have not always charged a rent for using the land. In the case of mineral extraction this made no difference, since this was done by state enterprises and rent would just have been a fictitious transfer between sections of the state. Failure to charge agricultural rents to collective farms will, however, accentuate differences in income between fertile and less fertile agricultural regions.

In the immediate situation in Venezuela, the nationalisation of land may not initially be politically opportune since it could drive the small farmers into alliance with large landowners. An alternative, which over the long term would produce a similar effect, would be to introduce a land tax on the rentable value of land. The threshold for the tax could be



set high enough to ensure that small farmers paid nothing or only a token amount, but for larger more fertile estates it could be set at a level that would confiscate the greater part of rent revenue. The effect on the landowners would be similar to that which would be achieved by nationalisation – depriving them of their unearned income and making it available for communal uses – but it is ideologically harder for them to mount a campaign to justify tax evasion than it is to mount one to justify resistance to expropriation.

## State finance and foreign currency

This brings us onto the general topic of state finance.

Socialist economies typically have a higher level of state expenditure than capitalist ones at a comparable level of economic development. It is essential that the state has an efficient revenue raising mechanism, with taxes that are easy to collect and difficult to avoid. Venezuela is unusual in having large oil exports, which helps somewhat, but the principle still remains.

Social democratic states like Sweden relied mainly on income taxes along with an efficient civil service. East European socialist states like the USSR relied upon turnover taxes on industry and on profits earned by state firms. Because of the importance of oil revenue to the Venezuelan state, it currently leans more towards the Soviet model.

Which of these models of tax revenue should be used is one of the major strategic issues that has to be faced by Venezuela as it moves towards a socialist economy.

In their book *Towards a New Socialism*, Cottrell and Cockshott argue that the Soviet model of taxation had several drawbacks, which, in the long run, contributed the final collapse of the Soviet socialist economy.

The use of indirect taxation, such as turnover or value added taxes<sup>2</sup>, and a-fortiori a reliance on profit income, puts the state in the position of being a collective capitalist vis a vis the workers.

The use of indirect taxation, has also traditionally been opposed by socialists as these are regressive rather than progressive forms of taxation<sup>3</sup>.

It resulted in a distorted price structure that systematically undervalued labour to the detriment of economic efficiency.

Reliance on the profit of state industry is a hidden form of revenue, which is not easily amenable to democratic control.

In the case of Venezuela there is the additional complicating factor that profits from oil revenue are dependent on the very volatile world market price of oil. This can cause unexpected fluctuations in state revenue. The recent sharp rise in oil prices has been very

beneficial to the government, but it must be remembered that prices can go down as well as up.

It is said Venezuelan government has plenty of money thanks to oil, but it is important to understand in what sense it has plenty of money. What it has is plenty of dollars. These are fine if the government wants to directly purchase manufactured commodities made in other countries. Dollars are also fine for giving aid to other countries. But dollars are no use for paying the wages of government employees or when the government wants to buy domestically produced goods, for these the government needs Bolivars not dollars.

The government can get Bolivars in several ways:

It can raise them from taxes.

It can issue bonds denoted in Bolivars and sell these on the money markets.

It could purchase Bolivars on the open market using its dollar reserves.

It can get the state bank to extend its credit.

The fact that the black market rate for the dollar is well above the official rate, and that there is significant inflation indicates that the state has been relying excessively on the last of these methods of finance.

It must be realised that dollars can not be used to meet a shortfall of tax revenue in Bolivars so long as foreign exchange controls are retained. Dollar revenue can only be freely converted to revenue in Bolivars by the state buying Bolivars on the open market. This in turn implies that Venezuelan citizens would have to be free to sell dollars in the open market.

It is understandable that the government maintains exchange controls to prevent the upper classes expatriating their Bolivar assets, and in the process using up the government's foreign exchange reserves, so there is obviously a dilemma here. This dilemma indicates that the government has not yet felt itself to be strong enough to face down the economic power of the oligarchy. We could suggest two possible policies under these circumstances:

Increases in higher rate income taxes and abolition of tax exemptions sufficient to fund government domestic expenditure from domestic tax revenues.

More radically, a sharp reduction in the amount of privately held Bolivars could be brought in along with the projected currency reform. If there was a limit to the amount that any one person could change from old Bolivars to new Bolivars – for instance this might be set at a certain number of months of average wages – then the money capital of the rich would no longer be sufficient for them to threaten the state's foreign exchange reserves following the

removal of exchange controls. It would also incidentally greatly reduce the social power of the capitalist class.

Each of these policies has obvious political risks involved, which have to be weighed against the future benefits of a more stable system of public finance.

## Foreseeable consequences

The policies described above would go a long way to transforming the economy into a new socialist one. However, since they undermine what are important functional components of capitalism there would be consequences if alternative mechanisms were not put into place.

Ending the production of surplus value by paying workers the full value they create would make employment unprofitable. There is a danger under these circumstances that capitalists would find it more profitable to leave their money in the bank and earn interest on it than use it to employ workers.

It would thus be important that the payment of interest was abolished prior to introducing the right to the full value of labour.

It would also be necessary to introduce the right for employees to be able to vote for their firm to be co-managed with a co-management committee having a clear majority of employees on it, in order to prevent owners' asset stripping and closing the now unprofitable firm.

## Appendix A Economic Factors in the failure of Soviet Socialism

Paul Cockshott was asked by Gen. Jose Angel to elaborate on remarks made about the economic causes of Soviet Collapse. This is a very brief personal perspective on what is obviously a huge and very controversial subject.

The collapse of the Soviet and later the Russian economy under Gorbachov and then Yeltsin was an economic disaster that was otherwise unprecedented in time of peace. The world's second super-power was reduced to the status of a minor bankrupt economy with a huge decline in industrial production and in living standards. Nothing brings out the scale of the catastrophe than the demographic data which show a huge rise in the mortality rate brought

about by poverty, hunger, homelessness and the alcoholism that these brought in their wake.

**Excess deaths consequent the introduction of capitalism in Russia amount to some 12 million over 20 years. Data from successive UN Demographic Yearbooks.<sup>1</sup>**

| Year | Thousand deaths | Excess relative to 1986 |
|------|-----------------|-------------------------|
| 1986 | 1498            | 0                       |
| 1987 | 1531            | 33                      |
| 1988 | 1569            | 71                      |
| 1989 | 1583            | 85                      |
| 1990 | 1656            | 158                     |
| 1991 | 1690            | 192                     |
| 1992 | 1807            | 309                     |
| 1993 | 2129            | 631                     |
| 1994 | 2301            | 803                     |
| 1995 | 2203            | 705                     |
| 1996 | 2082            | 584                     |
| 1997 | 2105            | 607                     |
| 1998 | 1988            | 490                     |
| 1999 | 2144            | 646                     |
| 2000 | 2225            | 727                     |
| 2001 | 2251            | 753                     |
| 2002 | 2332            | 834                     |
| 2003 | 2365            | 867                     |
| 2004 | 2295            | 797                     |
| 2005 | 2303            | 805                     |

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<sup>1</sup> ( The article originally had a graph showing the following: Soviet Economic collapse let to huge increase in mortality with 5.7 million Excess Russian deaths 1991-2001. Vertical axis 1,000 deaths per annum. Given the availability of more data I have replaced it with this table)

|       |       |       |
|-------|-------|-------|
| 2006  | 2166  | 668   |
| 2007  | 2080  | 582   |
| 2008  | 2075  | 577   |
| 2009  | 2010  | 512   |
| total | 48388 | 12436 |

In determining what caused this one has to look at long term, medium term and short term factors which led to relative stagnation, crisis and then collapse. The long term factors were structural problems in the Soviet economy and required reforms to address them. The actual policies introduced by the Gorbachov and Yeltsin governments, far from dealing with these problems actually made the situation catastrophically worse.

## Long Term

During the period from 1930 to 1970, and excluding the war years, the USSR experienced very rapid economic growth. There is considerable dispute about just how fast the economy grew, but it is generally agreed to have grown significantly faster than the USA between 1928 and 1975, with the growth rate slowing down to the US level after that<sup>4</sup>. This growth took it from a peasant country whose level of development had been comparable to India in 1922, to become the worlds second industrial and technological and military power by the mid 1960s.

Observers have given a number of reasons for this relative slowdown in growth in the latter period.

It is easier for an economy to grow rapidly during the initial phase of industrialisation when labour is being switched from agriculture to industry. Afterwards growth has to rely upon improvements in labour productivity in an already industrialised economy, which are typically less than the difference in productivity between agriculture and industry.

A relatively large portion of Soviet industrial output was devoted to defence, particularly in the latter stages of the Cold War, when they were in competition with Regan's 'Star Wars' programmes. The skilled manpower used up for defence restricted the number of scientists and engineers who could be allocated to inventing new and more productive industrial equipment.

The USA and other capitalist countries imposed embargoes on the supply of advanced technological equipment to the USSR. This meant that the USSR had to rely to an unusually

high degree on domestic designs of equipment. In the west there were no comparable barriers to the export of technology so that the industrial development of the western capitalist countries was synergistic.

Labour was probably not used as efficiently in Soviet industry as it was in the USA or West Germany. In one sense, of course the USSR used labour very effectively, it had no unemployment and the proportion of women in full time employment was higher than in any other country. But a developed industrial economy has to be able transfer labour to where it can be most efficiently used. Under capitalism this is achieved by the existence of a reserve of unemployment, which, whilst it is inefficient at a macro-economic level, does allow rapid expansion of new industries.

The Soviet enterprise tended to hoard workers, keeping people on its books just in case they were needed to meet future demands from the planning authorities. This was made possible both by the relatively low level of money wages, and because the state bank readily extended credit to cover such costs. The low level of money wages was in turn a consequence of the way the state raised its revenue from the profits of state enterprises rather than from income taxes.

Although Soviet industrial growth in the 80s slowed down to US levels, this by itself was not a disaster, after all the USA had experienced this sort of growth rate (2.5% a year) for decades without crisis. Indeed whilst, working class incomes in the USA actually stagnated over the 80s, in the USSR they continued to rise. The difference was in the position of the intelligentsia and the managerial strata in the two countries. In the USA income differentials became progressively greater, so that the rise in national income nearly all went to the top 10% of the population. In the USSR income differentials were relatively narrow, and whilst all groups continued to experience a rise in incomes, this was much smaller than had been the case in the 1950s and 1960's. This 2.5% growth was experienced by some of the Soviet intelligentsia as intolerable stagnation – perhaps because they compared themselves with managers and professionals in the USA or Germany. A perception thus took root among this class that the socialist system was failing when compared to the USA.

Again this would not have been critical to the future survival of the system were it not for the fact that these strata were disproportionately influential within the USSR. Although the ruling Communist Party was notionally a workers party, a disproportionately high proportion of its members were drawn from the most skilled technical and professional employees, manual workers were proportionately under represented.

The slowdown in Soviet growth was in large measure the inevitable result of economic maturity, a movement towards the rate of growth typical of mature industrial countries. A modest programme of measures to improve the efficiency of economic management would probably have produced some recovery in the growth rate, but it would have been unrealistic to expect the rapid growth of the 50s and 60s to return. What the USSR got however, was not a modest programme of reform, but a radical demolition job on its basic economic structures. This demolition job was motivated by neo-liberal ideology. Neo-liberal economists, both with the USSR and visiting from the USA promised that once the planning

system was removed and once enterprises were left free to compete in the market, then economic efficiency would be radically improved.

## Medium Term

The medium term causes of Soviet economic collapse lay in the policies that the Gorbachov government embarked on in its attempts to improve the economy. The combined effect of these policies was to bankrupt the state and debase the currency.

One has to realise that the financial basis of the Soviet state lay mainly in the taxes that it levied on turnover by enterprises and on sales taxes.

In an effort to stamp out the heavy drinking which led to absenteeism from work, and to poor health, the Gorbachov government banned alcohol. This and the general tightening up of work discipline, led, in the first couple of years of his government to some improvement in economic growth. It had however, unforeseen side effects. Since sales of vodka could no longer take place in government shops, a black market of illegally distilled vodka sprang up, controlled by the criminal underworld. The criminal class who gained money and strength from this later turned out to be most dangerous enemy.

Whilst money from the illegal drinks trade went into the hands of criminals, the state lost a significant source of tax revenue, which, because it was not made up by other taxes, touched off an inflationary process.

Were the loss of the taxes on drinks the only problem for state finance, it could have been solved by raising the prices of some other commodities to compensate. But the situation was made worse when, influenced by the arguments of neo-liberal economists, Gorbachov allowed enterprises to keep a large part of the turnover tax revenue that they owed the state. The neo-liberals argued that if managers were allowed to keep this revenue, they would make more efficient use of it than the government.

What actually ensued was a catastrophic revenue crisis for the state, who were forced to rely on the issue of credit by the central bank to finance their current expenditure. The expansion of the money stock led to rapid inflation and the erosion of public confidence in the economy. Meanwhile, the additional unaudited funds in the hands of enterprise managers opened up huge opportunities for corruption. The Gorbachov government had recently legalised worker co-operatives, allowing them to trade independently. This legal form was then used by a new stratum of corrupt officials, gangsters and petty business men to launder corruptly obtained funds.

## Immediate

The Soviet economy had gone through the stages of slowdown, mismanaged crisis and now went into a phase of catastrophic collapse, quite unprecedented in peacetime.

Following a failed coup by sections of the armed forces and security services, Yeltsin, instead of helping restore the constitutional government of President Gorbachov, seized power for himself. Acting on the instructions of US advisers he introduced a shock programme to convert the economy from socialism to capitalism in 100 days.

In the old USSR there was no capitalist class. In the west governments could privatise individual firms by selling them off on the stockmarket where the shares would be quickly snapped up by the upper classes, or in the case of Thatcher's privatisation, by sections of the middle class. But in the USSR things were very different. There was no class of individuals wealthy enough to buy up state companies by legal means. Also the scale of the privatisation was so vast, that even in a market economy, the savings of the population would have been insufficient to buy up the entire industry of the nation. Logic alone would predict that the only way that industry could pass into private hands was through corruption and gangsterism. This is exactly what happened, a handful of Mafia connected oligarchs ended up owning most of the economy.

Neo liberal theory held that once enterprises were free from the state, the 'magic of the market' would ensure that they would interact productively and efficiently for the public good. But this vision of the economy greatly overstated the role of markets. Even in so called market economies, markets of the sort described in economics textbooks are the exception – restricted to specialist areas like the world oil and currency markets. The main industrial structure of an economy depends on a complex interlinked system of regular producer/consumer relationships in which the same suppliers make regular deliveries to the same customers week in week out.

In the USSR this interlinked system stretched across two continents, and drew into its network other economies : East Europe, Cuba, North Vietnam. Enterprises depended on regular state orders, the contents of which might be dispatched to other enterprises thousands of miles away. Whole towns and communities across the wilds of Siberia relied on these regular orders for their economic survival. Once the state was too bankrupt to continue making these orders, once it could no longer afford to pay wages, and once the planning network which had coordinated these orders was removed, what occurred was not the spontaneous self organisation of the economy promised by neo-liberal theory, but a domino process of collapse.

Without any orders, factories engaged in primary industries closed down. Without deliveries of components and supplies secondary industries could no longer continue production, so they too closed. In a rapid and destructive cascade, industry after industry closed down. The



process was made far worse by the way the unitary USSR split into a dozen different countries all with their own separate economies. The industrial system had been designed to work as an integrated whole, split up by national barriers it lay in ruins.

The following figures show how far the economy had regressed. These figures show how little recovery there had been, even after 13 years of operation of the free market.

Output of Selected Branches of Industry in Russia in 2003 Compared to 1990 (1990 = 100)

|                              |    |
|------------------------------|----|
| Total Industry               | 66 |
| Electric power               | 77 |
| Gas                          | 97 |
| Oil extraction               | 94 |
| Oil refining                 | 70 |
| Ferrous metallurgy           | 79 |
| Non-ferrous metallurgy       | 80 |
| Chemicals and petrochemicals | 67 |
| Machine building             | 54 |
| Wood and paper               | 48 |
| Building materials           | 42 |
| Light industry               | 15 |
| Food                         | 67 |

Source: Goskomstat, 2004, Table 14.3.

If the economy had continued to grow even at the modest rate of the later Brezhnev years (say 2.5%) then industrial production would, on this scale have stood at 140% of 1990 levels. The net effect of 13 years of capitalism was to leave Russia with half the industrial capacity that could have been expected even from the poorest performing years of the socialist economy.

## Key Economic Lessons

I am ignoring for now, the political lessons, which we elaborated on at length in our book *Hacia el Socialismo del siglo XXI*,

It is vital that the state maintain a strong, honest and efficient system of tax revenues.

It is important that when attempting to rapidly change social relations that one does not dismantle the old economic mechanisms faster than new ones can be put in their place.

One should never overestimate the ability of markets to organise an economy.

One should beware the risk that a corrupt managerial strata attempts to divert state property into their own private domain.

Allowing the existence of criminal black markets is dangerous in the long run.

Until such time as money can be phased out and replaced by direct labour accounting, it is dangerous to allow prolonged inflation to take hold.

1This should be contrasted to the current policy of attempting to fix the value of the Bolivar in terms of dollars.

2The German term for such taxes Mehrwertsteuer translates incidentally as 'surplus value tax', encapsulating very well what its economic function is from the standpoint of marxian political economy.

3A progressive tax is one which bears most heavily on people with higher incomes.

4For more details see the attached appendix which is reproduced from the web-site 21st Century Socialism.