



Command *Versus* ‘Shadow’: The Conflicted Soul of the Soviet Economy¹

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This essay surveys the seminal contribution of Gregory Grossman to comparative economics contained in his analysis of the Soviet economic system. The paper focusses on his theory of the ‘command economy’, its nature and logic, and its inherent weaknesses, which spawned the ‘second economy’, waves of futile ‘reforms’, and sowed the seeds of that system’s collapse.

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INTRODUCTION

This essay represents an appreciation of the work of Gregory Grossman on the Soviet economic system. Greg’s approach was and is ‘fundamentalist’; he looks to the essential nature, the internal logic of the economic system, to its defining characteristics and fundamental core, in order to understand how and why it functions as it does. In doing so, he has developed fundamental insights into the strengths and weaknesses, the problems and prospects of the Soviet, indeed ‘Soviet-type’, economic system. From the beginning, his work has highlighted factors that, while not at the focus of Sovietological interest at the time, proved critical to the growing problems and eventual crisis that

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brought about the demise of the system. These derived from an intuitive feel for, and a truly profound understanding of, the essence of the Soviet economic system, which has informed and inspired the work of many in the succeeding generations of 'Sovietological' economists, myself included.

In focussing on 'fundamentals', Greg Grossman began his career studying the heart, the engine, of the Soviet system – the industrial core of the economy.² Here, at the centre of the priorities of the system's 'directors', the nature and the essence of the economic system was most clearly revealed, and its strengths and weaknesses most clearly displayed. These were distilled into his analysis of the ideal type, the 'command economy' (Grossman, 1963), and its approximate implementation in the Soviet Union. Driven by the urgency of encirclement, backwardness and 'historical necessity', and broadly informed by a socialistic, messianic, antimarket ideology, the Soviet leadership struggled to build a powerful, modern industrial economy on a profoundly backward base through the extraordinary efforts and sacrifices of the unenlightened masses led by a dedicated, committed and fully 'enlightened' elite.³ This could be accomplished only through all-encompassing social control, brooking no questioning or opposition. It, however, placed an overwhelming burden on the elite and their agents, and cracks had to appear in the system of command and control. Even at the highest priority industrial core of the system, not all could be commanded and controlled properly, and so alternative, illegitimate activities and mechanisms appeared – a 'second economy' filling in and supplementing the command economy in ways both supportive of its essential functioning and stability and subversive of its ultimate viability. And running through this analysis, *krasnoi nit'yu*, lies Grossman's analysis of the anomalous role of money in the command economy, both unavoidable and subversive, facilitating and undermining, and feeding that cancer of central planning and command implementation – the 'second/shadow economy'.

Thus at its very core, the Soviet economic system was built on a fundamental contradiction. Its spirit derived from the command principle, the need for those who 'truly know' to have absolute discretion and control to make sure that what is needed, what is 'right', is done as it should be. But this spirit inevitably struggled with a recalcitrant body of intractable interconnectedness and imperfect human material whose 'imperfections' surfaced in

² His dissertation defended in 1953 and its subsequent NBER book (Grossman, 1960) and AER paper (Grossman, 1959) studied industrial production statistics and the pricing of producers' goods.

³ This is a theme brought up in Grossman's Slavic Review survey of the Soviet economy (1962), and more fully developed in his 'Economics of virtuous haste' (1983a).



a secondary 'shadow economy' symbiotically imbedded into the first, official, 'command economy.'

As Greg Grossman noted at the beginning of his analysis in 'The structure and organization of the Soviet economy' (1962), 'Economic systems are best known by the institutions they keep'. The formal structure of those institutions is of course well known to this audience.⁴ What I want to focus on here is the particular light cast on those institutions by Greg Grossman's approach. In particular, I want to highlight the systemic logic of two key faces of the Soviet economic system – the state owned, centrally planned and administered command economy, and the privately driven, often complementary second economy – with an emphasis on a key link between them, the social contrivance of money.

THE COMMAND ECONOMY

The economic system of the Soviet Union can be described and analysed from many perspectives. However, I would argue that there is one that truly goes to the roots of the economic phenomenon represented by the Soviet Union: the 'Command Economy'. As Grossman stated in a conference volume introduction:

'Significant as the elements of "socialism" and "planning" are, functionally they are no more important than the fact that in a Soviet-type economy production and investment are guided chiefly not by market mechanisms but by means of commands (directives, targets) emanating from the center'. (1960, p. 3)

This perspective captures the essence of the economic system that was developed, as much inadvertently as by intention, functioned for over four decades, and finally died in the Soviet Union.

Grossman's (1963) understanding of the 'command economy', most fully explicated in his seminal 'Notes ...', first appeared in print in the book and AER paper from his dissertation, where it described his analysis of Soviet industrial statistics and the industrial price system. The concept has grown from an idiosyncrasy, eliciting a rather bemused comment by his series editor, G Warren Nutter on 'what Grossman refers to as a "command economy"', (Grossman, 1960a, p. xi) to the conventional wisdom, a basic paradigm for understanding the Soviet economic system. Indeed, it was even accepted as

⁴ There are a number of good basic discussions, including Grossman (1967, Chapter 6), the various editions of Gregory and Stuart (1981–2001), Nove (1977), and Bornstein (1985).



fundamental by the last General Secretary of the Communist Party of the Soviet Union, Mikhail Sergeevich Gorbachev.⁵

The 'prime imperative' – balance

As Grossman argued, a 'complex social economy' must, for its very survival, maintain at least a 'tolerable' micro-balance,

'... that minimal degree of coordination of the activities of the separate units (firms) which assures a tolerably good correspondence between the supply of individual producer and consumer goods and the effective demand for them'. (1963, p. 101)

In such an economy, appropriate balance can be achieved through decentralised, market-based (monetised, price-mediated) interaction of autonomous units, or by virtue of explicit specific coordinating directives (commands, targets) from some higher authorities. While the former is characteristic of a market economic system, the latter is defining of a 'command economy'. In the latter, operational-level units (eg firms) must merely 'implement' commands; they become 'executants' of plans and directives from above, plans that must ensure balance through the coherence and consistence of the instructions they give. Thus, the command mechanism requires relative centralisation and severe restriction on the autonomy of subordinate operational units.⁶ It derives from the overwhelming priority of social goals, and requires the destruction of autonomous social and economic powers and the enforcement of strict obedience to directives.

As Grossman notes, 'command economies do not arise spontaneously; they are imposed' (1963, p. 106). They arise from a 'millennialist' elite, with unique access to 'the truth', achieving the political power to impose its will absolutely, while facing a crisis of overwhelming proportions. The perception of a life-threatening crisis, driving the need for massive mobilisation of all social resources and rendering any hesitation or dissent, any questioning of ways and means, potentially disastrous, naturally leads, pushed by the 'logic of events', to the usurpation of all power of discretion, all legitimate

⁵ At both the January and June Plenums of the CPSU in 1987 at which *Ekonomicheskaya Perestroika* was announced and then promulgated, Gorbachev explicitly framed his programme in terms of a critique of the 'command administrative' system in terms echoing the analysis of the 'command economy' begun by Greg Grossman.

⁶ Of course, Grossman is more nuanced and cautious in making comparisons, due both to his lengthier discussion and to the rather 'statist' Keynesian intellectual atmosphere in the economic profession of the time. Indeed, as a look over the textbooks of the time readily reveals, far greater centralisation and national economic planning, 'rational' social control, was the expected wave of the future for market economies.



authority, by the 'knowing' elite, which then becomes responsible for all that is done or not done in the society and the economy. The crisis may be artificial or real ('hostile encirclement?'), externally or internally imposed (the need to industrialise, to 'catch up?'), but it requires moving resources rapidly and massively, forcing new activities and interactions in the face of severe scarcities, of shortage of competent personnel, of massive uncertainties, and of strongly held, stark priorities. Indeed, Grossman has cogently argued that

'the actual Soviet pattern of development, including its noneconomic aspects, ... was a consistent product of the logic of haste under conditions of relative backwardness and (to put it mildly) with a highly authoritarian political milieu. The logic of haste is above all a powerful centralizing force in social affairs'. (Grossman, 1962, p. 206)⁷

A sense of overwhelming urgency and need for haste drove the elite of the Soviet Union in the 1930s to test and establish, through trial and error over several decades, the institutional structure of a 'command economy', albeit *less than absolute* from both necessity and choice (eg the 'lessons' of 'War Communism').⁸

The logical consequences of command

The consequences of the command mechanism derive largely from the above-noted prime imperative of a social economy – 'balance'. The task of elemental coordination, of micro-balance, so effortlessly accomplished by any functioning (however poorly) market system is overwhelmingly large, and grows rapidly with industrialisation and economic development, both of which lead to exponential growth of the complexity of the economy. With centralisation and the abandonment of markets comes the need for massive, detailed coordinative planning, for 'making ends meet' in the expanding web of interconnections that must be maintained for economic life to continue.

'(I)ts chief daily task and chore is the maintenance of balance with regard to each economic good over the short term. It is this task that in fact consumes the largest part of the so-called planning in the command economy, ... Coordinative planning as it is conducted in the Soviet Union does little by way of consciously steering the economy's development or finding efficient

⁷ This theme is further developed in Grossman's (1983a) essay, 'The economics of virtuous haste: A view of Soviet industrialization and institutions'.

⁸ In a recent paper, Grossman (2000) shows how similar considerations drove the development of an earlier, if less intensive, command economy in 19th century America, the Mormon Zion in the Utah territory of the United States, run by the 'saints' of the Church of Jesus Christ of the Latter-Day Saints under the leadership of the 'prophet, seer and revelator' at the head of the Church.



patterns of resource allocation. Its overwhelming concern is simply to equate both sides of each 'material balance' by whatever procedure seems to be most expeditious'. (Grossman, 1963, p. 108)

This problem is aggravated by the logic of haste that drove imposition of the command economy – 'the pressing contrast between urgent political goals and available resources'. The necessary attention to the growing problem of balance further militates against any effort to consider developmental objectives or efficiency in making allocative decisions, so that 'a bias against allocative efficiency' is built into the command economy *via* the underlying logic of haste. Coupled with limited ability to gather, filter, process, and communicate information, and to compute solutions to planning problems ('bounded rationality'), this creates a fundamental and growing inability to acceptably solve the underlying coordination problem, further undermines any consideration of efficiency, and hence generates a well-known litany of the 'problems' of the Soviet economy:

- overly ambitious (unfulfillable) targets;
- a dearth of *usable* stocks, despite massive and growing inventory holdings;
- systematic misallocation of available stocks;
- repeated production disruption and breakdown due to input problems;
- chronic shortages and the Soviet 'sellers' market';
- subsequent planning and coordination mistakes;
- various reactions of operational agents to these problems, such as hoarding of supplies, further aggravating them.

The logic of 'command' has a number of further necessary consequences characterising the institutions of the Soviet economic system. Planning in a command economy must be largely in *physical terms* due to the crucial importance of balance. The bottom line of the planning process must be the available physical units of required inputs, in appropriate assortment, quantity and timing, necessitating physical targets for production and input utilisation. Thus, tens of thousands of materials and equipment balances must be drawn up and coordinated for each plan period, and then broken down and allocated in directives to specific implementors. And to be directly usable, these must be in physical, or crypto-physical (constant price) units that directly relate to the production processes being coordinated. Using value units requires flexible and changing, marginal scarcity-based prices for valuation, and giving significant autonomy to subordinate units who inevitably then will make the trade-offs in assortment, quantity and timing within planned constraints on values (ie 'budgets'). As we will argue below, following Grossman, such valuations pose a fundamental challenge to the command economy.



Planning in physical terms, however, leads to 'enormous waste and inefficiency, to production for waste as much as for use' (Grossman, 1963, p. 110). Grossman highlights three, among many, fundamental sources of this elemental waste: '*grossness*', '*aggregation*', and '*unit of measure*'.⁹ The need for these arises in the overwhelming complexity of the task of planning for, and directing the operation of, a complex social economy and the limited information gathering, processing, and dissemination capabilities of any economic agent or agency. Thus each of these is essential for the feasibility of directive central planning of the command mechanism, yet each loses or destroys essential information for the 'proper' (in the eyes of the system directors) implementation of plans, and opens space for the creative interpretation of instructions/commands, and hence for 'sub-optimization' by implementing units with interests not perfectly aligned with those of the centre.¹⁰

While the command mechanism logically requires unauthorised initiative to be forbidden, and strictly punished when exercised, the size of the task it faces inevitably opens the opportunity, and indeed often the need, for such unauthorised initiative. All commands inevitably contain some aggregation (over time, product space, or location), and all commands require a unit of measurement in order to permit accountability, reward, and/or punishment. These characteristics imply that all recipients of commands will have some discretion that is outside the ability of higher authorities to control.¹¹ Thus, the physical quantity planning required by the command economy to maintain minimal functional 'balance' contains its own antithesis, unleashing forces that undermine the consistency of the plan and the coherence and balancedness of its realisation. This fundamental contradiction lies behind most of the critical problems of the command economy, and the myriad efforts to resolve them within the framework of the command mechanism, that comprise the endless waves of reform following victory in, and recovery from, the Great Fatherland War (1941–1945).

⁹The emphasis on *gross output* leads to 'input intensiveness', waste, and ignoring cost considerations. *Aggregation* leads to persistent sub-category imbalance in assortment, quality, type, timing, etc, while *units of measurement* determine sub-optimization objectives, distorting implementation decisions, particularly when they are, for Material Balance reasons, input oriented. (1963, pp. 110–112)

¹⁰The wonderful stories from the Soviet press that fill the masterful study by Nove (1977) beautifully illustrate this.

¹¹This is characteristic of any centralised hierarchical structure and lies at the root of the problems analysed in the 'principal-agent' framework. It is addressed in Grossman (1963, p. 107ff) as the problem of finding 'the optimal degree of centralisation'.



Another consequence of the 'logic of command' is the need to restrict autonomy and the capability of economic units to pursue any other than 'planned' (commanded) purposes. Economic agents must not have the capability to autonomously acquire and deploy resources for any purposes outside the plan. Comprehensive material balance planning and centralised materials and equipment allocation provide a necessary component, but one that is insufficient unless resources, including human, are denied the capability of autonomous movement and application. Severe restrictions on labour mobility, albeit not as severe as under Stalin, are required, as are comprehensive restrictions on the use of any 'generalized command over goods and services', that is, money, that might be used to alter their pattern of allocation and use in the economy.

Thus money must be deprived of 'moneyness', and prices must be kept 'passive' – mere accounting and measurement units. Monetary prices do not, and indeed should not, reflect to a substantial degree social goals and priorities; they merely reveal and measure the flow of commanded activity. 'Money ... as a medium of exchange and store of value becomes necessary only with the introduction of some decision-making autonomy' (Grossman, 1963, p. 115). According to the logic of the command economy, the availability of money and the prices at which commodities and products are available should have no essential impact on the allocation of goods and services or on the nature and direction of economic/industrial development; all real activity is preordained in the plan and its subsequent implementing commands. This partial demonetisation's 'functional purpose was to constrict the ... range of choice in the face of the state's demands' (Grossman, 1966, p. 232).

Finally, an absolutely essential, indeed defining, institution of the command economy is the rationing of resources and producers' goods. This is where the market is most fully and directly replaced, and where the central authorities have the ability to most directly influence and control the behaviour of subordinate operational units. It implements the centralised mobilisation of resources to priorities, the most direct response to crises and challenges. And it most directly denies subordinates the capability to produce, to develop, in ways outside those authorised in the plan. Thus Grossman presciently argues that

'co-existence between the command principle and the market mechanism would seem to be unstable and ephemeral. Since the two are apt to be continuously in conflict, the command principle, aided by the club of materials rationing, will inevitably push back and eventually eliminate the market mechanism – unless a full fledged market economy be deliberately adopted'. (1963, p. 119)



Thus, the nature of the command system makes it fundamentally incompatible with real markets, although apparently market institutions were allowed to function within the non-state sectors, and as an interface with the state and its economic sectors.

The critical challenges to command

As Grossman notes in his seminal article:

'The chief persistent systemic problem of a command economy is the finding of the optimal degree of centralization (or decentralization) under given conditions and with reference to given social goals'. (1963, p. 107)

A fundamental dilemma is posed by the fact that full centralisation poses an insoluble problem, while decentralisation abandons the ability to direct, to control development, and to ensure the pursuit of social goals and priorities. Looked at through the prism of relative advantages, decentralisation shortens 'lines of communication', increasing flexibility, adaptation, and responsiveness to a changing environment through local initiative and innovation, and vastly simplifying the decision problem of economic agents. However, it does so at the cost of loss of the 'advantages of centralisation', including enforcement of regime values, capability for large-scale resource mobilisation, concentration of scarce talent in central decision-making organs, and the maintenance of macro-balance. In particular, decentralisation compromises the ability of the centre to directly manage the development and structure of the economy, and to force the achievement of critical priorities regardless of cost. Furthermore, decentralisation requires the introduction of the alternative coordination mechanism to insure tolerable micro-balance – the market – as decentralization undercuts the ability to coordinate, to balance from above. Thus to prevent disaster, a more active money and economically flexible market prices must be allowed to function.

Decentralization versus priority

Thus the impossibility of planning and commanding the performance of all economic agents in full operational detail forces some decentralisation. This creates a

'... chronic threat to balance (which) is thus a continuous argument for (re)centralization of planning and materials allocation. For this reason the Soviet economy is constantly subject to "creeping re-centralization" on this account. For the same reason, a partial decentralization of planning and management in a command economy may do more harm than good; it may impair balance without yielding sufficient benefit ... A virtually complete decentralization, in the sense of a virtually full devolution of the major



*production decisions to the firm level, would be disastrous from the standpoint of balance, unless the price structure were properly altered to provide proper signals to firms and suitable behavioral rules were prescribed, ie unless a market mechanism were introduced.*¹² (Grossman, 1963, p. 114)

Thus the theory predicts a 'treadmill of reforms' (in Schroeder's (1979) felicitous phrase), an array of countervailing strengthening of the oversight and control organs (in particular, the Party; see Grossman, 1983b), and enhancements of their role in the economy accompanying moves toward decentralisation in the state sector. It also explains the Soviet institutional arrangement of inter-firm contracts as a decentralised implementation device. These are required to specify details of interaction within planned categories, and establish observable, and hence legally enforceable, commitments to planned implementation, constraining the autonomy necessarily granted through the minimal decentralisation. And it explains the logic of the continuing restraints on the use of money and the continuing efforts at effective price control to keep the autonomy of agents restricted to the minimum necessary for the continued functioning of the 'less-than-absolute' (Grossman's phrase) command economy.

Money and prices had to have a role in determining terms of alternate resource uses only *within planned/commanded categories*, and money acquired a role of limiting total claims to resources in areas/detail beyond the reach of plan directives. This requires 'businesslike management' within the firm – *khozraschet*, which is a 'set of behavioral rules that is supposed to govern the actions of Soviet managers beyond their primary responsibility, the fulfillment of output targets'. It pushes the firm toward 'technical efficiency' and limitation of

'claims on society's resources for productive use ... khozraschet is a system that is well devised to control the behavior of managers in a command economy where a certain amount of devolution of power to them is inevitable, and where, further, managers' goals and values do not necessarily coincide with the official ones'. (Grossman, 1963, p. 117)

Another critical challenge noted by Grossman is the 'conflict between the will, purposes, incentives and priorities of the higher authorities and those at lower levels, particularly of the firms and their managements' (1963, p. 118). Even the best motivated managers, following all official rules and incentives, will sometimes fail to replicate the decisions that would have been made by their superiors, had they been in a position to make them. This problem is

¹² Herein lies a prescient analysis of the failure of *Perestroika*, giving insight into much of the pain of the 'transition' in the 1990s.



aggravated by the inevitable ambiguity, incompleteness and inconsistency of those rules, incentives and the information available on the spot. Only binding physical constraints and observable outcomes can be systematically enforced, making 'centralized materials allocation the most powerful weapon at the disposal of the central authorities' (Grossman, 1963, p. 118). Thus, where material inputs are less determinate of a unit's activities, this information and incentive problem is greater, and the defiance of central will relatively more widespread and successful. This observation allowed Grossman to predict the non-viability of the then forthcoming 'Liberman' reforms, as well as of any further reform that fails to fundamentally alter the materials allocation system.¹³

Under-planned, ill-commanded sectors

A major challenge to the command economy from its very inception has been the existence of sectors outside, or only partially affected by, the command principle. In the Soviet Union, these included most of the agriculture sector, much of housing, the household sector, and some consumer goods and services. 'Markets' were allowed to function for the distribution of final consumer goods and services, including agricultural produce, and for much of the activity of the 'collective' sector in agriculture, as well as for household labour supply. For transactions with 'personal property' within the household and collective sectors, money was active and agents responded to market prices, while in the quasi-markets interfacing with the state sector, for example, labour and consumer goods 'markets', money was relatively active but prices remained largely controlled and non-market. These are sectors where information on needs/preferences and capabilities proved too difficult to acquire reliably in real time for acceptable allocation and balance to be commanded, and so at least one side of a market was allowed to function with active money. Here, the command mechanism proves too crude and clumsy, and hence politically counterproductive, to be used outside of pressing emergencies.¹⁴

In view of the theoretical incompatibility of command and market, how could these 'market' sectors be successfully grafted onto the command mechanism? Grossman (1963, pp. 119–120) explains this in terms of what might cause 'failure' in the eyes of the authorities, leading them to shut down the relevant market. The first would be an unpredictability in the flow of goods between the command (C) and market (M) sectors, rendering 'physical

¹³ That, indeed, includes all 'reforms' through Gorbachev's *Perestroika*.

¹⁴ Indeed, this might be considered a lesson of the 'war communism' first experience with a command economy.



planning and plan-fulfilment in C difficult, especially if C depends on M for significant inputs'. On the other hand, if M can be treated as a residual for purposes of materials planning and allocation, a buffer for C, its coexistence with C is acceptable. Second, if production in M violates regime values and priorities, it is not to be tolerated. And finally, if M fails to mobilize its production resources sufficiently, and cannot be forced to do so by other means, it will not be tolerated.

However, if M's operation is characterised by rapid change and complexities outside the core interests of the regime; if without disrupting the industrial core, greater incentives and risk can be placed on peripheral agents in M; and if non-market constraints can force the desired market response from M, then the centre will want to separate M out from the command sphere, lowering its burden by shifting the burden to the agents in M. These considerations, Grossman (1963) argues, were indeed active in the case in those sectors 'left to the market': consumer goods retailing, the acquisition of labour services, the support of households in the agricultural sector through a private agricultural sector, and a few peripheral and interstitial activities. In a far more nuanced discussion than this, Grossman (1963, pp. 121–123) makes a convincing case that attempts to truly 'marketise' any other sectors or activities in the command economy are doomed to fail, unless the loss of fervour, of the sense of mission and urgency, leads to abandonment of the command mechanism.

The cancer of 'money'

A final (for this discussion) challenge lies in the role of money in any *less-than-absolute* command economy, as is beautifully illustrated in Grossman's writings (especially 1963, 1966, 1968, 1977b).

'An "absolute command economy", the complete centralization of decisions in the production sector (let alone in the household sector), is an impossibility. Something must be left to local initiative and dispersed decision making. So khozraschet remains a logical necessity, an unfriendly bridgehead that threatens to seize ground whenever the planner fails or defaults'. (1966, p. 228)

With the inevitable devolution of some decision making to firms and households, money acquires a necessary and critical role in the command economy. That role arises from the need to economise in making those decisions, and as a medium of exchange and store of value in the decentralised interactions that relate to those decisions. In acquiring this



role, this 'moneyness', it allows accumulations of power outside the control of the regime. For,

'so long as money is money, any amount of it in someone's hands is also a certain amount of power that lies outside the effective control of the central authorities, power that may be used contrary to the authority's values and system of priorities'. (1963, p. 116)

Money is a 'bearer of options' whose power and influence must be restrained if the command mechanism is to operate properly – to determine priorities and to ensure maximal commitment to their achievement. As Grossman (1962, p. 214) noted,

'Money is a form of social power that may lead resources astray and is subject to only imperfect control by political authority'.

Thus the power of money has to be curbed in a command economy by limiting balances available to households and firms, by compartmentalising money into 'cash' (*nalichnye*) and 'firm' (*beznalichnye*) circuits, and by erecting barriers and limits to the use of 'monies' in each category, although that undercuts the effectiveness of any attempted decentralisations. Liquidity, 'moneyness', is constrained by the institutional structures and by all the characteristics and conditions of the 'sellers' market', rendering 'money' the only non-scarce commodity, in unusable excess to the extent that the command mechanism is effective. Monetary policy in the properly functioning command economy is reduced to limiting the volume of cash in the economy ('macro-monetary' control) through wage fund restrictions and cash control absorption plans of the retail sector, and the allocation of firm balances in restricted categories ('microfinancial' control) in just sufficient quantity to support the implementation of the plan (*kontrol' rublem*), with the confiscation of excess funds to prevent unauthorised activity by the firm.¹⁵

Similarly, the price system, expressed in terms of that money, must also be mobilised to the purpose of control. As Grossman (1977a, pp. 133–138) cogently argues, the inflexible, administratively segmented, average-cost based prices are a logical necessity of command and haste-based shortage. For all the problems they caused, and the unintended consequences and distortions in the behaviour of subordinates, such prices kept money largely passive, at least in the core state sectors, and allowed both money and prices

¹⁵ See G Garvy (1966) for a concise yet comprehensive survey. The parenthetical terminology is Grossman's (1963; 1966, p. 217).



to remain instruments, rather than disrupters, of command. More than being ideologically justified,

'... they responded to the pragmatic and pressing requisites of running a shortage economy with a rapidly developing system of materials allocation and of centralized direction of enterprises'. (Grossman, 1977a, p. 138)

Money, however, is not so easily contained. Once in unobserved hands, it exercises its 'command over goods and services' without reference to plans, commands or regime priorities. Hence, given any discretion, any sphere of activity not directly monitored, agents will naturally use money in ways they find desirable, placing demands on a physical system otherwise tautly planned and characterised by general scarcity. And the possibility of acquiring money provides incentives for unauthorised activities, for unplanned interactions and reallocations.¹⁶ An active money vastly expands the sphere of discretion of 'subordinate' agents beyond any authorised by a decentralising reform, and hence calls for severe administrative restrictions, a reduction to passivity, if it is not to disrupt the planned activities and discretion of the central authorities.

Yet attempts to administratively constrain the influence (*razgul'*), the 'corruptive' power, of money become increasingly futile once the 'genie' has been 'let out of the bottle'. Even limited decentralising reform, allowing money to influence some (subcategory) production and allocation decisions, inevitably lets loose more liquidity, more of a command over goods and services, than desired. This arises from a multitude of factors: errors in both physical and financial plans, inherent incompleteness of plans and commands due to limited information and time and the necessity of aggregation, changing circumstances and shocks to the economy, mistakes in implementation and in responding to shocks, the irregularity and disruptions in the materials allocation system, the behavioural response of even the most enthusiastic and best intentioned agents to these problems, etc. All of these can lead to an unexpected lack of funds for doing what was commanded (if only implicitly), and hence disruption of commanded performance, unless additional liquidity is provided.

Thus monetary policy in a command economy, once money is allowed any room for activity, must be accommodating; a lack of funds can never be allowed to disrupt planned performance, just as an excess of funds cannot be

¹⁶In discussing the possibility of liberalising (decentralising) small-scale investment, a GOSBANK official noted it would mean 'disruption of proportions in confirmed plans, amendment of plans, diversion of budget funds, ... and weakening of control of the economy and of finances'. (1966, pp. 225-226)



allowed to facilitate unplanned/unauthorised activity. Thus the role, the influence of money has a natural, inexorable tendency to grow: insufficient funds become an immediate problem generating new money through credits or additional allocations, while unused funds tend to stay hidden, surreptitiously influencing allocations, until ferreted out by inspection or accidental discovery. Thus, as the influence of 'money' grows, so does the challenge to the command principle. An increasing number of agents, in both the state and non-state sectors, has a growing ability to access resources, to divert them in the name, if not the interest, of implementing decentralised plans, and thus to challenge the priorities of the political authorities. This growing challenge becomes a cancer in the system, a growth that undermines its health and feeds tendencies destructive to the priorities of the regime and its rulers.

THE 'SECOND ECONOMY'

That cancer gathered strength with the failed 'decentralisations' of Khrushchev's *Sovnarkhoz* reforms, the monetising recentralisations of the Kosygin administrative and pricing reforms, and the economic experiments of the late 1960s and 1970s. Attempts to strengthen 'material incentives' and activate 'the profit motive' in order to increase the effectiveness and technical efficiency of the implementation of central plans and directives and to stimulate technological progress and innovation, and the growing monetisation of the agricultural sector, opened the door to massive expansion of money supply and eroded the barriers between the currency (*nalichnye dengi*) and bank account (*beznalichnye dengi*) monetary circuits. Collective farms and their subsidiary enterprises, owners of 'small means of transport', vodka manufacture, both legal and *samogon*, and distribution, and the Caucasus republics (Georgia in particular) proved particularly rich sources of illicit (from the system's perspective) monetisation and private 'entrepreneurial' activity (Grossman, 1977b, pp. 31–32). This both raised the spectre of inflation and opened the door to vastly increased opportunities for manipulation by self-interested subordinates. As Grossman (1977a, p. 166) noted, the use of 'economic levers' greatly increased the opportunity for and incidence of 'bribery, corruption, peculation and speculation, and even "honest" labor, but on one's own account'.

Thus growing 'monetisation', the existence of ready and waiting market sectors, and the decline in the use of violent instruments of enforcement, led to a growing sphere and importance of activities in the 'shadow', outside the purview of 'planning' and 'command'. These activities were at times supportive, helping to achieve tolerable micro-balance in the increasingly



complex economy,¹⁷ but often were in violation of planned implementation and regime values. Private interests, necessarily allowed some leeway, grew in significance, increasingly 'seizing ground from command', as Grossman's (1966) earlier analysis had suggested would be the case. In particular, the private agricultural sector, initially allowed in order to secure survival of the peasantry under the extractive pressure of rapid industrialisation, and the consumers' personal services' sectors provided the basis for a ubiquitous, if still marginal, 'second/shadow economy'.

Ubiquity and growth

Grossman's seminal article begins by defining the 'second economy' as

'all production and exchange activity that meets at least one of two criteria: (a) being directly for private gain; (b) being in some significant respect in knowing contravention of existing law'. (1977b, p. 25)

Although much of it is thus legal, all of it operates on principles contrary to those of the official, command economy, and legal and illegal aspects are typically deeply intertwined. The essence of the 'second economy' is in the opposition to the principles, incentives and processes of the first, command economy.

As argued in Grossman (1979, pp. 836–842), there are four general categories of illegal private activity in the second economy: theft from the state of goods, money and/or work 'time'; 'speculation' (resale for profit and/or 'middleman' activity); illicit production (in eight categories); and corruption and bribe extraction. In a detailed taxonomy, Grossman shows how virtually every area of economic life is touched on, and often entangled with, 'second economy' activities, and how private legal activity naturally opens a loophole for illegal trading and entrepreneurship, generally below the purview of the legal authorities. And it goes hand in hand with the extension of corruption, ensuring that it remains outside of official notice. Further, between the legal and strictly illegal are a multitude of behaviours and activities, undertaken largely for, or under the influence of, private gain that are tolerated by the systems' authorities as they are in some significant respect 'functional', supportive of the proper functioning of the official command economic system.¹⁸

Those 'violations' of Socialist legality within the Socialist sector, a part of the 'second economy', built informal interenterprise relations that were

¹⁷ Indeed, complexity (eg number of interactions) can be shown to grow quadratically in the size of the economy, rendering the planners' problem ever less soluable and planners' decisions increasingly inadequate.

¹⁸ A partial and crudely aggregated listing of the various types of activities in the second economy, differentiated by degree of legality and with some indication of how legal fades into illegal (in following parentheses), is provided in Table A1 the Appendix.



generally beneficial to the operation of state enterprises, and were later called by Grossman, following Zaslavskaja (1980), the 'shadow economy'.

'The term pertains to the socialist sector alone; illegal activity on private account is not subsumed, although ... is closely related to it.' (Grossman, 1982b, p. 100)

They worked to substantially correct the allocative failures of the command mechanism, improving firm performance and hence benefiting its management, and provided lucrative opportunities for managers to directly benefit through the activation of barter, *blat*, and bribery. They however, also spawned further distortions in economic behaviour, as managers sought to generate access to cash, the life blood of the 'second economy', to extract rents, and to hide their activity from supervisory and statistical organs.

While the fundamental cause of the appearance and growth of the 'second economy' undoubtedly lies in the congenital institutional weaknesses of the command economy discussed above, there are a number of proximate sources that make it unsurprising (Grossman, 1979, pp. 842–845). These include extensive price control, with consequent scarcity and misallocation, high taxes on non-state activities/incomes, prohibitions of private activity, unmet individual consumption needs, poorly protected impersonal (state) property, the personal power of bureaucrats and 'gatekeepers', and other historical factors, including the end of terror. These provide both motives and opportunities for officially illicit activity and for the authorities to overlook that activity. With the aging of command and the decay in enthusiasm of its agents, the growth of such a second economy appears natural, *zakonomerno*.

Grossman, however, was quite cautious in making assertions about the size of this set of activities, although he confidently and convincingly argued its pervasiveness throughout the Soviet economy of the mid-1970s. Noting that the legal private sector had shrunk substantially since 1950, he provided anecdotal evidence of a substantial growth in the illegal second economy during the Khrushchev and Brezhnev years, and corroborating evidence of complementary changes in car ownership, incoming foreign goods, growth in officially noted economic crime, and the liquidity of the Soviet household over the prior two decades (Grossman, 1977b, pp. 35–36). In a succeeding analysis, Grossman, (1979, pp. 847–851) extends speculation on the size of the 'second economy's' illegal side by drawing on the, by then, rapidly expanding research effort into the Soviet Second Economy.¹⁹ Grossman,

¹⁹ Along with the work of a number of Soviet emigres, and a couple of Soviet statisticians, a primary source of evidence was the on-going Second Economy research project of Gregory Grossman and Vladimir Treml, housed at Duke University. For example, Treml estimated that narcotics generated some 15 billion roubles, organised religion about 10 billion roubles, and middle-man activities about 6–7 billion roubles income, while some 50% of all gasoline sales were stolen from the state.



however, declined to go beyond specific activity estimates, noting general problems of more aggregate measurement such as netting out and adjusting the price basis. Other researches indicated a second ('shadow') economy size of 15–18% of national income, with about a third of urban personal incomes coming from the second economy.²⁰ A Soviet analyst, Professor Koriagina, also estimated its growth at the end of the 1970s at some 10% per year. Thus the second economy had truly become a significant part of the Soviet economic system, holding its own against, and in many areas directly challenging, the first, command economy.

Its fundamental role

The Soviet 'second economy', however alien to the nature of the command system, was not an entirely dysfunctional growth on the command economy. It fulfilled a number of important roles in the economic system, not all of which were harmful to its functioning. A partial list, readily distilled from Grossman's writings (1977b, 1979, 1982b), includes:

1. providing many consumer goods and services, including illegal ones (eg religious items), filling important gaps in planned state activity;
2. reallocating consumer goods to those willing to pay more;
3. generating incomes: labour, middleman services, rents, entrepreneurial returns, 'protection' payments;
4. diverting resources to unplanned uses:
 - (a) from State to individuals (private sector);
 - (b) reallocating production inputs within the State sector;
5. facilitating plan fulfilment, by preventing disastrous breakdown/bottle-necks;
6. strengthening the influence of financial incentives, making 'economic levers' of the reform more influential;
7. reducing repressed inflation, 'neutralizing' the 'monetary overhang';
8. making a major contribution to housing and agricultural construction [investment];
9. enhancing political control:
 - (a) entrepreneurial outlet, outside politics (safety pressure release valve);
 - (b) everyone guilty under Socialist legality; must break law to get job done (eg doctor getting needed drugs).

These roles are largely enhancing of consumer welfare, production stability, and social stability. Thus the 'second economy,' and in particular its 'shadow' side, played an essential role in the first economy as a 'pressure valve',

²⁰ See Ofer and Vinokur (1980), and also Grossman (1987, pp. 220–225; 1989, p. 94).



a release 'fixing' 'command' by maintaining micro-balance and covering 'holes' in economic life, left by the mistakes or oversight of the planners.

It was a role that had to become increasingly important as the economy grew and became more complex and diversified, and hence less susceptible to conscious oversight and direction. As the central authorities struggled with their loss of control, searching through reform, decentralisation and recentralisation, monetisation and administrative restriction, agents in the economy took advantage of gaps in control, of the autonomy and discretion offered by growing liquidity of the quasi-money in the system, to deal with problems of coordination and balance, inconsistency of plans and commands, and ubiquitous shortages/scarcities.²¹ Of course, they operated in the light of their own partial information, and in their own (private as well as official) interests, but in doing so saved the system from collapsing under its own weight and rigidity.²² Thus the 'second/shadow economy' proved to be

'a spontaneous surrogate economic reform that imparts a necessary modicum of flexibility, adaptability and responsiveness to a formal setup that is too often paralyzing in its rigidity, slowness, and inefficiency. It represents a de facto decentralization, with overtones of the market.'
(Grossman, 1977b, p. 39)

In doing so, the 'second economy' also proved to be a valuable stabilising influence on society and the polity, making life livable, and the system humanly manipulable and responsive to private inducement. It made everyone complicit in the way things work, equally 'guilty' before state and society, while providing an almost legitimate and not politically dangerous or directly destructive outlet for individual initiative and entrepreneurship.

Its corrosive impact

Despite its positive functional role, the second economy also had a less positive *systemic* impact touched on by Grossman (1977b, pp. 37–38; 1986, pp. 191–193). It worked to undermine, to corrode the legitimacy of the official system. It

'controverses such philosophical bases of Soviet society as the solidarity of various population groups with one another and with the Party and its

²¹ Grossman (1982b, pp. 110–111) provides clear Soviet evidence of these phenomena from the Soviet economic press and literature, including increasing failures of the the planning and allocation hierarchies and of the growth of the 'shadow economy' in the state sector.

²² This is the 'cindynophobia' of the interlinked 'first' and 'second' economies so nicely argued by Powell (1977).



leadership, the moral transformation of Soviet man since the revolution, and the inevitable progress of society toward full communism'. (Grossman, 1977b, p. 36)

Its very existence and usefulness thus undercuts the ideology of the regime, the Marxist-Leninist verities underlying its legitimacy. The second economy further works against and undercuts regime priorities by exposing the incompetence and incapacity of the 'all-knowing' authorities. Its provision of alternatives weakens the 'plan, production, and labour discipline' so essential to the proper operation of the command mechanism. Indeed, it attacks the core of the command mechanism as it

'...elevates the power of money in society to rival that of the dictatorship itself, rendering the regime's implements of rule less effective and less certain'. (Grossman, 1977b, p. 36)

In particular, it corrupts officialdom and distorts prices, adding a (positive or negative) 'second economy margin', both 'in kind' and in money, breaking prices as an effective instrument of control. This undercuts monetised incentives for State activities, by providing competing, and often better alternatives to them. Hence the 'second economy', and in particular the 'shadow economy' in the state sector, completes the cancerous development of agent autonomy, of the ability to work outside the plan and its subsequent commands, by providing viable alternatives to the plan.²³

Other dysfunctional impacts, undermining the operation of the command system, arise from its diverting of resources and products to unplanned sectors/activities, including diversion from development/investment priorities to consumers. This naturally generates undesirable (from a system perspective) redistribution of incomes, although recipients including many high placed officials find it very desirable. Indeed, it is further disruptive of command by creating a 'two-tiered' system of prices and incomes, of consumer goods and labour markets (Grossman, 1977b, p. 236; 1982b, pp. 108–109).

One tier comprises the low-priced, scarcity-ridden quasi-markets of the 'less-than-absolute' command economy, where the unenterprising, the overly scrupulous, and the 'slow' can survive. The other tier consists of real, albeit highly distorted, markets in the generally high-priced, risky but well endowed, second economy where the enterprising, entrepreneurial, and

²³ Indeed, as Grossman (1983a, pp. 212–214) argues, efforts to impose quasi-market controls over agents, such as personal contractual liability (*material'no otvetstvennoe litso*) for preservation of state assets, proved counterproductive, mostly providing new incentives to manipulate and exploit state assets for personal gain.



criminal can thrive. In this high tier, substantial incomes are generated and allocated, although they largely accrue to corrupt officials, and 'gatekeepers' of scarce materials or permissions who can extract rather phenomenal 'rents' (Grossman, 1977b, p. 32; 1979, pp. 849–851). The inequities that this generates further undermine the legitimacy of the regime and generate potentially explosive social pressures, only partially relieved by the second economy's 'pressure valve' aspects.

Finally, it is worth noting that the second/shadow economy, through its activity outside the officially measured sphere, seriously distorts statistical data and the information available to planners and allocators in the official economy, and due to its illegality, also hides necessary information from other agents in the shadow economy. This undercuts the ability of superior organs to manage the economy, and further aggravates the economic problems that spawn 'second/shadow economy' activities, deepening the contradictions between the centre and decentralised agents, and further corroding the institutional structures of the command economy.

THE INHERENT CONFLICT

We are now in a position to summarise the implications of this pathbreaking work of Gregory Grossman. He has defined and analysed the two truly fundamental 'forces', the 'demi-urges', driving the evolution of the Soviet economic system, and has felicitously captured them in the title of his piece in the Gerschenkron Festschrift (1966), 'Gold and the Sword'. These forces have struggled from the very beginning of the Soviet economic system, with the nature of the conflict and the role of 'leader' changing over time.

Riding a wave of Bolshevik enthusiasm in the presence of a single, overriding priority – survival in war – the Sword, the 'command mechanism', took absolute precedence and strove to operate without money, markets, or any individual or social autonomy, under what came to be called 'War Communism'. Despite heroic effort and terror, it failed, and that failure revealed a need for some role for 'Gold', for the market mechanism. The pendulum then swung toward Gold, the 'market', for recovery under NEP, but the looming loss of control, the impending need to compromise in objectives and priorities, and the apparent urgency of industrialisation for military strength, returned the Sword to dominance, relegating Gold to the margins of the system, where it handled areas and activities in which the Sword had been revealed to be counterproductive during War Communism.

The resulting system, Grossman's 'less than absolute command economy', substantially industrialised, triumphed in the Great Fatherland



War, and recovered to an almost perfect replica of its pre-war self by 1950. However, by then the strains of its inherent inflexibility, and the bounded rationality of the system's managers began telling on continuing growth and the development of the economy. With economic growth came increasing complexity and growing intractability of the planning and economic management problem. Some decentralisation became essential, and increasingly so as time passed, opening the door once again to the rise of Gold as a significant influence on the operation and development of the economy.

The remaining years of the Soviet system witnessed an epic struggle, barely perceptible at first, but increasingly evident as reforms, decentralisations, reorganisations, and recentralisations cycled round each other in the search for a solution to the increasingly evident and destructive malperformance and waste, and aggravating behavioural distortions in response thereto, between the 'command principle' (Sword) and the weak, but inexorable emerging, 'market' (Gold). Initially reflected in the dysfunctions of the marginal and quasi-markets of the command economy, and in the struggle to harness a 'passive' money to the purposes of command, the role of Gold grew along the 'treadmill of reforms' into the rival, if still largely subordinate, and complementary 'second economy, and in particular its "shadow" component', on which the Sword, the 'command principle', increasingly came to depend for its effectiveness. As long as the Soviet system remained a 'command economy' the Sword had to have last word, and Gold remained largely relegated to the secondary 'shadow' economy, exercising its influence within the quasi-monetised instruments ('economic levers') of the command mechanism and the distorted markets of the second economy. As Grossman noted,

'the essential duality of the Soviet economy – first-second, planned-shadow – is likely to persist with both functional and dysfunctional effects, so long as the main institutions of the command system endure'. (1982b, p. 114)

This inherent conflict, which played out over Soviet history, revolves around a number of fundamental dualities, elemental oppositions that characterise these primary forces. The 'command principle' derives most basically from the urge, the will to control, to 'rationally' determine and direct the future, exercised by a 'gnostic' elite, imminent in the Party.²⁴ It knows what needs to be done, by whom and how, and can tolerate no dissent or deviation. Juxtaposed to this 'Will of Society', stand the millions of independent 'wills',

²⁴ The earlier Mormon command experiment (Grossman, 2000) was similarly derived from the gnostic vision of the church leadership ('prophets').



desires, and objectives, anarchically coordinated through 'the market', whenever that set of institutions broke through the barriers and limits placed by 'command'. This provides the foundation for the eternal struggle of 'central priorities and control' *versus* 'agent incentives and capabilities'.

This opposition is severely aggravated by urgency, by 'virtuous haste', in the pursuit of overriding social goals and central objectives. For the mobilisation of, and the focus of resources on, these priorities tramples on the information, capabilities, and goals of individual and organisational agents, which must perforce implement that mobilisation and focus, implement those priorities. 'Effectiveness' in the pursuit of social objectives becomes opposed to 'efficiency' in the attainment of any objectives, denies trade-offs based on local information and incentives, and hence blocks flexibility in response to changing circumstances. Indeed, the single-minded pursuit of overriding objectives, of absolute priorities, naturally disrupts the fine coordination, the requirements of 'balance', necessary to consistently pursue any objectives. This Grossman captured in his assertion

'The chief persistent systemic problem of a command economy is the finding of the optimal degree of centralization (or decentralization) under given conditions and with reference to given social goals'. (1963, p. 107)

Throughout the history of the Soviet Union, the needs of centralisation, given Soviet social goals, stood in fateful opposition to the necessity to decentralise in order to keep the system functioning tolerably. The latter necessity spawned repeated (partial) reorganisations and remonetisations, and a 'second economy' that both shored up the operational foundations of the 'first economy' and undermined its long term viability, corroding its ideological and systemic foundations. 'Gold', so unleashed, intensified the dysfunctions and contradictions of the 'command economy', spurring further repeated 'reforms' and 'experiments' that merely further aggravated the inconsistencies, the 'oppositions' in the system, until the central leadership, largely unintentionally and out of ignorance (I would argue), destroyed the 'command economy' in the radical systemic and economic 'restructurings' beginning with *Perestroika* in 1987.

PRESCIENT FORESIGHT – A CONCLUSION

Gregory Grossman's analysis of the Soviet economic system, and of the two fundamental 'spirits' that struggled within it, has proved prescient in



a number of significant cases. In particular, it clearly foretold the pitfalls and problems of 'marketisation' in a command economy. In discussing a conference paper in 1959, he used his insight into the command economy to correctly predict the failure of Khrushchev's *Sovnarkhoz* reforms because of the inherent contradictions between the Soviet 'sellers' market' and regional striving for autarchy, arguing that political imperatives would triumph over economic, that 'control' would trump 'efficiency' (1960b, pp. 238–240). Indeed, the subsequent analysis of the theory of the command economy clearly indicates why industrial reform must be fundamentally inconsistent with that system, and subversive of 'command' as well as of regime objectives.

Thus reforms, particularly those activating 'money', sacrifice too much control for the limited increase in efficiency within firms, and hence are inevitably far more 'conservative in implementation than in blueprint'. (1968, pp. 11–13). The early analysis essentially predicted the 'treadmill of reforms', that

'... the coexistence between the command principle and market mechanism (is) unstable and ephemeral ... the command principle, aided by the club of materials rationing, will inevitably push back, and eventually eliminate, the market mechanism unless a full-fledged market economy is adopted'. (1963, pp. 118–119)

This analysis elegantly argued why a single integrated sector can not be monetised and marketised, why partial reform of a command economy must fail, and hence be reversed. Thus it is perhaps the most succinct, insightful analysis of the fate of Soviet economic reform from 1965 through the closing of Andropov's last 'Large-Scale Economic Experiment' and the final enthusiastic thrust of 'command' in Gorbachev's 'Acceleration' (*Uskorenie*) programme in 1985.

This analysis would also seem to cast light on what we should have expected with the end of the system – the trials and tribulations of the collapse of 'command' and the potential triumph of the 'market'. The massive Soviet industrial edifice, artificially held together and operating by fiat and command in the face of arbitrary and economically bizarre prices/valuations ungrounded in any conception of scarcity or opportunity cost, could not remain viable in the absence of forced coordination and control. In addition, the analysis of the growing role of money, and the ever more significant shoring up and patching of an increasingly distorted and dysfunctional command system by the second economy, should have led us to expect the disastrous collapse of formal economic activity when command was finally abandoned.



Similarly, the 'shadow economy' was clearly an artificial mechanism, built upon, and dependent on, the structures, inconsistencies, and irrationalities of the command mechanism.²⁵ It, together with the intermediating activities of the lower Party organs, gave life to configurations of capacities and assets, to patterns of activities increasingly divorced from any real relationship to either ultimate system priorities and goals or to any conception of relative scarcities or social values. The 'second economy' made Soviet centralisation more enduring, more viable, even as it became ever more artificial and divorced from underlying economic reality. It provided a crutch that could only hold up, support the system, with a continuing, unrestrained influx of liquidity, such as Grossman noted was taking place in his analyses of the late years of the Soviet Union (1982a, 1982b, 1983b, 1986, 1987). The accelerating growth of uncontrolled purchasing power in the face of still fixed official prices provided powerful incentives to maintain the (facade of) the system and the growing corruption and private rents it generated, even as its structure grew increasingly unrealistic.

This 'house of cards' had to collapse, as did the 'shadow economy' as a substitute for the market. But 'the market' as a coherent balancing mechanism was unable, for many reasons partially adumbrated in the writings of Grossman, to spring forth from the rubble of that collapse. Rather, that collapse left, as a model, a caricature of 'the market', a redistributive mechanism without a 'bottom line' that was well adapted only to feeding off the carcass of the command economy, off the massive, economically irrational structures and stockpiles that had been built over some 40 years of wasteful investment and production. With the elimination of the role of the Party, with the full activation of money through elimination of command institutions and agencies and the massive, if inconsistent and incomplete, freeing of prices, and with the inability to control emission of liquidity, productive economic activity could hardly avoid collapsing. Grossman's analysis should have told us not to expect the rapid appearance of real markets and of economically informed incentives and signals. Rather, previously system-marginal but flexible elements from the 'second economy', including the 'children of the Party', seized and continued to exploit inherited assets, the organs, and the remaining powers of the State, for their own benefit, without having to satisfy any constraints from the 'first' economy. Rather than 'market', a distorted 'transition' system arose. However, that is another story.

²⁵ In his essay 'Bane or Boon for Reform' (1989), written at the height of hopes for *Perestroika's* success, Grossman concludes (p. 94) that '... the overall effect of the second economy is still against reforms', due to the behaviours and interests it fosters and protects, which depend on the continuing existence of the command economy.



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APPENDIX

A partial and crudely aggregated listing of the various types of activities in the second economy, differentiated by degree of legality and with some indication of how legal fades into illegal (in following parentheses), is shown in Table A1 below.

Table A1: Types of second economy activity

Legal	Strictly illegal	Illegal, but tolerated
Private plot & animal husbandry (but – illegal inputs)	Use of 'socialist' property for personal gain Buying and selling for a profit (speculation)	Construction and repair teams (<i>shabashniki</i>) Information brokering
Farmers' markets; flea markets (but – others' or stolen goods)	Hiring other than household help Currency transactions, especially with foreigners	Taking 'advantage' of official position Private production 'on the job'
Housing maintenance and construction (but – bribery, state inputs, 'black' labour)	Theft from the State, particularly in large amounts	Parallel production in plant 'Creative accounting,' for example, 'losses' in transport, 'spoilage,' plan 'underfulfilment'
Sale of 'personal property' Professions: doctor, dentist, teacher, lawyer, prospector	Corruption at any level Underground entrepreneurship: production with or without a socialist facade Bribe taking and giving (<i>mzdoimstvo</i> , <i>likhoimstvo</i>)	Sharing favors; showing 'concern' for those who could be useful
Individual labour: repair services, personal services, crafts and trades, trapping Subsidiary enterprises of collective farms	Sale and purchase of Government/Party positions	

Source: Author's extraction and compilation from Grossman (1977, 1979).