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BANKS, CREDIT, AND MONEY IN SOVIET RUSSIA

BANKS, CREDIT, AND MONEY IN SOVIET RUSSIA

BY

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To

Marie B. Arnold

FOREWORD

THE internal economic structure of Soviet Russia has, for a number of years past, continued to be a source of extreme interest and curiosity in the older "capitalistic" nations. Many theorists were concerned to hear how their doctrines of consumption and production in a "socialistic" economy were likely to work out, recognizing that when tested by the touchstone of reality, practical organization would be likely to furnish a much more severe test than would be supplied by a theory or logic.

Others familiar with the difficulties of organization and technique growing out of modern industry and finance have wondered exactly what could be put in the place of the older procedures. Would a socialist Soviet state find it necessary to evolve an economic and banking system of its own, conducted on new lines and discarding all older canons of efficiency, or would it find more expedient the continuation of the older mechanism—the chief change being found in the distribution of the profits and rewards of business which reverted mainly to the state as the owner of the business instead of to private citizens as individual capitalists; but, in any case, governed by the recognition of capital ownership as a measure for determining the distribution of the results of business? Would the new type of state succeed in doing away altogether with the "profit motive," so much belabored by "forward-looking" administrators and writers, or would it find necessary to continue the appeal to the old motives as a means of stimulating and encouraging participation in business?

All these, and many more, questions of a like kind have lacked answers, due to the fact that specific and authoritative information was absent in regard to actual developments in Russia. The remoteness of the country, the comparative smallness of the circle of those foreigners who could read, write, or speak Russian, and the stringent restrictions upon the conveyance of information as to happenings in Russia have all stood in the way. It is for these

reasons, therefore, that complete and careful analyses of Soviet financial and industrial institutions have not only an outstanding interest for the foreign reader everywhere, but must also be regarded as the basis upon which many of his first impressions will be revised and his ultimate opinions regarding the new type of industrial organization will be eventually made up.

These considerations furnish the background which renders the work of Dr. Arnold, in his review of the history of money and banking in the Soviet Union, a useful contribution to the general scope of economic literature. It is the more valuable as such a contribution in that the author has not confined himself to a discussion of technique but has introduced into his work a considerable amount of economic and cultural material, without which purely technical or institutional analysis loses a great part of its worth. It is thus as a contribution to the broader economic history of Russia and of socialistic organization that Dr. Arnold's monograph must be taken and appraised.

In addition to its general value as thus described, this study must, moreover, be given an acceptable place among the inquiries into money and banking in different parts of the world which have of late years so greatly increased our actual knowledge of monetary procedure. As a thorough student of money and banking at large, Dr. Arnold writes the financial history of the Russian evolution in language that is sufficiently detailed and specific to meet the requirements of the financial student, at the same time that he has afforded a background of interest that should commend it for the intimate knowledge he has shown of actual legislation, and of the administrative bearing of the latter upon the rebuilding of the banking system of the Soviet Union, and the introduction of a new monetary base.

How significant this branch of study is conceded to be may be inferred from the fact that two or three authors of outstanding knowledge and ability have, in the recent past, devoted themselves to an attempt to treat the Russian situation, one notably whose results were made public only during the current year. Comparisons are odious, but the present writer wishes to record his opinion that this work of Dr. Arnold's is not only distinctly superior in de-

tail to its predecessors, but is entitled to high rank as a sympathetic analysis of financial organization without special reference to country. The author shows an appreciation of the underlying principles which must govern the creation of a money and banking system, whether it be established in the United States or elsewhere. Because of this recognition of principle and because of its catholicity in the use of material, what might otherwise be limited in interest to technical students becomes also a treatment of large interest to the general observer of economic conditions.

It is, therefore, with confident hope that this new study of Russian finance and banking will be given its proper weight by those who are seeking to estimate with accuracy and care both the successes and the failures of the Russian economic experiment, that the present writer commends it to the attention of the economic and financial community.

H. PARKER WILLIS

COLUMBIA UNIVERSITY
November 12, 1936

PREFACE

DESPITE the enormous output in recent years of books pertaining to Soviet life and institutions, there is not a book in Russian, English, or any of the better known languages which deals comprehensively with the development of Soviet banks, credit, and money. The present book is, therefore, an attempt to fill that need. It was begun some five or six years ago while the author was a graduate student at Columbia University.

Some of its features require comment. It will be noticed, for instance, that several chapters are devoted to the development of banks, credit, and money in old Russia. This is not only to make the tasks of students of Russian and Soviet finance easier, but also because an acquaintance with the history of old Russian institutions is a prerequisite to an intelligent study of Soviet institutions. It will also be noticed that the financial institutions are presented here against an economic background. The reason for this is not difficult to see. Financial institutions, as a rule, are closely interwoven with the national economy which they serve, and their growth and shape tend to be molded by it. This is as true of financial institutions under a regime of "planned" economy, as under a regime of *laissez faire*. A study of the national economy is, therefore, indispensable if we are to understand the forces which gave direction to the organizational structure and technique of a country's financial institutions, particularly if we are to attempt to evaluate those institutions. Because the Soviet national economy underwent such kaleidoscopic changes and was characterized by such unusual forms, it is deemed necessary to illuminate it more fully than would otherwise have been done.

Much has been said relative to the reliability of Soviet statistics. There have been incriminations and refutations. Statistical "virtuosi" and prestidigitators are, of course, to be found everywhere. To assert, however, that figures issued by the Soviet government are false is absurd. All economic activity in the Soviet Union is

based upon and governed by statistics. It would be, therefore, suicidal for the government to base its actions upon false figures. However that may be, I weighed my data carefully and have qualified my statements concerning those portions which, in my opinion, required it.

I wish to acknowledge my deep obligation to Professor H. Parker Willis for guidance and encouragement at all stages of the writing, as well as for the reading of the entire manuscript. To Professors Benjamin Haggott Beckhart and John Martin Chapman of the Banking Department of the School of Business, Columbia University, thanks are due for reading the manuscript and for giving kindly aid. A debt of gratitude is owed to Professor Geroid Tanquary Robinson of the History Department and to Dr. Michael T. Florinsky of the Economics Department of the Faculty of Political Science, Columbia University, for the careful reading of the manuscript and the many valuable suggestions which helped to improve its quality.

I am heavily indebted to Dean R. C. McCrea not only for his inspiring teaching but also for the interest shown and the help and encouragement given. My indebtedness is also great to Dr. Eveline M. Burns who helped me to overcome difficulties which at one time seemed insurmountable.

To Professor George W. Edwards, Head of the Economics Department of the College of the City of New York, I am grateful for the aid and advice received. Acknowledgment must also be made to the following members of the Economics Department of the College of the City of New York: Professor Ray A. Sigsbee, whose interest in my work was a constant help to me, as well as to Doctors Boris Gregory Dressler, Thomas P. Kelly, and Bernard Meyer.

I am also under deep obligation to Professor James Dysart Magee of New York University for helping me to solve a number of my problems. To Dr. Richard Anthony Girard of New York University I am very thankful for the many illuminating and helpful discussions of topics dealt with in this work.

I wish especially to state my great indebtedness to my dear friend Dr. Emanuel Stein of New York University for painstaking

reading of the entire manuscript and for the offering of numerous suggestions which have resulted in its improvement, as well as for the moral support given throughout its writing. His deep sympathy and thoughtful foresight made it possible for me to proceed with this project and in many ways accelerated its completion.

I am indebted also to Miss Elizabeth J. Sherwood for splendid help in the preparation of the final draft of the manuscript for the press and for watching its progress through the press, to Mrs. Esther M. Poole for her conscientious work on the earlier drafts, to Miss Lucie E. Wallace for discriminating reading of the proofs, and to Mr. Lazar B. Woll for assisting me at one time in the burdensome task of copying material.

To the directors of the Economics Department and the Slavonic Department at the New York Public Library and to their intelligent, extremely able, and industrious staffs I am indebted beyond measure.

Without, however, the co-operation, aid, and inspiration of my wife this book would never have been written. It is to her that this book is inscribed.

Needless to say, I alone am responsible for the errors contained herein, for the interpretations made, and the conclusions drawn.

ARTHUR Z. ARNOLD

NEW YORK CITY
January 1, 1937

CONTENTS

FOREWORD, by H. Parker Willis VII

PREFACE XI

I. BANKS, CREDIT, AND CURRENCY BEFORE 1860 . . 3

Debasement of coins.—The assignats.—The early monetary reforms.—Early banking.—The State Loan Bank for the Nobility and the State Commercial Bank (1754).—The State Loan Bank (1786).—Charitable boards, widows' banks (1763–73).—The State Commercial Bank (1817).—The catastrophe of the late fifties.

II. BANKS, CREDIT, AND CURRENCY, 1860–1914 . . . 10

The organization of the imperial State Bank in 1860.—The Monetary Reform of 1897.—A critical evaluation.—The State Bank as a central bank; its policy with respect to note issue, 1897–1914.—The bank's loan and discount policy.—The commercial and investment banks.—Joint-stock commercial banks.—Municipal banks and mutual-credit societies.—Mortgage banking.—Joint-stock land banks.—The Nobles' State Land Bank.—The Peasants' Land Bank.—The state savings banks.—Conclusion.

III. BANKS, CREDIT, AND CURRENCY, 1914–17 . . . 26

The severe test to which Russia's economic system was subjected by the World War.—The initial confusion.—The Law of July 27, 1914.—Disappearance of metallic coins.—Financing the war.—Changed character of the State Bank's operations.—Commercial loans and discounts.—Loans against securities.—Short-term treasury bills.—Gold reserves.—Deposits and notes in circulation.—The commercial banks during the war.—The change in the character of their operations.—Inflation.

IV. NATIONALIZATION AND LIQUIDATION OF THE CREDIT SYSTEM, 1917–21 53

War Communism, 1918–21.—The fate of the banks in balance.—The nationalization of banks: the decree of December 14 (27), 1917.—The inspection of the safe deposit boxes.—Confiscation of all the funds and the annulment of all shares of private banks.—The liquidating technical collegiums; the renaming of the State Bank; the liquidation of the joint-stock commercial banks.—The liquidation of the mortgage banking institutions.—The liquidation of the mutual-credit societies and city public banks.—The liquidation of foreign banks.—The liquidation of the central bank of co-operative credit (Moscow People's or Narodnyi Bank).—The People's Bank of the R.S.F.S.R.—The abolition of the People's Bank.

V. TOWARD THE ABOLITION OF MONEY (THE MONETARY SYSTEM, 1918–21) 72

The budget during 1918–21.—The volume of notes in circulation.—The extension of the issuing rights of the bank. The nature of the notes in circulation.—The depreciation of the ruble and the foreign exchange rates.—The depreciation of the ruble and the price of gold.—The depreciation of the ruble and the price level.—The currency famine.—Local note issues.—Toward the abolition of money: the socialist philosophy.—The "tred."

VI. THE RE-ESTABLISHMENT OF BANKS AND CURRENCY IN 1921–22 111

The New Economic Policy.—The establishment of the State Bank.—Preliminary steps.—The purpose of the bank.—Capital and surplus.—Relations with the state.—Administration and management of the bank.—General business of the bank.—The loan and discount committee.—Branches.—Clearing houses.—An evaluation of the bank's statutes of 1921.—The depreciation of the ruble during 1921–22.—The work of the State Bank during 1921–22.—Its resources.—Its loans and discounts in 1921–22.—Other activities of the bank.—Other banks.—Toward the restoration of a stable currency.

VII. THE CHERVONETZ IN 1922–24 146

The State Bank acquires the right of note issue.—An analysis of the October decree.—Early difficulties.—The security behind the chervonetz.—The purchasing power of the chervonetz in terms of foreign exchange and gold.—The chervonetz and the price level.—The circumstances surrounding the decline of the chervonetz' purchasing power in 1923–24.—The "scissors" crisis.

VIII. THE "BIPAPER" STANDARD AND HYPER-INFLATION . 175

The chervonetz and the treasury notes from the end of 1922 to March, 1924.—Position of treasury notes with respect to banknotes, gold, and foreign exchange.—Treasury notes and the price level in 1923–24.—Revenue from note issue.—The evils of inflation under the "bipaper" standard.

IX. THE MONETARY REFORM OF 1924 200

The eve of the Monetary Reform.—The introduction of the Monetary Reform.—The issue of new treasury notes: the decree of February 5, 1924.—The link between the treasury note and the banknote.—Cessation of printing and of issuing Soviet tokens (sovznaks): the decree of February 14, 1924.—The minting and issue of silver and copper coins: the decree of February 22, 1924.—The redemption of sovznaks: the decree of March 7, 1924.—Other measures.—The discontinuation of the "commodity" ruble.—The stabilization of the price level.—The stabilization of the exchanges.—The shortage of notes of low denominations.—An appraisal.

X. THE STATE BANK, 1924–28 244

The credit operations of the State Bank, 1924–28.—The discount rate and the discount policy.—The capital of the bank.—The deposits of the bank.—The note issue.—Financing of foreign trade.—The settlement of international balances.—Foreign exchange policy.—Other activities of the bank.—Branches, offices, and agencies.—The relation of the bank with other banks: the Committee of Banks of 1924.—The Laws of June 15, and June 20, 1927,

delimiting the activities of the banks.—Comparison between the imperial State Bank and the State Bank of the U.S.S.R.—The distinguishing characteristics of the State Bank and of Soviet banks in general.—Credit planning.

XI. The Evolution of a System of Specialized Banks . 281

A general view of the development of banks during 1922–28.—The Bank of Long-Term Credits for Industry and Electrification of the U.S.S.R. (Prombank).—Cooperative credit (the Vsekobank).—Agricultural credit (Selkhozbank).—Municipal credit (Tzekombank).—The Bank for Foreign Trade (Vneshtorgbank).—Mutual-credit societies.—Savings banks.—Miscellaneous banks.

XII. The State Bank and the Credit Reform of 1930 . 332

Rapid industrialization and socialization of the national economy beginning with 1928.—The State Bank's statutes of 1929.—The Credit Reform of 1930.—Background.—Preliminary steps.—The Act of January 30, 1930.—The Credit Reform in action.—"Leftist ideology" as a cause of the difficulties.—Amendatory legislation.—The reconstitution of the clearing departments.—The effect of the policies of this period upon the credit work of the bank.

XIII. The Present Credit and Planning Apparatus of the State Bank 375

The net changes in the bank's credit procedure.—The paradox: credit expansion accompanied by a qualitative improvement of the credit machine.—The expansion of the bank's resources.—Interest rates: recent changes.—The Law of May 25, 1932: the new planning apparatus.—The branches.—The planning technique.

XIV. Money, Prices, and Gold since 1928 404

Currency circulation under the First Five-Year Plan.—Changes in the ratio between banknote and treasury currency circulation.—Gold reserve and total firm cover.—The spread of non-cash settlements.—Valuta checks.—The rise of prices: introduction of ration cards.—The small-change famine of 1930.—The question of whether there was inflation in the Soviet Union during 1928–34.—The

extent of the ruble's depreciation.—Present position of the ruble.—The nature of Soviet money and the present monetary policy.—Revaluation of the ruble.

XV. THE PRESENT SYSTEM OF LONG-TERM INVESTMENT INSTITUTIONS 450

The reorganization of the special banks.—The shift to grants as a method for financing capital construction of state enterprises: the Law of March 9, 1934.—The Prombank.—The Vsekobank (Torgbank).—The Agricultural Bank and the agricultural credit system.—The Tzekombank and the municipal bank system.—The savings banks.

XVI. SUMMARY AND CONCLUSION 507

BIBLIOGRAPHY 525

INDEX 545

TABLES

1. Monetary Circulation and Gold Reserves, 1897–1914 . 16
2. Changes in Loans, Discounts, and Deposits of the State Bank, 1861–1914 18
3. Loans and Discounts of the Various Russian Banks Outstanding at the Beginning of the Years 1909–14 . 19
4. Principal Balance Sheet Items of the Joint-Stock Commercial Banks, 1875–1914 21
5. Total Mortgage Indebtedness of Owners of Rural Lands to the Nobles' State Land Bank, the Peasants' Land Bank, and Private Mortgage Banks . . . 25
6. State Receipts and Expenditures, 1914–17 . . . 34
7. The Changes in the Balance Sheet Items of the State Bank, 1914–17 37
8. Combined Balance Sheet Accounts of the Joint-Stock Commercial Banks, 1914–17 45
9. Indices of Foreign Exchange, Price Level, and Currency Circulation, 1914–17 49
10. Receipts and Expenditures, 1918–20 75
11. The Volume of Notes in Circulation, 1917–22 . . 76
12. The Kinds of Currency in Circulation, 1918–21 . . 81
13. Foreign Exchange Rates, 1918–20 85
14. Gold Ruble Rates, 1918–21 87
15. Indices of Currency Circulation and Prices, 1918–22 . 91
16. Percentage Increase in the Volume of Currency and Prices, 1914–21 92
17. The Purchasing Power of the Total Volume of Paper Money, 1914–22 93
18. Revenues in 1918–21 95
19. Issue, Increase, and Purchasing Power of Treasury Notes (or Sovznaks, or Soviet Rubles), 1921–22 . . 128
20. State Revenues in 1922 130

21. The Penetration of Banknotes into Circulation, 1923–24 157
22. The State Bank of the U.S.S.R. Firm and Bank Cover, 1922–24 159
23. Rates on Dollars, Sterling, and Gold Coin in Chervonetz-Rubles, 1923–24 162
24. The Price Level and the Purchasing Power of the Chervonetz, 1923–24 168
25. The Disparity between Agricultural and Industrial Prices, or the "Scissors," 1922–25 173
26. Rates of Chervontzy, Dollars, Sterling, and Gold in Terms of Soviet (Treasury) Notes, 1922–24 . . . 182
27. Soviet Notes in 1923–24 186
28. Circulation of 1922–24 Expressed in Pre-War Rubles . 191
29. Revenue Yielded by Treasury Notes, 1917–24 . . 193
30. Foreign Trade of the U.S.S.R., 1918–1927/28 . . 210
31. Banknote Issue in 1924–25 226
32. The Volume of Means of Payment in 1924–25 . . 227
33. Relative Increase of Means of Payment, Output of Large-Scale Industry, Trade Turnover, and Carloadings, 1924–26 228
34. Wholesale and Retail Price Indices, 1924–25 . . 230
35. Absolute and Relative Distribution of Treasury Notes in Circulation by Denominations, 1924–25 . . . 235
36. Unified State Budget of the U.S.S.R., 1924/25–1927/28 242
37. Balance Sheets of the State Bank of the U.S.S.R., 1923–28 246
38. The State Bank's Deposits and Loans and Discounts, 1924–28 252
39. Total Currency in Circulation and Bank Cover, 1924–28 255
40. Total Means of Payment, Trade Turnover, Price Indices in 1924–28 257
41. Moscow Foreign Exchange Rates on New York, London, Paris, Berlin, in 1928 264
42. Comparison between Balance Sheets of the Imperial State Bank and of the State Bank of the U.S.S.R., 1914–28 271
43. The Credit Plans of the State Bank and Actual Performance, 1926/27–1927/28 279

44. The Development of Credit Institutions in the U.S.S.R., 1922–28 284
45. Principal Items in the Balance Sheets of the Prombank, 1923–28 289
46. Movement of the Principal Accounts of the Electrobank, 1925–27 294
47. Principal Accounts of the Vsekobank, 1923–28 . . 298
48. Movement of the Principal Items in the Balance Sheets of the Central Agricultural Bank, 1924–28 . . . 304
49. Principal Accounts of the Mosgorbank, 1923–28 . . 309
50. Principal Accounts of the Tzekombank, 1925–28 . . 311
51. Detailed Analysis of the Loans and Resources of the Entire System of Municipal Credit, 1926–28 . . 314
52. Principal Accounts of the Vneshtorgbank, 1924–28 . 317
53. The Growth and Decline of the Mutual-Credit Societies, 1923–28 320
54. Private Trade in 1926/27–1929/30 323
55. Savings Banks: Distribution of Costs, 1913 and 1924–25 327
56. Savings Banks: Movement of Deposits, 1924–29 . . 328
57. Foreign Trade of the U.S.S.R., 1928–34 . . . 335
58. Balance Sheets of the State Bank of the U.S.S.R., 1929–32 372
59. Unified State Budget of the U.S.S.R., 1928/29–1932 . 406
60. The Balance Sheets of the Issue Department of the State Bank of the U.S.S.R., 1928–35 408
61. Notes and Coins Placed in Circulation by the People's Commissariat of Finance of the U.S.S.R., 1928–35 . 410
62. Total Currency in Circulation and Retail Trade, 1928–35 412
63. Banknote Issue and Firm Cover 415
64. Production of Gold in the Soviet Union . . . 417
65. Principal Accounts of the Vsekobank, 1929–30 . . 469
66. The Vsekobank: Balance Sheet Items as of January 1, 1933 472
67. The Investments and Deposits of the Agricultural Bank in 1934 and 1935 484
68. The Savings and State Credit System, 1928–33 . . 503

BANKS, CREDIT, AND MONEY IN SOVIET RUSSIA

I

BANKS, CREDIT, AND CURRENCY BEFORE 1860

THE history of money and banking in Russia can be conveniently divided into four periods: the period before 1860; that between 1860 and 1914; the period between 1914 and the November, 1917, Revolution; and, finally, the postrevolutionary period. The present chapter deals with the early period.

Debasement of coins.—The inflation that took place in Russia during the World War and after is not the only blemish on the monetary history of that country, which is the history of a currency that suffered from chronic depreciation until the very end of the nineteenth century.

The Russian government, like governments of other countries, learned to tamper with the medium of exchange at an early date.[1] In the sixteenth century, for instance, the Russian government recoined foreign money at a profit of 100 percent. In the seventeenth century Czar Alexei (1645–76) managed to turn copper worth 5 rubles into coins whose nominal value was 312 rubles. As a result one silver ruble began to command 17 copper rubles in exchange.[2] The "flight" from the rapidly depreciating copper coins, the rebellions and unrest accompanying it, led in 1667 to the coining of more silver money. By a process of devaluation the government gave effect to the then prevailing rate of exchange between silver and copper coins.

During the reign of Peter the Great (1689–1725) the silver ruble

[1] Kovalevsky, ed., *Russia at the End of the 19th Century* (St. Petersburg, The Ministry of Finance, 1900), p. 794. In the early period of Russian history skins, leather, and silver slugs were used as money. By the eighth century such trading cities as Pskov and Great Novgorod used foreign coins. From the thirteenth century (while Russia was under the Mongolian yoke) there were in circulation Russian coins made of silver and copper. The coins were called *dengi* (the Russians adopted this word for money in general) and *copeiki* (copecks). The count was in terms of *grivny* which was a measure of weight (applied, e.g., to a piece of silver). The fact that the silver had to be cut into smaller pieces, perhaps accounts for the name of the Russian monetary unit "ruble" (from *rubit*—to cut).

[2] I. Ozerov, *Principles of Fiscal Science* (Riga, 1923), I, 227.

was debased by about 42 percent.[3] A pud of copper, which in 1700 yielded less than 13 rubles, was made to yield 40 rubles.[4] The debased copper coins drove out of circulation all other coins and retained the position of the most important medium of exchange until the beginning of the reign of Catherine II (1762–96).

The assignats.—The introduction of paper money had been projected by Peter the Great, but it was not until 1769, during the reign of Catherine II, that the first paper money, the assignat, was introduced. In that year there were established by the government two assignat banks, one in St. Petersburg, and another in Moscow, with a capital of 500,000 copper rubles each.[5] Against their combined metallic fund the government issued 1,000,000 rubles in assignats. Those banks stood ready to redeem assignats in copper coin. The ease with which such money could be obtained led the treasury to increase those issues. In 1777 their redemption was discontinued.

Despite the decree of 1784 that there must never be issued more than 20,000,000 rubles in assignats, and despite the decree of 1786, which raised the maximum to 100,000,000 rubles, the volume of assignats continued to mount rapidly. In 1795 their volume amounted to 150,000,000 rubles; in 1800, to 212,500,000; and by 1817, after the Napoleonic War, to 836,000,000 rubles.

It is therefore not surprising that the assignat's purchasing power dropped very low. Even in 1810, that is, before Napoleon's advance into Russia, when the country had only 533,000,000 rubles in circulation, a ruble in silver commanded about 4 rubles in assignats. As a result of such progressive depreciation of the ruble "prices rose very high, property relations lost their bases, credit transactions were rendered exceedingly difficult, production took on a speculative character, and the very foundation of the economic life of the nation was shaken." [6]

The early monetary reforms.—To remedy the above evils the

[3] I. I. Kaufman, *The Silver Ruble in Russia, from Its Beginning to the End of the 19th Century* (St. Petersburg, 1910), p. 150.

[4] H. Parker Willis, "Monetary Reform in Russia." *Journal of Political Economy* (June, 1897), p. 280. Also Kaufman, *op. cit.*, pp. 129, 149.

[5] In 1786 the two banks were replaced by the Imperial Assignat Bank.

[6] *Ministry of Finance, 1802–1902* (St. Petersburg, 1902), Pt. 1, p. 62.

government, in the early part of 1810, adopted the plan of the well-known statesman M. M. Speransky and proclaimed the silver ruble the monetary unit of the land. The issuance of assignats was to be discontinued. But the War of 1812 put an end to all intended reforms and led to the removal of Speransky.

In 1817 the new Minister of Finance, D. A. Guriev, renewed the attempt to improve the position of the ruble. By means of loans the total volume of assignats was reduced from 836,000,000 rubles in 1817 to 595,776,310 in 1823, that is, by 28 percent. There followed, however, very slight improvement in the market rate of the assignat. Instead of commanding 25 1/6 silver copecks as in 1817, it could now be exchanged for 26 2/5 silver copecks, an increase of merely 5 percent in value.

Considering such attempts unwise and too costly, Guriev's successor, E. F. Kankrin, in 1823 stopped the further withdrawal of assignats from circulation. He proceeded, however, to pave the way for more thorough reforms. On July 1, 1839, the silver ruble was once more proclaimed the standard monetary unit, and a fixed and unvariable relationship was established between it and the paper money (3.5 assignat rubles to one silver ruble). Next, the state issued on July 1, 1841, a new type of paper money, so-called "credit notes." In 1843 the 595,776,310 "assignat" rubles were exchanged for 170,221,800 rubles in silver coin and in credit notes.[7]

The Crimean War (1853–56) caused the volume of credit notes to expand from 311,400,000 in 1853 to 735,300,000 by the end of 1857. Specie payment was suspended, and the cycle of inflation was repeated.[8]

It was not before the Reform of 1897 and the introduction of the gold standard that the country became endowed with a stable currency.

Early banking.—The early banks were of a very rudimentary nature. Nor could they be otherwise, inasmuch as until 1861, the year in which the serfs were emancipated, Russia lived under

[7] *Ibid.*, pp. 197, 215. The Assignat Bank passed out of existence in 1847, and all its affairs and assets were transferred to the State Credit Notes Chancellery.

[8] *Ibid.*, pp. 261-62.

a more or less self-sufficing serf economy. Trade and industry could play, relatively speaking, but a subordinate part in such an economy.

The State Loan Bank for the Nobility and the State Commercial Bank, 1754.—In 1754 the state had established two banks which it owned and managed, one a State Loan Bank for the Nobility, the other a State Commercial Bank. The former was instructed to grant long-term credit to the landed aristocracy against their estates, and the latter to grant against their merchandise loans to merchants trading in the port of St. Petersburg. Those banks, however, did not follow the precepts of sound banking. They granted loans to those who wielded influence; so common was this practice that in 1762 the government let it be known that the Commercial Bank was not being operated as it should be, "for the benefit of the whole society," and that the loans granted by it were still in the hands of the first borrowers. In 1770 the Commercial Bank was ordered to stop lending, and in 1782 it was closed altogether. Its assets were transferred to the Loan Bank for the Nobility. The latter terminated its existence four years later (in 1786). Mismanagement, complete absence of good book-keeping, and the granting of unsecured loans were given as the reasons.

The State Loan Bank, 1786.—The place of the Loan Bank for the Nobility was at once taken by a reorganized institution known as the State Loan Bank. Its purpose, as stated in the imperial decree, was to protect trade, and especially agriculture, so as to enable each landed proprietor to retain his estate, improve it, and create a perpetual income for his family and descendants. The loans to the landed aristocracy constituted the main assets of the bank. It was, of course, to be expected that in a country living under a serf economy loans to the landowning classes would predominate. Favoritism, however, continued to be the basis for the extension of loans. The records of the Ministry of Finance show that in the first quarter of the nineteenth century Guriev recommended the closing of the bank, inasmuch as it was difficult to get the borrowers to repay the loans. Indeed, when the bank was granting loans to the nobility, it, as well as the government,

knew that "it may be for years and it may be forever." "Although the borrowed funds are not always used for productive purposes," said Kankrin before the Imperial Council when Guriev recommended the closing of the bank, "nevertheless it is essential to maintain the estates of the nobility." [9] So the bank continued in the old ways. At the end of 1820, for instance, of the total loans granted by it less than 10,000,000 rubles were secured, while loans in excess of 23,000,000 rubles were granted on the strength of special imperial orders. In 1854 the latter type of loan constituted about 300,000,000 rubles out of a total of 341,000,000 rubles.[10]

Charitable boards, widows' banks, 1763–73.—The State Loan Bank, however, was not the only institution in Russia which granted loans to the landed aristocracy. As early as 1763–73 the government established a number of savings institutions known as "charitable boards," "widows' banks," and so forth, all of which had as their purpose the granting of aid to the nobility. In 1854 their deposits amounted to 575,000,000 rubles out of a total of 848,000,000 rubles for all credit institutions. Similarly, their loans in the same year constituted 581,000,000 rubles out of a total of 943,000,000 rubles by all credit institutions. The size of the loans granted by these banks generally depended upon the number of serfs or "souls" possessed by the borrower.[11]

The State Commercial Bank of 1817.—Continuing its efforts to aid trade and industry, the government established at the State Loan Bank in 1797 a Bill Discount Office, a Goods Mortgage Office, and an Insurance Office, the names of which explain the nature of the functions which they were called upon to perform. The old practice of favoritism, however, continued, and whatever loans were granted were monopolized by a few influential persons, who reloaned them at usurious rates.

A new attempt to aid trade and industry was made in 1817, when the government established the State Commercial Bank with a capital of 30,000,000 rubles. The bank was authorized to accept funds for deposit or transfer, to grant loans against merchandise, and to discount bills. The management of the bank

[9] *Ibid.*, p. 45. [10] *Ibid.*, pp. 45, 215. [11] *Ibid.*, p. 44.

no longer consisted exclusively of government officials, for a few merchants were admitted to the board, where they were to give "impartial advice and positive information." Its deposits increased from 3,000,000 rubles at the end of 1818 to 204,000,000 rubles in 1854. The discount of bills and the loans against merchandise, which at the close of 1818 amounted to 11,000,000 and 1,400,000 rubles, respectively, showed, however, but little activity. In 1854 they stood at 23,000,000 and 650,000 rubles, respectively. In 1858, that is, shortly before the liquidation of the old banks, the bank had 240,000,000 rubles in deposits and only 27,000,000 rubles in commercial loans and discounts—the rest (together with its own capital of 30,000,000 rubles) was transferred to the Loan Bank and thus placed at the disposal of the landed aristocracy.

The catastrophe of the late fifties.—As a result of the inflationary policies of the government during the Crimean War, the total deposits of the banks increased from 873,000,000 rubles at the beginning of 1855 to 1,276,000,000 rubles by the middle of 1857. Finding it difficult to invest the newly created deposits and yet being compelled to pay 4 percent interest on them, the banks turned to the Ministry of Finance for help. It so happened that at the same time some influential persons connected with a newly formed company for the development of Russian railroads were demanding that the Ministry of Finance should cause the savings of the people to be invested in their company. Instead of permitting the banks to invest a portion of their deposits in those securities, the government ordered them on July 20, 1857, to reduce the interest rate on deposits from 4 to 3 percent. At the same time the government guaranteed the securities of the railroads, on which 5 percent interest was being paid. This, together with the fact that during the second half of 1857 the formation of joint-stock companies began to gain momentum, caused the deposits of the banks to decrease from 1,276,000,000 rubles in 1857 to 970,000,000 rubles in 1859. The cash on hand during the same period fell from 140,000,000 rubles to 20,000,000 rubles. The banks and the government became alarmed, and not without reason. The banks had in their portfolios nothing but "frozen" assets consisting of long-term loans to the nobility and of loans

to the government.[12] To stem the tide of withdrawals the government resorted to a number of measures. For example, it banned for a time the formation of new joint-stock companies. Borrowing at the banks was made difficult and, finally, stopped altogether. The treasury placed at the disposal of the banks 77,000,000 rubles, printing some 33,600,000 rubles of credit notes for that purpose. It also borrowed 12,000,000 pounds sterling abroad and about 23,000,000 rubles at home (by means of 4 percent income-bearing certificates). The run, however, continued. It was then decided to liquidate the old credit institutions which seemed to have outlived their usefulness.

On September 1, 1859, the government ordered the banks to issue to holders of certificates of deposit so-called "5 percent bank notes." The State Loan Bank was closed on May 31, 1860, and all of its affairs were transferred to a government savings institution (*Sochrannaia Kazna*) in St. Petersburg. The various savings institutions were directed to wind up their affairs. They were likewise instructed to turn over all collections to the new bank (the State Bank) which was to come into existence on May 31, 1860. It was also ordered that to the new State Bank, upon which devolved the responsibility for the old deposits, should be transferred all of the affairs of the old State Commercial Bank.

It may be added that even without this financial panic, which demonstrated the disadvantages of unsound banking methods, a change in the Russian credit system would have become imperative because of the growth of trade and industry and the contemplated abolition of serfdom—that is, because of changes in the economic and social conditions.

[12] By January 1, 1858, the treasury owed the banks 521,000,000 rubles, of which 218,000,000 rubles was borrowed during 1854–57 for military purposes.

II

BANKS, CREDIT, AND CURRENCY, 1860–1914

The organization of the imperial State Bank in 1860.—The State Bank (Gosudarstvennyi Bank), the bank destined to play the rôle of a central bank in Russia, came into existence on May 31, 1860, as a product of the reorganization of the old State Commercial Bank. Its purpose as stated by the government was "to promote trade and to stabilize the currency." [1] It was owned, like the previous credit institutions, by the state, which placed its original capitalization at 15,000,000 rubles and which instructed it to accumulate a reserve of 3,000,000 rubles, permitting it to set aside for that purpose not more than one-third of its profits annually.[2] The bank was placed under the jurisdiction of the Minister of Finance, who directed its general policies. The immediate management of the bank, however, devolved upon a manager, or "governor" (appointed by the Czar), and a council.[3]

Its original statutes authorized it to discount commercial paper; to grant loans against precious metals, merchandise, and government and government-guaranteed securities; to accept time and demand deposits; to buy and sell gold, silver, and securities; and to make money transfers.[4]

Dissatisfaction with the progress made by the bank in promoting trade, industry, and agriculture resulted in a complete revision of those statutes in 1894. At that time the bank was given the right to accept time and demand deposits; to discount

[1] *Ministry of Finance, 1802–1902,* Pt. 1, p. 437.

[2] *Ibid.* The capital of the bank grew so that by 1879 it was 25,000,000 rubles and by 1894, 50,000,000 rubles, while the reserve was increased to 5,000,000 rubles, at which level it remained until the bank was taken over by the Soviet government.

[3] The bank council included the manager, who acted as chairman, two of his assistants (vice-governors), the director of the Special Credit Chancellery, the manager of the St. Petersburg office of the bank, two representatives from the Ministry of Finance, and one from each of the following—state control, nobility, and merchants. Prior to 1894, in which year its statutes were amended, the bank was also supervised by the Council for the Imperial Credit Institutions.—*Ministry of Finance, 1802–1902,* Pt. 2, p. 46.

[4] *Ibid.,* Pt. 1, pp. 437-38. Also *Russia at the End of the 19th Century,* p. 824.

commercial paper with two or more names; to grant loans, directly and through middlemen, on government and private securities, on merchandise, bills of lading, and warehouse receipts; to grant loans on their real estate and other securities to those engaged in agriculture and industry with a view to providing a working capital; to grant loans for the purpose of buying agricultural and industrial machinery, accepting the articles so bought as security; to open special demand deposits against notes, collateral, and merchandise; to buy and sell securities, bills of exchange, domestic and foreign, precious metals, and so forth. Neither the original nor the revised statutes authorized it to issue banknotes, although, following the example of the Bank of England, the State Bank had a special section in its balance sheet that was devoted to the issue department where on one hand it showed the volume of notes in circulation, and on the other the amount of firm cover transferred to it by the state, and a claim against the treasury for the difference in those two accounts (that is, treasury debt).

The Monetary Reform of 1897.—Among the first difficulties with which the newly created State Bank was called upon to cope was the derangement of the currency. At that time Russia was in the throes of the financial and commercial crisis that came as an aftermath of the Crimean War.[5] Inflation, with all the attendant evils, was at its height. As is usually the case under such circumstances, high prices caused a decrease in the exports and an increase in the imports—that is, an unfavorable balance of trade. Since a large portion of the redundant paper currency was used for the purpose of buying securities, the prices of the latter soared and caused foreign investors to throw large blocks of those securities on the Russian market. All this led to a fall in the exchange rate of the ruble and to the export of precious metal from Russia. Metallic coins (even copper coins) were disappearing from circulation.

It was necessary to balance the budget by drastic reduction of

[5] The notes in circulation, which before that war amounted to 311,300,000 rubles, increased by the end of 1861 to 713,600,000 rubles, while the firm cover amounted to a little more than 80,000,000 rubles, that is, to 11.2 percent of the total volume of notes in circulation.—*The Ministry of Finance, 1802–1902,* Pt. 1, p. 461.

governmental expenditure and by increased taxation so as to render unnecessary the use of the printing presses for that purpose. It was also necessary to restrict imports and to stimulate exports so as to improve the position of the ruble on the foreign markets, arrest the flow of gold from Russia, and insure its counterflow.

The Minister of Finance, Reutern, selected, however, a different plan. By means of foreign loans the bank's gold reserve was raised in 1862 to about 25 percent of the volume of notes in circulation, and specie payment thereupon was resumed.[6] In November, 1863, however, Russia was once more on an irredeemable paper money basis. Also, as a result of the abortive attempt, the bank's gold reserve was seriously depleted. The treasury set out once more to accumulate a large gold reserve. But as a result of the Turkish War of 1877–78, the currency in circulation increased from 766,900,000 rubles at the beginning of 1877 to 1,150,000,000 rubles at the end of 1878. The paper ruble, which was valued in 1876 at 81.5 copecks in gold, was now valued at but 63.2 copecks, while in April, 1878, it was quoted on the London market at 22 to 25 pence—42.3 per cent below parity.

The new Minister of Finance, Bunge (1881–87), proposed the legalization of transactions in coin and the circulation of coins even at a premium. Like his predecessor, he believed that this would serve to promote trade and industry and so create a demand for the redundant paper currency, as well as to attract foreign capital. The Imperial Council, however, did not translate his opinion into law.

Both Reutern and Bunge considered it necessary to bring the rate of the paper ruble up to parity. Bunge's successor, Vyshnegradsky, believed that such procedure would lead to an increase in imports and a decrease in exports. To avoid this he proposed to devaluate the ruble, but no action was taken with respect to his proposal. Meanwhile, gold continued to accumulate.

S. Y. Witte, who had been appointed Minister of Finance in 1892, resorted to a series of measures resulting in the completion of the task of reorganizing Russia's currency, a task to which his

[6] *Ibid*, p. 463.

predecessors contributed no small amount of effort. He at once took steps to eliminate the danger from silver, which threatened to supplant the paper money, by bringing about the abrogation of its free coinage (imperial order of July 16, 1893).[7] To stop the assault against the paper ruble, all forward transactions in gold were prohibited. Furthermore, Witte was authorized to supervise the foreign exchange transactions of the various financial institutions. This, together with his successful campaign against short-sellers of the ruble on the Paris and the Berlin markets, caused the ruble's fluctuations to decrease considerably.[8] The paper ruble became stabilized at 66 2/3 copecks in gold—that is, one gold ruble commanded one and a half paper rubles in exchange.

Next, by a series of acts passed between 1895 and 1897, Witte introduced what is known as the Monetary Reform of 1897. Thus, on May 8, 1895, it was ordered that any lawful transactions might be expressed in terms of gold coin and that payments arising therefrom might take the form of gold or credit notes at the current rate of exchange.[9] On May 24 the State Bank was authorized to buy and sell gold at a fixed rate. The monetary unit was devaluated (Act of January 3, 1897) by one-third, and specie payment was resumed.[10]

The State Bank, which until then had no right to issue notes, was given that right on August 29, 1897 (imperial ukase). The volume of notes issued, according to the ukase, was to be strictly limited by the needs of circulation and was to be covered by half

[7] Due to the fall in the price of silver on the foreign markets, which was occasioned primarily by the monetary changes in a number of countries, the paper ruble commanded more in gold than the silver ruble. The irredeemable paper money was in danger of being supplanted by the "bad" silver money. Even as early as 1876 the paper ruble was valued at 81.5 copecks in gold, while the pure metal contents of a silver ruble (legally still the standard monetary unit) was valued at only 76.9 gold copecks. For a discussion of this see *Ministry of Finance,* Pt. 2, p. 180. Also H. Parker Willis, "The Monetary Reform in Russia," pp. 294-97.

[8] *Ministry of Finance, 1802–1902,* Pt. 2, p. 119.

[9] *Ibid.,* p. 410.

[10] It was ordered that the five- and ten-ruble gold coins which circulated at that time as equivalent to 7.5 and 15 rubles in credit notes, as well as pieces of similar weight and fineness coined in the future, be stamped 7.5 and 15 rubles, respectively. —*Ibid.,* pp. 412, 124-25.

its amount in gold when it did not exceed 600,000,000 rubles; credit notes for more than that amount were to be covered ruble for ruble by gold.[11] The introduction of the gold standard necessitated a change in the monetary statutes, which were framed when the country was on a monometallic silver basis. This was directed by a decree of June 7, 1899.[12]

In criticism of the manner in which the Monetary Reform was accomplished it may be pointed out that this was done in the face of budgetary deficits.[13] Furthermore, the foreign balance of payments during those years while favorable to Russia was not large enough to enable her to get along without loans. Yet, as has already been stated, the budget and the international balance of payments are of vital importance to any plan for monetary reform or stabilization of the currency.

In further criticism it may be stated that by permitting the old bank statutes to remain in force the government sanctioned practices likely to endanger the newly adopted gold standard. The bank, for instance, continued to be required to grant the treasury loans against a deposit of government bonds, as well as to be responsible for servicing government loans and in connection with certain other government transactions—a practice which could easily lead to inflation and to the suspension of specie payment.[14] The bank also retained its right to grant loans and to create deposits against stocks and bonds of business concerns, as well as against merchandise, bills of lading, warehouse receipts, and so forth. Yet a central bank and bank of issue must be very careful to keep its portfolio liquid because its obligations (notes and deposits) are payable on demand and also because it is the place of last resort to which other banks turn in emergencies.

[11] *Ibid.*, pp. 427-28. It may be interesting to note that on January 1, 1897, the total amount of gold held by the bank in Russia (904,800,000 rubles) and abroad (190,600,000 rubles) exceeded the volume of notes in circulation (1,067,900,000 rubles).

[12] *Ibid.*, p. 430. The gold ruble contained 17.424 *dolias* (11.94792 grains) of fine gold.

[13] *Ibid.*, pp. 646-49.

[14] See M. W. Bernatzky, "Monetary Policy of the Russian Government during the War," *Russian Public Finance during the War* (Yale University Press, 1928), pp. 346-48.

The gold standard, despite the faulty methods involved in its introduction, helped to inspire confidence and thus to attract foreign capital, which played a very important part in the economic growth of the country.

The State Bank as a central bank; its policy with respect to note issue, 1897–1914.—Even before the Monetary Reform of 1897, the State Bank acted as a fiscal agent for the treasury, served as a depositary for other banks, and in short performed certain functions which are characteristic of central banks. However, to insure the smooth working of the credit system, which may be said to be the main function of a central bank, it is necessary to exercise control over the volume of notes in circulation and the volume of credit granted. Both constitute purchasing power, and both therefore influence the value of the monetary unit and the price level of a country. It was, however, only in consequence of the Monetary Reform of 1897 that the bank was given the sole right of note issue and thus became a full-fledged central bank and bank of issue.

The bank's policy with respect to note issue was most conservative. It was on the whole successful in its desire to make the credit note a gold certificate. The Russo-Japanese War (1904–5) and the revolutionary outbreaks which swept the country during 1905–6 put, however, the gold standard to a severe test. Indeed, as can be seen from Table 1, the notes in circulation jumped from 578,400,000 rubles on January 1, 1904, to 1,207,500,000 rubles on January 1, 1906, and then receded to 1,194,600,000 rubles by the beginning of 1907. The gold reserve held by the bank within Russia on those dates amounted to only 734,000,000 rubles, 716,000,000 rubles, and 889,900,000 rubles, respectively. If the bank's claims to gold abroad be disregarded, then the bank might be said to have exceeded the legal limit of its fiduciary issue (300,000,000 rubles) in both 1906 and 1907. A large loan raised abroad enabled the government to avoid the suspension of specie payment, although a draft for that purpose was held in readiness.

Thereafter a steady improvement followed, and by January 1, 1914, the gold reserve in the bank's vaults amounted to 1,527,800,000 rubles as against a note circulation of 1,664,700,000 rubles.

TABLE I

MONETARY CIRCULATION AND GOLD RESERVES

JANUARY 1, 1897, TO JANUARY 1, 1914 [a]

(*In millions of rubles*)

January 1	*Gold Coins in Circulation*	*Silver Coins in Circulation*	*Credit Notes (i.e., State Bank Notes) in Circulation*	*Total Circulation*	*Gold Held by State Bank in Russia*	*Gold Held by State Bank Abroad*	*Total Gold Reserves*
1897	36.0	29.9	1,067.9	1,133.8	904.8	190.6	1,095.4
1898	147.8	78.9	901.0	1,127.7	1,146.8	17.4	1,164.2
1899	451.4	121.5	661.8	1,234.7	990.3	15.1	1,005.4
1900	641.3	145.3	491.1	1,277.7	833.4	5.4	838.8
1901	683.1	145.7	555.0	1,383.8	708.2	24.3	732.5
1902	694.2	140.3	542.4	1,376.9	682.2	18.6	700.8
1903	731.9	137.5	553.8	1,423.2	708.5	57.3	765.8
1904	774.8	133.2	578.4	1,486.4	734.0	169.0	903.0
1905	683.6	123.0	853.7	1,660.3	880.4	149.0	1,029.4
1906	837.8	133.4	1,207.5	2,178.7	716.0	203.8	919.7
1907	641.9	119.8	1,194.6	1,956.3	889.9	300.6	1,190.5
1908	622.4	119.6	1,154.7	1,896.7	948.5	219.8	1,168.3
1909	561.1	110.5	1,087.1	1,758.7	1,079.0	141.0	1,220.0
1910	580.9	112.5	1,173.8	1,867.2	1,173.6	240.9	1,414.5
1911	641.7	115.9	1,234.5	1,992.1	1,231.6	218.7	1,450.3
1912	655.8	117.6	1,326.5	2,099.9	1,259.3	176.9	1,436.2
1913	628.7	120.5	1,494.8	2,244.0	1,327.9	227.5	1,555.4
1914	494.2	122.7	1,664.7	2,281.6	1,527.8	167.4	1,695.2

[a] Based upon the *Annual Reports* (*Otchety*) *of the State Bank.*

The bank's loan and discount policy.—Prior to the nineties the loans and discounts of the bank suffered from a stunted growth. The bank, though, was not entirely to blame for this. From the very first day of its existence and for about thirty years thereafter, the bank was required to devote much of its effort and resources to the task of discharging the obligations of the old credit institutions as well as to the making of other disbursements for the account of the treasury. Besides, a great deal of its energy and resources were being devoted towards the accumulation of a large gold stock and the stabilization of the currency. Since the bank did not possess the right of note issue during those years, it is clear that the volume of its commercial loans could not be large.

Beginning, however, with the nineties, the treasury indebtedness to the bank underwent a rapid decline, while the treasury funds left on deposit with it underwent a rapid increase. This, together with its right of note issue, furnished it with adequate resources and enabled it to expand its commercial loans and discounts. As shown by Table 2, during 1881–85, when the treasury indebtedness to the bank averaged 831,000,000 rubles and the treasury deposits averaged 72,400,000 rubles, the bank's loans and discounts averaged but 230,700,000 rubles. During 1911–14, however, when the treasury indebtedness averaged but 31,000,000 rubles, and the treasury deposits attained an average of 833,100,000 rubles, the bank's loans and discounts averaged 907,400,000 rubles.

This expansion, however, did not come as a result of competition between the State Bank and other short-term credit institutions. The State Bank aimed, with a large degree of success, to become a bankers' bank and did not regard other banks as competitors. Indeed, when the industrial upswing of the nineties, with its ever-expanding activity in the development of basic industries, railroads, and so forth, was followed by a depression at the turn of the century, the bank at once came to the rescue of the private joint-stock commercial banks. It placed at their disposal additional credits and helped to organize a consortium of private bankers for the purpose of stabilizing security prices. To tide over those whom the joint-stock banks were pressing for payment during the crisis

and thus forcing into bankruptcy, the bank increased its own loans from 274,800,000 rubles in 1899 to 406,200,000 rubles in 1900 and to 561,000,000 rubles in 1902.

This was repeated in 1904–6 when, due to the flight of capital from the country during the Japanese War and the Revolution, Russian bankers and industrialists were once more hard hit. The

TABLE 2

CHANGES IN LOANS, DISCOUNTS, AND DEPOSITS
1861–1914 [a]
(*In millions of rubles*)

January 1	*Loans and Discounts*	*Treasury Indebtedness to Bank*	*Deposits and Other Funds of the Treasury Left with the Bank*	*Savings Banks' Balances with the State Bank*	*Other Time and Demand Deposits*
1861–65	49.1	710.8	41.6	4.5	123.7
1866–70	79.6	706.1	46.7	0.6	174.0
1871–75	92.8	630.8	30.6	0.4	193.9
1876–80	204.0	819.8	43.9	0.7	247.9
1881–85	230.7	831.0	72.4	0.5	253.5
1886–90	234.8	634.8	140.7	1.5	269.1
1891–95	248.0	464.8	210.9	39.8	219.4
1896–1900	348.1	156.3	428.1	35.8	198.1
1901–5	483.5	2.3	447.6	61.2	219.0
1906–10	568.2	23.6	361.8	35.5	245.5
1911–14	907.4	31.0	833.1	17.8	262.2

[a] Based upon the *Annual Balance Sheets of the State Bank.*

bank's loans and discounts rose from 410,400,000 rubles on January 1, 1905, to 776,800,000 rubles on January 1, 1906. As before, the bank stood ready to curtail the volume of its loans and discounts as soon as the emergency was over.

The bank's rôle as a bankers' bank was rapidly growing more important. In 1909, for example, more than 50 percent of the

total credit of 1,916,000,000 rubles granted by the State Bank during the year went to bankers. In 1913, however, the share of the latter in the 6,166,000,000 rubles credit extended by the bank during that year reached almost 75 percent.[15]

Although the State Bank did not seek to compete with other banks it nevertheless furnished an appreciable part of all the credits granted in the Russian money market. As shown by Table 3 its loans and discounts outstanding at the beginning of each year during 1909–14 constituted about one-fifth (20 percent) of the

TABLE 3

LOANS AND DISCOUNTS OF THE VARIOUS RUSSIAN BANKS OUTSTANDING AT THE BEGINNING OF THE YEARS 1909–14 [a]

(*In millions of rubles*)

	1909	*1910*	*1911*	*1912*	*1913*	*1914*
The State Bank	502	466	667	924	967	1,072
The joint-stock banks	1,197	1,440	2,076	2,403	2,890	3,162
Mutual-credit societies	316	371	509	688	794	813
Municipal banks	144	153	166	189	211	232
Total	2,159	2,430	3,418	4,204	4,862	5,279

[a] *Balance Sheets of the State Bank; Consolidated Statements of the Joint-Stock Commercial Banks;* also Mukoseyev, *Money and Credit*, pp. 384-85; and Bernatzky, *Monetary Policy*, p. 357.

total. Those of the joint-stock banks amounted in 1909 to 55 percent and in 1914 to 60 percent of the total.

The discount rate of the State Bank was generally much higher than the rates of other European central banks. It was not unusual for the rate to be twice as high as that in London or Paris, and about 1 or 1½ percent higher than the Berlin rate. Russian industry, it must be borne in mind, despite its late start, was developing very rapidly and demanded a larger fixed and working capital than the savings of the country would permit, thus making it necessary to attract funds from wealthier nations.

[15] *Vestnik Finansov*, No. 25, 1914, p. 556.

The Commercial and Investment Banks

The joint-stock commercial banks.—The most important and dominating group among Russian credit institutions was that of the joint-stock commercial banks. The first joint-stock commercial bank, the St. Petersburg Private Commercial Bank, came into existence in 1864 not only upon the initiative of the State Bank but aided by the latter's purchase of one-fifth of its capital stock. Between 1864 and 1873 there sprang up thirty-one such banks.[16] The number did not increase materially, for as late as 1912 there were only 34 of them. Their branches, however, increased quite rapidly, and by January 1, 1914, Russia had 47 such banks together with 743 branches. They helped to mobilize the savings within the country as well as to attract funds from foreign lands. Their development and their activities can be seen best from an examination of some of their most important accounts.[17]

The figures in Table 4 show that the end of the nineteenth century and the beginning of the twentieth century marked a new era of development for the commercial banks. Especially rapid was that development after the depression which followed the Russo-Japanese War and the Revolution of 1905–6. It is interesting to note that of the 3,162,000,000 rubles of loans and discounts on January 1, 1914, almost 1,000,000,000 rubles were backed by securities. In addition, the banks owned on that day 315,000,000 rubles' worth of securities. Furthermore, not less than four-fifths (or about 1,250,000,000 rubles) of the "correspondents" account on the assets side represented syndicate participations, ownership of securities, and extension of other forms of credit to enterprises in which the banks were directly interested.[18] The Russian banks were in this respect following the precepts of the German banks. They conducted both commercial and investment banking under the

[16] *Ministry of Finance, 1802–1902,* Pt. I, p. 440.

[17] *Consolidated Balance Sheets of the Joint-Stock Commercial Banks.*

[18] Epstein, *Les Banques de commerce russes,* p. 24. Also Gindin, *Banks and Industry in Russia,* p. 71. The "correspondents" account on the liabilities side represented largely (about four-fifths of the total) funds of "others" (Russians and foreigners) placed at the disposal of the banks.

same roof, thus resorting to a practice which caused a large portion of their assets to become illiquid and which, therefore, endangered the deposits of their clients.

The ownership of stock and control of business enterprises by banks had yet another aspect—the granting of commercial loans for the purpose of enabling those enterprises to warehouse the

TABLE 4

PRINCIPAL BALANCE-SHEET ITEMS OF THE JOINT-STOCK COMMERCIAL BANKS; 1875–1914

(*In millions of rubles on the first of the year*)

	1875	*1885*	*1895*	*1900*	*1905*	*1910*	*1912*	*1914*
Assets								
Commercial discounts	240	157	205	406	632	837	1,240	1,546
Loans on securities	113	131	231	274	250	331	633	998
Loans on merchandise	20	6	20	34	67	183	338	319
Loans on commercial paper	...	0 9	5	19	49	88	191	298
Total loans and discounts	374	295	461	734	999	1,440	2,403	3,162
Correspondents	130	96	192	282	315	431	818	1,471
Securities (owned by the banks)	12	24	52	109	108	147	244	315
Capital and Liabilities								
Capital and reserves	108	120	174	275	269	332	560	836
Total deposits	300	219	308	548	776	1,262	1,817	2,539
Correspondents	102	91	223	293	439	529	986	1,458

commodities and hold out for higher prices, rather than for the purpose of facilitating the exchange of those commodities.

The joint-stock commercial banks established close ties not only with commercial and industrial enterprises, but also with foreign financiers. In fact, a considerable portion of their capital stock was held by foreign bankers.[19] The sale of their stock abroad en-

[19] Ronin, *Foreign Capital and Russian Banks*, ch. IV. During 1907–9 German ownership of stock in Russian banks amounted to about 22,000,000 rubles, or to 81.5 percent of the total Russian bank stock sold abroad, while French ownership

abled Russian banks to increase their capital, and this in turn made possible larger loans to industry. Of great importance to Russian industry were also the short-term credits obtained from abroad through those banks. Thus, despite their many shortcomings, the joint-stock commercial banks were largely instrumental in making possible the rapid development of Russian commerce and industry. In this they were helped by the State Bank and by the Ministry of Finance, which were always ready to come to their rescue in an emergency.[20]

Municipal banks and mutual-credit societies.—Besides the joint-stock commercial banks there were two other types of banks granting short-term credit and therefore operating in the money market—the municipal banks and the mutual-credit societies.

The municipal banks were small banks under the administration of town councils. They were authorized to receive deposits, to grant short-term credit against securities and real estate, and to grant loans to municipalities. The minimum capital for such banks was fixed at 10,000 rubles, and their total liabilities could not be greater than ten times their capital and reserves. They functioned quite unsatisfactorily, either because of the incompetence of the managers whose appointment depended upon the town councils,

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amounted to 5,000,000 rubles or 18.5 percent of the total stock sold abroad. In the years 1910–13, however, was witnessed a significant shift in that relationship, for although the ownership of Russian bank shares in Germany rose to 87,500,000 rubles, that in France rose to 128,500,000 rubles so that the relative holdings of those shares in Germany and France became respectively 38.8 percent and 56.8 percent of the total Russian bank shares sold abroad. By the beginning of 1914 French financiers were able to wield their "influence" over a number of Russian banks, the combined capital stock of which amounted to 45 percent of the capitalization of all joint-stock commercial banks. The ownership of Russian bank stock, it must be remembered, offered not only an opportunity to invest idle funds but also a link with Russian industry whereof large blocks of shares were held by the Russian banks.

[20] The banks, however, resented and circumvented (as in the case of the disguised "correspondents" accounts) the many regulations imposed upon them by the state. Thus, according to the laws of 1872 and 1883 their minimum capital was set at 5,000,000 rubles; their primary reserves consisting of cash on hand and on deposit in the State Bank had to be at least 10 percent of their liabilities; no more than 1/10 of the banks' capital stock could be loaned to one party, while the ratio of their liabilities to their capital and reserves was required to be greater than 5 to 1. *Ministry of Finance, 1802–1902,* Pt. 2, p. 72. Also Mukoseyev, *Money and Credit,* pp. 382-83.

or because of their political corruption which resulted in the granting of loans to those who controlled political sinecures.[21] As a result quite a number of them had to be closed. On January 1, 1914, Russia had 319 such banks with a combined capital and reserves of 59,700,000 rubles, with deposits amounting to 198,400,000 rubles, and loans and discounts, to 232,000,000 rubles.

The mutual-credit societies were institutions organized on a co-operative basis the purpose of which was to grant short-term credit to the small tradesman and artisan. The funds paid by the members—10 percent of what they expected to borrow—furnished the societies with working capital. Their number increased from 117 in 1900 to 467 in 1910, to 776 in 1912, and to 1,108 in 1914 (in each case on the first of the year). Their banking operations, too, experienced a rapid growth. Thus their capital and reserves increased from 38,000,000 rubles on January 1, 1900, to 73,500,000 rubles ten years later, and to 150,900,000 rubles on January 1, 1914. Their deposits increased from 168,300,000 rubles to 329,500,000 rubles, and to 595,400,000 rubles, respectively, on the first day of 1900, 1910, and 1914. Their loans and discounts on the last-mentioned dates were 204,400,000 rubles, 371,000,000 rubles, and 813,000,000 rubles, respectively.[22]

Mortgage banking.—As might be expected land credit in an agricultural country like Russia was well developed. It was carried on by the ten joint-stock land banks which sprang up during 1871–73, by the two state banks—one for the landed aristocracy (the Nobles' State Land Bank), the other for the peasantry (Peasants' Land Bank), and by some forty other banks, most of which were co-operative land banks.

The joint-stock land banks substituted their own credit for that of the borrower by giving him a mortgage bond that ran from ten to sixty-six years and that was issued by them in exchange for his own mortgage and by charging him a higher rate than they themselves undertook to pay on their bonds (4½ percent). The borrower paid about 6 percent interest and in addition bore the loss resulting from the sale of the bond below its face value.

[21] *Ministry of Finance, 1802–1902,* Pt. 2, pp. 73-75.
[22] See Mukoseyev, *op. cit.,* p. 384.

The nominal value of the bonds of those banks outstanding on January 1, 1914, was more than 1,250,000,000 rubles.

The Nobles' State Land Bank was founded in 1885 for the purpose of granting long-term credit to the nobility. Until 1889 the bank charged a 2 percent commission for selling the bonds which it substituted for the borrowers' mortgages, but after that date it discontinued those charges and even refunded such commissions to those who had paid them in the past. Thus the Nobles' Bank offered the nobility credit at much lower rates (5 percent per annum covered all costs) than the private banks did. Moreover, the impoverished and indebted nobility was from time to time accorded special favors in the form of still lower interest rates, renewals, and the writing off of arrears. Instead of granting loans for productive purposes only and on the amortization plan, the bank was granting long-term loans for what frequently turned out to be the satisfaction of the landlords' needs as consumers accustomed to a relatively high standard of living. The bank was, of course, actuated by a desire to save the nobility from ruin, but its policy merely encouraged waste and extravagance. Many of the nobility borrowed all that could be obtained from the bank on first mortgages; and after that was consumed, from private banks at high rates on second and third mortgages; and finally, when no more could be borrowed, they would sell their heavily mortgaged land to peasants. The activities of the bank from 1904 to 1913 were quite stagnant especially when compared with the activities of the Peasants' Bank and other land banks. That is illustrated by the figures in Table 5.

Whereas the total loans granted by the Nobles' State Land Bank and the acreage mortgaged to it decreased over the period under review, the loans of the Peasants' Land Bank over the same period of time tripled, and the acreage mortgaged to it doubled. The reason is clear. The Peasants' Bank organized in 1883 as a state-owned institution (similar to the Nobles' Bank) was facilitating the purchase by the peasantry of lands from the nobility, and beginning with 1895 the Peasants' Bank was even instructed to buy such land for its own account with a view to

reselling it later to peasants.[23] Following the agrarian unrest the activities of the bank were further widened to include loans to the full value of the land to be purchased (law of Nov. 3, 1905) and to grant loans on original land allotments (law of Nov. 15, 1906).[24]

The state savings banks.—Organized under the law of 1862, these banks steadily increased in number from 6,400 in 1903 to more than 8,000 in 1912.[25] The savings on deposit with them increased from 860,000,000 rubles at the beginning of 1904 to

TABLE 5

TOTAL MORTGAGE INDEBTEDNESS OF OWNERS OF RURAL LANDS TO THE NOBLES' STATE LAND BANK, THE PEASANTS' LAND BANK AND PRIVATE MORTGAGE BANKS, TOGETHER WITH THE AREA MORTGAGED [a]

(*In millions of rubles and millions of acres*)

Date	*To the Nobles' Bank*		*To the Peasants' Bank*		*To Private Banks*	
	Area Mortgaged (acres)	Indebtedness	Area Mortgaged (acres)	Indebtedness	Area Mortgaged (acres)	Indebtedness
Jan. 1, 1904.....	47.25	729	18.63	380	89.1	950
Jan. 1, 1909 ...	40.77	665	27.27	696	94.5	1,053
Jan. 1, 1912	38.34	709	38.88	1,151	101.79	1,258

[a] *Ministry of Finance, 1904–1913*, Table 32.

1,283,000,000 rubles in 1909 and to 1,595,000,000 rubles on January 1, 1913. On January 1, 1913, the savings fund was invested by those banks as follows: 38 percent in government securities; 21 percent in railway bonds; the rest in bonds issued by the land banks.[26]

There were also a number of small credit institutions in the rural communities, small *Zemstvo* banks, various credit co-operatives, pawnshops, and so forth.

[23] *Ministry of Finance, 1802–1902*, Pt. 2, pp. 58-65, 384. Also *Ministry of Finance, 1904–1913*, Section on Mortgage Credit.

[24] A. D. Bilimovich, *The Land Settlement in Russia and the War*, pp. 319-22.

[25] *Vestnik Finansov*, No. 3, 1914.

[26] *Ibid.*, No. 5, 1914.

Conclusion.—The Russian credit institutions did not in the years preceding the World War develop to a point where, without the aid of foreign financiers, they could take care of the needs of the country for fixed capital and for short-term funds. The Russian capital market was but weakly developed. Of the 5,200,000,000 rubles of new issues of Russian securities brought out during the years 1908–12, for instance, some 30 percent were marketed abroad.

Nevertheless, the deposits in the savings banks, as seen above, showed a decided increase. The total capital of the joint-stock commercial and industrial enterprises, which at the end of 1900 amounted to 1,000,000,000 rubles, increased by the end of 1908 to 3,100,000,000 rubles and by the end of 1911 to 3,500,000,000 rubles. The volume of commercial loans and discounts granted by the State Bank, commercial banks, mutual-credit societies, and municipal banks, which on January 1, 1909, amounted to 2,200,000,000 rubles increased by January 1, 1914, to 5,300,000,000 rubles. The development of the capital and money market was, however, stopped short by the World War.

III

BANKS, CREDIT, AND CURRENCY, 1914–17

The severe test to which Russia's economic system was subjected by the World War.—Pre-war Russia depended to a considerable extent upon foreign capital. Included in her balance of international payments there were some 400,000,000 rubles paid on account of indebtedness to foreign investors.[1] It was with the assistance of foreign capital that Russian joint-stock commercial banks were able to render the services of commercial and investment bankers to the many enterprises in which they were interested, to acquire control over them, and to help them form monopolistic combinations. Foreign capital was also prominent for its direct participation in the financing of various Russian undertakings.[2]

Pre-war Russia depended not only upon foreign capital but also upon foreign commodity markets. During 1909–13 her imports averaged 1,139,000,000 rubles and her exports 1,501,000,000 rubles annually.[3] In 1913, the last peace year, her imports amounted to 1,374,000,000 and her exports to 1,520,000,000 rubles. Paradoxical as it may seem, 48.6 percent of her imports in the latter year con-

[1] *Vestnik Finansov,* No. 17, 1914, p. 196, and *The Stock Exchange Official Intelligence,* London, 1914. But see also M. Bernatzky, *Monetary Policy of the Russian Government during the War* (Yale University Press, 1928), pp. 350 ff. Half the above amount was in connection with the service of government loans, about 40,000,000 rubles on account of railroad securities, and some 100,000,000 rubles represented remittances by Russian banks to financial houses abroad on account of loans obtained from them or investments made by them.

[2] Out of an aggregate joint-stock capital of 4,000,000,000 rubles invested in Russian industry, about one-third (1,343,000,000 rubles) belonged to companies registered as "foreign." See Zagorsky, *State Control of Industry in Russia during the War,* p. 16. It must be borne in mind, however, that foreign capital was also invested in companies registered as "domestic." P. V. Ol, an authority on the subject (*Foreign Capital in Russia,* Moscow, 1922, pp. 290-91), estimates the total foreign investments in Russian industry, banks, and other undertakings at 2,250,000,000 rubles. Of this total 32.6 percent was of French origin; 22.6 percent, of English; 19.7 percent, of German; 14.3 percent, of Belgian; and 5.2 percent, of American.

[3] Department of Customs, *Review of Russian Foreign Trade,* Year-books. Also Central Statistical Administration, *Trudy,* VII, Pt. 2, p. 2. For a thorough analysis of Russia's foreign trade from 1904 on, see *Vestnik Finansov,* No. 9, 1916, pp. 345-50. But see Zagorsky, *op. cit.,* pp. 15-16.

sisted of raw materials and semi-manufactures.[4] The textile industry, for instance, for whose products there was a tremendous demand, was importing some 50 percent of its raw cotton. The wool and the silk industries depended upon the importation of foreign raw materials. Even such indispensable raw materials as coal, iron, and oil, of which Russia had rich deposits, had to be imported, for the Russian output was either inadequate or the industrial centers were situated so far from the deposits that it paid to import those materials. Russia depended upon the outside world also for such metals as lead, copper, and zinc, for metal wares, machinery in general, agricultural machinery in particular, and chemicals.

Bearing this in mind, one can easily picture the extent to which the World War affected Russia's economic and financial systems. Let us, for example, glance at her foreign-trade figures for 1914–17.[5] During 1914 the imports amounted to 1,098,000,000 rubles and the exports to 956,000,000 rubles. The respective figures for 1915 were 1,139,000,000 and 402,000,000 rubles; for 1916, 1,717,000,000 and 476,000,000 rubles; and for 1917, 1,966,000,000 and 464,000,000 rubles. Her total unfavorable trade balance for those years, therefore, amounted to 3,622,000,000 rubles.

It must, however, be borne in mind that the ruble's purchasing power was continually declining[6] and that the real change in her imports and exports was even more serious. Indeed, expressed in millions of puds[7] the imports in 1913 weighed 937 and the exports 1,472. In 1914 the imports weighed 649 and the exports 814. In 1915 the respective figures were 240 and 150; in 1916, 250 and 144; and in 1917, 178 and 59.6. So despite the increased outlay during those years for imports their weight drastically declined.[8]

[4] Of the balance: 17.3 percent consisted of foodstuffs; 32.8 percent, of manufactured goods (capital goods included); and 1.3 percent, of animal products.

[5] Central Statistical Administration, *loc. cit.* The figures for 1916 and 1917 cover trade over the European frontiers, including the Black Sea and the Caucasian sections, and trade with Finland.

[6] See Table 9.

[7] One pud equals 36.11 English pounds.

[8] Allowance, however, must be made for the fact that the import of raw materials and semi-manufactures declined during those years, while that of finished commodities, armaments, and the like increased.

Industry, trade, and in fact the entire national economy was subordinated to the war machine. Commercial credit, as will be seen, sharply decreased during those years. Nor was there much room for private initiative in the sphere of capital investments in industry. The government itself began to grant advances and loans to the various enterprises manufacturing equipment, materials, and supplies for the military forces.[9]

The initial confusion.—Following the declaration of war panic-stricken depositors began to withdraw their funds from the banks. The joint-stock banks, for example, lost between July 1 and August 1, 1914, more than 200,000,000 rubles of their deposits.[10] Other banks fared no better. The flow of foreign funds, which helped to feed Russia's capital and money markets, was now stemmed. The precipitate fall in security prices, due to the panic on the Stock Exchange, threatened to make matters worse. The joint-stock commercial banks, it will be recalled, engaged also in investment banking, so their portfolios were filled with industrial stocks. To put a stop to the panic, as well as to prevent the export of capital abroad, the Minister of Finance, on July 16, ordered the closing of the Petrograd Stock Exchange.[11] Other exchanges followed suit. The banks were now unable to dispose of their securities even at sacrifice prices. Many of their clients were unable to pay off the maturing obligations. To save them from bankruptcy, into which the hard-pressed bankers were likely to force them, on July 25 the government declared a moratorium on all commercial paper drawn in the western and southern districts prior to the declaration of war.[12]

The State Bank was quick in coming to the rescue of the perplexed banks. As a result the discounted paper in its portfolio rose during the month of July, 1914, from 406,000,000 to 712,000,000 rubles, that is, by some 75 percent. A further very small increase

[9] See *Vestnik Finansov*, No. 29, 1916, pp. 95-96; also No. 3, 1917.

[10] *Consolidated Balance Sheets of the Joint-Stock Commercial Banks.*

[11] It remained closed until the end of 1916.

[12] See *Vestnik Finansov*, No. 39, 1915. See also Bernatzky, *op. cit.*, pp. 374-75. The original moratorium was to expire on September 25, 1914, but was renewed on a number of occasions. In the districts where the military operations were carried on, moratoria of a more general character (applying to bank deposits and real-estate mortgages as well as to commercial paper) were applied.

(to 734,000,000 rubles) occurred during the month of August, but thereafter commercial discounts began to taper off, falling by the end of 1914, 1915, and 1916 to 638,000,000 rubles, 395,000,000 rubles and 258,500,000 rubles, respectively.[13] The State Bank, due to the exigencies of the war, was becoming more of a treasury department and less of a "bankers'" bank.

The Law of July 27, 1914.—For the moment at least the treasury and the State Bank were financially embarrassed themselves, since a large portion of their foreign balances which they were unwisely keeping with bankers in Germany, France, and England could not be extricated. They succeeded in withdrawing a substantial part of their balances from Germany before the declaration of war, but were unsuccessful in their attempts to withdraw their deposits from France, for the French moratorium applied to bank deposits.[14] Meanwhile, the State Bank was called upon to pay out the large deposits of the treasury. It became evident that specie payment must be suspended, that the fiduciary issue of the bank must be expanded, and that provision must be made for the financing of war expenditures by the bank. Accordingly, on July 27, 1914,[15] there was enacted a law to that effect. The State Bank was authorized to increase its fiduciary issue of 300,000,000 rubles to 1,500,000,000 rubles. Subsequent acts on March 17, 1915, August 22, 1915, August 29, 1916, and December 27, 1916, however, increased that right to 2,500,000,000, to 3,500,000,000, to 5,500,000,000, and to 6,500,000,000 rubles, respectively.[16] Besides suspending the payment of specie and making provision for the expansion of note issues, the Law of July 27 authorized the bank to discount short-term treasury bills.

[13] *Balance Sheets of the State Bank.*

[14] The negotiations between the two countries were finally settled in the following manner: the Bank of France agreed to rediscount for the French bankers dealing with the treasury an amount of bills required for the service of the Russian government and government-guaranteed bonds; the actual payment on the Russian government bonds was made by the Crédit Lyonnais, while the payment on the railroad bonds was made by the Banque de Paris. The payments were, of course, made with funds belonging to the Russian government and held in France.

[15] The dates mentioned here are "old style" differing by 13 days from the "new style." Thus, July 27, 1914, corresponds to August 9, 1914.

[16] *Vestnik Finansov,* No. 2, 1917.

Disappearance of metallic coins.—As soon as specie payment was suspended gold disappeared from circulation. A few months later silver coins with a high percentage of silver content began to disappear, while toward the end of 1915 all metallic coin disappeared from circulation. To fill the need for small change there were introduced into circulation beginning September 29, 1915, postage "change stamps." Their size, however, rendered them impracticable, and on November 13, 1915, it was decided to introduce "treasury change tokens." [17] By January 1, 1916, the country had 39,800,000 rubles of change stamps and change tokens in circulation, and a year later, 128,300,000 rubles.[18]

Financing the war.—"Treasury Chests," or gold reserves that used to be relied upon to help defray war costs, are a thing of the past. The cost of modern wars cannot be met by such special funds. It is probable, therefore, that in the course of a war a belligerent nation will have to resort to one or more, possibly to all, of the following devices: borrowing at home; borrowing abroad; the increase in the rates of the old taxes, duties, and tariffs and the imposition of new ones; and finally issuance of paper money. Whether the government borrows from its citizens or subjects, taxes them, or increases the volume of its note issue relative to the volume of goods and services to be had, it accomplishes the same objective, namely, to deprive them directly or indirectly of a portion of their purchasing power which when transferred to the treasury will enable the latter to finance the war.

Not all the above devices for raising revenue, however, are equally desirable. Because large note issues are sure to disrupt the equilibrium of the economic life of a country and even endanger the political regime that initiates them, economists oppose their use as a means of raising revenue. An ideal method for financing a war is offered by a combination of loans and taxes that results in a mere shifting of purchasing power from the people to the treasury but that avoids increasing the total volume of means of payment relative to the volume of goods and services.

[17] *Vestnik Finansov,* No. 49, 1915, p. 344.

[18] Central Statistical Administration, *op. cit.,* p. 92.

This latter requisite means that the holders of the bonds are not to use them as collateral for bank loans, since such loans enable them to replace the purchasing power that they had transferred to the treasury and thus result in the creation of additional means of payment and, therefore, in inflation. It also precludes the use of such bonds by the treasury for discount purposes.

It is difficult, however, to prevent borrowing of this kind. In fact, a substantial portion of such bonds generally finds its way into the banks, which make possible their purchase or which are helping the buyers to retain title in them and which are themselves financed by the central bank to which these bonds, therefore, gravitate. Furthermore, some time must elapse before a successful bond campaign is initiated, or before the increased revenue from taxes and other sources will begin to come in, yet the financial needs of the government are immediate. Hence, the treasury begins to issue short-term bills and the central bank is called upon to discount them and furnish the former with banknotes or bank credit—both of which cause an increase in the means of payment and bring about inflation. It is possible, of course, to retire those bills with the proceeds from taxation or long-term bonds, but when the treasury is pressed for funds it is not likely to do so. It is idle to attempt to devise ways and means for inflationless wars. A major war nowadays without inflation is hardly conceivable. It is nevertheless possible to avoid unnecessary inflation by resorting to long-term borrowing and taxation and by inducing the people to hold their bonds or by making it difficult for them to replace the purchasing power that was shifted to the treasury. Furthermore, the short-term bills that are issued in anticipation of taxes or bond issues should be paid off as soon as the proceeds from the latter begin to come in. The taxes that are levied must be high enough to permit servicing the debt and its gradual extinction.

Circumstances, however, compelled Russia to lay too much emphasis upon short-term treasury bills and note issues as means for financing the war. To begin with, it was difficult to sell bonds to a population that was culturally backward and that regarded all such transactions with suspicion. Nor was it possible to use

taxes for the purpose of defraying war costs. Examination of the revenue receipts for 1913, that is, the last peace year, will show the reason for it. The revenue obtained by the state in that year amounted to 3,431,200,000 rubles, of which close to a billion came from the state monopoly of alcohol; 891,600,000 rubles came from railroads (of which 813,600,000 came from state-owned railroads); 708,100,000, from indirect taxes; and 272,500,000, from direct taxes.[19] As soon as war had been declared, however, Russia found it advisable to discontinue the sale of liquor. This, together with the decrease in customs and the decline in the actual revenue from railways, due to the fact that the latter became deflected to war uses, explains why, despite the substantial increases during 1914–17 in the rates of taxes, duties, and tariffs, as well as the imposition of new taxes, Russia was unable to use that revenue for war purposes.

Several attempts have been made to compute the cost of the World War to the participants. Those computations do not, of course, include the human cost, i.e., such items as the number of lives destroyed, the crippled, the suffering of war prisoners, unhappy homes, sacrifices on the part of noncombatants, and the effect upon future generations, and so forth, items which cannot be converted into pecuniary units. They do not even include the cost of devastated property. Neither do they include the cost of anticipating the war, nor the cost which the country had to bear in the post-war period. Those computations as a rule include only those pecuniary expenditures which have been sustained during the course of the war. But even with respect to such expenditures it is often difficult to distinguish between those necessitated by the war and those which could be classed as civil expenditures. In the case of Russia this problem is even more complicated by the fact that the approved budget generally differed from the *actual* receipts and expenditures, and that during

[19] Central Statistical Committee, *Statistical Year-Book of Russia for 1914* (Petrograd, 1915), Section XII. But see also Central Statistical Administration of the U.S.S.R., *World Economy, Compiled Statistical Materials for 1913–27* (Moscow, 1928), pp. 500-501; and A. M. Michelson, "Revenue and Expenditure of the Russian Government during the War," *Russian Public Finance during the War* (Yale University Press, 1928), p. 70.

the war there was created a special War Fund account, expenditures from which were being approved directly by the Czar and attended by a minimum of statistics and reports. Combining the

TABLE 6

STATE RECEIPTS AND EXPENDITURES, 1914–17

(*In millions of rubles*)

	1914	*1915*	*1916*	*1917*
Receipts				
Ordinary	2,898.1	2,827.7	3,974.5	5,700.0
Extraordinary (except loans)	8.3	196.4	327.0	680.0
Loans	1,595.3	8,142.6	13,449.3	12,718.2
Total	4,501.7	11,166.7	17,750.8	19,098.2
Add: Balance from Previous Budgets	54.4	36.2	30.0	30.0
Grand Total	4,556.1	11,202.9	17,780.8	19,128.2
Expenditures				
Ordinary	2,927.1	2,642.7	2,921.8	4,800.0
Extraordinary (except Military)	276.4	193.9	230.0	580.0
Necessitated by War	2,540.0	8,818.4	14,572.8	25,200.0
Total	5,743.5	11,655.0	17,724.6	30,580.0
Add: Cost of Discounting Short-Term Obligations	.....	48.1	376.0	800.0
Grand Total	5,743.5	11,703.1	18,100.6	31,380.0

budgetary figures with those of the War Fund account, G. Dementiev attempts to present (Table 6) a picture of Russia's state finances during 1914–17.[20]

According to his estimate, Russia's total expenditures during

[20] Central Statistical Administration, *Russia in the World War 1914–18* (Moscow, 1925), p. 46. But see also M. Bogolepov, "The Financial System of Pre-War Russia," *Soviet Policy in Public Finance* by Sokolnikov and Associates (the Stanford University Press, 1931); also B. Eliacheff, *Les Finances de guerre de la Russie* (Paris, 1919), and A. Michelson and P. Apostol in *Russian Public Finance during the War.*

1914–17 amounted to 66,927,200,000 rubles, while her receipts—not including borrowing—equaled 16,762,600,000 rubles. The difference—50,164,600,000 rubles—which roughly represents the war expenditures for 1914–17, was covered to the extent of 19,500,000,000 rubles by long-term loans of which 11,400,000,000 rubles were raised at home and the balance abroad. The government also issued short-term treasury bills, of which about 16,500,000,000 rubles were outstanding on September 1, 1917. It is estimated that by October 23, 1917, at the time the Provisional government was overthrown, their total rose to 18,700,000,000 rubles. The currency in circulation rose from 1,630,400,000 rubles on July 1, 1914, to 18,917,000,000 rubles on October 23, 1917.[21]

[21] The government finances of other belligerent nations were as follows:

(a) *France.* It is estimated that her total expenditures during 1914–18 was 169,112,702,000 francs and the receipts, not including borrowing, only 26,770,746,000, or less than 16 percent of the former. The huge deficit of 142,000,000,000 francs had to be covered by loans, and her total indebtedness rose from 33,500,000,000 francs at the beginning of 1914 to 154,600,000,000 at the end of 1918. The note circulation of the Bank of France increased from 6,683,200,000 francs on August 1, 1914, to 30,249,612,000 at the end of 1918, and the deposits from 1,330,200,000 to 2,671,413,000 francs. The advances of the bank to the government rose from 3,900,000,000 francs at the end of 1914 to 17,150,000,000 at the end of 1918.

(b) *Germany.* Her total expenditures April 1, 1914–March 31, 1919, amounted to 163,900,000,000 marks, of which only 29,900,000,000 (18.2 percent) were raised by means other than borrowing. The deficits, 134,000,000,000 marks, were covered by long-term loans (97,000,000,000) and short-term borrowing at the Reichsbank. Her banknote circulation rose from a pre-war 2,000,000,000 marks to 22,128,000,000 by the end of 1918. Other paper money, treasury notes (*Reichskassenscheine*) and loan-bureau notes (*Darlehnkassenscheine*), principally the latter, rose by over 10,000,000,000 marks.

(c) *Great Britain.* Total expenditures April 1, 1914–March 31, 1919, amounted to £9,600,000,000, of which £2,700,000,000 (28.5 percent) were raised by means other than borrowing. Her total indebtedness during the same period rose from £1,166,000,000 to £7,481,000,000. Borrowing took the form of treasury bills, exchequer bonds, certificates, long-term bonds, and other obligations. The total note circulation (the government issued a new type of currency reaching £323,644,000 by the end of 1918) rose from less than £30,000,000 at the beginning of 1914 to a little less than £400,000,000 at the end of 1918. Total bank deposits, largely due to government borrowing, rose from £716,367,000 in the middle of 1914 to £1,631,616,000 in the middle of 1919.

Annuaire Statistique de la France; Weekly reports of the Bank of France; James Harvey Rogers, *The Process of Inflation in France 1914–27* (Columbia University Press, 1929), *passim: Statistisches Jahrbuch für das deutsche Reich* (Berlin, 1919) *passim;* Frank D. Graham, *Exchange Prices and Production in Hyper-Inflation: Germany 1920–23* (Princeton University Press, 1930); *Economist* (London); John Parke Young, *European Currency and Finance* (U. S. Senate Gold and Silver Inquiry Commission, 1925). Serial 9, I.

The change in the character of the bank's operations.—It has already been related that the State Bank helped the money market to avert a very serious panic at the beginning of the war in the face of a large withdrawal of deposits on the part of the treasury.[22] Thereafter, its chief task became to aid the treasury in its efforts to raise the means for the prosecution of the war. It discounted for the treasury short-term obligations running into thousands of millions of rubles and helped it to sell securities to the various credit institutions, public and private organizations, and to the public.

A comparison of certain accounts of the bank on July 16, 1914, on March 1, 1917 (at about the time of the fall of the monarchy), and on November 1, 1917, will make clear the changes that took place in the bank's operations during the war.[23]

Commercial loans and discounts.—As shown by the figures in Table 7, commercial discounts, which before the war occupied an important place among the assets of the bank, were gradually sinking to a position of minor importance, falling by March 1, 1917, to not much more than their pre-war volume. A similar or even more pronounced decline could be observed in the case of industrial loans and loans to small credit institutions. In fact, their real decline was even greater than is shown by the above nominal amounts, for the total resources of the bank, due to war-time finance, had increased tremendously and the ruble itself underwent a serious depreciation. Under the Provisional government, however, the various loans and discounts of the bank began to rise and by November 1, 1917, had outstripped the pre-war figures. It would be an error, though, to suppose that the relegation of commercial discounts to a place of lesser importance during the war was due solely to the fact that all of the bank's available resources were tied up in loans to the treasury. There were, in fact, certain forces in operation tending to bring about a decrease in the demand for such credit. Due to the limitation of the stocks of goods on the market and the irregularity in the delivery of goods, because of

[22] From 517,900,000 rubles on August 1, 1914, they fell to 230,800,000 on the first of the following month and 208,300,000 rubles on October 1, 1914.

[23] See *Vestnik Finansov*, No. 7, 1917, and Central Statistical Administration, *op. cit.*, Pt. 2, p. 101.

deflection of the railroads to war purposes, retailers began to compete with one another for what was available. They began to pay cash in advance in order to make sure that the wholesalers would favor them. Moreover, the treasury, one of the most important buyers during the war, not only paid cash on all of its orders, but even financed enterprises producing for the War Department. This, together with the occupation by the enemy of some of the

TABLE 7

CHANGES IN THE BALANCE SHEET ITEMS OF THE STATE BANK 1914–17

(*In millions of rubles*)

	July 16, 1914	*March 1, 1917*	*Nov. 1, 1917*
Gold reserve	1,603.0	1,476.0	1,292.0
Gold abroad	141.0	2,142.0	2,308.6
Commercial discounts	407.6	213.6	500.0
Short-term treasury bills	....	7,882.0	15,507.0
Loans on securities	129.0	580.0	1,512.0
Loans on merchandise	50.0	43.0	90.0
Loans to small credit institutions	135.6	54.0	85.0
Industrial loans	14.0	7.0	10.0
Notes in circulation	1,633.0	9,950.0	18,917.0
Treasury deposits	514.0	202.0	206.6
Special funds and deposits	349.0	598.0	688.0
All other deposits	260.0	1,781.0	2,491.6

most industrial sections of the country (such as Poland), undoubtedly accounted for a considerable portion of the shrinkage in the volume of commercial paper offered for discount. According to the *Vestnik Finansov* (No. 3, 1917) the volume of such paper held by Russian banks decreased by 10 percent in 1914; by 50 percent in 1915; and by 75 to 80 percent in 1916.

For this reason the State Bank did not have to rely upon a

high discount rate to bring about a diminution in the volume of paper offered for discount. In fact, its discount rate, which on July 16, 1914, was increased (from 5½ percent March 20–July 16, 1914) to 6 percent on three-month paper and to 6½ percent on six-month paper, remained at that level until October 23, 1917.[24] It must be borne in mind, however, that during a war (and very often in peace time when the leadership of a central bank is weak and its policies are influenced by the treasury) the discount rate is kept down for the purpose of enabling the latter to borrow cheaply, and, therefore, does not measure the demand for such credit.

Loans against securities.—Russia created no special organization for the purpose of preparing and floating war loans on the home market. That important task devolved upon the State Bank. In order to facilitate the sale of those bonds the bank agreed to accept them as collateral for loans to banks and to individuals—a practice, as has already been explained, which tends to inflate prices, inasmuch as it leads to the creation of additional means of payment.

As may be seen from Table 7, the volume of loans on securities rose from 129,000,000 rubles on July 16, 1914, to 580,000,000 rubles on March 1, 1917, and to 1,500,000,000 rubles on November 1, 1917.[25]

Short-term treasury bills.—Although known in Russia, treasury bills, which are generally used in anticipation of collections, had not been employed there in the two decades that preceded the war. During the war, however, for reasons already explained, instead of being used in anticipation of revenue from taxation and long-term loans and being extinguished as soon as that revenue came in, they were employed as vehicles for inflation. From a meager start of 175,000,000 rubles on September 1, 1914, the volume of short-term treasury obligations in the bank's portfolio mounted to 663,100,000 rubles by the end of 1914, to 3,270,100,000 rubles by the end of 1915, and to 6,866,100,000 rubles a year later. By March 1, 1917, their volume rose to

[24] *Balance Sheets of the State Bank.*

[25] *Ibid.* The bank's resources on March 1, 1917, amounted to 13,200,000,000 rubles, and on November 1, to 24,200,000,000.

7,882,000,000 rubles, and by November 1, 1917, to 15,507,200,000 rubles. On the two last-mentioned dates the discounted treasury bills constituted about three-fifths of the bank's total resources.

Of maturities not exceeding one year and bearing 5 percent interest, they were presented by the treasury at the State Bank, which discounted them as it would commercial paper, and advanced the proceeds in bank currency. But not all these bills were taken by the treasury directly to the State Bank. Some were marketed abroad, while a certain portion were used by the treasury as part payment on the goods and services delivered to the state. The bank, however, announced that it stood ready to discount all such bills at moderate rates and that it would advance in cash up to 95 percent of their nominal value. Apparently, it was not understood that such policy on the part of the bank would result in neutralizing the effort of the government to keep the volume of notes as low as possible. Those bills were, of course, promptly discounted at the State Bank or other banks by their recipients. Inasmuch as the treasury did not employ a portion of its revenue from taxation or long-term loans for the purpose of curtailing the volume of short-term bills outstanding, and the bank, consequently, did not call in the currency issued on the strength of those bills, the purpose of the above policy is quite doubtful. The inflationary effect upon the price level that was exerted by the issue of bank currency (on the strength of those bills) was in nowise changed by their employment. Thus, the exigencies of the war caused the State Bank's assets to become highly illiquid. Its holdings of commercial paper were now insignificant, especially when compared with its total resources.

Gold reserves.—Among the remaining assets in the bank's statement that deserve especial attention are: "gold at home" and "gold abroad." Both of these were represented by large figures and to both of these the bank and the statesmen seem to have attached too great importance.

The gold reserve in the vaults of the bank, which on July 16, 1914, amounted to 1,603,000,000 rubles fell to 1,476,000,000 rubles by March 1, 1917, and was further reduced under the Provisional government to 1,292,000,000 rubles on November 1,

1917.[26] This decline was largely due to the shipments of gold to England under an arrangement between the two governments which resulted in the placement of large credits by England at the disposal of the Russian treasury.

The figures representing "gold abroad" show an entirely different picture. From 141,000,000 rubles on July 16, 1914, they rose to 2,142,000,000 rubles, an increase of more than 2,000,000,000 rubles, on March 1, 1917, and to 2,309,000,000 rubles on November 1, 1917. In reality, however, the increase was due to English credits some of which were in fact "nonnegotiable," "intangible," and were granted for the purpose of enabling Russia to disguise the actual decrease in her gold reserve. Describing an arrangement between England and Russia by which the former agreed to open for the latter a "nonnegotiable" credit for $973,000,000 and which the State Bank included in its "gold abroad" account, one writer says: [27] "Thanks to this arrangement, which was pure camouflage, in banking parlance 'kiting,' the decrease in the gold stock from the exportation of the gold, was not perceived by the public at large. . . . This was one of the financial secrets of the war, which only came to light after the fall of the Czarist government."

Russia, which even before the war overemphasized the importance of gold reserves, made the error, during the war, in common with other belligerent nations, of thinking that those reserves were possessed of nothing short of magic power. It is true, of course, that gold, even though a country suspends specie payment, can be used in international trade and for the purpose of facilitating a resumption of specie payment. But, once a country is off the gold standard and the circulating currency is no longer redeemable in gold, the link between the two is broken, and the gold reserve, no matter what its size, ceases to influence the price level. It might be said, of course, that when the gold reserve in such a country is large other countries will feel that specie payment can easily be resumed by it, and the resulting confidence

[26] The actual loss of gold was even larger, for the gold mines were in operation during those years, and, besides, some gold was retrieved from circulation.

[27] Harvey E. Fisk, *The Inter-Ally Debts* (Bankers Trust Company, 1924), p. 138; Eliacheff, *op. cit.*, pp. 133-39.

will translate itself into higher exchange rates, which in turn will influence internal prices. Confidence in a country depends, however, not only upon its gold reserves but upon the general economic, financial, and political conditions prevailing therein. At any rate during the World War success on the battlefields exerted a stronger influence in the foreign exchange of a belligerent country's currency than the size of her gold reserves. As for Russia, her note issues during the war continued to increase so rapidly as to make resumption of specie payment on the old basis. that is, without devaluating the currency, a quite impossible task, even if her gold reserves were several times higher than they were represented to be.

Deposits and notes in circulation.—The changes in the bank's assets were accompanied by changes in its liabilities. Thus, the "Treasury Deposits," which before the war furnished the bank with large resources, due to war financing, fell from 514,000,000 rubles on July 16, 1914, to 202,000,000 rubles on March 1, 1917, but showed a slight gain by November 1, 1917, when it rose to 206,600,000 rubles. The "Special Funds and Deposits," and, especially, "All Other Deposits," on the other hand, showed, as can be seen from Table 7, a very substantial increase. The increase in the "Special Funds" was due chiefly to the placement of funds at the disposal of the various government departments, while the increase in "All Other Deposits" (from 260,000,000 rubles on July 16, 1914, to 1,761,000,000 rubles on March 1, 1917, and to 2,491,600,000 rubles on November 1, 1917), was due largely to inflation.

A far greater increase, however, was shown by the account "Notes in Circulation." From 1,630,400,000 rubles (backed by a gold reserve in the vaults of the bank—amounting to almost 1,600,000,000 rubles, or 98 percent) on July 1, 1914, their volume steadily rose, as the treasury presented more and more of its short-term obligations for discount, to 2,946,600,000 rubles at the end of 1914, to 5,616,800,000 rubles at the end of 1915, and to 9,097,400,000 rubles by the end of 1916. By March 1, 1917, their volume expanded to 9,949,600,000 rubles. Between March 1, 1917, and October 23, 1917, their volume jumped to

18,917,000,000 rubles—showing an increase of almost 9,000,000,000 rubles.[28] In other words, during the short reign of the Provisional government the volume of notes experienced a larger increase than during 1914–17 under the monarchy.

The sweeping victories of the enemy on the battlefront, the brewing dissatisfaction of the soldiers, the growing hostility of the workers and peasantry, the disorganization of the economic life of the country, and, paradoxically enough, the depreciation of the currency [29] were among the factors that compelled the government to lean heavily on the printing press. That the danger of such methods of raising revenue was realized, but that the Provisional government saw no other way out, can be seen from the following interesting statement of Michael W. Bernatzky, Minister of Finance in the Provisional government: [30]

However good the intentions of the Provisional Government, it had no alternative but to print still more notes, a measure bound ultimately to reduce Russia to bankruptcy. Circumstances arising out of the War and the internal political situation forced the Government to act hastily and to resort to measures which were technically inadequate. By the end of August 1917 it became clear to the Government that a great financial and monetary catastrophe was bound to occur in about a month's time, for the receipts of the Treasury and the output of the printing press were together insufficient to keep abreast of the increasing expenditure. The very possibility of continuing to prosecute the War was in balance. The impending catastrophe would strengthen the hands of the Bolsheviks, who had quickly recovered after the defeat of their rising in July. This extremely critical situa-

[28] *Balance Sheets of the State Bank.* The Provisional government raised the legal limits of the fiduciary note issue of the bank on five occasions: On March 4 to 8,500,000,000 rubles; on May 15 to 10,500,000,000; on July 11 to 12,500,000,000; on September 7 to 14,500,000,000; and on October 6 to 16,500,000,000 rubles.

[29] The higher the price level, the larger the volume of means of payment that is required to support it.

[30] The "order" to which reference is here made was for notes of *American* design and was placed in the U.S.A. These notes were to be in denominations of 25 and 100 rubles. Since their delivery was promised for 1918 the government was compelled to rely upon domestic production. It became necessary to simplify the technique and the design of notes in order to increase their output. The unpopular treasury note (a part of the fiduciary issue of the State Bank) or "Kerenky" (from the name of Kerensky), e.g., were printed on water-marked paper, were not signed or numbered, and were issued in uncut sheets. Needless to say counterfeiting boomed.

tion demanded immediate and drastic remedies. The present writer, at that time Minister of Finance, decided to place an order abroad without delay for a sufficient supply of new notes, and pending their delivery, to issue temporary notes of a design that could be easily printed at short notice and in large quantities.

At the time of the overthrow of the Provisional government, there were in circulation old "Romanov" notes, "Duma" notes,[31] and, finally, "Kerenky." As the new notes, especially the "Kerenky," whose appearance differed from other notes, were being introduced into circulation the people began to hoard the old "Romanov" notes.

The commercial banks during the war.—The change from peacetime to wartime production, which wrought such deep changes in the economic life of the country and in consequence of which the State Bank became transformed into little more than an auxiliary of the treasury for the purpose of financing the war, could not fail to affect the activities of the entire credit system. A brief review of the operations of the most important group, the joint-stock commercial banks, will help to make clear the part played by them during the war, the changes in their activities, and, finally, the effect of those activities upon the price level as a cause for their unpopularity.

The author of a well-known French work on the Russian commercial banks lists in more or less detail the following achievements of those banks during the war: [32]

1. They helped to place some 40 percent (about 5,000,000,000 rubles) of the internal loan.

2. Despite the assistance from the government, industrial plants, especially the metallurgical group, had to depend upon the commercial banks for capital for the procurement of equipment, extension and enlargement of existing plants, and the construction of new plants. He estimates that some 2,000,000,000 rubles were advanced by the banks to industry for that purpose.

[31] On April 26, 1917, the Provisional government ordered the printing of State Bank notes of the denomination of 1,000 rubles. They were nicknamed "Duma" ("Dumskie") because of the picture of the Duma (Parliament) that appeared on them.

[32] E. Epstein, *Les Banques de commerce russes,* pp. 70-72.

3. The government in certain cases granted loans to industry only upon the presentation of bankers' guarantees, and the banks accordingly granted such guarantees to an amount of about 300,000,000 rubles.[33]

4. The banks helped to float railroad securities amounting to about 1,000,000,000 rubles. Before the war such securities had to be floated abroad.

5. The banks extracted from circulation about 7,000,000,000 paper rubles.[34]

Doubtless, the banks did render useful service during the war.[35] Certain of their credit transactions, however, tended to promote speculation in commodities and securities, and this, together with the excessive note issues by the State Bank, contributed to the depreciation of the ruble.

The change in the character of their operations.—We have seen that during the war the volume of commercial bills in Russia greatly decreased, and yet when we look at Table 8 we find nothing to corroborate that fact. On the contrary, the commercial discounts as well as the loans and the "correspondents" account show a substantial increase, which was only in part due to the inflation that it helped to promote.

The quantitative change, however, was to a large extent made possible by a qualitative change. Undaunted by the falling off in the volume of genuine self-liquidating commercial paper whose purpose it was to facilitate the exchange of commodities, the banks began to discount paper and to grant loans secured by it for entirely different purposes, such as the purchasing of equipment, extension and construction of plants or for other purposes that promised a profitable return. Inasmuch as the private joint-stock commercial banks were also carrying on investment banking and owned a substantial interest in various enterprises, they were especially interested in the size of profits made by those enter-

[33] There were rumors, however, that some of the banks violated the trust imposed in them by the government.

[34] The uses, though, to which this money was put nullified the effect of its withdrawal from circulation.

[35] Epstein also speaks of the help rendered by these banks to the treasury in the procurement of loans in Italy and Sweden, as well as their service in the matter of helping France to make purchases of foodstuffs in Russia.

prises. In a variety of ways the banks supplied them with funds which were often used for the purpose of keeping commodities warehoused, or, in general, off the market, at a time when the demand for them by far exceeded the supply. Nor was evidence lacking that the banks themselves were buying up commodities with

TABLE 8

COMBINED BALANCE SHEET ACCOUNTS OF THE JOINT-STOCK COMMERCIAL BANKS

1914–17 [a]

(*In millions of rubles*)

	Jan. 1 1914	*July 1 1914*	*Jan. 1 1915*	*July 1 1915*	*Jan. 1 1916*	*July 1 1916*	*Jan. 1 1917*	*Mar. 1 1917*
Assets								
Commercial discounts	1,546.5	1,799	1,667	1,754	1,967	2,530	2,991	3,438
Loans on securities	998	912	931	931	1,011	1,069	1,557	1,744
Loans on merchandise	319	....	....	....	....	....	....	....
Loans on comm. paper	298.4	565	591	561	738	798	1,043	1,118
Total	3,162	3,275	3,189	3,246	3,716	4,397	5,591	6,300
Correspondents	1,471	1,547	1,646	2,148	2,343	2,895	3,488	3,514
Securities owned	315	393	486	597	690	743	866	913
Capital & Liabilities								
Capital and reserves	836	897	906	920	931	959	994	1,029
Total deposits	2,539	2,808	2,873	3,392	3,931	5,119	6,748	7,279
Rediscounts	335	196	363	360	432	296	278	329
Correspondents	1,458	1,645	1,546	1,734	1,965	2,210	2,346	2,503

[a] Based upon the *Consolidated Balance Sheets of the Joint-Stock Commercial Banks.*

the intention of holding them off the market.[36] In this manner the banks were able to compel the government to revise the price

[36] *Vestnik Finansov,* Nos. 25 and 26, 1916, where Professor Friedman analyzes some of those operations. The banks, although forbidden to engage in trade, were buying up, through the medium of tradesmen with whom they split profits, such important commodities as meat, sugar, butter, leather, and so forth.

schedules (of commodities whose price was fixed and regulated by the government) and bring them up to a desired height.

What in the early part of the war was accomplished with the aid of commercial paper was later done with the aid of securities. The banks acted as promoters and as syndicate underwriters. Transactions involving securities figured prominently in their accounts. In addition to owning securities they granted loans backed by such securities, opened current accounts against them, and in general accepted securities as collateral for commercial loans from enterprises in which they were interested (the latter transactions were generally entered in the "correspondents" account). At the same time the traffic in securities assumed large proportions, their prices began to soar, and this was, of course, accompanied by all the evils which such speculation engenders. While it is true that the regulation of prices in the face of scarcity of commodities tends to encourage the hoarding of commodities and their sale at illegal prices, and while it is equally true that the anticipation of war profits, as well as the inequity that results from the purchase of securities with a fixed return during a regime of rising prices, tend to encourage speculation in stocks even when the bankers' initiative in such matters is lacking, nevertheless it is clear that the active participation by bankers in it and the encouragement and aid given by them to those whose activities they were in a position to control, made matters worse. It is, of course, impossible to determine the exact effect of the transactions described above upon the price level. Much was done secretly and in circuitous ways. No single account of the banks reflected all the transactions—most of the asset accounts were used for that purpose. It should be observed, however, that it was the carrying on of the functions of investment and commercial banking under the same roof and the laxity of governmental supervision and regulation which made it possible for the banks to evade even the few laws that did exist for their regulation.

In response to public demand and pressure from the General Army Headquarters [37] the Czar on September 10, 1916, approved

[37] The General Army Headquarters, amusing as it may sound, asked the Czar that it be given permission to investigate the banks.

an act to authorize the Minister of Finance to examine the banks for the purpose of enforcing the laws which prohibited dealing with foreign institutions and subjects, as well as all laws, decrees, and statutes pertaining to their dealing in merchandise and foreign exchange,[38] and finally the regulations concerning bank guarantees. This measure was intended to be temporary and was to expire within a short time after the conclusion of peace. At the same time a special committee was empowered to conduct an investigation into the bankers' operations.[39] Neither the above measure nor the special committee, however, accomplished anything of real importance.

Inflation

It is interesting to note that, despite the increase in the volume of circulating notes from 1,630,400,000 rubles on July 1, 1914, to 2,946,600,000 rubles on January 1, 1915, the price level during 1914 remained almost stationary. Among the circumstances that made this possible were: the placement upon the domestic market of extra supplies of consumers' goods that could no longer be exported and the "vacuum" created by the disappearance of gold coins from circulation. The productive processes of the country, however, were being so canalized as to serve the military needs of the country. As a result the output of enterprises supplying war needs underwent a marked increase, while that of industries supplying the needs of the civil population underwent a marked decrease.[40] It is but logical that the rising volume of means of payment should produce under those circumstances a rise in prices.

It is equally logical that, when due to war conditions the volume of exports dwindled while that of imports steadily and greatly

[38] Foreign exchange was still another field of speculation that attracted the bankers.

[39] The committee ordered the arrest of several financiers and believed that it was about to uncover a vast criminal plot linking the bankers with the enemy.

[40] See Central Statistical Administration, *Trudy*, VII, Pt. 1, *passim*. See also Central Statistical Administration, *Russia in the World War*, p. 5. Also P. I. Popov, "The Industry of the R.S.F.S.R., 1912 to 1922," *On the New Path*, III, pp. 168-69. Also S. O. Zagorsky, *State Control of Industry in Russia during the War* (Yale University Press, 1928), *passim*.

increased causing the demand for foreign bills to outstrip by far their supply, the ruble's external purchasing power should decline.

Table 9 shows the relative changes in the external and internal purchasing power of the ruble and in the volume of currency circulation. As may be seen, by the beginning of 1915, when currency in circulation rose by some 80 percent, the price index showed a 30 percent rise and the ruble's internal purchasing power amounted to about 81 pre-war copecks. The index of exchange at the same time showed a rise of 23 percent, and the ruble's external purchasing power amounted therefore to some 77 pre-war copecks.

A year later when the currency in circulation was almost three and a half times as large as on July 1, 1914, prices were some 1.4 times as high as before the war, that is, the ruble's internal purchasing power corresponded to about 70 pre-war copecks, while the index of exchange as compared with parity rose by slightly less than three quarters, so that the ruble's external purchasing power at that time amounted to but 57 pre-war copecks.

By the end of 1916 the currency in circulation amounted to about 5.7 times what it was before the war. The price level, however, was about three times as high as that in 1913, and the internal purchasing power of the ruble therefore amounted to some 34 pre-war copecks. Due primarily to the support that was given the ruble on the exchanges, the index of exchange which showed a distinct improvement in the ruble's position during 1916, was precisely the same as in January, 1916, and the external purchasing power of the ruble, therefore, was still 57 copecks.

At the beginning of April, 1917, the currency in circulation exceeded the pre-war volume by some 6.8 times. The price level showed but a smaller rise and amounted to 3.35 times what it was before the war. The internal purchasing power of the ruble, therefore, amounted to about 30 pre-war copecks. The index of exchange, as a result of speculation due to an increased confidence in Russia under the Provisional government, remained approximately what it was at the beginning and the end of 1916, so that the external purchasing power of the ruble still amounted to 57 pre-war copecks.

TABLE 9

INDICES OF FOREIGN EXCHANGE, PRICE LEVEL AND CURRENCY CIRCULATION

1914–17

Date (First of the month)	1 [a] Foreign Exchange Rubles per £10 (Par = 1)	2 [b] Retail Price Index 1913 = 1	3 [b] Currency Circulation July 1, 1914 = 1
1914			
July	1.01		1.00
October	1.18	1.01	1.65
December	1.24	(for the entire year)	1.75
1915			
January	1.23		1.81
April	1.21	1.30	2.03
July	1.45	(for the entire year)	2.30
October	1.50		3.00
1916			
January	1.73	1.43	3.48
April	1.62	1.63	3.78
July	1.64	1.95	4.13
October	1.62	2.35	4.74
1917			
January	1.73	2.94	5.68
April	1.75	3.35	6.85
July	2.15	5.76	8.13
August	2.40	6.55	8.79
September	3.04	6.80	9.58
October	3.29	7.40	10.78
November	3.84 [c]	10.20	12.01
December	....	15.45	15.51

[a] The index of foreign exchange is based upon beginning-of-month figures as quoted by the *Torgovo-Promyshlennaya Gazeta* (*Trade and Industry Gazette*). No adjustment was made for the depreciation of the pound sterling.

As to dollar exchange see footnote 43.

[b] The price index is that of the Central Bureau of Labor Statistics. See *Our Monetary Circulation, Materials on the History of Currency Circulation, 1914–25*. Prof. L. N. Yurovsky, ed. (Commissariat of Finance, 1926). Other sources, however, indicate that the rise in prices, at least during 1914-15 was higher than the above estimates. According to Demostenov's index of food prices ["Food Prices and the Market in Foodstuffs," *Food Supply in Russia during the World War* (Yale University Press, 1930), p. 232], during the first half of 1914 prices rose to 104.7; during the second half to 110.1; during the first half of 1915, to 141.9 while during the second half, to 155.1; during the first half of 1916 they rose to 195.6, and during July–August of the same year (latest figures to which he brings up the calculations), to 215.

[c] Middle of November.

During the summer months of 1917 the economic decline which had been growing progressively worse since the second half of 1916 reached catastrophic dimensions.[41] At the same time the growing hostility of the workers and peasants to the Provisional government pointed to the instability of the political regime. It was then that the rate of depreciation of both the internal and external purchasing power of the ruble considerably increased in general, especially relative to the rate of increase in the volume of currency in circulation. Thus, an increase in the index of currency circulation from 5.68 in January, 1917, to 6.85 in April of the same year was accompanied, as has been shown above, by an increase in the price index from 3.00 to 3.35 with the index of exchange undergoing negligible change. Already in July of the same year a further increase of the index of the currency in circulation to 8.13 was accompanied by a rise in the price index to 5.76 —a doubling of the price level relative to its level in January, 1917. The significance of this change becomes especially apparent when it is borne in mind that in July, 1916, exactly one year earlier, a doubling in the price level went hand in hand with a quadrupling of the volume of currency in circulation.

The index of foreign exchange due to an increasing wave of speculation in rubles during the summer of 1917 lost its relative stability, and the control of the exchanges became increasingly difficult. At the time of the November Revolution it stood at 3.29 [42] and the external purchasing power of the ruble, therefore, amounted to but 30 pre-war copecks.[43] A far greater collapse was

[41] See Central Archives of the R.S.F.S.R., *Red Archives*, I (VIII) (Moscow State Press, 1925), pp. 67-86, where M. V. Rodzianko's report to the Czar (in February, 1917) on the catastrophic decline of the national economy is given. Also pp. 86-94, where Stepanov (Acting Minister of Trade and Industry), in his report to the Provisional government in June, 1917, describes the further disruption of the economy.

[42] This figure is based on October beginning-of-the-month quotations. On October 10, however, the index stood at 3.59, and the external purchasing power of the ruble was therefore equal to some 28 pre-war copecks.

[43] The above figures were computed with reference to the pound sterling, inasmuch as during the war London constituted the principal foreign market for rubles. Average monthly exchange rates on New York (par 51.46 cents per ruble) were as follows: during 1914 in July, October, and December: 51.28, 48.00, and 42.00 cents, respectively. In January, April, July, and October of 1915: 42.94, 43.12, 35.00, and 34.25 cents, respectively.

experienced by the ruble's purchasing power on the domestic market. There, during October, with the index of currency circulation standing at 10.78, the price index climbed to 7.4 and the ruble, therefore, purchased approximately what 13 copecks did before the war. In November, when the volume of currency was 12.01 times as great as that before the war, the price index stood at 10.2 so that the purchasing power of the ruble equaled some 10 pre-war copecks. Already in December a volume of currency 15.5 times as great as the pre-war volume was accompanied by a price level almost that many times as high as the pre-war level. The period of moderate, albeit from the middle of 1916 accelerated, inflation, when the rate of increase in the volume of currency circulation was accompanied by a smaller rate of increase in the depreciation of the currency, came to an end, and a period of hyper-inflation, when a given rate of increase in the volume of currency circulation was accompanied by a far greater rate of increase in the price level, was setting in.

It appears, therefore, that the quantitative relationship between the above indices of exchange, prices, and currency was on the whole a loose one.[44] There is no evidence whatsoever that exchange influenced prices, or that prices influenced exchange. The two in fact were not always moving together. Both exchange and prices were rather influenced by the volume of currency in circulation and the confidence in the country.

Confidence in a country is, of course, an important factor at all times. Upon it depends the opinion of speculators in foreign exchange and hence the movement of exchange. In 1915, for example, the defeat and the retreat of the Russian armies gave

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In January, April, July, and October, 1916: 29.69, 31.00, 30.56, and 31.20 cents, respectively.

During 1917 the rates were as follows: January, 29.00; March, 28.07; April, 28.52; July, 22.35; August, 19.35; September, 14.50; November, 13.00. *Harvard Review of Economic Statistics,* July, 1919, quoted by John Parke Young, *op. cit.,* Ser. 9, II, 360.

[44] And if the price of gold be added, then between the four. The "appreciation" of gold was as follows: Immediately after the war broke out it began to command a premium of 10 percent. By 1915 the premium rose to 13 percent, and by 1916 to 45 percent. It also commanded a type of premium that is difficult to measure —thus, if one wished to pay with gold for his railroad ticket, he did not have to stand in line, etc. In February, 1917, the premium reached 100 percent. Thereafter the premium began to mount to greater heights.

rise to a speculative wave of ruble selling on the exchanges. Upon it also depend the unspent margins of the holders of currency within a country. It was confidence in the stability of the country which accounted for the hoarding of paper currency when the monarchy was in power, and during a part of the period under the Provisional government—a powerful force which tended to neutralize in part the effect of large note issues. On the other hand, toward the end of 1917 lack of confidence was among the principal factors responsible for the wave of spending all that one earned as quickly as one earned it—a phenomenon which served to step up the velocity of circulation. Inasmuch as the effect upon prices of the spending of one ruble (whether currency or credit) a thousand times during a certain period is the same as that of spending one thousand rubles only once during that time, it can be readily surmised what effect this had upon the course of inflation.

IV

NATIONALIZATION AND LIQUIDATION OF THE CREDIT SYSTEM, 1917–21

War Communism, 1918–21.—The October-November, 1917, Revolution began in Russia a series of extraordinary changes, which rendered obsolete the old institutions and relationships in the socio-political and economic life of the country. Among the early changes was the abolition of private ownership in land on October 26, 1917. On November 14 was established workers' control over all branches of the national economy. A month later the banks were nationalized. On January 28, 1918, all public debts were annulled. On April 23, 1918, foreign trade was declared a state monopoly.[1]

The exigencies of the Civil War, which broke out in the middle of 1918 and which lasted until the end of 1920, the blockade, and the intervention caused the new regime to take an even sharper turn to the left. The name "War Communism," by which the period from the middle of 1918 to 1921 is known, aptly describes the resulting system. Industry and trade were nationalized.[2] Agricultural products were being requisitioned.[3] The output of the state and co-operative enterprises, the requisitioned agricultural products, and the old supplies were being collected by the all-powerful Commissariat of Supplies and distributed to the people. Inasmuch as the prices "fixed" by the government were not being adjusted so as to give effect to the rapid depreciation of the currency, exchange at those prices (particularly beginning with the second half of 1919) partook of the nature of free distribution. Finally, by a series of decrees in 1920 and during the early part of 1921, the government ordered the free distribution of goods and services to the population.[4]

[1] *Collected Decrees,* 1917, Decrees 3, 35, 150; *op. cit.,* 1918, Decrees 353 and 432.
[2] *Op. cit.,* Decrees 559 and 879.
[3] Decree 634.
[4] *Op. cit.,* 1920, Decrees 43, 109, 165, 422, 505, 531, 539; *op. cit.,* 1921, Decrees 20, 45, 47, 60, 81, 211, 237.

In so doing the Soviet government hoped to effect a transition to a "natural" economy in which purchase and sale, and the medium with which they are carried out—i.e., money—would have no place. As is well known, however, the extraordinary decline of production throughout the national economy during this period [5] and the unrest of the people (particularly such uprisings among the peasants as those in Tambov and the revolt at Fort Kronstadt) made it necessary to discontinue the policies of War Communism. A *complete* transition to a "natural," "moneyless" economy was, therefore, never made in the Soviet Union. Even at the beginning of 1921, that is at the height of that period, things were being bought and sold on the "illegal" markets.

In view of the transformation of the political, social, and economic structure in Russia during the Civil War described above, a parallel change in the banking and credit system was to be expected. It could not have been otherwise. The old banking and credit system was based upon the former relationships in the sociopolitical and economic life of the country and was not at all adapted to serve the country under the new and vastly different relationships which were established in the course of 1918–20. The complete metamorphosis and final disintegration of the banking and credit system during that period did not, however, come solely in response to the new relationships. Its course, like that of the rest of the national economy, and perhaps even more so, was charted by the socialist philosophy held by those who were then in power.

For the understanding of the march of events in the field of banking and credit during those years, it is obviously also necessary to know what the socialist philosophy on that subject was. Let us, therefore, turn to Marx and Engels. "The credit system," we are told, "has for its premise the monopoly of social means of production in the hands of private people (in the form of capital and landed property) . . . it is itself on the one hand an immanent form of the capitalist mode of production, and on the other hand one of the impelling forces of the development of this mode of production to its highest and ultimate form. . . . But at the

[5] See Central Statistical Administration, *Totals of Ten Years' Soviet Rule*, 1917–27, p. 4.

same time banking and credit thus become the most effective means of driving capitalist production beyond its own boundaries. and one of the most potent instruments of crises and swindle." [6] The crises in their periodic recurrence become more and more menacing to the existence of bourgeois society.[7] As time goes on "the way is paved for more wide-spread and more disastrous crises . . . the capacity for averting such crises is lessened." [8]

Finally, the proletariat rises and overthrows the bourgeoisie. The political supremacy thus won will be used by the proletariat "in order, by degrees, to wrest all capital from the bourgeoisie, to centralize all the means of production into the hands of the State. . . ." [9] To accomplish this it will be necessary to resort in the first instance to "despotic inroads upon the rights of property." [10] These inroads will take the form of certain measures of no small importance, among which is the "centralization of credit in the hands of the State by means of a national bank with State capital and an exclusive monopoly." [11]

[6] Marx, *Capital, a Critique of Political Economy,* Engels, ed. (Chicago, 1909), III, pp. 712-13. Bankers are regarded by the socialists as "parasites," "bandits" who "despoil periodically the industrial capitalists" (*op. cit.,* p. 641), inasmuch as interest is "merely another name . . . for a certain part of the profit" which the lender of capital received (*op. cit.,* pp. 398, 434). But profit itself is due to the fact that a businessman "offers something for sale for which he has not paid anything." Profit, or surplus value, it must be remembered, "consists of the excess of the total amount of labor embodied in the commodity over the paid labor contained in it" (*op. cit.,* p. 55). Accordingly, N. Bukharin and E. Preobrazhensky [*The ABC of Communism, a Popular Explanation of the Russian Communist Party (Bolshevists),* American edition, in Russian, 1921, p. 223], tell us that "bankers lend to entrepreneurs who open factories, exploit labor and give part of the profit to the bank for the loan . . . Banks themselves go into business . . . or finance business already in existence. Finally, they lend to governments and charge interest for it . that is, they rob the peoples of those countries through the governments . . . The work of the banks in the last analysis consists of pumping surplus value with the aid of their own capital as well as with that belonging to depositors."

[7] Marx and Engels, *The Communist Manifesto* (New York, International Publishers, 1930), pp. 32-33.

[8] *Ibid.* [9] *Ibid.,* p. 52. [10] *Ibid.*

[11] *Ibid.,* "Centralization" of credit was, in fact, embodied in the principles of the Saint-Simonians. The Saint-Simonians, however, did not link the centralization of credit with the abolition of private property in the means of production or the regulation of production. (Although Charles Pecqueur, in his *Theorie nouvelle d'economie sociale et politique* [Paris, 1842], p. 434, to whom Marx refers as "essentially a Saint Simonian, only much more radical," demanded that the banks "should rule production.") Or, take Proudhon, who advocated people's banks (and "credit gratuit") but who at the same time favored small capitalist production. With Marx,

Marx and Engels, however, did not say that a banking and credit system could not be used after the power passes into the hands of workers. On the contrary, we are told that "the credit system will serve as a powerful lever during the transition from the capitalist mode of production to the production by means of associated labor; but only as one element in connection with other great organic revolutions of the mode of production itself." [12] "As soon," however, "as the means of production have ceased to be converted into capital (which includes also the abolition of private property in land), credit as such has no longer any meaning." [13] But then neither Marx nor his followers believed an immediate or rapid change from capitalism to socialism possible.

Lenin and his party accepted the above views as well as the preconceptions that lay at their foundation. It may also be added that Lenin firmly believed that the noninterference with the Paris banks on the part of the communards was among the most important factors which contributed to the fall of the Paris Commune.[14]

The following lines, written by Lenin in April, 1917, in the form of questions and answers on the platforms of the various

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however, "the centralization of credit in the hands of the State" was but a part of a general scheme which sought to sweep away capitalist society. He and the socialists, we are told, would use such centralization for the purpose of directing credit into industries that need to be developed and diverting it from industries that stand in no such need. In short, they would plan production and thus avoid crises.

[12] Marx, *Capital*, p. 713.

[13] *Ibid.* Accordingly Bukharin and Preobrazhensky (*op. cit.*, pp. 223-24) explain that "the banks are not only spiders that suck the surplus values of workers and peasants. They have yet another function . . . thus banks inadvertently become, so to speak, bookkeeping and controlling offices of the capitalist society. And this shows the part that the banks can play in a socialist society and what the proletariat must do with them after it seizes power . . ." Inasmuch as the banks taken over by the proletariat will be used for the purpose of accounting, control, and allocation of funds, "the proletariat state will have a complete picture of what it spends and for what purpose, and of what it gets and from what source." As the state will be evolving into a manager of a single gigantic economic apparatus of a country, "it is clear that the Bank will then become what a bookkeeping office is to a business enterprise." "The Bank as such will by degrees be eliminated and will evolve . . . into a central bookkeeping office of the communist society."

[14] Lenin, "The Commune and its Lessons," *Collected Works*, XI, Pt. II, 510. By not only depriving themselves of financial resources but by placing those resources at the disposal of the enemy. Also by permitting the banks (which were hostile to the communards) to maintain connections with the Versaillese.

political parties in Russia, in which he states the stand of his own party concerning banking and credit institutions, are, therefore, not surprising. "Workers' soviets . . . and representatives of bank employees should be immediately prepared for the task of taking the practically feasible and totally realizable steps—first, to merge all banks in one National Bank, then to establish a control of Soviets of Workers' Deputies over banks and syndicates and after that to nationalize them, that is, to make them the property of the entire nation." [15] This view was repeated by Lenin on a number of occasions, and in an article entitled "The Threatening Catastrophe and How to Combat It," in September, 1917, about six weeks before the fall of the Kerensky government, one finds at the head of the list of basic measures proposed by him the following: "all banks be merged in one and the state control its operations, that is, the nationalization of banks." [16] "To talk about 'regularization of economic life' and to evade the question about the nationalization of banks," continues Lenin, "means either to betray complete ignorance, or to fool the 'simple folk' with high-sounding words. . . . To control the delivery of bread, or, in general, the production and distribution of goods, without regulating banking operations is an absurdity." [17]

But when Lenin in those early days spoke of the nationalization of banks he did not mean the confiscation of the assets of the banks and of the valuables in the safe deposit boxes. Indeed, he was very careful to explain that nationalization of banks did not mean confiscation of private property. Thus, in the same article, Lenin says: "that nationalization of banks is so often confused with the confiscation of private property is due to the bourgeois press. . . . The ownership in the funds with which the banks operate and

[15] Lenin, "Political Parties in Russia and the Problem of the Proletariat," *Collected Works*, XIV, Pt. I, 70.

[16] Lenin, *op. cit.*, XIV, Pt. II, 182. The remaining proposed measures (in the order in which they were enumerated by him) were: (1) nationalization of syndicates, that is, of the monopolies in the sugar, oil, coal, and metal industries; (2) abolition of business secrecy; (3) compulsory trustification of all industry, trade, and business in general; (4) compulsory membership of the population in consumers' co-operative associations.

[17] *Ibid.*, pp. 182-83. See also his article "The Threatening Catastrophe and Boundless Promises" in *Pravda*, May 29, 30, 1917.

which are concentrated in those banks is attested by printed and written certificates which are known as shares, bonds, notes, certificates, etc. Not one of those certificates gets lost or is changed when the banks are nationalized, that is, when they are merged in one State Bank. He who had 15 rubles according to his pass book remains the owner of 15 rubles after the nationalization, while he who had 15 millions will have 15 millions in the form of shares, bonds, notes, and so forth after the nationalization . . ." [18] In a paragraph preceding this Lenin says "in reality, the nationalization of banks decisively does not take away even a single copeck from anyone . . ."

"Of what significance then is the nationalization of banks?" asks Lenin, and answers: "In that no real control of banks and their operations is possible while they are separate entities, it is impossible to follow up all of the complicated, involved, and clever tricks that are used in drawing up financial statements, in setting up fictitious enterprises and affiliated branches, in the use of 'dummies,' etc., etc. The mere merger of all banks in one, in itself, does not mean any change whatsover in property relations, does not take away, we repeat, a single copeck . . ." [19]

The fate of the banks in balance.—On the day following the overthrow of the Kerensky government, the new Soviet government posted at the offices of the State Bank (a state-owned institution it will be remembered) a detail of trusted soldiers. Soon after, the Soviet government turned to the bank for funds with which to carry on governmental functions, ordering the latter to place at its disposal twenty million rubles.[20] The manager of the bank, who was hostile towards the new regime, refused, however, to honor that order under the pretext that the bank could not spare any funds. When the order was repeated the manager called a meeting of the employees of the bank at which it was decided to turn down the government's demand and to declare a strike against

[18] *Ibid.*, p. 183.

[19] *Ibid.*, pp. 183-84.

[20] *Our Monetary Circulation*, p. 47. According to other sources the order called for less. See G. Y. Sokolnikov, *Financial Policy of the Revolution* (Moscow, Commissariat of Finance, 1925), I, 35; also G. Lemaire, *Le Systeme bancaire de la Russie Sovietique* (Paris, 1929), p. 24.

it. The government immediately marched a detachment of troops with fixed bayonets into the bank, appointed a commissar to take the place of the manager, and permitted those employees who wished to continue at work to return to their jobs. In a like manner, the government proceeded to appoint commissars as heads of many branches and offices of the State Bank.

Meanwhile, on the third (sixteenth—new style) of December the commissar of the State Bank came to an understanding with the private bankers. They were permitted to draw weekly up to fifty million rubles of their balances at the State Bank, and were in addition permitted to draw checks in excess of that sum, provided the sums so drawn were used to finance industry. It was also agreed that the state would exercise *control* over all payments made by those banks.

The communists hoped that the control thus established over the banks would enable them to accomplish, among other things, the following: prevent the financing of a campaign against themselves, prevent the withdrawal and concealment or transfer abroad of funds by the bourgeoisie, as well as a possible move on the part of bankers to defeat the attempt of the state to control industry.

The nationalization of banks. The decree of December 14 (27), 1917.—The arrangement with the private bankers proved, however, to be short-lived, for on the morning of December 14 (27), 1917, before the Petrograd banks opened their doors for the day's business they were occupied by troops.[21] In the evening of the same day Lenin argued before the All-Russian Central Executive Committee the necessity of issuing immediately a decree for the nationalization of banks:

We wanted to introduce a control over the banks. We invited the bankers and together with them and with their approval worked out measures for a complete control and accounting to accompany loans.

[21] In Moscow this was done on the following day (December 15, 1917). This is how Lenin described the incident, "We said: we have armed workers and peasants. This morning they must occupy all private banks . . . And after this is done, when the power [over banks—Author] will be in our hands, we shall discuss what measures we are to take. And in the morning the banks were occupied, while in the evening the central executive committee resolved that 'the banks are declared to be national property.' . . ." Quoted by J. Rubinshtein, *The Rôle of Banks in the Soviet Economy* (Moscow, State Press, 1928), p. 44. From Lenin, *op. cit.*, XV, 84.

But among the employees of the banks were men who held the interests of the people close at heart, and so they said: "the bankers are deceiving you, make haste to stop their criminal activity which is aimed against you." [22] And so we made haste.

We know that is a complicated measure. None of us, not even those who have a training in economics, will undertake to prepare it. We shall employ experts, people who are skilled in such work, but only after we have the keys in our own hands. Then we can even employ as consultants ex-millionaires . . .

We wished to follow the path of conciliation with the bankers, we supplied them with credit for the purpose of financing business, but they resorted to a sabotage of unprecedented dimensions, and so experience compelled us to adopt different measures in order to insure control. . . . If we do not affirm the decree right now the bankers will take all the necessary steps to shatter our economy.[23]

Accordingly, the Central Executive Committee signed on that day what is known as the decree for the nationalization of banks.[24] The decree read as follows:

In the interests of a rational organization of the national economy, in the interests of a thorough eradication of banking speculation and the complete emancipation of workers, peasants, and all toilers from the exploitation of bankers' capital, and with a view to establishing a bank that would really serve the interests of the people and the poor classes, a single People's Bank of the Russian Republic, the Central Executive Committee decrees that:

1. Banking is declared to be a state monopoly.

2. All existing private joint-stock banks and banking houses are merged in the State Bank.

3. The assets and liabilities of the banks subject to liquidation are to be taken over by the State Bank.

[22] Apparently the bankers had no difficulty in evading the control set up by the communists, whose ranks included very few who knew anything about the banking business, accounting, or auditing. Especially weak was the control in the provincial towns where the banks had branches. It was charged that the banks, taking advantage of this weakness, were transferring funds to certain strategic points where the anti-communists could claim them, or from which points the funds could be sent abroad, and that the bankers assisted the bourgeoisie in withdrawing their deposits for the purpose of sabotage and open warfare against the communists. It was further charged that the bankers were not only encouraging the industrialists to fight the imposition of state control over industry, but threatened "that no credit whatsoever would be given to those enterprises whose actions will in any way be subject to such control." See Sokolnikov, *op cit.*, I, 42-43.

[23] Lenin, *op. cit.*, XV, 48-50.

[24] Decree 150.

4. The manner in which the merger of the private banks in the State Bank is to be carried out is specified in a special decree.

5. The temporary management of the affairs of the private banks is transferred to the council of the State Bank.

6. The interest of the small depositors will be fully protected.

The inspection of the safe deposit boxes.—On the same day the Central Executive Committee decreed [25] the inspection of the "strong boxes." According to that decree those who had safe deposit boxes in the banks were to present themselves within three days after notification (unless an extension was obtained) and open their boxes for the government inspection. Money found in those boxes was to be deposited in the State Bank and a checking account in the name of the owner was to be created.

Gold, whether in coin or bullion, was to be confiscated and turned over to the government.

The boxes of those who had failed to open them as required by the decree were to be opened by the inspectors and the contents confiscated.

On the basis of the above decree the Commissariat of Finance on April 29, 1919, ordered that the maximum which one could claim from the government was not to exceed ten thousand rubles.[26]

Confiscation of all the funds and the annulment of all shares of private banks.—On January 26, 1918, the government decreed the confiscation of all funds of the private banks and their transfer to the State Bank.[27] The same decree provided for the annulment of all bank stock and forbade the further payment of dividends thereon. The owners of bank stock were instructed to deliver it or to indicate its whereabouts at once to the local branches of the State Bank, and one's entire property was to be confiscated for non-compliance with the provisions of the above decree.[28]

[25] Decree 151.

[26] The same amount was set as the maximum compensation to owners of "liquidated" securities. Anything above that amount was transferred to the government. At the end of April, 1919, 10,000 rubles, according to the All-Union Index of Labor Statistics, amounted to approximately 25 pre-war rubles, or to $12.50.

[27] *Collected Decrees*, 1918, Decree 295.

[28] To prevent, of course, its transfer to foreigners who would then enter claims against the government. Also, Russian bank stock carried with it, so to speak, a control over industry.

All transactions in such stock were forbidden and the offenders were subject to imprisonment for a term not to exceed three years.[29]

The liquidating technical collegiums. The renaming of the State Bank. The liquidation of the joint-stock commercial banks.—Special committees consisting of from three to five skilled former bank employees, known as the "liquidating technical collegiums," were installed at each of the private banks. These were instructed to draw up, as of December 13, 1917 (that is, as of the day preceding the nationalization decree), liquidating balance sheets preparatory to the transfer of the assets and liabilities of those banks to the State Bank, which in 1918 was renamed *People's Bank,* and of which they were to become branches.

To co-ordinate and direct the work of these collegiums in April, 1918, a council of experts was established at the bank. Except for the commissar of the bank, Stunde, the vice-commissar, Krestinsky, and a few other communists, the council was composed largely of directors and officers of the former private banks, and, in general, of people who were hostile to the new regime. The work of the council was progressing very slowly, and it was soon dissolved. It was alleged that its bourgeois members were resorting to dilatory tactics in the hope that in the meantime the soviets would be overthrown.

It was furthermore alleged that they were particularly interested in the taking of a minutest inventory of the seized banks in order to enable their former owners to present claims to a successor government. However that may have been, the process of nationalizing the banks without the aid of a directing and co-ordinating agency had to proceed along lines different from those originally contemplated. The various private banks were nationalized piecemeal and seemingly without any prearranged plan. The entire process proved to be long drawn out.

By the end of 1919 the liquidating committees submitted liquidating balance sheets for about two-thirds of the former private banks, and as a result the balance sheet of the People's Bank

[29] A decree forbidding all dealings in securities in general was published as early as December 29, 1917 (Decree 185).

swelled by 12,700,000,000 rubles.[30] This figure, however, is quite misleading, for it measured neither the state's pecuniary gains from the nationalization of those banks nor their former owners' losses. The liquidating value of the banks' most important group of assets, the loans and discounts, shrank to a fraction of the nominal amount. Many of the borrowers were either shutting down their factories and other enterprises or else surrendering them to the government.

The collateral in the form of stocks and bonds, in which all dealings became illegal, no longer represented any value inasmuch as the government had annulled its own debt and was nationalizing the very enterprises which were represented by securities held in the portfolios of the banks. The collateral in the form of merchandise (as well as merchandise owned by the banks) was being seized, requisitioned, confiscated, and otherwise taken away by the government. The economic and political policies of the government could not fail to cause the assets of the banks to evaporate.

The liquidation of the mortgage banking institutions.—The joint-stock commercial banks were not the only, nor even the first, credit institutions to be liquidated by the Soviet government. In fact, the Nobles' State Land Bank and the Peasants' Land Bank, the two mortgage banks owned by the state, were the first ones to be abolished. The socialization of the land and the projected "liquidation" of the nobility as a class rendered the two land institutions obsolete. Accordingly, on November 25 (December 8), 1917, the government instructed the State Bank to liquidate them.[31] As shown by the liquidating balance sheets (which were submitted only on June 1, 1920), the loans of the Nobles' State Land Bank amounted to a little over 1,000,000,000 rubles, and those of the Peasants' Land Bank to about 1,400,000,000 rubles. The bonds, mortgages, and certificates that were sold by them for the purpose of raising funds roughly approximated the loans extended by them.

[30] *The Social Revolution and Finance,* pp. 72-78. That not all joint-stock commercial banks could be liquidated by the committees was due to the fact that the assets of some of the banks, as well as their records, disappeared during the Civil War.

[31] Decree 56.

The forces which rendered the two state mortgage banks obso lete also sealed the fate of the ten private joint-stock land banks, and the municipal and district credit societies, all of which engaged in mortgage banking. Not all of these, however, were ordered liquidated at the same time. The liquidation of the joint-stock land banks, for instance, was ordered on December 24, 1918, while that of the municipal and district credit societies was decreed in May, 1919. The liquidating statements showed that the outstanding loans of joint-stock land banks were somewhat below 1,500,000,000 rubles, while those of the municipal credit societies amounted to almost 1,000,000,000.[32]

An attempt was made to collect the debts from borrowers who were still in possession of city real estate. The attempt, however, met with no success and on May 4, 1920, the Council of People's Commissars decided to cancel all mortgage indebtedness.

The liquidation of the mutual-credit societies and city public banks.—Although the joint-stock commercial banks were nationalized and liquidated at an early date, other short-term credit institutions, such as the numerous (some 1,200) mutual-credit societies and the city public banks, were permitted to go on undisturbed until the end of 1918.[33] Several reasons account for that seeming oversight. The government as yet lacked the proper organization and personnel. Besides it hesitated to proceed with the nationalization of such popular, democratic institutions as the mutual-credit societies. Its action was finally prompted by the suspicion that the latter were carrying out transfers of funds to places over which the Soviet government had no jurisdiction, and that the middle and upper classes began to show preference for the unnationalized banks.[34]

The liquidation of foreign banks.[35]—This was accomplished on

[32] *The Social Revolution and Finance*, p. 74.

[33] The order for the liquidation of the mutual-credit societies was issued on October 10, 1918 (Decree 806). The order for the liquidation of the city public banks was issued on December 2, 1918 (see *The Social Revolution and Finance*, p. 41).

[34] *Ibid.*

[35] There were two foreign banking houses in Russia, the Crédit Lyonnais and the National City Bank of New York. The Crédit Lyonnais had agencies in Petrograd, Moscow, and Odessa, and had been doing business in Russia since 1891. The Na-

the strength of a decree that was signed by the Council of People's Commissars on December 2, 1918.[36] The instructions for their liquidation were announced by the Commissariat of Finance on April 22, 1919. According to those instructions whatever was to be realized from the liquidation of the banks' assets was to be used first of all to discharge the obligations of those banks to the treasury and to the People's Bank; then to satisfy the claims of Russian depositors and creditors; and finally to satisfy foreign depositors and creditors, the poorest of them to be paid off first. Anything over and above that was to be turned over to the owners of the banks. But as has already been remarked, the economic and political policies of the government rendered the greater portion of bank assets quite valueless.

The liquidation of the central bank of co-operative credit (Moscow People's or Narodnyi Bank).[37]—The decree for the nationalization of the Moscow Narodnyi Bank was also signed on December 2, 1918.[38] According to that decree the Moscow Narodnyi Bank was declared nationalized and was to be merged in the People's Bank of the R.S.F.S.R. to which all of the bank's assets and liabilities were to be transferred. Those who had contributed to the capital of the Moscow Narodnyi Bank were to be credited on the books of the People's Bank (former State Bank), and checking accounts were to be opened in their names—an operation which, as we have seen, was quite meaningless in view of the rapidly depreciating currency.

The circumstances surrounding its nationalization and liquidation are interesting. Undisturbed for about a year after the publication of the nationalization of banks decree on December 14, 1917, the Moscow Narodnyi Bank quite successfully competed with the People's Bank and with the nationalized joint-stock commercial banks which were now branches of the latter. Since the

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tional City Bank of New York began its operations in Russia in 1916, that is, in the year preceding the Revolution.

[36] Decree 907.

[37] It will be noticed that the name of this institution resembled that of the People's Bank (former State Bank). The name of this bank was, however, *Moscow* People's Bank (*Moskovskii* Narodnyi Bank).

[38] Decree 912.

Moscow Narodnyi Bank offered no interference whatsoever with the deposited funds, permitting depositors to withdraw as much of their deposits as they wished, while the People's Bank and its branches resorted to a procedure which was very much akin to the confiscation of the deposited funds, deposits were, of course, flowing into the former and not into the latter.[39]

It could not be said, however, that it was only the bourgeoisie which was shunning the state credit institutions. To its great amazement the government found out that such an important institution as the Commissariat of Supply, as well as a number of other Soviet organizations, were depositing all of their receipts (among them subsidies and funds allocated to them through the budget and withdrawn by them from the People's Bank) in the Moscow Narodnyi Bank.[40]

The government suspected the Moscow Narodnyi Bank and the co-operatives which it financed of disloyalty, but for obvious political reasons did not wish to seize them. Instead, it issued an order to all its agencies requiring them to carry their balances with the People's Bank. Government agencies began to withdraw their balances from the private bank and deposit them in the state-owned institution. The Commissariat of Supply, for instance, wrote out a check for 90,000,000 rubles and demanded pay-

[39] Following the nationalization of banks, the government adopted a policy of withholding depositors' balances. In part, due to a desire to avert a run on the government banks, the action undoubtedly aimed to shatter the bourgeoisie as a class, render impossible the financing by them of a counter-revolution, and break the resistance of the "intelligentzia" and compel them to work for the government. The maximum that could be withdrawn by an individual within any one week was fixed at 125 rubles, which, according to the All-Union Index of Labor Statistics, purchased in January and February of 1918 the equivalent of four to six pre-war rubles. In practice, however, the former bourgeoisie could not get even that much. On April 8, 1918, the maximum that one could withdraw for his own needs was raised to 750 rubles, but the depreciation of the ruble rendered the gain illusory. The postponement of payment under these circumstances was akin to confiscation. Realizing that as a result of this policy the people would begin to distrust the government-owned banks, the commissar of the People's Bank announced that under no circumstances would any restrictions as to withdrawals apply to accounts opened after January 1, 1918. Nevertheless, many felt that at best they had nothing to gain by dealing with the government, and that on the whole it was wiser not to let the latter know just how much one possessed.

[40] A. Potiaev, *Financial Policy of the Soviet Government* (Petrograd, Commissariat of Finance, 1919), p. 27.

ment. Faced by an organized run, which it was unable to meet, the Moscow Narodnyi Bank decided that there was nothing left for it to do except to notify the government that it wished to become nationalized.[41] The government promptly complied with its request and converted it into a co-operative branch of the People's Bank of the R.S.F.S.R.[42]

The People's Bank of the R.S.F.S.R.—The nationalization of the Moscow Narodnyi Bank completed the government's task of merging all private banks in the People's Bank. The People's Bank and its branches also took over the functions which were performed by the subtreasuries (*mestnye kaznacheistva*).[43] On December 28, 1918, the bank swallowed the Credit Chancellery and the Department of Plants for the Preparation of State Papers, while on May 4, 1919, it added to its trophies the Department of State Treasury (*Departament Gosudarstvennogo Kaznacheistva*).[44] The government further ordered (in June and July, 1919) the establishment within the bank of an estimate, and of a budget department, so that with the exception of tax matters, which were quite unimportant during this period, the People's Bank acquired

[41] As Potiaev (*op. cit.*, p. 29) puts it, "As soon as we did to the Moscow Bank what was being done to us for a whole year—withdrawing the balances and making no further deposits—it became unable to meet the demand for payments and asked to be nationalized."

[42] Since the co-operatives acted as purchasing and distributing agents of the Commissariat of Supply, they looked to it for whatever funds were needed for these operations. The state therefore decreed (on December 13, 1920) that a co-operative that is commissioned to purchase or produce certain commodities is to look for funds to the commissariat upon whose orders such purchase or production is carried out. This decree therefore relieved the "co-operative branch" of the People's Bank from any further credit operations. *Collected Decrees*, 1920, Decree 530.

It will be remembered that by the decree of January 27, 1920, all forms of co-operatives were united with the *Consumers' Co-operatives* (in what was known as the *All-Russian Central Union of Consumers' Co-operatives or Centrosoyuz*) as special sections of the latter, and that the assets and liabilities of the various credit, and loans and savings co-operative associations were transferred to the respective local consumers' co-operatives. *Loc. cit.*, Decree 37.

[43] This led to the liquidation of the subtreasuries in places where branches of the bank were found. Where there were no such branches, existing subtreasuries were converted into branches of the People's Bank. This process was going on even before the state had decreed (on October 31, 1918) that the branches of the bank be vested with those functions.—*Our Monetary Circulation*, p. 48; also *Collected Decrees*, 1918, Decrees 848, 849.

[44] *Our Monetary Circulation*, p. 48.

almost all functions of the treasury agencies.[45] But, as will presently be seen, the bank, as if suffering from a wasting disease, remained lean despite what it consumed. The inability of the state to digest its acquisitions over a short period of time, the changed conditions, the new ideology—all these contributed heavily to the breakdown of this hapless institution.

To begin with, the bank and its branches continued to be manned by former employees whom the government clearly distrusted but whom it was compelled to retain because very few communists knew the principles of banking. In fact, the credit policy of the nationalized banks was in numerous instances directed against the interests of the state.[46] But even apart from this defect the People's Bank, together with its acquisitions, was no more than a mere shell of the old banking system. The former volume and variety of transactions were now but a remembrance. The low productivity of industry, the regime of fixed and unadjusted prices in the presence of a rapidly depreciating currency, the destruction of free markets and the attempted substitution in their stead of a "natural" economy—rendered industry profitless and tended to undermine the very base upon which bank credit is granted. Nevertheless, because the state had not been successful in satisfying *in natura* the needs of industry and of the men employed therein, and since many commodities could be purchased for money, the various enterprises could not keep going without financial assistance. Under these circumstances the government decided to subsidize industry through the state budget. The funds so provided were placed by the state at the disposal of the Supreme Council

[45] *Ibid.*, pp. 48-49.

[46] In describing the operations of one of the branches of the People's Bank (a nationalized, formerly private bank), Potiaev (*op. cit.*, p. 31) says: "It worked in the following manner: the Supreme Council of National Economy declares that such and such commodities are henceforth subject to confiscation or requisition. And so the owner of those commodities goes to the nationalized banking enterprise, hypothecates his commodities at higher prices [than those the government was going to pay him.—Author], receives full value, and on the next day the commodities are requisitioned by the Supreme Council . . . This was done in a countless number of cases. I must say that 99 percent of all the confiscated and requisitioned commodities were in one way or another paid for by the People's Bank."

It will be remembered that during the early period some of the nationalized banks granted loans against commodities, provisioning being one of the most important operations.

of National Economy, to which various enterprises had to look for aid.[47]

Meanwhile the branches of the bank were being continually subjected to a process that caused the loosening of their ties to the parent institution. This was brought about by the following circumstances: right after the Revolution local soviets began to select from their midst executive bodies of which *financial sections* or *committees* formed a part. Although at first they aimed merely to supervise the activities of the various agencies carrying on fiscal operations, the financial sections soon began to take an active part in the former's operating functions. During those troubled times when territory was intermittently gained and lost, it was inevitable that the local soviets should take for themselves many of the rights which the central authority would have liked to wield. In that manner the financial sections began to exercise control over the branches of the People's Bank, and by the beginning of 1919 most of those branches were in reality agencies of the former. The decree of September 29, 1919, merely legalized the existing relationship.[48]

Earlier in the year, in the month of March, 1919, the Eighth Congress of the Russian Communist Party met and adopted a program wherein it advocated, among other things, not only monopolization of banking by the Soviet state but also "a radical change and simplification of banking operations by transforming the banking apparatus into an apparatus of uniform auditing and

[47] A. B. Shtern, *State Financing of Industry* (Moscow, 1924), pp. 12-38. In presenting this plan before the Second Congress of the Councils of National Economy in 1918, G. Y. Sokolnikov said: ". . . if financing of industry is to remain a function of the bank, we will follow the capitalistic mode of procedure where in reality it should be broken . . . at present the commanding rôle must pass from the Bank to the agencies that organize production—to the Supreme Council of National Economy, which unifies this activity . . . we need finance committees that are closely interconnected with the central organs of management and that will finance industry that is placed under their aegis, according to the plans of the S. C. of N. E. . . ." *Ibid.*, pp. 15-16. The resolutions of the Congress—which called for extreme centralization of production, for the financing of the latter through the state budget, for the transition to a "natural" economy, for the gradual elimination of the use of money, and for the conversion of the People's Bank into an auxiliary of the Supreme Council of National Economy—certainly show a reflection of the above views. *Ibid.*, pp. 23-25.

[48] *Our Monetary Circulation*, p. 49.

general accounting of the Soviet republic . . . As a planned social economy becomes organized this will lead to the extinction of the bank and to its transformation into a central bookkeeping apparatus of the communist society." [49]

Impatient, however, with the slow, transitory, evolutionary process that was predicted by Marx and Lenin, and yearning for what, according to those teachings, was not likely to come within their lifetime, some communists either forgot or ignored the words of those men, or, misreading the signs of the time, confused the order of the day with the order that is to come under "the higher phase of socialism." At any rate, they demanded for the national economy changes which, according to Marx and Lenin, were supposed to take place only upon the coming of that "higher phase"—a *sine qua non* condition.[50]

The abolition of the People's Bank.—As a result of these aberrations, the People's Bank, already deprived of its banking functions and already bereft of its branches, was on January 19, 1920, decreed to be "abolished." [51] "Since," read the decree, "the nationalization of industry concentrated in the hands of the government the most important branches of production and distribution, and since the nationalized industry and trade were financed through the general budget, there was no *raison d'être* for the People's (State) Bank. And although credit institutions were still needed by the small private trade and those citizens who wish to deposit their savings," the decree added, "those operations have gradually lost their importance and do not require special credit institutions —these problems, at present of secondary importance, will be cared for by the new organizations of the Commissariat of Finance . . . Therefore . . .

[49] The Program of the Russian Communist Party (Bolsheviki), adopted by the Eighth Congress, March 18–23, 1919. Given in Bukharin and Preobrazhensky, *op. cit.*, p. 266.

[50] Lenin later said: "A none too long experiment brought us to a conviction that this construction was erroneous, that it contradicted what we had written earlier on the subject of transition from capitalism to socialism—a conviction that without passing through a period of socialist audit and control, it is impossible to reach even the lower phase of communism." Lenin, *op. cit.*, XVIII, Pt. I, 372.

[51] *Collected Decrees*, 1920, Decree 25.

(1) The People's (State) Bank of the R.S.F.S.R. with its entire staff, its organization and institutions is to be abolished.
(2) The decree . . . No. 849 of October 31, 1918[52] . . . is to be repealed.
(3) The assets and liabilities of the former People's Bank are to be transferred to the *Central Budgeting and Accounting Administration.*
(4) The above-mentioned Administration and local agencies will carry on those of the former banking operations which are still required and important.
(5) The Commissariat of Finance is to be entrusted to carry out this decree."

The net result of the above decree for the abolition of the bank and for the substitution in its stead of a Central Budgeting and Accounting Administration consisted, however, of no more than a mere change in the name of the institution. It was more important as a declaration of the belief or hope that the "higher phase of socialism" or communism was in sight, than as a legislative act purporting to bring about a change in the structure or functions of the credit mechanism of that country. The structure of the new institution closely resembled that of the old. The two important functions which the People's Bank performed before its "abolition," the work on the estimates and the budget, and the note issue, were now being performed by the Central Budgeting and Accounting Administration. Of the two functions by far the more important during this period was the note issue, a topic that is treated in the next chapter.

[52] *Supra,* footnote 43.

V

TOWARD THE ABOLITION OF MONEY
(THE MONETARY SYSTEM, 1918–21)

The budget during 1918–21.—Upon their seizure of power the communists were face to face with a problem all governments have to solve, how to raise revenue for necessary state expenditures. By spring, 1918, the Civil War had assumed major proportions; expenditures, of course, multiplied, and this served to inject further complications into an already difficult situation. We have seen that the earlier governments, the Czarist and then the Provisional, in order to raise revenue, had resorted to loans, taxation, and the printing press. The Soviet government, however, was prevented from following in the footsteps of its predecessors in the matter of raising revenue. For example, it could not, for a number of reasons, hope to raise either foreign or domestic loans.

It will be recalled that early in its career, on January 28, 1918, the government had announced that "all foreign loans are annulled unconditionally and without exception," and had likewise repudiated domestic loans, except that bondholders of small means whose holdings did not exceed 10,000 rubles were allowed to exchange them for new bonds,[1] a rather illusory privilege in view of the rapid and progressive depreciation of the currency. Such repudiation in itself would have caused lenders to refrain from advancing funds to the new government. It would be a mistake, however, to assume that, had it not been for this overt act of repudiation, the Soviet government might have counted on foreign loans as a source of revenue. It is hardly likely that international bankers would have rushed financial assistance to a country which was expropriating the wealthy, and was resorting to other measures equally distasteful to them.

In so far as domestic borrowing was concerned, it may be pointed out that even Kerensky's government, which had not repudiated any debts, had been unsuccessful in its efforts to float

[1] *Collected Decrees*, 1918, Decree 353.

the so-called "Liberty Loan." Continued inflation and high rates of interest, as is well known, are not conducive to the purchase of bonds yielding a fixed return. Nor could the communists look to taxation as a source of revenue. Before coming into power, they themselves had decried and agitated against the already oppressive taxes. Besides, the regime of "regulated" and "fixed" prices, which had been introduced by the Imperial government and continued by the Provisional government and later by the communists themselves, allowed for no adjustment on account of the depreciation of the currency, thus making any effort to increase the rates of taxation or to add new taxes awkward. Moreover, the Soviet government, under the pressure of Civil War, created conditions which made the existence of taxes meaningless and their collection impossible. Indeed, the abolition of private property in land, the nationalization of commercial and industrial enterprises, the repudiation of securities, and the prohibition of private trade destroyed the taxpayer's ability to earn an income and caused, so to speak, the disappearance of the very objects of taxation.[2]

It is thus evident that pecuniary taxes and loans, the two most important sources of revenue ordinarily available to a state, were lost to the Soviet government. But it still had the printing presses which had netted its predecessors large returns. Nothing could be simpler under these circumstances than the continued operation of these presses, and the note issue thus derived did enable the government to procure, especially during the early part of the period, much of what was needed for the army and the civil population. This, however, was only one of the sources of revenue during this period. Another important source consisted of the supplies left behind by the old regime. The compulsory levies and requisitions in the villages constituted one more important source. Besides, the government exacted certain services from the peas-

[2] Although insignificant as a source of revenue, the collection of taxes in money was formally stopped only in the early part of 1921, on the very eve of the "New Economic Policy." Insignificant as a source of revenue were also the various special levies and taxes *in money* assessed by the government against the former bourgeoisie and rich peasants, such as the so-called "Single Payment Extraordinary Ten Billion Rubles Revolutionary Tax" of November 2, 1918. See P. P. Hensel, *Taxation in the U.S.S.R.* (Moscow, 1926), p. 6.

antry (such as cutting wood, drayage, roadwork, removal of snow from railroad tracks, etc.) and even from the urban population (street cleaning, etc.). The production of the nationalized enterprises constituted an additional source of revenue in kind for the government.

The state budget during those years was, therefore, made up not only of revenues and expenditures in money, but, and to very large extent, in kind as well. The most important items among the expenditures were those connected with the Commissariat of War, with the Supreme Council of National Economy, which supplied the nationalized enterprises with resources, and the Commissariat of Transportation, which was entrusted with the operation of the railroads. The most important items among the revenues were those of the Supreme Council of National Economy, which was the recipient of the old supplies and of whatever was produced by the various enterprises, and of the Commissariat of Supply, which received the compulsory collections of foodstuffs from the peasants.[3]

It is, however, impossible to present even an approximate quantitative picture of the budgets of that period. Some of them, notably those for the second half of 1919 and for the year 1920, were approved by the Council of People's Commissars only in the fall of 1921 and were dated back.[4] In fact, there is no way of finding out whether the figures so approved correspond with the *actual* receipts and expenditures during 1918–21, for the Commissariat of Finance has no such data.[5] As one authority on the Russian budget says, "a perusal of the budget for those years will give a picture not of what actually transpired but merely of the desires and suppositions of the departments. . . ."[6] It is not difficult to see the reason for such a predicament. When inflation enters its advanced stages it disrupts all calculations and makes planning and the maintenance of a budget impossible, for the lapse between the

[3] G. G. Solovei, *State Budgets* (Moscow, State Press, 1928), pp. 73 ff.

[4] G. Y. Sokolnikov, *Monetary Reform* (Moscow, Commissariat of Finance, 1925), p. 89.

[5] L. N. Yurovsky, *Towards a Monetary Reform* (Moscow, Commissariat of Finance, 1924), p. 17.

[6] S. A. Golovanov, *On the New Path* (Moscow, 1923), II, 4.

time at which an estimate is made and the time at which the actual collections and expenditures are made is sufficient to reduce the purchasing power of the monetary unit in terms of which the estimate is made to a fraction of what it had been on the day of estimate.

In this instance matters, moreover, were complicated by the fact that the various revenues and expenditures were executed in heterogeneous units—one part representing transactions in kind; another, transactions in money, the latter being further divided into transactions involving "fixed" prices and transactions involving "free market" prices.[7] Due to the disorganization of the governmental machine and the fact that the number of men trained in fiscal matters at the disposal of the government was very small, a large part of those transactions remained unrecorded.[8] It is most likely, therefore, that the budgetary figures available for the period under review represent merely those transactions which involved for their settlement the issuance of paper money, thus leaving out entirely the very important section of transactions in kind.[9] The available figures are presented in Table 10.

TABLE 10

RECEIPTS AND EXPENDITURES, 1918–20[a]

(*In millions of rubles*)

	Receipts	*Expenditures*	*Deficit*
1918	15,580	46,706	31,126
1919	48,955	215,402	166,447
1920	159,604	1,215,159	1,055,555

[a] *The Social Revolution and Finance*, pp. 97-101, 117-22.

[7] Moreover the various monetary units then in use, in addition to having a purchasing power that was highly inconstant over a period of time, differed among themselves as to purchasing power at any one time. See *infra*, pp. 79-82.

[8] For a detailed discussion of the budget during 1918–21, see Sokolnikov and Associates, *Soviet Policy in Public Finance 1917–1928* (Stanford University Press, 1931).

[9] According to Golovanov's (*op. cit.*) calculation, e.g., the total budgetary revenue (that is the revenue derived not only from note issues but "in kind" as well) for

The volume of notes in circulation.—According to those figures the deficit for 1918, 1919, and 1920 was over 31,000,000,000, 166,000,000,000, and 1,000,000,000,000 rubles respectively. Inasmuch as the printing press was the instrumentality for bridging the gap between expenditures and revenues in money, the note issue during those years is represented by related quantities. As can be seen from Table 11, the note issue in 1918 amounted to 33,676,000,000 rubles, in 1919 to 164,401,000,000 rubles, and in 1920 to 943,581,-

TABLE II

THE VOLUME OF NOTES IN CIRCULATION

END OF 1917 TO 1922 [a]

(*In millions of rubles on the first of the month*)

	1917	*1918*	*1919*	*1920*	*1921*
January		27,650.2	61,326.2	225,015.2	1,168,596.9
February		29,563.5	65,526.5	260,231.3	1,298,828.9
March		31,019.3	69,349.4	293,063.0	1,488,222.9
April		33,975.6	75,185.5	340,662.3	1,686,683.5
May		38,266.2	81,050.0	387,706.7	1,917,251.8
June		40,743.4	92,479.9	450,668.9	2,122,292.3
July		43,711.9	101,030.7	511,815.8	2,347,164.1
August		46,394.9	112,350.0	580,703.8	2,808,096.7
September		48,674.0	126,207.8	651,345.6	3,510,674.2
October	17,577.9	51,525.5	148,201.5	745,157.5	4,529,427.9
November	19,577.4	54,295.7	170,108.8	862,765.8	6,479,713.1
December	25,295.0	57,370.6	192,452.3	995,636.6	9,845,194.9 [b]

[a] *Our Monetary Circulation*, p. 153.

[b] By the end of the month the circulation rose to 17,539,232,100,000 rubles.

1920 amounted to 1,726,000,000 *gold* rubles. Of these only 126,000,000 rubles (or 7.3 percent) were derived from note issues. But even this figure is far from exact, for on the expenditures side (by which the needed revenues are gauged) the item of depreciation of buildings, machinery, rolling stock, etc. is entirely overlooked. One would also have to appraise correctly the supplies left by the previous regime and used up during this period.

000,000.[10] During 1921, when the revenue amounted to 4,400,000,000,000 rubles and the expenditures to some 26,000,000,000,000 rubles and when the deficit, therefore, amounted to almost 22,000,000,000,000 rubles, the note issue was represented by 16,371,000,000,000 rubles.[11]

By adding to the note issues of 1918, 1919, and 1920 those issued during November and December, 1917 (approximately 8,000,000,000 rubles), and the notes issued during the first half of 1921 (1,178,600,000,000 rubles), a figure is obtained showing the total note issue during this period, 2,328,300,000,000 rubles.[12]

The extension of the issuing rights of the bank.—During the year following the November Revolution notes were being issued without any formal declaration as to the extension of the issuing rights of the bank. On October 26, 1918, however, when the volume of notes in circulation was climbing to 54,000,000,000 rubles, the government had *ex post facto* extended that right by 33,500,000,000 rubles, which, with the already extended rights under the Czar's and Provisional governments, permitted a 50,000,000,000-ruble maximum of uncovered notes.[13] Thereafter, notes were issued without any declaration as to the extension of the issuing rights of the bank, and on May 15, 1919, the Council of People's Commissars removed all such limitations and permitted the bank to issue as much "as was actually needed by the country's economy."[14] It may seem at first that such formalities are of no importance and that it really makes no difference whether a government keeps on raising that maximum or not, once circumstances demand that the printing presses be kept going. It must, however, be borne in mind that the fixed maximum operates as a danger signal. When it is reached the government must "stop, look, and listen." It is an automatic reminder of the fact that steps must be taken to stem inflation.

[10] *Our Monetary Circulation*, p. 15.

[11] *Ibid.* The discrepancy between the budgetary deficit and the volume of notes is most likely caused by the fact that the expenditures were overestimated. See Katzenellenbaum, *Russian Currency and Banking, 1914–1924* (London, 1925), p. 70.

[12] *Our Monetary Circulation*, p. 13.

[13] L. N. Yurovsky, *Currency Problems and Policy of the Soviet Union* (London, 1925), pp. 29-30.

[14] *Ibid.*

Apparently the change which was taking place in the ideas of the communists concerning the possibility of avoiding a "period of transition" and of ushering in communism at once was responsible for the decree of May 15, 1919.

The nature of the notes in circulation.—The notes, amounting to some 8,000,000,000 rubles, which were issued by the Soviet government during November and December, 1917, consisted of the "old" designs used by the Czarist and Provisional governments. Of the same design were the more than 33,000,000,000 rubles in notes issued during 1918. On January 1, 1919, for instance, of the total note circulation of 61,300,000,000 rubles, 23,100,000,000 consisted of imperial notes,[15] 22,900,000,000 of so-called "Duma" notes designed by the Provisional government,[16] and 14,700,000,000 of another variety of notes (treasury notes) also designed by the Provisional government and popularly known as "Kerenky" (after Kerensky).[17]

Notes of a Soviet design were decreed only on May 15, 1919, and made their first appearance in the middle of that year, despite the fact that they were designated as "credit notes of 1918."[18] The printing and issuing of the notes of the "old" design was, however, continued even after the appearance of the "credit notes of 1918."

By January 1, 1920, when the channels of circulation were overflowing with a huge mass of paper notes of a Soviet design, the notes of old designs, although showing an appreciable absolute increase as compared with the preceding years, constituted slightly less than half (about 44 percent) of the total mass of paper money in circulation.

[15] These were nicknamed "Nikolaevskie" or "Romanov" after Czar Nicholas (Nikolai) Romanov.

[16] They bore a picture of the Duma (Parliament) and so were nicknamed "Duma" or "Dumskie." They were issued in denominations of 250 and 1,000 rubles.

[17] Issued in denominations of 20 and 40 rubles.

[18] Decrees 179 and 269. They were nicknamed *Piatakovki* and *Penzenki* because they were printed in Penza and were signed by G. L. Piatakov. They appeared in the following denominations, 1, 3, 5, 10, 25, 50, 100, 250, 500, and 1,000 rubles, that is, in the same denominations as the imperial notes, but with an addition of one-thousand-ruble notes. Later, on October 21, 1919, the government authorized (Decree 506) the issue of five- and ten-thousand ruble notes, and also of "small change" in the form of 15, 30, and 60 ruble notes.

In 1920 the government, however, began to issue large quantities of an additional variety of notes, known as "settlement" or "reckoning tokens of 1919" (*raschotnye znaki*).[19] The new name, which in accordance with the decree of March 4, 1920, was to be applied to all Soviet note issues, owed its introduction to the philosophy then prevalent that an immediate, rather than gradual and slow, transition to communism was to take place, and that in the new society *money* and all reference to it were to have no place.

By January 1, 1921, when the issues of "credit notes of 1918" and of "settlement tokens of 1919" already exceeded 1,000,000,000,000 rubles, the notes of the old designs, although again showing an absolute increase, amounted to about 104,000,000,000 rubles, or to but 9 percent of the total mass of paper currency in circulation.[20] Thereafter as the quantities of notes designed by the Soviet government rapidly increased, the "old designs" in circulation became relatively very small. Finally, in 1922, when all pre-1922 note issues were called in, their legal existence came to an end.

A factor often ignored or forgotten by those who deal with the pecuniary phenomena of 1918–21 and which is doubtless responsible for the introduction of serious errors into their calculations is that *all monetary units on any given day during the period did not have the same purchasing power.* A note of the old design purchased many times that of a note of the same denomination but of Soviet design. As one writer points out: "After the appearance . . . of Soviet monetary tokens . . . money of the old designs began to disappear from circulation, and a premium was put upon them on the illegal market as against Soviet money, a premium which at times was as much as 50,000 to 60,000 Soviet rubles

[19] Settlement or reckoning tokens in the denominations of 1, 2, and 3 rubles were decreed as early as February 4, 1919, and issued in March of the same year. On October 21, 1919, the government decreed the issuance of the following denominations, 15, 30, and 60 rubles; they were issued in November, 1919. On March 4, 1920, the government decreed "tokens" of 100, 250, 500, 1,000, 5,000 and of 10,000 ruble denominations. These were issued during March-August of that year. All notes were called in in 1922 and exchanged for "denznaks of 1922" each ruble of which was declared to equal 10,000 rubles of the old issues (Decrees 514 and 793 of June 28 and September 28, 1922, respectively).

[20] See Table 12.

TABLE 12

THE KINDS OF CURRENCY IN CIRCULATION DURING 1918–21

(In thousands of millions of rubles)

	January 1 1918		*January 1 1919*		*January 1 1920*		*January 1 1921*		*January 1 1922*	
	Absolute	% of Total	Absolute	% of Total	Absolute	% of Total	Absolute	% of Total	Absolute	% of Total
Imperial credit notes (or kreditnye bilety)	18.0	65.3	23.1	37.7	27.0	12.0	27.9	2.4	29.5	0.1
"Duma" notes (credit notes) of 1917	5.9	21.3	22.9	37.4	33.7	15.0	37.3	3.2	37.6	0.2
"Kerenkies" (treasury notes) of 1917	3.4	12.2	14.7	24.0	37.9	16.8	38.7	3.3	38.5	0.2
Credit notes of 1918	....	....	....	....	123.1	54.7	462.5	39.6	499.9	2.9
Settlement or reckoning tokens of 1919 (raschotnye znaki)	....	....	....	....	3.3	1.5	602.2	51.5	2,075.9	11.8
"Change" stamps [a]	0.2	0.8	0.4	0.6	....	....	....	....	....	....

Treasury "change" tokens [b]	0.1	0.4	0.2	0.3	....	....	....	....	....	....
Settlement or reckoning tokens of 1921 [c]	....	....	....	....	....	....	....	....	12,495.7	71.2
Obligations of the R.S.F.S.R. of 1921 [d]	....	....	....	....	....	....	....	....	1,515.0	8.6
Denznaks of 1922 [e]	....	....	....	....	....	....	....	....	847.0	5.0
Total	27.6	100.0	61.3	100.0	225.0	100.0	1,168.6	100.0	17,539.2	100.0

The figures were adapted from *Our Monetary Circulation*, pp. 13, 81-88, 103, 121, 167, 169, 171.

[a] These were of the type of postage stamps. They began to be issued as early as September, 1915, in denominations of 1, 2, 3, 10, 15, and 20 copecks. By the beginning of 1916 the stamps in circulation amounted to 48,700,000, and by 1917 to 105,600,000 rubles. By the middle of 1919 their distribution was stopped, and, inasmuch as their value by that time was quite insignificant, they are treated as having disappeared from circulation and are not included in the remaining columns.

[b] Their history is quite analogous to that of the "change stamps." They were issued for the first time in December, 1915, in denominations of 1, 2, 3, 5, and 50 copecks. By the beginning of 1916 their circulation amounted to 2,600,000 and by 1917 to 60,500,000 rubles.

[c] Decreed June 16, 1921; issued in the second half of 1921 in denominations of 100, 250, 500, 1,000, 5,000 and 10,000 rubles. On July 30 of that year the government decreed the following additional denominations, 25,000, 50,000, and 100,000 rubles. According to the decrees of June 28 and September 28, 1922, settlement tokens of 1921 in denominations up to 50,000 rubles were to be exchanged for the new currency not later than October, 1922; tokens of 1921 in denominations of 50,000 and 100,000 rubles, not later than January, 1923.

[d] Obligations of the R.S.F.S.R. of 1921 were issued in December, 1921 (in pursuance of the decree of September 15, 1921), in denominations of 1,000,000, 5,000,000, and 10,000,000 rubles. These too were called in by the government (decree of June 28, 1922 and January 4, 1923), and exchanged for denznaks of 1922. They had to be exchanged not later than January, 1923.

[e] "Denznak" (singular) represents a merger of two Russian words of which the first was an abbreviation of denezhnyi znak, or "monetary token." A ruble in denznaks of 1922 equaled 10,000 rubles of pre-1922 paper money. They were placed in circulation in pursuance of the decree of November 3, 1921, in denominations of 1, 3, 5, 10, 25, 50, 100, 250, 500, and 1,000 rubles. On June 19, 1922, the government decreed additional denominations, 5,000 and 10,000 rubles.

to 1,000 Tsarist." [21] This, as the same writer explains, was caused "in the beginning, during the Civil War . . . by suggestion of the possibility of the re-establishment of the old regime . . . that the Soviet money could be annulled and the old money might become 'real' money." Apparently Gresham's law can be applied not only to metallic money, but to paper money as well. Indeed, when the "Kerenkies" made their appearance, the Czarist notes began to be increasingly used as a store of value, and later when notes of a Soviet design appeared great respect began to be bestowed upon the "Kerenkies." In other words, in the case of paper money, as in metallic money, users of money will retain the types of money which they esteem, and will pass on the inferior type; provided, of course, that the total quantity of money exceeds the needs of circulation.

Originally caused "by suggestion of the possibility of the re-establishment of the old regime," the esteem for the paper money of the old designs later became enhanced because of the fact that the notes of the old designs, particularly the Czarist notes, could be used for some time in the newly created states, Esthonia, Latvia, Lithuania, and Poland.

The government was apparently fully aware of the preference that was shown for the notes of the old designs and of the fact that this preference could be capitalized by the treasury if only the issue of such notes were limited. It is most likely that the Soviet government would never have extracted as great a quantity of commodities from the peasantry had it resorted from the very start to the issue of currency of its own design instead of issuing currency of designs already esteemed as a store of value. The Hungarian Soviet government, for example, was in this respect immeasurably worse off. The prerevolutionary currency which enjoyed the confidence of the people of that country and which was in consequence employed by them as a medium of exchange, as a standard of value, and as a store of value, used to come from the government printing presses in Vienna, access to which

[21] Katzenellenbaum, *op. cit.*, pp. 80-81. See also Magnus Feitelberg, *Das Papiergeldwesen im Räte-Russland, Statistische Beiträge zur Währungsfrage Russlands* (Berlin, 1920), pp. 29-43, 51.

was not open to the Hungarian revolutionists. Accordingly, the Hungarian Soviet government began to issue notes of its own design, but those notes were not very useful for the purpose of extracting commodities from the peasantry inasmuch as the latter was suspicious of a new currency and insisted on being paid in "old" money.[22]

The depreciation of the ruble and the foreign exchange rate.— The large note issues during those years could not fail to cause a further shrinkage in the ruble's value on the foreign and domestic markets. And although certain insurmountable obstacles, the nature of which will presently become clear, block any attempt at exactitude and completeness, an endeavor will be made to assemble here such data as are available that might illuminate the interesting monetary phenomena of that troublesome period. Let us first analyze the position of the ruble with respect to foreign currencies.

The Russian exchange market, like the rest of that country's economy, became separated from the rest of the world by the October-November Revolution of 1917. True, during the early part of 1918 some foreign exchange transactions could be consummated with the help of the various foreign missions which had remained in Moscow. Thereafter, however, when postal, telegraphic, and, in fact all other communication with the outside world came to a stop, the transfer of money between Soviet Russia and other countries became almost impossible. The supply of foreign currencies and media of payment which had remained within the country was now eagerly sought by those who wished to insure themselves against the depreciation of the ruble.

The government, although slow to understand the significance of those transactions, responded with a series of administrative (rather than legislative) measures. Of these the first one of importance was issued by the Commissariat of Finance only on October 3, 1918.[23] In accordance with that measure all persons and enter-

[22] E. Varga, *Die wirtschaftspolitischen Probleme der proletarischen Dictatur*, pp. 113-23.

[23] D. A. Loevetzky, *Foreign Exchange Policy of the U.S.S.R.* (Moscow, the Commissariat of Finance, 1926), p. 16.

prises, whether private or public, were directed to surrender to a special chancellery within a fortnight all the foreign exchange of which they were possessed, with the exception of whatever part the Commissariat permitted them to retain for their specific needs. All exchange of which an individual or enterprise was to become possessed thereafter was to be promptly turned over to the same agency. The foreign exchange so turned over to the chancellery was to be paid for in paper rubles at a rate determined by that agency.[24]

Buyers and sellers of foreign exchange managed, however, to get together despite the vigilance of the Extraordinary Commission ("Cheka"). But, since those dealings were not legitimate and therefore were shrouded with secrecy, the rates at which exchanges took place were not being published and were for that reason difficult to obtain. Besides, since under those conditions one buyer did not know what other buyers were willing to pay and one seller did not know what other sellers were willing to take, there existed more than one rate on the same currency at any one time. An idea of what the movement of those rates was can be gleaned from the figures published by a student of the subject (Table 13).

Those rates, however, show the prices which foreign *currencies* commanded in Moscow. It was inevitable under those circumstances that *claims* upon foreign countries should be valued at a much lower figure than their currencies, for in the case of bills of exchange and checks an additional element entered, the credit standing of the drawer. The variety of rates at which such paper was negotiated therefore must have been great. According to the same writer, bills of exchange expressed in pounds sterling sold at from 250 up to 2,000 rubles to the sovereign, at a time when English banknotes commanded 10,000 rubles per sovereign.[25]

In consequence of the isolation of the Russan market, arbitrage transactions were no longer possible and this led to wide variations between the rates on same currency in Russia and in other

[24] *Ibid.*

[25] Feitelberg, *op. cit.*, p. 51.

countries. For example, while in Moscow at the end of May, 1920, a pound sterling commanded 10,000 rubles, in Berlin it commanded 140 marks. In Berlin, however, at the same time one mark purchased two Czarist rubles or 38 Soviet rubles, and a pound sterling there could, therefore, be purchased with but

TABLE 13

FOREIGN EXCHANGE RATES, 1918–20 [a]

	Rubles for German Mark	*Rubles for £ Sterling*	*Rubles for Swedish Krona*
1914	0.47	9.50	0.60
1917 first quarter	....	16.00	1.00
1917 second quarter	....	22.50	1.20
1917 third quarter	....	32.50	1.50
1917 fourth quarter	....	40.00	2.50
1918 first quarter	....	45.00	3.00
1918 second quarter	1.00	60.00	3.50
1918 third quarter	1.50	80.00	6.00
1918 fourth quarter	2.00	150.00	8.00
1919 first quarter	4.00	400.00	12.00
1919 second quarter	10.00	900.00	20.00
1919 third quarter	20.00	1,200.00	40.00
1919 fourth quarter	30.00	1,300.00	80.00
1920 first quarter	60.00	6,000.00	200.00
1920 second quarter	100.00	10,000.00	500.00

[a] Feitelberg, *op. cit.*, p. 50. It will be noticed that the rate of the ruble's depreciation with respect to the mark, sovereign, and krona was not the same, due to the differences in their supply and the demand for them, to the degree of their own depreciation, and, of course, to the confidence in their recovery.

5,320 rubles as against the 10,000 rubles paid for the same note in Moscow.[26]

The depreciation of the ruble and the price of gold.—While foreign bills of exchange and other means of payment abroad during this period were being confiscated only when their holders failed to sell them to the agencies of the Commissariat of Finance at low fixed prices or when an attempt was made to smuggle them out of the country, precious metals, whether in the form of bullion or coin, were subjected to a more drastic regulation. We have seen that as early as December 14, 1917, the Soviet government conducted an inspection of the safe deposit vaults in the banks. On January 12, 1918, there was formed at the Supreme Council of National Economy a special department of precious metals, the government at the same time retaining for itself the sole monopoly of buying and selling gold and platinum.[27] By the decree of July 22, 1918, the government fixed the penalty for receiving, trading in, or possessing platinum, gold, and silver in the form of bullion or coin at not less than ten years of imprisonment at hard labor and the confiscation of one's entire property.[28] In fact even as late as October 17, 1921, that is, during the period known as "New Economic Policy," the government let it be known that its policy with respect to the trading in, possession, and so forth, of precious metals remained the same.[29]

Despite, however, the severe punishment meted out to the traders in precious metals and coins, there existed secret exchanges where such transactions were consummated. The available figures seem to indicate that in Moscow the price of the gold ruble in terms of paper money was as shown in Table 14 (in semi-annual averages).[30]

[26] *Ibid.*

[27] *Collected Decrees*, 1918, Decree 232.

[28] Decree 605. By a much later decree (July 25, 1920) the government permitted the retention of articles made of precious metals, fixing the maximum by weight that one person was entitled to own.

[29] *Collected Decrees*, 1921, Decree 564. Under the new decree, however, the Commissariat of Finance was authorized to compensate those who willingly brought to it their precious metals or coin in accordance with the rates set by the former.

[30] Based upon the data given in *Our Monetary Circulation*, p. 16.

It would seem, according to those figures, that the depreciation of the paper ruble in terms of gold was much smaller than in terms of all other commodities and that the value (or purchasing power) of gold during this period fell considerably. Such a drop in value could, of course, be said to have been the result of an excess

TABLE 14
GOLD RUBLE RATES
1918–21

Date	*Paper Tokens for Gold Ruble*	*Price Level (1913 = 1)*
1918 1st half	7.8	56.8
1918 2d half	20.2	139.2
1919 1st half	105.0	468.0
1919 2d half	523.0	1,896.0
1920 1st half	1,633.0	6,983.0
1920 2d half	4,083.0	13,963.0
1921 1st half	11,300.0	48,758.0

of the supply of gold coin relative to the demand for it. The excess of the supply over the demand was probably brought about by the severe penalties meted out by the government as well as by the fact that articles of prime necessity were very scarce.

The depreciation of the ruble and the price level.—The depreciation of the purchasing power of the ruble which set in during the World War progressed at a relatively moderate rate at first. The pressure of an ever increasing number of notes in circulation, however, compelled the purchasing power of the ruble to beat a more hasty retreat. By the time that the Provisional government had been set up, the ruble's purchasing power was less than one-third of what it had been in 1913. More than two-thirds of it had been sacrificed during the Czarist regime on the altar of war. The further loss during the eight-month regime of the Provi-

sional government was so swift that at the time of the November Revolution the ruble possessed less than one-tenth of the purchasing power that it had had in 1913.

In other words, when the communists came into power the purchasing power of the ruble was equivalent to but 8 to 10 pre-war copecks. The communists, as has been shown, were nevertheless compelled to rely upon the printing presses for a substantial portion of their revenue. It will be recalled, however, that during this period industry became disorganized and its output was probably less than 20 percent of the pre-war output, and that the requisitions, sequestrations, and levies in kind led to a tremendous diminution of the volume of foodstuffs brought by the peasants to the city markets. This and the loss of territory served to narrow the sphere within which currency could circulate.

The transfer of goods and materials between the nationalized enterprises, frequently without any payments whatsoever, the fact that workers and government employees were paid largely "in kind" and that pecuniary taxes were no longer important, combined to limit further the sphere within which currency circulated and thereby greatly to reduce the demand for it. Curtailment of the demand was also facilitated by some of the legislative and administrative acts of the period. On May 2, 1918, for instance, the Council of People's Commissars decreed that all cash, except for petty expenses, held by the various Soviet organizations and officials was to be deposited in the People's Bank or in the treasury and that all payments were to be made by check or book transfer.[31] Further, on August 30, 1918, the Supreme Council of National Economy directed all nationalized enterprises to turn over their output to the various central agencies which controlled them (*centers* and *glavki*), to look to them for raw materials and supplies, and to make all their settlements by means of bookkeeping entries.[32] This policy of substituting checking and bookkeeping transactions for payments in money was reaffirmed and restated in the decrees of January 23, 1919, and of January 5, and July 15, 1920.

[31] *Collected Decrees*, 1918, Decree 460. [32] Decree 691.

Thus the government on the one hand was introducing a "natural," *moneyless* economy, paying wages in kind and distributing (especially towards the end of 1920 and at the beginning of 1921) commodities and rendering services to the people free of any charge, while on the other hand, since it depended upon paper money for a considerable part of its revenue, it continued to issue large amounts of notes. As a result of that policy the demand for paper money woefully decreased, while the supply increased inordinately. At the same time the crystallization in the minds of the people of the idea that inflation operates as a hidden tax which falls upon the possessors of currency led to an ever increasing hoarding of available commodities and to a consequent diminution in the velocity of their circulation. When the holders of currency understood that the shorter the period between the receipt of that currency and its expenditure the lighter the tax, they began to spend their money incomes as fast as they were obtained. They began to shun the ruble as they would a plague. The "flight from the ruble" led to a phenomenal increase in the velocity of its circulation and hence helped to depreciate it so much faster.

Now it is true that some of those tendencies were discernible even in 1916. Then, too, there was a shortage of commodities, but certainly that shortage was insignificant when compared with the shortage during the period of War Communism. There was also a hoarding of commodities (although this was done principally because it afforded an opportunity to make profit), and, therefore, a decrease in the velocity of trade turnover to that extent. But in those years there existed, as has been explained, confidence in the stability of the country. People were willing to hoard the currency and to keep their unspent margins in their registers, pockets, or in the banks. That confidence was destroyed by the rapid changes in government and particularly by the policies of War Communism. It was, therefore, inevitable that the purchasing power of the ruble should, under the crushing weight of its billions and the lightness of the demand for them, decline catastrophically.

As may be seen from Table 15, at the end of 1917 a volume of currency which was 17 times as great as the pre-war volume was accompanied by a price level about 21 times as high as the pre-war level. About a month earlier, when the November Revolution was only a few weeks old, a volume of currency some 15 times as great as the pre-war volume was accompanied by a price level about 15 times as high as the pre-war level.[33] The year 1918 witnessed a more rapid pace in the depreciation of the currency and this is reflected by the changed relationship between the growth of the volume of currency, over 37 times the pre-war volume, and the rise of the price level, 164 times as high as the pre-war level. At the end of 1919 a volume of currency 138 times the pre-war volume was accompanied by a price level 2,420 times as high as the pre-war level. At the end of 1920 the respective figures were 717 and 16,800. At the end of June, 1921, which approximately marks the end of the period of War Communism, the respective figures were 1,440 and 80,700 while at the end of 1921, when the effect of the New Economic Policy was already felt, those figures stood at 10,758 and 288,000.

A comparison of the data relative to the volume of currency in circulation and to the price level in November, 1917, with the corresponding data for July, 1921, shows that during the period beginning with the November Revolution and ending with War Communism the volume of currency had increased 120 times while the price level increased by more than 7,910 times. Apparently the rate of the currency's depreciation during this period was some 65 times faster than the rate at which its volume was increasing. Table 16 shows the annual increases in the volume of currency and in the price level during 1914–21 in terms of percentages.

Thus it may be seen that a definite rate of increase in the volume of currency was not accompanied by an equal or even proportionate increase in the rate at which the currency was depre-

[33] It will be recalled that, as compared with the pre-war volume of currency in circulation and the pre-war price level, the respective increases stood as 1.8 and 1.3 at the end of 1914; as 3.5 and 1.5, at the end of 1915; and as 5.7 and 3.0, at the end of 1916.

TABLE 15

INDICES OF CURRENCY CIRCULATION AND PRICES [a]

Date (First of Each Month)	*Notes in Circulation (July 1, 1914=1)*	*Prices* [b] *(1913=1)*	*Notes in Circulation (July 1, 1914=1)*	*Prices (1913=1)*
	1918		*1920*	
January	17.0	20.8	138.0	2,420
February	18.1	26.9	159.6	3,090
March	19.0	33.0	179.7	3,810
April	20.8	43.2	208.9	4,770
May	23.5	57.4	237.8	5,780
June	25.0	70.6	276.4	6,570
July	26.8	88.5	313.9	8,140
August	28.4	101.0	356.2	9,070
September	29.8	93.5	399.5	9,230
October	31.6	93.5	457.0	9,620
November	33.3	107.5	529.2	10,500
December	35.2	135.0	610.7	12,000
	1919		*1921*	
January	37.6	164	716.7	16,800
February	40.2	203	796.6	21,600
March	42.5	258	912.8	27,600
April	46.1	336	1,034.5	35,700
May	49.7	414	1,175.9	42,700
June	56.7	516	1,301.7	62,000
July	62.0	656	1,439.6	80,700
August	68.9	750	1,722.3	80,300
September	77.4	814	2,153.2	76,400
October	90.9	923	2,778.1	81,900
November	104.3	1,360	3,974.3	95,500
December	118.0	1,790	6,038.5	138,000
			1922	
January			10,757.6	288,000

[a] Based upon *Our Monetary Circulation*, Tables 182 and 227, on pp. 206 and 248, respectively.

[b] The prices are those of the Bureau of Labor Statistics (U.S.S.R.). They comprise what is known as the All-Union Budget Index.

ciating. The early increase in the volume of notes in circulation was accompanied by a very small rise in the price level. As inflation progressed the rate of the increase of the volume of notes in circulation began to be accompanied by steadily and progressively increasing prices until a point was reached where a given

TABLE 16

PERCENTAGE INCREASE IN THE VOLUME OF CURRENCY AND PRICES 1914–21

	% Increase in the Volume of Currency (Over Preceding Year)	*% Increase in the Price Level (Over Preceding Year)*
During 1914	77	28.7
During 1915	92	10.0
During 1916	63	105.0
During 1917	198	606.0
During 1918	122	690.0
During 1919	267	1,376.0
During 1920	419	635.0
During 1921	1,400	1,616.0

rate of increase in the volume of currency was accompanied by a larger rate of increase in prices.

Since the rate of depreciation had outstripped the rate at which the volume of notes was increasing, it was inevitable that the total value or purchasing power of the rapidly increasing mass of paper money should keep on decreasing. A good method for calculating the total value or purchasing power of a nation's currency is to multiply the total volume of currency outstanding at a given time by the then prevailing exchange rate on a gold standard country.[34] It has been seen, however, that the exchange rates for this period were neither complete nor very reliable. Some idea of

[34] But even this method cannot be said to be wholly free from objections. Exchange rates often anticipate a rise or fall in the price level and are influenced by political and various other factors.

the total value of Russia's currency (in terms of pre-war rubles), beginning with 1914, may nevertheless be obtained from Table 17.

According to the figures in Table 17 the purchasing power of the currency in circulation on August 1, 1914, amounted to some

TABLE 17

THE PURCHASING POWER OF THE TOTAL VOLUME OF PAPER MONEY 1914–22 [a]

(*In millions of rubles*)

January 1, 1914	2,379	January 1, 1919	374
August 1, 1914	3,015	April 1, 1919	224
December 1, 1914	3,092	July 1, 1919	154
January 1, 1915	2,482	December 1, 1919	108
July 1, 1915	3,012	January 1, 1920	93
December 1, 1915	4,168	April 1, 1920	71
January 1, 1916	4,092	July 1, 1920	63
July 1, 1916	3,454	December 1, 1920	83
December 1, 1916	3,105	January 1, 1921	70
January 1, 1917	3,151	April 1, 1921	47
April 1, 1917	3,334	July 1, 1921	29
July 1, 1917	2,302	October 1, 1921	55
November 1, 1917	1,919	December 1, 1921	71
December 1, 1917	1,637	January 1, 1922	61
January 1, 1918	1,332	April 1, 1922	32
April 1, 1918	786	July 1, 1922	55
July 1, 1918	493	October 1, 1922	166
December 1, 1918	425	December 1, 1922	90

[a] *Our Monetary Circulation*, Table 159, p. 190. The figures were obtained by dividing the volume of paper money in circulation by the All-Union Price Index of the Bureau of Labor Statistics (U.S.S.R.). This method presupposes that the velocity of circulation remained the same throughout, which, of course, was not the case. Furthermore, in practice the currency listed as being in circulation used to be sent to the various subtreasuries, where it lay for some time before it was really issued. By the time it would find its way into circulation, the index number would shoot up to more formidable heights. Nevertheless the above figures give an idea of the decline of the purchasing power of money.

3,000,000,000 rubles. Almost a year and a half later, in December, 1915, the total purchasing power of the currency rose to 4,200,000,000 rubles. By January 1, 1917, it dropped to 3,100,000,000 rubles, and when the communists came into power it was still as high as 2,000,000,000 rubles. In the years that followed it experienced a serious shrinkage, and by July, 1921, it dropped to its lowest value, 29,000,000 rubles. The shrinkage in the purchasing power of the currency was, of course, reflected in the yield obtained by the treasury from the note issues. Calculated on the same basis as above, in pre-war rubles, that yield during 1918–19 amounted to 523,000,000 rubles, during 1919–20 to 390,000,000 rubles, and during 1920–21 to 186,000,000 rubles.

The lowest yield, 3,100,000 rubles, was obtained in July, 1921. Commenting on the exceptionally low yield, one writer remarked that "If from this paltry sum were deducted the cost of printing those notes and the upkeep of the entire Treasury Department, and if the yield from those notes were computed as of the day when the currency actually got into circulation . . . it would be found that the game was not worth the candle." [35] It is, of course, true that towards 1921 the revenues obtained by the state from the various taxes in kind, levies, and confiscations was much larger than the revenue obtained from the note issues. That this was so may be seen from a comparison of the yields from those two sources.

Thus, the yield from the note issues, which in 1918–19 constituted as high as 81 percent of the total, fell in 1920–21 to 27 percent, while the yield from taxes in kind, levies, confiscations, and the like advanced from 19 percent in 1918–19 to 73 percent in 1920–21. Plainly their positions became reversed. Nevertheless the importance of paper money during that period must not be underestimated. Even during 1920–21 it yielded 27 percent and that certainly is not an insignificant figure. The paper issues proved of inestimable value to the Soviet government in the matter of financing the Civil War, and of supporting the urban population.

[35] Yurovsky, *Towards a Monetary Reform*, pp. 21-22.

Furthermore, the rapid depreciation of the currency helped to deepen the effect of the change in the distribution of wealth and income which was brought about by the various measures for the expropriation of the wealthy. Stocks, bonds, mortgages, and various other claims became converted into so much rubbish and the income from those sources was therefore no longer available. Rents were fixed at a very low figure and when paid in a depreciated currency were not worth the trouble of collecting. The sums of money that the moneyed class succeeded in salvaging from the nationalized banks were rapidly becoming so much

TABLE 18

REVENUES IN 1918–21

COMPARISON OF YIELDS

(*In millions of pre-war rubles*)

	1918–19	*1919–20*	*1920–21*
From note issues....	523	390	186
From taxes in kind, levies, confiscations, etc..	121	253	480
Total..	644	643	666

worthless paper. In short the class that was likely to finance a counter-revolution saw a considerable portion of their resources crumble into dust. No wonder that one of the well-known Soviet economists eulogized the paper money of that period in the following words:

Paper money of the Soviet Republic gave support to the young regime at the most critical period of its existence when there was no possibility of raising direct taxes to meet the outlays of the Civil War. Hail to our printing press. It is true that its days are numbered but it has already completed three quarters of its work. In the archives of the proletarian revolution, along with the cannon, rifles, and machine guns of our epoch that vanquished the enemies of the proletariat, the place of honor will be given to the printing press, the machine gun of the Commissariat of Finance that poured fire into the rear

of the bourgeois system and that made use of the laws of currency circulation of that regime for the purpose of destroying it and of financing the revolution.[36]

The currency famine.—The rapidity with which prices were rising produced, paradoxical as it may seem, an acute shortage of currency. Some fourteen or fifteen thousand workers were busily engaged in the government printing shops of Moscow, Leningrad, Penza, Perm, and Rostov on the Don turning out tons upon tons of paper money. The printing of notes was simplified to a point where counterfeiting became easy, the denominations of the notes were increased, and, notwithstanding all that, the attempt to catch up with the steadily rising price level failed. Indeed, since people tried to get rid of the currency as fast as their legs would take them to the nearest market and since the sellers of commodities, to insure themselves against loss, kept on increasing their prices *in anticipation* of new issues, not even a thousand times as many workers could cause the rate of increase in the volume of notes to outstrip the rate of their depreciation.

The various governmental departments, the nationalized enterprises, the railroads, and other branches of the national economy, all operating at a deficit, clamored for more and more currency. Since it was not feasible to satisfy that demand fully, the government attempted to ration the available funds in such a manner as to provide for the most important needs of these organizations. To make certain, however, that these needs would be met the government began to specify with each allotment of cash the purpose for which it might be used, holding the respective officials personally responsible for the diversion of the "earmarked" funds to any other use. It cannot be said, though, that this scheme worked satisfactorily. In numerous instances the local officials found it difficult to dispense with other expenditures and so were compelled to violate the injunction of the government. In other instances, where the officials were intent upon observing the above injunction, it often happened that the earmarked currency had to be kept for a short while and that would cause it to lose

[36] E. Preobrazhensky, *Paper Money during the Epoch of the Dictatorship of the Proletariat* (Moscow, State Publishers, 1920), p. 4.

a considerable portion of the purchasing power it had when first obtained. In an attempt to improve matters the Council of People's Commissars organized in February, 1920, a "Special Interdepartmental Committee of the Council of People's Commissars for the Allocation of Paper Tokens" that was instructed "to take immediately measures to insure a proper supply of currency in the country." [37]

The Commissariat of Finance, however, besieged by numerous delegations of representatives from the various governmental agencies and enterprises, found it difficult to follow the decisions of the Interdepartmental Committee. As a result of friction between the two the All-Russian Central Executive Committee at its second session in June, 1920, decided that the allocation of currency was to be entirely in the hands of the Commissariat of Finance, and that the Interdepartmental Committee was to be retained merely as a deliberative body at the Commissariat. Towards the end of 1920 the Commissariat of Finance, in search of a scientific plan for the distribution of currency, sent out special investigators who were instructed to ascertain on the basis of an examination of records, materials, and so forth, whether the amounts asked for were really needed. The chaotic condition of those records and materials at that time, however, precluded the possibility of such an examination within the course of a few days, and the Commissariat of Finance was, therefore, compelled to give up that idea.

Local note issues.—Another interesting phenomenon associated with the period is presented by the large quantities of money and money substitutes placed in circulation by agencies other than the central government. The anti-Soviet chiefs or "white" generals, and foreign invaders and interventionists, too, resorted to the printing press for financing their operations. As a result there were in circulation media of exchange that were issued upon the orders of the various generals and commanders, such as Vandamme, Rodzianko, Yudenich, Avaloff-Bermondt,[38] Denikin, Wrangel, Kolchak, and others. The parts of the country which

[37] *Our Monetary Circulation*, p. 51.

[38] German marks.

fell into the hands of the anti-Soviet forces or which declared themselves independent, particularly the border and maritime provinces, proceeded, of course, to issue their own media of exchange. Among these were Northern Russia,[39] Siberia, the Far East, the Ukraine, the Caucasian Republics, as well as Lithuania, Esthonia, Poland, Finland, and others. The German armies issued currency in the regions which they occupied, such as the rubles introduced by them in Poznan (Posen) and the marks in Kovno. In the Transcaspian Region the English proceeded to issue a medium of exchange expressed in rupees and signed by General Malisson, while in the Far East the Japanese introduced the yen. Currency was also issued by railroads (Chinese Eastern, Vladikavkaz, and a few others). It was even issued by prisoners of war (in the region of Irkutsk, Chita, and a few other places).

The purely local issues of media of exchange were brought out by a number of diversified organizations and even private individuals. The list of issuers includes the various branches of the State Bank, other banks, subtreasuries, municipal governments, various co-operative organizations, stores, factories, mines, restaurants, theaters, and the like. Political and fiscal considerations weighed heavily, of course, in the balance of reasons which influenced such issues. However, the original cause responsible for the many local issues lay in the currency famine aggravated by the inability of the central government to maintain intercourse with the various cities, whether on account of enemy operations in those districts or due to the breakdown of the transportation system. Once tried, local note issues were likely to be continued for fiscal reasons.[40]

[39] Of the histories of the various media of exchange in Northern Russia, that of the so-called "northern rubles" (December 1, 1918–November 15, 1919) is especially interesting. The English interventionists, desirous of having a convenient currency for local settlements and perhaps with a view to bringing about closer relations between that district and England, were responsible for the plan. The "northern rubles" were tied to the pound sterling (40 northern rubles were made to equal one pound). The Issuing Office was given a special reserve consisting of gold and foreign exchange to the amount of £750,000 (or 30,000,000 northern rubles). The reserve was kept at the Bank of England. The fiduciary issue was fixed at one-third of the reserve.

[40] See Ch. Denis, *Catalogue des monnaies émises sur le territoire de la Russie, 1914–1925* (Paris, 1927), *passim*. Also the section on Local Note Issues in *Our Monetary Circulation*, pp. 257-79; A. M. Brailowsky, *Historical Account of the*

Toward the abolition of money. The socialist philosophy.—It is sometimes asserted that the communists had a preconceived plan of abolishing money, and that upon seizing power they therefore resorted to a diabolical scheme of debauching the currency so as to ruin the capitalists and obtain in the meantime as much revenue as possible. This explanation, however, is not based upon fact. Not that the socialists idolized money, or that they were opposed to its abolition; in common with radical thinkers of all ages they berated the power that gold (money) wielded over mankind and the esteem in which it was held.[41]

Even centuries before Marx's time there were writers who dreamed of a social order in which money would have no place. One of them, Sir Thomas More (1478–1535), living at a time when feudal England was changing to a money economy and being convinced that injustice and misery flowed from the unequal distribution of wealth, proposed in a roundabout and indirect way a system free from those institutions.[42] Through the mouth of one of his characters he describes the Island of Utopia where the people deliver to public warehouses whatever they produce and take from those warehouses whatever they need "without money, without exchange." Gold, silver, and precious stones are in disrepute on that island and are thrown away by children as soon as they grow up.

Currency Tokens during the Russian Revolution (Tiflis, 1922), *passim;* A. I. Pogrebetsky, *Currency Circulation and Currency Tokens of the Far East during the War and Revolution* (1914–24), *passim.*

[41] Marx, for example, quotes (*Capital, a Critique of Political Economy,* I, 148) from the letter of Columbus (from Jamaica, 1503): "Gold is a wonderful thing! Whoever possesses it is lord of all he wants. By means of gold one can even get souls into Paradise." He further quotes from Shakespeare (Timon of Athens):

> "Gold, yellow, glittering, precious gold!
> Thus much of this, will make black white; foul, fair;
> Wrong, right; base, noble; old, young; coward, valiant.
> . . . This yellow slave
> Will knit and break religions; bless the accurs'd;
> Make the hoar leprosy ador'd; place thieves,
> And give them title, knee and approbation,
> With senators on the bench . . ."

Numerous writers and thinkers before and after Shakespeare voiced the same opinion.

[42] Sir Thomas More, *Utopia, passim.*

A number of later writers, believing that greater justice for labor could be obtained by a change in the standard of value, preached the substitution of labor time for the prevailing standard. Of these John Bellers (1655–1725), a member of the Society of Friends, reasoned that "when the rich lose their money they can't employ the poor, though they have still the lands and hands to provide victuals, which are the true riches of the nation and not money." And so he thought that "money in the body politic is what a crutch is to the natural body, crippled; but when the body is sound, the crutch is troublesome."

As a solution he proposed [43] that the rich finance the establishment of co-operative agricultural colonies for the poor, where labor and not money will be the "standard to value all necessaries by." The rich were promised a handsome return on their investment.

The outstanding social reformer of the first half of the nineteenth century, Robert Owen (1771–1858), who was well acquainted with the philosophy of Bellers, traced social misery to several factors. It was unfortunate, he thought, that people failed to understand that man's character is made for him (by environment) and not by him. Since by nature man is neither bad nor good and since at the present he is mostly bad, it follows that the environment is detestable. To change the environment it is necessary to do away with the profit economy, since it is not only unjust but is a perpetual menace as well. The institution of profit makes it impossible for the worker to repurchase the products of his labor and so leads to economic crises. Inasmuch as profits take the form of gold or money, it is necessary to do away with the latter and substitute for it labor notes based upon the labor time expended in the production of commodities.[44]

An adherent of Owen, John Gray (1799–1850), maintained that the "commercial system was at variance with the whole system of nature" and that the "state of things ought to be reversed

[43] "Proposals for Raising a College of Industry of All Useful Trades and Husbandry" (1696). Quoted in M. Beer, *A History of British Socialism* (London, 1919), I, 75-77.

[44] Charles Gide and Charles Rist, *A History of Economic Doctrines* (New York, D. C. Heath and Co.), pp. 235-44.

—that production, instead of being the effect of demand ought to be the cause of it." He believed that under the existing conditions laborers were deprived of four-fifths of their produce. As a remedy he proposed a change in the system of exchange. All goods, according to his scheme, were to be brought to national warehouses, where, after their cost was ascertained and a profit added, they were to be paid for in notes issued by a specially established national bank. In that way he hoped to make sure that the amount of money would always be in exact proportion to the goods produced, that the producers would be paid the just price for their goods and also be certain of being able to obtain from those warehouses whatever goods they might need.[45]

Schemes for national banks and labor currency, that to a certain extent resembled Owen's scheme, were developed by John Francis Bray [46] and several other writers who believed that the laborer was entitled to the whole product of his industry. Of these Pierre Joseph Proudhon (1809–65) and Karl Rodbertus (1805–75) are especially interesting. Although of the opinion that landlords and capitalists were unjustly depriving workers of their produce and that property constituted theft, Proudhon was nevertheless violently opposed to socialism and communism and preferred to retain individualistic production and free competition. He thought that if the worker were enabled to borrow capital gratuitously for the purchase of all that is requisite in production, rent and interest would be abolished and the whole of the produce would revert to him that works. Accordingly, Proudhon advocated an exchange (national) bank (*banque d'échange* or *banque du peuple*) which would grant gratuitous credit without any limit. The credit would take the form of a paper currency (*bons de circulation*), redeemable not in gold but in goods and services.[47]

[45] John Gray, *The Social System, Treatise on the Principle of Exchange* (Edinburgh, 1831), *passim.*

[46] *Labour's Wrongs and Labour's Remedy* (Leeds, 1839). See also Anton Menger, *The Right to the Whole Produce of Labour . . .* (London, 1899), Foxwell's Introduction, pp. lxv-lxxi.

[47] *Ibid.*, pp. 74-82. Also Gide and Rist, *op. cit.*, pp. 290-300. Note the difference between the rôle that Proudhon believed banks and credit could play in stamping out the "exploitation" of the workers, and the rôle that Marx assigned to them. "There is, finally," Marx says, "no doubt that credit will serve as a powerful lever

Rodbertus, on the other hand, did not advocate the total abolition of "unearned" income. He estimated that out of 10,000,000 normal labor hours the state would assign 3,000,000 to workers, 3,000,000 each to the recipients of rent and interest, and that 1,000,000 it would take for itself. Wages and prices, in his scheme, would be fixed not in terms of metallic currency but in a labor currency that is based upon labor time. The state would grant cheap credit in labor currency to employers of labor, and accept goods in repayment of loans. It would redeem the labor currency in metallic coin.[48]

The philosophy of Marx differs materially from that of the above writers. Marx believed that after a revolution takes place in a country the proletariat will gradually centralize all means of production in the hands of the state. When that is completed "products and not commodities" will be the result of industry. That is, goods will no longer be produced for the market, there will be no exchange, no sales, no purchases. At first the allotment of products among the members of society will be on the basis of actual labor performed, but ultimately "when the opposition between brain and manual work will have disappeared," as Marx states in his *Criticism of the Gotha programme* . . . "when, with the all-round development of the individual, the productive forces, too, will have grown to maturity . . ." and when certain other conditions are removed, "society will be able to inscribe on its banner: 'From each according to his ability; to each according to his needs.' "

With Marx, therefore, the changes in production and distribution take place first and money loses its importance as a result of those changes. With the other writers a change in the medium of exchange or standard of value was relied upon to bring changes

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during the transition from capitalist production to the system of production by social labour; but only as an element taken in conjunction with other radical transformations of the mode of production itself. On the other hand, the fallacies regarding the miraculous socializing influence of credit and banks are due to complete ignorance of the laws of capitalist production, and of the credit system which is one of the forms of that mode of production" (*Capital*, III, Pt. 2, Ch. 29).

[48] Anton Menger, *op. cit.*, pp. 83-100.

in production and distribution.[49] It is, therefore, not at all surprising that we do not find any statements concerning the abolition of money in Lenin's pre-November writings. The one-time Commissar of Finance, Sokolnikov, was quite right when he declared that "never, nowhere, not in a single Marxist, bolshevist work written before the October Revolution can one find it pointed out that that is the way to attain socialism." [50]

What the communist philosophy on the question of money was in the early days of the Revolution can be learned from the theoretician of the communist movement, Bukharin. In the *Program of the Communists* (Bolshevists) written in May, 1918, Bukharin says:

Money, at the present time, is a means of procuring commodities. For this reason, anyone who has money can buy much; he is rich. . . . The businessmen and tradesmen, the capitalists and the speculators in the city; the bloodsuckers in the country, who, during the war, became almost impossibly rich, have hoarded up hundreds of thousands of different kinds of paper money. . . . On the other hand, the Workers' and Peasants' government needs money. Further issues of money would decrease the value of money: the more that is issued the cheaper it becomes. But the factories and the foundries must be supplied with money; the workers must be paid. Where shall the money come from? For this purpose it is necessary, in the very first place, to tax the rich. . . . But now, while we are living in the heat of the Revolution . . . other forms of procuring revenue are permissible and practical. For example . . . the government declares that at a certain time, all money must be changed into new, and that the old money loses its value. This means, that everybody must shake all of his money out of his dishes, trunks, and closets, and must carry everything to the bank to be changed. But here the following can be carried out. The savings of the small people shall not be touched; they receive ruble for ruble, the old ruble is changed into a new one, but

[49] His criticism of Gray's and Proudhon's approach will be found in his *A Contribution to the Critique of Political Economy*, pp. 102-7.

[50] *Financial Policy of the Revolution*, III, 135. It will be observed that the above statement applied only to the followers of Marx. It does not apply, for instance, to the writings of anarchists such as Bakunin who differed with Marx on the questions of the state, dictatorship of the proletariat, and political struggle. Bakunin's statement, "We invite anarchy, convinced that out of this anarchy, that is, out of a full expression of an unbridled people's life, must rise liberty, equality, justice, new order," explains his philosophy.

everything over a certain sum will be withheld for the advantage of the government. . . . Then the power of the rich would be sufficiently reduced, the necessary sum for the needs of the Workers' government would be procured, and all incomes would be more or less equalized." [51]

The government did levy an extraordinary 10,000,000,000-ruble tax against the rich (on October 30, 1918) in the hope of obtaining revenue and at the same time arresting inflation. That measure, as has been shown, proved unsuccesful. The government likewise proceeded to withhold "everything over a certain sum" in the case of bank and vault deposits. It is likewise known that in a further attempt to raise revenue and to check inflation the government planned to exchange the old currency for new.[52] According to the original plan everything above a certain sum was to be credited to the holder's account in the bank. Due, however, to the currency famine, the government found it impossible to carry out that plan.[53]

As to the "disappearance" or "abolition" of money, Bukharin says:

The more organized production is in the hands of the workers, so much the less will the socialized worker be paid in cash and so much the more in products. . . . In accordance with the entries in the

[51] In the United Communist Party of America edition, pp. 56-59. At the All-Russian Congress of Representatives of the Financial Branches of the Soviets in May, 1918, Lenin, in a similar vein, declared (Lenin, *Collected Works*, XXIII, 20-21): "One of the results of the War is an abundance of paper money in all countries. Upon transition to socialism it is necessary to replace the present monetary tokens with other certificates against social well-being. . . . Money, paper—that which is now called money—acts as a decomposer and is dangerous in that the bourgeoisie, which has reserves of such paper, retains economic power. To weaken this phenomenon, we must take the following measure: the strictest accounting of the existing paper money by means of a replacement of all present money with new. Doubtless, there are major economic and political difficulties in the way of this measure. It requires careful preparation, but we have already begun that preparation. Each one will be required to declare the amount of money in his possession and within a stated, very brief period of time to exchange it for new money. If the amount he has is small, he will get a ruble for a ruble. If it exceeds the norm, he will get only a part. This measure will undoubtedly meet with the strongest opposition, not only from the bourgeoisie but also from the petty peasantry, which became enriched during the War and which buried in the ground bottles filled with paper money. We will meet shoulder to shoulder with the class enemy."

[52] *Collected Decrees*, 1919, Decree 179.

[53] *Social Revolution and Finance*, p. 49.

workers' time books, the products which the workers need will be handed out from the common depots of supply, for which the worker will need not money but simply a certificate showing that he has done his work. Of course this method cannot be introduced at once. Much time must elapse before everything can be arranged, ordered, and organized. . . . But one thing is clear: the more the workers take control of the production and the distribution of the products, so much the smaller will be the necessity of money and gradually money will disappear altogether. . . . We saw that money, when production and distribution are *finally* organized, will not play any rôle at all. . . . Money, generally, will cease to be necessary. Consequently, it will cease to be necessary even for the government. So Finance will *die*. We repeat it will be a long time before this is the case. It cannot be accomplished in the very near future. We must now occupy ourselves with getting money. But even now, measures are being taken which will lead to the final elimination of the money system. Society becomes an enormous workers' association, which produces and distributes the product without using any gold or paper money. The power of money is approaching its end.[54]

The Civil War, which was spreading like wildfire and which by the middle of 1918 assumed gigantic proportions, necessitated large note issues.

The government had no choice whatsoever in the matter of selecting its source of revenue. It was clear that there was no way to stop the accelerated depreciation of the currency. This, together with the various economic and political measures which were being adopted by the government under the pressure of the Civil War, gave rise to a school of "justifiers." Inflation, originally a consequence of dire necessity, became surrounded by a halo and was looked upon as a steppingstone to the abolition of money. The changes that were taking place, as a result of the drastic emergency measures, in the realm of production, distribution, and exchange were quite deceptive. Laymen, economists, and statesmen began to believe that money would be abolished within a short time. The Second National Economy Congress made the following declaration in December, 1919: [55]

The development of the social reconstruction of economic life requires the abandonment of capitalistic relations in production and

[54] Bukharin, *op. cit.*, pp. 58-59.
[55] Yurovsky, *Currency Problems and Policy of the Soviet Union*, p. 30.

the elimination in the last instance of any and every influence of money in the relations between the various economic elements. The uprooting of private financial undertakings and the concentration of the fundamental branches of production, and of the functions of distribution in the hands of the state, offer sufficient grounds for the systematic disestablishment of the monetary circulation to the extent to which it has hitherto prevailed.

Even more significant is the declaration of policy with respect to the monetary unit in the program of the all-important Russian Communist Party (Bolshevists) adopted at its Eighth Congress in March, 1919:

> During the early stage of transition from capitalism to communism, while communist production and distribution have not been fully organized, it is impossible to abolish money. Hence, during this period the bourgeois elements will continue to make use of money . . . for the purpose of speculation, gain, and the robbing of the toiling classes. Leaning upon the nationalization of banks, the Russian Communist Party aims to carry through a number of measures which will widen the sphere of moneyless settlements and which will pave the way for the abolition of money: the compulsory keeping of money in the People's Bank; the introduction of budget books;[56] the displacement of money by checks, and short-term tickets entitling one to products, etc.[57]

Meanwhile, on February 4, 1919, it was decreed that the 1919 medium of exchange was to be known as "settlement" and not "money" tokens. A few months later, on May 15, 1919, all limitations with respect to note issue were declared to be at an end. The change of name did not, of course, in any way change the function that was performed by the "new" medium. It was still money, even though very bad money. Foolish things, as Engels has said, are done during a revolution as during any other time. Resolution after resolution, and measure after measure were passed with a view to expediting the abolition of money. Thus, on June 18, 1920, the All-Russian Central Executive Com-

[56] Where the amount of work performed by a worker shall have been entered and can, therefore, be used as evidence that he is entitled to services and products.

[57] The program of the Russian Communist Party (Bolshevists). Adopted by the Eighth Congress of the Party, March 18–23, 1919. From Bukharin and Preobrazhensky, *op. cit.*, p. 266.

mittee instructed the Commissariat of Finance "to endeavor to establish moneyless settlements with a view to the total abolition of money. . ."[58] And by the end of 1920 the Commissariat of Finance, in a preface to a review of its own activity that was submitted to the Eighth Soviet Congress, triumphantly proclaimed that

in the field of money it expected to adapt its activity and institutions to the requirements of the Civil War, to make free use of the money system, anticipating a progressive depreciation and finally a complete disappearance of money.[59]

Time and again Lenin cautioned them to be careful. On November 30, 1920, for example, he issued the following admonition:

It is essential to give more thought . . . to the conditions of the transitory period. . . . The transition from a money system to moneyless exchange of products is not doubted. But in order to effect such transition successfully there must be created an exchange of products [and not of commodities that are manufactured for the market.—Author]. So long as we are unable to bring about an exchange of products, that is, so long as we are unable to furnish the peasants with manufactured goods, the peasantry is compelled to remain under the ruins of a commodity (and, therefore, of a monetary) circulation. It is economically incorrect to dispense with money (or with its substitutes) before the peasantry is furnished with things and before the uses of money are eliminated. This must be very seriously considered.[60]

The "tred."—The "abolitionists," however, were too numerous and too far advanced with their fantasies to heed this advice, and so by the end of 1920 a special commission was formed to draft a measure for the abolition of the monetary unit and the substitution in its stead of a *labor unit.* Paradoxical as it may sound, in May, 1921, when the New Economic Policy was already being

[58] Yurovsky, *Currency Problems . . .* p. 34. Less than a month later, on July 15, 1920 (Decree 305), Soviet enterprises and institutions, except those specifically authorized, were forbidden to resort to the "free" market for the procurement of things needed by them. They were likewise forbidden to demand payment whether by cash, check, or money transfer from Soviet organizations buying from them. The settlement was to be made by a transfer from the purchaser's account to that of the treasury. But even as early as January 23, 1919 (Decree 22) all Soviet organizations were directed to effect settlements by means of bookkeeping entries.

[59] *Social Revolution and Finance,* p. 42.

[60] Bronsky, *Financial Policy during Ten Years,* p. 9.

ushered in, outstanding Soviet economists and important governmental agencies were putting the finishing touches on a projected decree of the Council of People's Commissars which dealt with the introduction of the new measure of value. Its first paragraph read as follows:

> In order to provide the regulating economic organs with a more exact and entirely comparable accounting relative to the rationalization of the economic organizations, enterprises, and economic units of the R.S.F.S.R., there is being introduced a labor unit of account, the only unit of account for all branches of the state economy and administration.

According to the third paragraph of the projected decree,

> It was the average production of a normal day of simple labor of an intensity normal to the given type of work that was being adopted as the unit of labor account. The labor unit was to be named "tred." [61]

It may be noted from the above that the author of the projected decree, Strumilin, proposed the average *product* of a day's "simple" labor and not *labor time* as the new unit of labor account. Another economist, Shmelev, author of a projected "Regulation concerning a Labor Unit of Account," proposed as the labor unit a *normal workday* of a worker of the first category in the wage schedule who fulfills his task 100 percent. An acquaintance with such a plan ought to help one to understand the tremendous difficulties that stand in its way. Shmelev (whose project is better illuminated than that of Strumilin), for instance, considered the following measures as prerequisite to a change to the labor unit of account:

1. The preparation of labor indices by means of which complex labor can be reduced to units of simple labor.
2. The preparation of a standard nomenclature covering all products, parts, and materials, and the standardization of all grades and brands so as to render the products of the various enterprises comparable.
3. The preparation of tables showing the normal amount of labor contained in each product.

[61] The word "tred" is an abbreviation and merger of two words (*trudovaia edinitza*) meaning "labor unit."

4. The preparation of a general catalogue (or price list) in which each commodity would be expressed in terms of labor units.

But how did Shmelev expect to derive the labor indices by means of which he was to convert complex labor into units of simple labor? Did he really mean to carry out quantitative and qualitative comparisons of the various kinds of labor? Not at all. Those indices were to be obtained as a result of comparing the average pre-war (1911–13) wages of the various categories of labor.[62] The same principle was to be followed in the preparation of the general catalogue (in which all commodities were to be evaluated in labor units). Thus, paragraph 24 of the projected "Regulation" proclaimed that the first general catalogue was to be based upon the average pre-war (1911–13) prices which those commodities and services commanded in the places where they originated. The average pre-war prices were to be converted into "treds" by means of dividing them by the number of gold rubles equivalent to one "tred" (paragraph 29). The latter figure was to be obtained by comparing the cost of the product in terms of "gold" rubles with that in "treds" or labor units (paragraph 28). The authors of the projected legislation apparently did not sense that they were tying the "tred" to the old standard, and, in fact, devising a *new money* based upon it.

In general, it must be remembered that it makes no difference whatsoever whether the medium of exchange takes the form of

[62] "But though labour be the real measure of the exchangeable value of all commodities," says Adam Smith (*Wealth of Nations*, Book I, ch. V), it is not that by which their value is commonly estimated. It is often difficult to ascertain the proportion between two different quantities of labour. The time spent in two different sorts of work will not always alone determine this proportion. The different degrees of hardship endured, and of ingenuity exercised, must likewise be taken into account. There may be more labour in an hour's hard work, than in two hours' easy business; or, in an hour's application to a trade which it costs ten years' labour to learn, than in a month's industry at an ordinary and obvious employment. But it is not easy to find any accurate measure, either of hardship or ingenuity. In exchanging, indeed, the different productions of different sorts of labour for one another, some allowance is commonly made for both. It is adjusted, however, not by any accurate measure, but by the higgling and bargaining of the market. . . ." See also David Ricardo (*The Principles of Political Economy and Taxation*, ch. I, sec. II), who quotes Adam Smith on this point, and who says, "If a day's labour of a working jeweller be more valuable than a day's labour of a common labourer, it has long ago been adjusted, and placed in its proper position in the scale of value."

a ruble, check, "settlement" token, "tred," button, or anything else. Once a thing serves as a medium of exchange and is accepted as such by a community, it is money. In fact, on the "free" market where people shunned the depreciating currency, bread, salt, vegetable oil, and many other commodities served as money. Money, however, serves not only as a medium of exchange but also as a standard of value. It matters little whether it is gold, a "tred," an "ened," [63] or anything else—once it expresses price and serves as a measure of value it is money.[64] According to the terms of the projected decree, the labor unit of account was to be adopted throughout Soviet Russia in its full form "not later than January 1, 1922." There is no question but that the transition from one unit of account to another requires a great deal of time. One wonders, however, whether Strumilin's utopia could be turned into a workable scheme even if a much longer period of time were taken for its perfection. Owing, however, to the rapidly unfolding epochal events of 1921, the projected decree had been thrown into the rag bag of history before it ever became law. The world, consequently, was deprived of an opportunity to watch a very interesting experiment.

[63] The word "ened" is derived from "energeticheskaia edinitza" meaning "energy-unit." The advocate of this rival scheme, Klepikov, urged the adoption of units of man-machine energy expressed in common energy-units as a basis for measuring the value of products and labor.

[64] That a country may employ as its measure of value something that is entirely different from the medium of exchange is, of course, not new. It has been abundantly demonstrated in the post-war period in Soviet Russia and elsewhere.

VI

THE RE-ESTABLISHMENT OF BANKS AND CURRENCY IN 1921–22

The New Economic Policy.—The policies of War Communism, which caused the national economy to undergo a catastrophic decline,[1] began to crumble in the spring of 1921. The epoch-making piece of legislation which made way for the New Economic Policy (Nep) was published by the All-Russian Central Executive Committee on March 16, 1921, after the adoption of a resolution to that effect by the Tenth Congress of the Communist Party on the preceding day.[2] It decreed the abolition of the forced requisitions, which had stifled all incentive, and the substitution of a tax in kind in their stead.

The peasants upon paying the government a tax in kind (i.e., a certain portion of their produce) were now free to dispose of the balance which remained to them as they chose, whether for their own needs, or in exchange for other commodities. It was at first intended that the resulting exchange should be direct, that is, without the employment of money. Moreover, it was to be confined within the limits of a local market.[3] But once permitted

[1] See Central Statistical Administration, *Totals of Ten Years' Soviet Rule*, 1917–27, p. 4; also Commissariat of Finance, *Social Revolution and Finance*, p. 25.

[2] For a declaration of the Nep see *Collected Decrees*, 1921, Decree 403.

[3] The communists did not mean to retreat farther than was absolutely necessary. Nor did they relinquish their ultimate goal. They merely acknowledged the fact that all of their attempts at a *direct* and *immediate* transition from capitalism to communism had failed.

In a speech before the All-Russian Congress of Political Educators on October 17, 1921, Lenin summed this up in the following words: " . . . In our attempt to make a direct transition to communism, we suffered at the beginning of 1921 on the economic front a far more serious defeat than at the hands of Kolchak, Denikin or Pilsudsky . . . it meant that the economic policy of our leaders had failed to revive the productive forces as called for in our program. The forced requisitions in the villages and the direct communist approach in the towns hindered the revival of productive forces and proved the basic cause of the tremendous economic and political crisis which befell us in the spring of 1921." N. Lenin, *Collected Works*, first edition, XVIII, Pt. 1, 343.

Speaking about the errors of War Communism, Lenin said: " . . . A none too long experiment convinced us . . . that without passing through a period of socialist

to function, the free market compelled the removal of the restrictions which were choking it. A medium of exchange began to be employed. Then, too, the market soon grew out of the narrow shell to which it was confined.

Just as the policy of forced levies and requisitions and the stifling of private trade in 1918 called for other measures which collectively gave rise to the phenomenon known as War Communism, so now the abolition of those levies and requisitions and the legalization of private trade called into being numerous other measures which collectively became known as "Nep." The state, being satisfied with the retention in its own hands of the key positions, encouraged private capital to enter trade and industry. State enterprises were required to adhere to such commercial principles as cost accounting and operation at a profit, principles which had been discarded during the preceding few years.

It was inevitable that these developments should bring about a change in the attitude towards money and credit. Once the administration and influential party workers sensed that the attempt at a direct transition to the highest phase of socialism had failed and that a period of waiting was in store for them, they found it necessary to change, for the time being, the attitudes they had held on these questions from 1918 to the early part of 1921. Just how radical that change was can be best appreciated when we recall the apology of the Commissar of Finance appearing in 1918 before the first All-Russian Congress of the Council of National Economy. "In a socialist society," he said, "finance is not supposed to exist, and therefore I beg to be excused for its existence and for my own appearance here."[4] The resolution of the Ninth All-Russian Congress of Soviets (December, 1921) registers the epochal change. It reads as follows:[5]

After having heard the report of the People's Commissar of Finance pertaining to the basic problems of Soviet financial policy at the present moment and on the measures proposed for the solution of those

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accounting and control it is impossible to enter even the very lowest stage of communism . . ." (*Loc. cit.*) The retreat, then, was merely for the purpose of enabling the Party "to make a better jump ahead."

[4] Sokolnikov, *Financial Policy of the Revolution*, I, 114.

[5] *Collected Decrees*, 1922, Decree 46.

problems, the Ninth All-Russian Congress of Soviets resolves: That . . . the realization of the new economic policy necessitates the adoption of a financial policy that is in full accord with it and that constitutes an inseparable part of it. There arises, therefore, the problem of effecting a gradual transition to a stable monetary unit, which is absolutely essential for the trade turnover among the smaller units of the economy as well as for the realization of economic accounting among the state enterprises. Therefore, the Congress approves the work of the People's Commissariat of Finance to that end, and in particular reaffirms the decision of the Council of People's Commissars relative to the limitation of the issue of paper money in the 1922 fiscal year as the first decisive step towards the improvement of the ruble's position.

It would be wrong, however, to conclude, as some did, that this constituted an abandonment of the communist philosophy of the place of money (gold) in a *socialist* society. The following lines from an address by Lenin are quite illuminating:[6]

When our victory becomes world-wide, I believe that we will place in the streets of some of the largest cities in the world public comfort stations made of gold. This would be a most "just" and instructive use of gold for those generations that will not have forgotten that it was on account of gold that ten million people had been killed and thirty million maimed in the "great liberating" war of 1914–18, in the war where the great problem: which peace is worse, the Brest or the Versailles? had to be settled; and that on account of that same gold they are surely going to kill twenty million and maim sixty million in a war, let us say, in 1925 or in 1928 between, let us say, Japan and America, or England and America, or something like that.

But, no matter how "just," how utilitarian, and how humane such application of gold would be, we nevertheless must say that to attain this it is necessary to work for another couple of decades with the same intensity and results as we did during 1917–21, only on a wider scale. Meanwhile, we must take special care of our gold, and see that we get full value for it. When you live with wolves you have to howl like a wolf . . .

The realization that the New Economic Policy demanded a new financial policy was reflected in a series of new legislative acts as well as in the rise of a series of new institutions. Already on June 10, 1921, the All-Russian Central Executive Committee permitted the various co-operative societies to hold and to dispose freely of

[6] Lenin, *Collected Works*, XVIII, Pt. 1, 380.

balances of cash not exceeding ten million rubles.[7] A few weeks later on June 30th the Council of People's Commissars decreed the repeal of all legislation limiting the amount of cash which private individuals, organizations, or state enterprises could have in their possession.[8]

In an introductory paragraph to this decree of June 30, the government states that its aim is "to remove the limitations that stifle economic life and to place currency circulation on a sound basis through the development of deposits and transfer operations." Inasmuch, however, as the people still remembered what had happened to their deposits in 1917–20 it was necessary to overcome their distrust. Accordingly, that same decree proclaimed that "sums deposited or left for transfer purposes with agencies of the Commissariat of Finance or with co-operative organizations were not subject to confiscation except upon the order of institutions invested with judiciary powers." Furthermore, those sums "were to be repaid to their owners upon demand, in cash, and without any restrictions as to the amounts of withdrawal." As a further assurance that the government would not pry into the financial affairs of depositors for the purpose of finding out what they had, and then through devious ways take it away from them, the decree recited that information pertaining to those deposits and transfer funds was to be disclosed "to no one, except their owners, courts, and investigating agencies." [9]

That the stabilization of the ruble was most important and that the very much needed reconstruction of the country's economic life would be exceedingly difficult and slow, if not impossible,

[7] *Collected Decrees*, 1921, Decree 275.

[8] Decrees 301 and 458. It will be recalled that by an act of July 25, 1920, the holding of cash balances in excess of ten times the minimum wage was prohibited. This principle was reasserted as late as January 3, 1921 (Decree 37).

[9] In practice, however, this ruling had been frequently violated and a good many private individuals, therefore, refrained from keeping their funds in the banks. To overcome this the Council of People's Commissars on February 25, 1925, amplified and reasserted the above ruling and the State Bank in its circular of March 17, 1925, issued an admonition to officers of the bank to observe that ruling. A similar decree was published by the Ukrainian Council of Commissars on July 4, 1925. On March 3, 1926, the Commissariat of Finance of the R.S.F.S.R. in response to inquiries from mutual-credit societies (*private* credit institutions) stated that they were not required to disclose to tax officials any information pertaining to the financial affairs of their clients (*Financial Gazette*, March 26, 1926).

without it, had, therefore, been realized early in 1921. It had also been realized that it was extremely dangerous for the government to acquiesce in the displacement of the exceedingly unstable ruble by such substitutes as gold, foreign currency, and ordinary commodities. After all, the treasury was still dependent to a large extent for its revenue upon the printing press. Mere realization of all this and a declaration of honorable intentions were, of course, not enough. It was necessary to find ways and means for the actual stabilization of the currency. This, however, is by no means an easy task.

Once inflation gets well under way it cannot be "controlled" or stopped at will. For this there are several reasons. Inflation is usually the result of an unbalanced budget and it takes some time before the causes which helped to place and maintain the budget in such chaotic state are eradicated. The state generally finds it necessary, as a preliminary step, to increase its revenue, reduce its expenditures, bring about a favorable balance of payments (principally through the curtailment of imports and the encouragement of exports), and, in all probability, to raise loans abroad. It cannot very well proceed with a policy of decreasing its note issue without resorting to the above remedies. Its expenditures will not permit it. On the contrary, as inflation continues and the monetary unit keeps on steadily depreciating, it becomes necessary to inject stronger and stronger doses of notes into the economic system to produce no more than the accustomed revenue.

But even if it were possible to decrease the volume of the means of payment in circulation at will, it does not follow that inflation would thereby be brought under "control." The price level and therefore the purchasing power of the monetary unit are influenced (on the means of payment side) not only by the volume of currency, but by the velocity of its circulation as well. The increase of the velocity of circulation, as previously explained, is caused by the people's lack of confidence in the currency and the consequent "flight" from the latter into tangible values. But as Professor Kemmerer says: [10] "If the public once loses confidence in

[10] "Controlled Inflation," *Papers and Proceedings of the American Economic Association*. March, 1934, XXIV, No. 1, Supplement, p. 100.

its money, controlling inflation is like controlling a hurricane. At such a time the volume of the circulating medium is of secondary importance. The public are seized by a panicky fear and the velocities which are whipped up into fantastic figures dominate the situation." Indeed, the torrent of inflation, swollen high by the avalanche of its ever mounting volume and whipped into terrific fury by the swiftness of its flow, may in its wrath sweep away not only whatever sluice-gates of control there are but the keepers of those gates as well. Government fiat cannot check the swiftness or velocity of that flow. Only a change of the people's state of mind is able to do that. In other words, only a resuscitation of confidence in the medium of exchange will check that velocity. But how can confidence be resuscitated? Sound government finance could be relied upon to accomplish much in that direction.

But the economic conditions in 1921 were not such as to permit the balancing of the budget without additional note issues. The improvements which had begun as a result of the New Economic Policy were not as yet sufficiently large to make this possible. The year 1921, it must be remembered, not only found Russia's economic life at a very low ebb, but brought with it an additional catastrophe—a famine so great that in the provinces along the Volga people resorted to cannibalism. Moreover, various state enterprises, factories, railroads, mines, and so forth, although ordered to become self-supporting, were still operating at a deficit. For this they were not entirely to be blamed. Sorely in need of cash, they felt compelled to dispose of their stores of products at very low prices and in this they were helped by the ensuing cut-throat competition among the unbridled trusts. Costs did not matter, depreciation and amortization were not even thought of, so that in the end instead of increasing their working capital they really decreased it. Furthermore the state itself until 1922–23, in an attempt to make ends meet, was procuring the commodities and services from those enterprises either without any compensation whatever, or below cost. Thus the various enterprises continued to depend upon the state for subsidies and the state budget of course reflected this in its section of expenditures. A comparison of the figures representing the expenditures with those representing the

revenue obtained during 1921 will express more eloquently than could words the fiscal situation of Soviet Russia during that year. With expenditures (in money) amounting to some 26,076,000,000,000 rubles, the state succeeded in procuring a revenue of but 4,139,000,000,000 rubles. The deficit was, therefore, represented by a figure that reached almost 22,000,000,000,000 rubles (or 84.1 percent of the expenditures), and the notes issued during that year attained, accordingly, to the unprecedented height of 16,300,000,000,000 rubles.[11]

That the revenue was, comparatively speaking, so small is of course explained by the fact that the sources of revenue which were destroyed in the period between 1918 and the beginning of 1921 were slow to reappear. Besides, the country no longer possessed an adequate tax apparatus, and moreover, it proved impossible to borrow either abroad or at home; abroad—because of the general hostility towards a communist regime and the repudiation by the Soviet government of the debts of the preceding governments; at home—not only because of the same reasons but also because public credit presupposes the existence of savings, and such institutions as banks, and an organized money and securities market, as well as the existence of a stable currency, all of which were prominent by their absence.

Nor was the situation with respect to foreign trade in a happier state. Imports during 1921 amounted to 210,700,000 pre-war rubles, while exports amounted to but 20,200,000 rubles.[12] The unfavorable balance, 190,500,000 pre-war rubles, constituted a severe drain upon the country's scanty gold supplies and proved to be an additional factor in making the immediate stabilization of currency impossible.[13] This, however, did not prevent the adoption of measures which, even though incapable of producing immediate results, promised to pave the way for an ultimate stabilization of the currency. It has already been pointed out that the New Eco-

[11] The discrepancy between the figures representing the deficit and the note issue is probably due to the fact that the actual pecuniary expenditures in that year were smaller than the estimated figure. See Katzenellenbaum, *Russian Currency and Banking, 1914–1924*, p. 70.

[12] *Infra*, Table 30.

[13] This, nevertheless, did not discourage some from advancing naïve schemes for the immediate adoption of the gold standard.

nomic Policy made possible an increase in the state's revenue. To attain a balanced budget and thereby remove the cause for the excessive note issues, it therefore remained to bring about a decrease in the state's colossal expenditures. Accordingly the government in 1921–22 proceeded with a drastic reduction in the number of the civil and military personnel, the closing of submarginal plants and mines, the separation of local expenditures from the main budget, as well as with a number of other measures which helped to free the state budget from its terrific load. It was apparent that the presence of a credit institution would not only bring about a resurgence of the national economy and facilitate the stabilization of currency but that it would also help to free the budget from one of its chief burdens, that of financing the national economy.

The Establishment of the State Bank

Preliminary steps.—Already in the summer of 1921 the Council of People's Commissars and the Commissariat of Finance were considering various plans for such a credit institution. One of these plans proposed that all work pertaining to the granting of credit be entrusted to the Central Union of Co-operative Societies (*Centrosoyuz*); another called for a People's Bank, and so forth.[14] On October 12, 1921, the All-Russian Central Executive Committee, stimulated by a report of the Commissar of Finance advocating the adoption of a number of financial measures, ratified an earlier decree (of October 4th) of the Council of People's Commissars with respect to the organization of a state bank.[15] It further resolved to ratify (after corrections and changes were entered by the Committee) the proposed bank statutes and advised the Council of People's Commissars to bring forth a final draft within a week, and the Presidium of the Central Executive Committee to affirm this draft within the same period of time. The Commissar of Finance, in whose commissariat the bank was to be included, was instructed to begin the operations of the bank not later than November 15, 1921. It was similarly ordered that the national treas-

[14] G. N. Dmitriev-Krymski, *Modern Banks and Credit in the U.S.S.R. and Abroad* (Leningrad-Moscow, 1924), p. 72.

[15] *Collected Decrees*, 1921, Decrees 593, 594.

ury grant the bank its initial capital of 2,000,000,000,000 rubles. The promptness of the various government agencies made possible a ratification of the bank statutes by the All-Russian Central Executive Committee on October 12.[16] A little over a month later (on November 16) the bank began its operation under the name of State Bank of the Russian Socialist Federated Soviet Republic (R.S.F.S.R.).[17]

The purpose of the bank.—An explanation as to the purpose for which the bank was established is found in the first article of its statutes: [18]

The State Bank of the R.S.F.S.R. is established for the purpose of aiding, by means of credit and other banking operations, the development of industry, agriculture, and trade, as well as to concentrate monetary transactions and to carry out other measures for securing a sound monetary circulation.

Capital and surplus.[19]—The bank was to have an authorized capital and a reserve capital or surplus. The authorized capital was made up of the above-mentioned grant by the treasury of 2,000,000,000,000 paper rubles.[20]

[16] Decree 615.

[17] On July 6, 1923, the Central Executive Committee of the U.S.S.R. decreed the change of the bank's name to the State Bank of the Union of Soviet Socialist Republics. *Collected Decrees,* 1923, Decree 786. The State Bank (*Gosudarstvennyi Bank*) is commonly referred to as the *Gosbank.*

[18] *Loc. cit.,* also *Statutes of the State Bank of the R.S.F.S.R.,* published by the State Bank in 1928.

[19] Articles 1–4 of the 1921 Statutes of the Bank. *Collected Decrees,* 1921, Decree 615.

[20] When computed on the basis of the All-Union Index of the Bureau of Labor Statistics it appears that this sum when granted was equivalent to about 25,000,000 pre-war rubles, but that at the time the bank had commenced its operations the amount had already depreciated to about 17,000,000 pre-war rubles. The estimates of various authorities on this subject differ, however. Thus, N. G. Tumanov (*The Valuta and Credit Policy of the State Bank,* Moscow, 1925, p. 50) states that the 2,000,000,000,000 rubles when granted amounted to about 50,000,000 rubles (gold), but that at the time the bank had commenced its operations and the cash had been transferred to its vaults it amounted to about 14,000,000 rubles. The same figures are given by Katzenellenbaum, *op. cit.,* p. 156.

On the other hand, the State Bank in its 1921–26 report (Moscow, 1927), pp. 20, 31, estimates that the real value of the 2,000,000,000,000 rubles "hardly exceeded 30,000,000 rubles." In the above report (p. 31) the State Bank carried its capital as equivalent to 33,300,000 rubles on November 17, 1921. By January 1, 1922, its capital shrank to 22,200,000 rubles, and further dwindled to 1,500,000 rubles on October 1, 1922. The State granted during 1922 new subventions and as

Inasmuch as the bank was to operate on self-supporting business lines it was expected to earn profits. A portion of those profits was to be used for the purpose of creating a reserve capital or surplus.[21] In case the losses sustained by the bank in any given year exceeded the total of the reserve capital, the difference, or deficit, was to be charged, upon the confirmation of the annual report and balance sheet,[22] to the special account of the People's Commissariat of Finance and covered out of the state budget.[23]

Relations with the state.[24]—The State Bank was set up as a constituent part of the People's Commissariat of Finance and was directly subordinated to the People's Commissar of Finance.

Although directing the bank to operate on self-supporting business lines, the state undertook to make good such losses of the bank as could not be absorbed by the surplus account of the latter.[25]

Administration and management of the bank.—The general supervision of the bank's activity was vested in the People's Commissar of Finance, who was to direct the general policy of the bank and upon whose approval depended the bank's interest rate and commission charges, as well as the basic rules for banking operations. It was to him that the annual estimates of expenditures as well as the reports and financial statements of the bank were to be submitted for ratification.

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a result, in its statement for January 1, 1923, capital is carried at 7,500,000 rubles. (See the *State Bank of the U.S.S.R. 1922–25, the Third Anniversary of the State Bank Note Issue* [Moscow, 1925], p. 13.) The introduction of the chervonetz enabled the bank to fix its capital more accurately and on May 1, 1923, it was stated to be 50,000,000 rubles. Thereafter it kept on increasing from time to time.

[21] According to Article 46 of the statutes "the net profits, after the confirmation of the annual report and balance sheet by the People's Commissar of Finance, shall be allocated as follows: 50 percent to reserve capital, a sum not exceeding 20 percent to the staff-welfare fund, and the balance to the state treasury."

[22] An annual audit of the accounts of the bank was to be made by an auditing committee appointed by the Commissar of Finance. The board of directors of the bank were required to forward the reports rendered by the auditing committee together with the bank's annual report and financial statements as well as its own explanatory memorandum to the Commissar of Finance for confirmation and further disposal. *Collected Decrees,* 1921, Decree 615, Articles 27, 41.

[23] Article 4.

[24] For changes, see the revised statutes of 1929. *Infra,* Chapter XII.

[25] Articles 1, 4.

The management itself was entrusted to a board of directors whose members were appointed by the People's Commissar of Finance. The chairman of the board was to be appointed by the Council of People's Commissars on the recommendation of the Commissar of Finance.[26]

General business of the bank.[27]—The bank was instructed to carry on its business "in consonance with the requirements of the developing industry and trade by granting credits against security and for purposes economically expedient to large state industrial institutions and undertakings, to co-operative and other organizations, to private enterprises, as well as to agricultural establishments and to handicraftsmen." In particular, it was authorized to carry out the following operations:

1. To grant earmarked productive credits for the promotion of definite enterprises either against collateral security or in the form of "on-call" overdrafts.

2. To grant "on-call" (overdrafts) credit against goods in warehouse, waybills, invoices, bills of lading, and the like, as well as against promissory notes, bills of exchange, and other instruments of credit maturing within a period not exceeding six months, and provided the total amount so granted does not exceed 75 percent of the market value of goods or notes.

3. To grant "on-call" credit against the deposit of foreign securities (up to 60 percent of their stock exchange value), currency, bullion (up to 90 percent of the legally fixed value of the metal in weight), drafts, and foreign bills of exchange (up to 75 percent of the rate of exchange value).[28]

4. To grant fixed-term credits against the securities mentioned in 2 and 3 in similar proportions of their value and for a period not exceeding three months.

5. To discount promissory notes and bills of exchange maturing not later than six months from the day of discount.

6. To buy and to sell goods on commission.[29]

[26] Articles 5–8. [27] *Loc. cit.*, Article 29. See footnote 24 above.

[28] In May, 1922, this paragraph was amended to authorize the bank to grant credits against "stocks, bonds, and various other securities of companies the statutes of which have been ratified in accordance with the laws of the R.S.F.S.R. (Decree 637).

[29] In November, 1922, this clause was amended and the words "and on its own account" added after "commission." In other words, the bank was given the right to sell and buy goods for its own account, as any trader would (*Collected Decrees*, 1922, Decree 923).

7. To buy and to sell (for its own account) foreign securities, drafts, foreign currency and precious metals, provided the funds so used do not exceed one-third of the bank's capital.[30]

8. To open credits against forwarding documents.[31]

9. To issue transfers and letters of credit on places at home and abroad.

10. To collect on commission bills of exchange, promissory notes, foreign drafts, warehouse and transit documents, and all other kinds of documents and valuables and to effect payments of various kinds on behalf of clients, provided the amount of such payments has been received in advance.[32]

11. To receive and pay out demand deposits, and time deposits (either for a fixed period or for an indefinite period).

12. To receive into safe custody various articles for a period not exceeding five years.

The loan and discount committee.[33]—The board of directors was instructed to set up a loan and discount committee. The wide representation on this committee given to the various government departments and branches of national economy constituted one of its outstanding features. Thus, in addition to the chairman and one member of the board of directors, the committee also included two representatives each of the Supreme Economic Council and the People's Commissariat of Agriculture, one representative each of the People's Commissariat of Finance, the Commissariat of Foreign Trade, the Commissariat of Workers' and Peasants' Inspection, the Central Union of Consumers' Societies (*Centrosoyuz*), the All-Russian Agricultural Co-operative Union (*Selskosoyuz*) and the Amalgamated Industrial Co-opera-

[30] In May, 1922, this clause was amended so as to include the purchase and sale of "stocks, bonds, and other securities of companies the statutes of which have been duly and properly ratified in accordance with the laws of the R.S.F.S.R."

[31] Article 32 of the statutes authorized the bank "for the purpose of transacting mutual transfer, commission, and other operations . . . to enter into relations with foreign banks and banking institutions on the basis of special agreements concluded with them." In order to develop relations with its foreign correspondents, the bank may, with the approval of the People's Commissar of Finance, "utilize the valuables at its disposal as security for its operations with the said foreign correspondents."

[32] By a decree of May, 1922, this paragraph was amended to include the subscription "on behalf of clients for stocks, bonds, and other securities of companies . . . the statutes of which have been duly and properly ratified in accordance with the laws of the R.S.F.S.R." (Decree 637).

[33] Article 24. This section was omitted from the bank's revised statutes of 1929. *Infra,* Chapter XII.

tive Society, as well as of representatives of trade and industry invited by the chairman of the bank's board of directors, and approved by the Commissar of Finance.[34]

Branches.[35]—The bank was authorized to establish district offices (in the capital cities of the constituent republics), branches (in provincial cities), and agencies subordinated to the branch offices.

Clearing houses.[36]—The bank was likewise authorized to set up clearing houses at the head office and at local branches, and charge to those using its services the cost of maintaining them.

An evaluation of the bank's statutes of 1921 (together with the early changes).—Although the above provisions speak for themselves, a brief evaluation of them will show even more clearly the outstanding characteristics of the new bank and the difference between it and the pre-October, 1917, State Bank.

It will be noticed that the new State Bank had not been accorded the privilege of note issue, the state reserving the sole monopoly of it for itself. Thus, the State Bank, although charged with the duty of bringing about a "sound monetary circulation," was quite helpless in this respect, inasmuch as it had no control over the printing presses which continued to supply the government with paper money for the purpose of covering budgetary deficits. The right of note issue, as will be seen in a later section, was acquired by the bank only towards the end of 1922.

Now this was not the only important difference between it and the old State Bank. It will also be observed that, unlike the old State Bank, the new bank was instructed to extend not only short-term commercial credit but long-term investment credit as well. Moreover it was given the right to buy and sell commodities for its own account, a function not in consonance with sound banking policy, not only because the bank by virtue of its position may engage in unfair competition with its clients, but also because it is an agency upon which devolves the duty (whether

[34] In December, 1922, this article was amended so as to include in the loan and discount committee a representative of the Consumers' Co-operative Bank (Pokobank). Decree 1042.

All members of the board of the State Bank attending the meetings were entitled to vote.

[35] Articles 12–22. [36] Article 33.

or not it is mentioned in its charter or statutes) of helping to maintain the price level at a point that is best for the national economy as a whole, rather than at a point which would insure for it a handsome profit on the sale of commodities.

It will further be noticed that the bank had been given authority to extend not only "time" but "demand" or "on-call" credits as well, and these not only against securities but against commercial instruments, merchandise, and the like. Now when a commercial loan is negotiated, the bank and the borrower are likely to fix the period of time for which the loan is granted in such a way as to take into consideration the length of time that it takes in the borrower's business to place the commodities on the market, sell them, and obtain payment for them. When this practice is followed, the bank, if the character of the borrower is known to be satisfactory and if there is a demand for his goods, really needs no other security than the borrower's written promise. The sale of the goods provides the means with which the loan is liquidated. By granting such loans the bank does not deprive its assets of that degree of liquidity which safe banking demands, for it is possible to arrange the maturities in such a way as to make provision for a continuous stream of payments which will help to maintain the liquidity or fluidity of those assets. When, however, "demand" or "on-call" loans are granted the lender apparently supposes that the borrower's line of business is of such nature that he is able to convert his wares into cash at any moment that the banker may direct him to do so. Now this assumption is quite untenable when applied to a commercial or industrial enterprise. Its validity is likewise questionable when applied to the type of loan with which our own banking practice usually associates the term "on-call," namely, loans for speculative or investment purposes.

It is often assumed that one may withdraw his funds from the investment market at will. It must, however, be remembered that when the security had originally been sold, the proceeds were presumably invested in plants, machinery, and other fixed assets. But, as Lady Macbeth said, what's done is done. All such expressions as "shifting funds from the investment into the com-

mercial market" are quite ambiguous. What is really meant by that is that the lender will attempt to find someone who is willing to take his place; whether he will succeed in that at the precise time that he desires and on terms satisfactory to himself will depend upon conditions which he does not control. Certain securities, real estate mortgages for example, may continue to clog a bank's portfolio for a long time before they can be disposed of even at a loss. But even the theoretically marketable stocks and bonds are in practice often found to be quite unmarketable because of the sacrifice which is involved when they must be sold at very low prices.

As may be suspected it was not entirely the lack of information as to what constitutes sound banking that was responsible for the inclusion or exclusion of certain of those provisions, but rather the economic and financial circumstances with which we are already familiar. It is important to remember that as constituted in 1921 the new bank was a state-owned (this, by the way, does not differentiate it from the old State Bank, for the latter too was owned by the state) commercial and investment bank, and not a central bank of issue. It must also be borne in mind that, when it was resolved to bring about a speedy reconstruction of the almost ruined national economy, there existed no financial capital within the country, that the prospect for an accumulation of savings in the immediate future by the population had to be discounted, and that foreign loans were unobtainable.

So much for the provisions pertaining to long-term financing. In so far as the inclusion of the provision granting the bank the right to deal in commodities is concerned, it may be said that this too was a product of the anomalous situation. The facilities for the distribution of commodities were slow in developing, commercial relations between the large centers and smaller towns were practically non-existent. It was under such circumstances that the State Bank, whose newly opened branches served as links between those points, undertook to facilitate the distribution of commodities. Its eagerness to do that could probably be explained on the ground that credit transactions were as yet dormant, but especially by the fact that such operations afforded the bank's

assets protection from loss on account of the depreciation of currency.

The Depreciation of the Ruble during 1921–22

The abnormal currency situation of 1921–22, the period during which the bank had been denied the privilege of issuing notes of its own, was largely instrumental in molding the trend of the bank's activities during that year.[37] An analysis of the situation will, therefore, aid our understanding of the impediments which lay in the path of the bank and which gave direction to its activities.

As shown in Table 19, the total amount of notes issued during 1921 was well in excess of 16,000,000,000,000 rubles, a huge amount of paper money. The year 1922, however, brought with it such a plethora of paper money that the issue of 1921 was dwarfed by comparison and soon appeared a mere bagatelle.

During that year the treasury issued almost two quadrillion rubles, an amount that has sixteen places and that under brighter economic skies is associated with astronomy rather than with finance.[38]

True, to increase the output of the printing presses and relieve its people of the trouble of dealing with such figures, the government devalorized the currency twice, first, by a decree of November 3, 1921, when it ordered that one ruble of the 1922 issue equal 10,000 rubles of the previous issues and be exchanged in that ratio.[39] The second devalorization was ordered on October 24,

[37] It may be of interest to note what a prominent Russian writer has to say about the employment of such a phrase as "abnormal currency situation." "To us, from the point of view of the dialectic method," he says, "there do not exist 'normal' and 'abnormal' monetary systems, for under given conditions the most abnormal system may become the most suitable in a given social-economic sphere." —Kuzovkov, *Fundamental Principles of the Disintegration and Reconstruction of the Monetary System* (Moscow, Communist Academy, 1925), p. 357.

[38] The staggering amounts were paralleled by the staggering weight of the notes that people found it expedient to carry around.

[39] Decree 643. The decree by conferring upon the new issues the title "money-tokens" gave effect to the changed attitude towards money. It will be recalled that earlier issues were referred to as "settlement-tokens," the word "money" being eschewed as incongruous with a communist regime.

1922.[40] According to the terms of the latter decree, a ruble of the 1923 issue was made to equal 100 rubles of the 1922 issue, or, what is the same, one ruble of the 1923 issue was exchangeable for 1,000,000 rubles of previous issues. It cannot be said that those measures were wholly devoid of fruitful results. To the extent, for instance, that the bewildered population was able to accustom itself (and that was a very slow process) to the new units, its tasks of calculation and bookkeeping were considerably simplified, especially after the second devalorization.[41] Also by requiring that notes of previous issues be exchanged for notes of a new pattern, those acts facilitated the elimination of the motley paper issues of previous years.[42]

They did not, however, and could not stop the depreciation of the ruble and the evils arising therefrom. Despite the fact that the New Economic Policy served to create a wider base for the demand for currency, the gradualness of that increased demand rendered it powerless to absorb the ever increasing supply of paper money being thrown upon the market by the government. The sources of state revenue, as we have seen, were slow in their reappearance, and the expenditures, now that the state was financing industry on a larger scale than before, were mounting. Column 5 of Table 19, for instance, shows that during the early months of the second half of 1921, from which the New Economic Policy really dates, the purchasing power of the ruble tended to become more or less stabilized. The greatly increased doses of paper money which were being put out by the government, however, wiped out that advantage. Again, in July and August, 1922, despite the new issues of money, another stabilization took place. This improvement was probably due not only to seasonal factors (the improvement in 1921, it will be noticed, took place during the same months), but to a number of additional factors.

[40] Decree 867.

[41] The first devalorization brought much confusion, the people finding it cumbersome to divide values to which they were accustomed by 10,000. It was far simpler to carry on such conversion in terms of a million.

[42] On September 8, 1922, the Council of People's Commissars decreed the establishment of a homogeneous monetary circulation (Decree 738).

TABLE 19

ISSUE, INCREASE, AND PURCHASING POWER OF TREASURY NOTES (OR SOVZNAKS, OR SOVIET RUBLES)

1921–22

Date	*Volume of Notes in Circulation* [a] In millions of rubles on the first of the month	*Index of Notes in Circulation* [b] July 1, 1914 = 1	*Amount of Notes Issued during the Month* [c] In millions of rubles	*Rate of Increase in the Volume of Notes in Circulation* [d] Column 3 to column 1 as a %	*Price Index* [e] All-Union Index of the Department of Labor Statistics on the first of the month 1913 = 1	*Monthly Rate of Increase of the Price Level*
1921						
January	1,168,596.9	716.7	130,232.0	11.1	16,800	28.6
February	1,298,828.9	796.6	189,394.0	14.6	21,600	27.8
March	1,488,222.9	912.8	198,460.6	13.3	27,600	29.3
April	1,686.683.5	1,034.5	230,568.3	13.7	35,700	19.6
May	1,917,251.8	1,175.9	205,040.5	10.7	42,700	45.2
June	2,122,292.3	1,301.7	224,871.8	10.6	62,000	30.2
July	2,347,164.1	1,439.6	460,932.6	19.6	80,700	—0.5
August	2,808,096.7	1,722.3	702,577.5	25.0	80,300	—4.9
September	3,510,674.2	2,153.2	1,018,753.7	29.0	76,400	7.2
October	4,529,427.9	2,778.1	1,950,285.2	43.1	81,900	16.6
November	6,479,713.1	3,974.3	3,365,481.8	51.9	95,500	44.5
December	9,845,194.9	6,038.5	7,694,037.2	78.1	138,000	108.7
Total	....	....	16,370,635.2	....	....	....

1922						
January	17,539,232.1	10,757.6	12,238,965.0	69.8	288,000	89.2
February	29,778,197.1	18,264.3	18,756,143.2	63.0	545,000	111.5
March	48,534,340.3	29,768.4	32,645,722.7	67.3	1,153,000	118.9
April	81,180,063.0	49,791.5	48,328,256.4	59.5	2,524,000	64.9
May	129,508,319.4	79,452.9	84,243,130.2	65.0	4,162,000	22.2
June	213,751,449.6	131,135.8	106,198,658.8	49.7	5,087,000	13.9
July	319,950,108.4	196,288.4	154,843,557.8	48.4	5,795,000	−3.5
August	474,793,666.2	291,284.4	221,348,047.6	46.6	5,589,000	7.2
September	696,141,713.8	427,080.8	155,345,142.39	22.3	5,995,000	22.5
October	851,486,856.19	522,384.6	244,002,600.90	28.7	7,342,000	57.5
November	1,095,489,457.09	672,079.4	383,729,848.99	35.0	11,561,000	42.2
December	1,479,219,306.08	907,496.5	515,245,147.67	34.8	16,440,000	29.2
1923						
January	1,994,464,453.75	1,223,597.8	633,677,519.33	31.8	21,242,000	30.4

[a] *Our Monetary Circulation*, p. 153. [b] *Ibid.*, p. 206. [c] *Ibid.*, p. 152. [d] *Ibid.*, p. 204. [e] *Ibid.* p. 248.

The ruinously low prices charged by the various state enterprises, whose need for cash drove them to cutthroat competition, constituted one such factor;[43] the promising outlook for a good crop and therefore lowered wheat prices, another. Besides, as time went on the fiscal machine was developing greater power. The figures given below will demonstrate the significance of this latter factor.

In other words, while at the beginning of the year the revenues from sources other than note issue was small, around one-eighth of the total, it steadily grew until by the end of the year it exceeded half of all the revenues received by the state.

The New Economic Policy was responsible for a number of other improvements. Despite, for instance, the fact that from July, 1921, to the end of 1922 the volume of currency had in-

TABLE 20

STATE REVENUES IN 1922 [a]

(*In percents*)

	From Note Issues	*Taxes (State and Local)*	*Revenue from State Enterprises and Properties*
January-March	86.7	2.7	10.6
April-June	69.4	8.9	21.7
July-August	56.8	13.6	29.6
October-December	46.3	24.4	29.3

[a] Yurovsky, *Currency Problems and Policy of the Soviet Union* (London, 1925), p. 66.

creased by about 850 times, or 84,895 percent, prices during the same period, due no doubt to the expanding volume of trade, increased but 263 times, or 26,222 percent. During the second half of 1921, when the volume of currency had increased 7.5 times, or by 617 percent, prices increased by about 3.5 times, or by

[43] The credit policy of the State Bank at this time was quite rigorous. Furthermore, they found it difficult to meet the demands of the government for high taxes. —V. J. Zheleznov, "Our Monetary Circulation since the New Economic Policy," *Vestnik Finansov*, 1924, No. 11, p. 12.

slightly more than 266 percent. A somewhat similar but less pronounced lag between the rate of increase of prices and that of the volume of currency is shown in the second half of 1922, when a 6.2 times, or 523 percent, increase in the volume of currency was accompanied by a 3.7 times, or 266 percent, increase in the price level. The rate of increase of the volume of currency during the first half of 1922 was very pronounced. Accordingly, we find quite a different trend during that half year, an 18.2 times, or 1,724.6 percent, increase in the volume of currency being accompanied by a 20.1 times, or 1,912 percent, increase in prices.

Important as these improvements were, their presence was nevertheless dwarfed by a more apparent situation, the continuing rapid decline of the ruble's purchasing power. At the beginning of 1921, for instance, the price level, according to official figures, was 16,800 times as high as the pre-war level. A month later, on February 1, it was 21,600 times as high, an increase for that month of over 28 percent. Two months later, on March 1, the price level was already 27,600 times as high as the pre-war level, thereby showing an increase of more than 64 percent over January 1, 1921, prices. Prices continued to climb and by the end of 1921 their average was 288,000 times as high as that of pre-war prices, thus registering a 1,612 percent increase for that one year. A year later, by the end of 1922, the price level surged to a point which was over 21,000,000 times higher than the pre-war level and which showed a 7,270 percent increase of prices for the year.

Thus the situation on the whole continued to remain critical.[44] And although the country was able to weather this storm as it had many before and would a good many others later, its economic and financial progress was impeded by the continuing inflation. The borrowing and lending of credit, the production of commodities, their sale and purchase, and all other transactions encountered in a modern economy took on a purely speculative

[44] Speaking, for instance, of the inordinately large note issues of the last three months of 1921 (the treasury had added some 13,000,000,000,000 rubles to a circulation consisting of some 4,500,000,000,000 rubles), and the ensuing grave crisis of January to March, 1922, when the rate of price increase outstripped that of the note issue, a prominent Russian authority in October, 1922, made the following declaration: "We are able at present to state definitely that we were within a hair's breadth of complete bankruptcy. . . ."—Sokolnikov, *op. cit.*, I, 236.

character. No one knew the extent to which the purchasing power of a sum of money loaned today would shrink thirty days hence, and, therefore, what interest rate to charge for the loan. The producer and the trader could not know what price would enable them to replace their stock and earn a profit. Wages, even if increased in the morning to a point which would insure a standard of health and decency, paid and spent later in the same day brought a lowered standard of living. Financial planning was impossible. Calculation as to cost of production was quite meaningless.

It was under those circumstances that the State Bank threw its doors open to the public on November 16, 1921.

The Work of the State Bank during 1921–22

Its resources.—The capital of a bank, the notes issued, and the deposits received provide the resources on the basis of which it may carry on credit operations. Inasmuch as the new State Bank possessed no right of note issue during the first year of its existence, its resources had to come from its own capital and from whatever funds it could attract in the form of deposits. Its own capital, especially when we consider that the bank was intended as the nation's sole credit institution, could not be said to be adequate even when granted. The continuing rapid depreciation of the currency (the bank received no gold or precious metals when it was organized), moreover, wrought havoc with it, reducing its real value considerably within a short time. True, the state furnished it with some more paper money, thus raising its capital on March 1, 1922, from 2,000,000,000,000 rubles to 5,750,000,000,000 rubles, and, then, on November 1, 1922, to 130,750,000,000,000 rubles.[45]

Owing to the fact that during an inflationary period people sooner or later learn that the faster they spend their incomes the less they lose on account of the depreciation of the currency, the bank could not hope in that early period to attract any sizable amount of deposits from private persons. As formerly when the Ministry of Finance used to maintain large balances with the

[45] *The State Bank of the U.S.S.R., 1922–25*, p. 13.

State Bank, so now the Commissariat of Finance placed its free funds with the bank.[46]

With a view to stimulating deposits by others, the government and the bank itself employed a number of unusual devices. The first, by a decree of March 30, 1922, enjoined all state enterprises and institutions from retaining in their own safes more cash than was absolutely needed for current expenses (an amount that was to be approved by the agencies of the People's Commissariat of Finance), and from effecting any cash settlements whatsoever, except through the medium of the State Bank in the form of checks, transfers, and the like.[47] The bank itself offered what amounted to compensation, if only in part, to the depositor for the loss in purchasing power sustained by him while his funds were on deposit. The compensation took the form of high interest rates. From December 1, 1921, to March 1, 1922, the bank maintained on deposits in paper money an annual interest rate which fluctuated between 36 and 60 percent; while from March 1 to July 1, 1922, it paid from 48 to 72 percent per annum.[48] On July 1 the bank introduced a different method of safeguarding such deposits. It now began to employ a bookkeeping device of converting the deposited paper rubles into "gold" rubles paying the depositor at the time of withdrawal an amount in paper rubles to which those "gold" rubles were equivalent on that day. But even then the bank continued to pay interest, albeit only 4 percent per annum.[49]

Its loans and discounts in 1921–22.—Just as it was unprofitable for one to extend credit to the bank by leaving with the latter one's funds for deposit, so it was unprofitable for the bank to extend credit to its customers by granting them loans. Credit in those days, unless the bank was willing and able to shift to the

[46] By the end of the year the total deposits are said to have amounted to 37,300,000 rubles, of which sum 11,300,000 rubles belonged to the Commissariat of Finance.—Katzenellenbaum, *Russian Currency and Banking*, p. 166. Cf. *The State Bank of the U.S.S.R., 1921–26*, p. 35.

It must be remembered that the bookkeeping was carried on in terms of a rapidly changing denominator of value that rendered the figures for different dates incomparable. The calculations of those amounts in gold rubles cannot pretend to any degree of exactitude.

[47] Decree 311. [48] *The State Bank of the U.S.S.R., 1921–26*, p. 37. [49] *Ibid.*

borrowers the loss which resulted when loans were repaid in a catastrophically depreciating medium, was bound to take on a charitable character.

As an agency of the state the bank could not place its own interests above those of the national economy. In consequence it did not seek to adopt measures which would fully transfer that loss to the infant industries which were sorely in need of encouragement. The measures it did adopt were not sufficiently strong to prevent the dissipation of its resources. Of these, among the first was what may be called a special "insurance against depreciation" rate of 8 to 12 percent[50] per month in addition to the regular discount rate. Already in January, 1922, it was discovered that that rate was entirely too small and it was raised to 12–18 percent (monthly).[51]

In March of the same year, however, special measures had to be taken to prevent the resources of the bank from disappearing entirely. Accordingly quite a new method was introduced. The bank began to share in the profits that came to the borrower as a result of the depreciation of the ruble during the life of the loan, charging him about 50–75 percent of that difference. To simplify this method the bank soon began to demand that the loan be repaid in part or in whole in commodities in which the borrower dealt or which he produced, the price at which those commodities

[50] State enterprises were required to pay 8 percent; co-operatives, 10 percent; private enterprises and persons, 12 percent.—*Report of the State Bank of the R.S.F.S.R. for 1921–22*, pp. 41-42.

[51] A. A. Dezen, *The System of Bank Credit: Operations of Present-Day Banks of the U.S.S.R.* (People's Commissariat of Finance, 1925), pp. 9-11. By way of comparison it may be pointed out that in 1922 the "private" interest rate reached 2 percent and higher per day, that is, over 700 percent per annum, and never fell below 1 percent per day, or 360 percent per annum. (See, e.g., A. A. Dezen, "Credit Under a Declining Currency," *Vestnik Finansov*, No. 10, May 8, 1922, p. 5.) It may be suspected that this rate also reflected the great scarcity of funds in the private market. For in that market in 1922 a loan that was granted in *gold*, and not in paper rubles, nevertheless, commanded 180 percent per annum as against a peacetime rate of 7–8 percent. (See S. Chalkushian, "The Velocity of the Ruble's Circulation," *Vestnik Finansov*, No. 44, December 22, 1922.) Of the total trade turnover even at a later date, as in 1922–23, 75.3 percent was carried out by the so-called private sector; 14.4 percent, by state enterprises; and but 10.3 percent by co-operatives. (G. Schwartz, "Gosbank and the Extension of Credit to the National Economy," *Economic Life*, June 20, 1932, p. 3.) The policy of the State Bank, as is well known, was, however, to extend practically all of the available credit to the state enterprises and co-operatives so as to enable them to displace the private trader. Hence the scarcity of funds in that market.

were to be accepted being determined at the time of granting the loan. Soon, in fact, the bank began to extend loans in the form of commodities and to receive payment in the same form. Such operations could hardly be regarded, however, as loans and discounts. The bank was selling and buying commodities as any trader would.

Another method of preserving its resources was employed in connection with the extension of credit to enterprises engaged in export operations. Although granted in paper rubles, the loan in such cases was calculated in terms of dollars or sterling and later collected in such foreign currency.[52] Still another method was to calculate the loan in terms of gold rubles.

Of the total loans outstanding on October 1, 1922,[53] 79 percent were granted by the bank in the form of so-called "earmarked" productive credits, a form of credit not employed by the old State Bank. The following were its outstanding characteristics: no specific security was required for the loan, the loan was granted for a specific purpose, and for a comparatively long period of time. It played a most important rôle in the financing of lumber exports and the moving of sugar crops. This type of loan owed its origin to the peculiar conditions of that time.[54] First, the borrower not infrequently possessed nothing in particular that the law permitted him to hypothecate. Secondly, the use of commercial instruments, which had been discontinued under War Communism, was not reintroduced until March 20, 1922.[55]

Of the balance, 6 percent was granted against goods (finished goods, semi-finished manufactures, and raw materials) as security, and 15 percent against commercial paper.[56]

In addition to these the bank also extended long-term credits "for nine months and longer" to industry.[57] In this it was, how-

[52] It is significant that of a total of 19,000,000 (chervonetz) rubles in loans and discounts which the Main Office of the bank had outstanding at the end of 1922, 10,400,000, or 57.7 percent, constituted credits of this type.—A. A. Dezen, *Bank Credit in Industry* (Moscow, 1925), p. 11.

[53] It is estimated that when translated into chervontzy they totaled 25 to 26 million rubles. *Ibid*, p. 19.

[54] Later, when the bank had the right of note issue, it as a rule granted such loans against commodities as security.

[55] Decree 285.

[56] Dezen, *op. cit.*, pp. 17, 53.

[57] *State Bank of the R.S.F.S.R.: First Year of Activity* (Moscow, 1922), p. 63.

ever, acting merely as an agent of the treasury, which continued its financial aid to industry.[58]

Other activities of the bank.—In addition to its credit operations, whose volume although expressed in billions was in reality quite moderate, the bank during this year spent much effort along organizational lines, particularly in the matter of spreading the network of its branches throughout the country. Numbering 45 on April 1, 1922, and on October 1 of the same year 115, these branches played an important rôle. In those days the opening of a bank or a branch of a bank in a given district amounted to the incorporation of that district into the national economy.[59]

To protect its resources from depreciation and possibly in anticipation of its becoming a bank of issue, the State Bank devoted some of its energy and a large part of its paper resources to the accumulation of precious metals and stable foreign currency.[60]

Other banks.—Although originally intended as the sole credit institution the State Bank did not remain such very long. As early as 1922 a number of other banks were created. Established later than the State Bank and hindered by the depreciation of the currency, they played a very negligible part in 1922. An analysis of their activities is therefore reserved for a later chapter.

Toward the restoration of a stable currency.—It was natural that the national economy, the development of which was so greatly hampered by the baneful influence of a rapidly shrinking "measure" of value, should set out in search for a better measure, despite the fact that it was not as yet possible to discontinue the large note issues. Among the first steps in that direction were those taken by

[58] A. B. Shtern, *State Financing of Industry* (Moscow, 1924), p. 56. The government in 1922 subsidized principally the so-called "heavy" industry which was supplying the needs of the state (at a substantial deficit to itself). According to a "rough and approximate" estimate by Shtern (whose work on this subject is regarded as authoritative) the government had advanced to industry in 1921–22 some 75,000,000 rubles. The principal recipients of this were the fuel and metallurgical industries. The government, however, obtained from industry without payment a part of the latter's output valued at 125,000,000 to 150,000,000 rubles. (*Ibid.*, pp. 57 ff.)

[59] Yurovsky, "Credit System," *Finance and National Economy*, No. 42, October 15, 1927, p. 11.

[60] By January 1, 1922, it already had accumulated such assets to the extent of 300,000 rubles, and by January 1, 1923, 31,500,000 rubles.—*The State Bank of the U.S.S.R., 1922–25*, p. 13.

the Council of People's Commissars on November 5, 1921, when it decreed that the budget for 1922 be drawn up in terms of "pre-war" rubles. It meant that the budgetary expenditures for 1922 were to be estimated in stable units, that is, in rubles of 1913, but that the actual amounts of paper money (*sovznaks*) allocated to the various agencies included in the budget were to be determined by multiplying the estimated amounts by certain index numbers. Such indices or "rates of the People's Commissariat of Finance" were being published by the latter once monthly (in advance) during the period beginning with November, 1921, and ending with March, 1922. The rates for the months of November and December, 1921, were set at 60,000 and 80,000, respectively. Those for January, February, and March, 1922, were set at 100,000, 150,000, and 200,000, respectively. Although those rates were far too low, when judged by a comparison between the price levels then prevailing and the pre-war ones, they nevertheless were in principle based upon a commodity price index with 1913 as a base. Inasmuch as the pre-war (1913) index of prices measured the purchasing power of a fixed weight of gold over certain types and kinds of commodities and services the new "ideal" unit of reckoning began to be referred to as the *pre-war ruble, pre-war gold ruble, index ruble,* and *commodity ruble.*

The regulation of November 5, 1921, was followed on November 14 by still another decree requiring that leases be drawn in terms of the units described above, but that payment on them be made in *sovznaks* (that is, paper money) on the basis of the officially published "rates." [61] By a series of decrees promulgated in January and February, 1922, the use of this method was extended to the calculation of state and local taxes and duties, to passenger and freight rates, to the sale and purchase of timber, and so forth.[62]

The use of an index as an aid in the settlement of obligations, although never before applied anywhere on a large scale, is nevertheless not new. A very simple index, composed of but one commodity, may be said to have been employed during the reign of

[61] *Collected Decrees,* 1921, Decree 637. On December 15, 1921, this law was made retroactive.

[62] *Collected Decrees,* 1922, Decrees 57, 72, 75, 199.

Queen Elizabeth when an act was passed obliging three colleges, Oxford, Cambridge, and Eton, to lease their lands in terms not of precious metals, the value of which was considered variable, but in terms of corn, the value of which was deemed to be more stable.[63] At a considerably later date, in 1778, Massachusetts, a pioneer in the matter of spreading the use of paper money on the American continent and consequently not unfamiliar with the dissatisfaction caused by the receipt of a depreciated currency, employed a commodity price index, albeit not a complicated one. It paid its soldiers in notes which were redeemable at maturity in a quantity of money "in a greater or less Sum, according as Five Bushels of *corn,* Sixty-eight Pounds and four-sevenths Parts of a Pound of *Beef,* Ten Pounds of *sheep's wool,* and Sixteen Pounds of *sole leather* shall then cost, more or less than One Hundred and

[63] W. Stanley Jevons, *Money and the Mechanism of Exchange* (New York, Appleton, 1890), p. 319. He speaks of those statesmen as having been "far-seeing," inasmuch as "the result has been to make those colleges far richer than they would otherwise have been, the rents and endowments expressed in money having sunk to a fraction of their ancient value."

Jevons did not, however, propose to adopt corn as a standard of value because any single commodity which, although "comparatively steady in value on the average of long periods, may be subject to great temporary variations of supply and demand" (p. 320). He believed that a double standard (bimetallism) was superior to a single standard because of what is known as the "compensatory" action, or, as he prefers to call it, "equilibratory" action (pp. 134-38). It was, however, the *tabular* or *multiple* standard of value (that is, a table of index numbers of the general price level) that he considered as being ideal because under it it was possible to preserve the constancy of the purchasing power of money.

Jevons was not the first to expound the principles of the multiple standard. In 1822 Joseph Lowe (in *The Present State of England in regard to Agriculture, Trade and Finance*) proposed that information concerning the prices of staple articles of household consumption be collected and used in the making of a "table of reference" which would help to determine the amount of currency one has to pay in order to return the equivalent of the borrowed purchasing power. A similar scheme was independently proposed eleven years later by G. Poulett Scrope (in *An Examination of the Bank Charter Question, with an Inquiry into the Nature of a Just Standard of Value*, London, 1833). It is also found in G. R. Porter's *The Progress of the Nation*, which appeared in 1838. It is believed that the inventor of index numbers as a device for measuring changes in the level of prices is G. R. Carli, an Italian, whose book *Del Valore . . .* was first published in 1764. Trying to determine the effect of the discovery of America upon the purchasing power of money, Carli, we are told, "reduced the prices paid for grain, wine, and oil in 1750 to percentages of change from their prices in 1500, added the percentages together, and divided the sum by three . . ."—Wesley C. Mitchell, *Index Numbers of Wholesale Prices in the United States and Foreign Countries,* Bulletin of the U. S. Bureau of Labor Statistics, No. 284 (1921), p. 7.

Thirty Pounds current Money, at the then current Prices of said Articles." [64]

Despite legislative prompting, the Soviet economy was at first rather slow in adopting the index number of prices as a measure of value. Some hesitated to adopt a device the workings of which they ill understood. Others who did understand it objected to certain of its shortcomings, namely, that it was being fixed only once a month although the price level was mounting rapidly, and, furthermore, that the government officials were fixing it too low. The theoretical basis for the attack upon the "commodity ruble" was furnished by a group of influential Soviet economists who believed that a *gold ruble* and not a *commodity ruble* was best as a measure of value. The criticism advanced by them incorporated not only the defects mentioned above, but a number of others that are generally urged against the adoption of index numbers as a measure of value. Chief among these are the following: an index number of prices is an average, and as such is possessed of all the faults which are attributed to averages; [65] it is difficult to construct a single index number which would be good for all purposes; an index number of prices measures past price fluctuations, and is, therefore, never up-to-date; it does not eliminate price fluctuation, but, on the contrary, tends to perpetuate the evils of inflation; it renders accounting extremely difficult, and the like.

In their zeal to get the government converted to the view that tying the country's currency to the currencies of the gold-standard countries was the most advisable step, they undoubtedly exaggerated some of these defects. They realized, of course, that it was impossible at that time to go on an actual gold standard, and so they counseled the adoption meanwhile of an "abstract" gold standard. All in all, their proposal differed from that of the protagonists of the "commodity ruble" in that it would make the

[64] Willard C. Fisher, "The Tabular Standard in Massachusetts History," *Quarterly Journal of Economics*, May, 1913, XXVII, 437; also George F. Warren and Frank A. Pearson, *Prices* (New York, John Wiley and Sons, Inc., 1933), p. 18.

[65] T. S. Adams, *Index Numbers and the Standard of Value*, 1902, *passim;* also Caroline Whitney, "Exchange and Price Stabilization," *The American Economic Review*, June, 1932, XXII, No. 2, pp. 231-40. See, on the other hand, such works of Irving Fisher as *The Purchasing Power of Money* (1911), *Stabilizing the Dollar* (1920), *The Money Illusion* (1928).

price of gold and of foreign exchange then current, rather than the price level of 1913 (which too, by the way, was based upon gold), the basis for converting unstable into stable values. As a result of this agitation, the government by a decree of March 30, 1922, repealed all previous legislation that prescribed the use of the "pre-war" index ruble in connection with the calculation of state and local taxes, rates, duties; railway, postal, telegraph, and other charges made by state agencies. These were to be fixed, instead, in Soviet currency.[66]

Concretely, how was the country to compare its price level with that of a gold-standard country?

The best known and most widely used device for that purpose consists of the exchange rate on that country as quoted in gold-standard countries. Such quotations, however, were not available abroad, while the foreign exchange rates as quoted in Soviet Russia could not give desirable results because the supply of and the demand for bills of exchange were controlled by the state, which had a monopoly of foreign trade.

Or, where gold bullion is *freely* traded in on the domestic market of a country, the premium which it commands in terms of paper money may be accepted as a measure of the latter's depreciation.[67] But here again it will be recalled that Soviet Russia had no free market in gold.

Other methods have been proposed for the purpose of making a comparison between the price levels of paper-standard and gold-standard countries. For example, it is maintained that if the wholesale price index of a paper-standard country be multiplied by the quotient obtained through dividing the actual rate of exchange as quoted in a gold-standard country by the old mint par, the paper prices will become converted to a gold basis. Or, that if the old mint par be multiplied by the quotient obtained through dividing the price index of the gold-standard country by that of the paper-standard country, the result will show the extent of the deprecia-

[66] Decree 310. It is not unlikely that the government feared that the employment of such devices might hasten the "flight" from the sovznak.

[67] David Ricardo, *The High Price of Bullion a Proof of the Depreciation of Bank Notes* (1810) and his *Reply to Mr. Bosanquet's Practical Observations on the Report of the Bullion Committee* (1811).

tion of the notes. This latter device had been discussed during the Bullion Controversy, over a century ago, by Wheatley in England, and in recent years was reintroduced by the Swedish economist Gustav Cassel, who named the ratio between the price levels of two countries "purchasing power parity." [68] It is doubtful, however, whether the results of such computations can be regarded as significant inasmuch as they are based upon a norm, in this instance the year 1913, despite the fact that the conditions which helped to determine that norm underwent a drastic change.[69] The so-called purchasing power parity theory is also criticized on account of the assumptions underlying it. The adherents of this theory, it will be noted, assume that, all other things remaining equal, an increase in the volume of currency and deposits leads to a higher price level (on the strength of the quantity theory of money), and this in turn leads to a change in the foreign exchange rates.[70] This causation, however, is denied by the critics, who call attention to the fact that there are instances where exchanges collapse first and where this is *followed* by a rise in the price level, and, finally, by an increase in the volume of means of payment. But, even if it had not a single blemish, this and similar formulae could not yield satisfactory results in Soviet Russia, where the price indices and the rates of exchange were not and could not be as significant as they are in a capitalist country under a regime of free private enterprise.

[68] For an exposition of the above theory, see Cassel's *Money and Foreign Exchange after 1914*, pp. 140 ff. The deviation of the calculated parities from the actual rates is, according to Cassel, "temporary" in its nature. Only a change in the price level can produce a permanent change in the exchange levels.

[69] Lionel D. Edie, *Money, Bank Credit and Prices* (New York, Harper and Brothers, 1928), p. 447.

[70] The market price (or rate) of exchange, however, is determined in the same way as the market price of any commodity or service—by the interaction of its supply and the demand for it. Without denying the above-stated causation, it may be asserted that whether an increase in the volume of currency and deposits in one country will lead to a depreciation of that country's currency on the foreign exchanges may depend upon the relative amount of means of international payment (such as bills of exchange, gold, investments and credits in foreign countries, foreign securities, debts due from foreign countries, etc.) which can be used for the protection of the exchange rate. See Arthur Feiler, "The Pressure for Monetary Depreciation," *Social Research: An International Quarterly of Political and Social Science* (New York, New School for Social Research), February, 1934, p. 67.

And yet it was impossible to compute costs, rates, and other charges without the aid of some such auxiliary device. In fact, the state agencies which, by the decree of March 30, 1922, were directed to discontinue the employment of index numbers in the calculation of taxes, rates, duties, and so forth, in practice, unofficially, continued to derive their figures with the aid of such devices.[71] The Council of People's Commissars sensed the situation and barely a month later, on April 29, decreed the use of a new device as an aid in the computation of costs, rates, payments under contracts, and the like. The new device consisted of the rates at which the State Bank was *buying gold* in the market, and which it was publishing. The law was made retroactive. All executory contracts which were entered into before March 30 of that year (the date on which state agencies were ordered to discontinue the calculation of values with the aid of index numbers) and which were expressed in "pre-war" rubles and payable in sovznaks (i.e. Soviet paper money) in accordance with the rates[72] of the People's Commissariat of Finance, were to be executed in terms of the bank's rate for gold as of the first of the month during which payment fell due.[73]

Just as the previously published rates of the Commissariat of Finance failed to express the real relationship between the price levels of 1921–22 and 1913, so these bank rates failed to express the real relationship between the value of gold and sovznaks in circulation. Even so, the one like the other rendered valuable service by affording some measure of protection against the depreciation of the currency. But whereas the earlier rates of the Commissariat of Finance were being published only once monthly (being intended primarily for use in budget making), the bank's rate for gold was being changed oftener and in that respect possessed an advantage over the old method.

The use of the bank's rates in calculations continued only for a few months. On August 25, 1922, the Council of Labor and Defense decreed a new change.[74] The change consisted in the ap-

[71] Decree 310.
[72] Discontinued in March.
[73] Decree 377.
[74] Decree 692.

pointment of a Special Commission on Quotations consisting of representatives of the People's Commissariats of Finance and of Foreign Trade, and of the State Bank, which was entrusted with the fixing of official rates of foreign exchange, of precious metals, and of gold rubles. The rates of the latter, so the decree specified, were to be in line with the rates of foreign currency, that is, in line with the world value of gold. All of which constituted a *theoretical* victory for those who advocated adherence to an "abstract" gold standard and who believed in the linking of Russian prices with those of countries on the gold standard, even though the country was in the throes of inflation. In *practice,* however, the new rates, although more realistic [75] than those that used to be fixed by the bank, were not in conformity with the world value of gold. The detachment of Soviet Russia from the rest of the world, the very nature of her economic and political set-up, served to make *local conditions* the paramount factor in the determination of those rates. So much so that, despite the legislative enactments, the condemned device—the index number of prices—continued to be used in the computation of those rates.[76] In compliance, however, with the spirit of the law, which required that the rates be related to foreign currencies, the resultant figures would then be corrected for the depreciation of gold since the pre-war years.

It can be seen, therefore, that the index number of prices played an important rôle during those years. Whatever planning the government and the various institutions and business enterprises were able to carry on between the beginning of the New Economic Policy and the introduction of the *chervonetz* (banknote) was in a large measure due to the employment of that device.[77] It was due to it that prices and costs which were expressed in rapidly changing units could be converted into stable units. It made possible not only the calculation of costs but their comparison as well. It served as a guide in the matter of adjusting prices of individual

[75] The bank, it will be noted, when determining the rate for gold was itself guided by the movement of the price level (an index number).

[76] *Economic Life,* May 10, 1922, also Yurovsky, *Currency Problems and Policy of the Soviet Union,* p. 83.

[77] It continued to be used as late as 1924.

commodities and services to the steadily and rapidly rising price level. It proved particularly helpful in enabling the working class to escape the full burden of inflation.[78]

It is thus seen that the index number of prices served as a *measure of value* and as a *standard of deferred payments.* It was cumbersome and inconvenient, but, nevertheless, served the purpose. Inasmuch, however, as the index number of prices is an abstract concept, it could not be employed as a *medium of exchange.* The country needed a stable medium of exchange. The expansion of trade which was made possible by the New Economic Policy could not go on without it. It was doubtless in response to that need that media of exchange other than the paper rubles (sovznaks) increasingly began to find their way into circulation. Especially strong was this movement in the provinces and republics on the borderlines and along the seacoast. In the fall of 1922, for instance, the media of exchange in the Far Eastern provinces consisted of the Japanese yen, which conquered for itself a predominant position, and also of Chinese and prerevolutionary Russian silver coins. In Central Asia Bokhara and Koresm, in addition to using their own paper money, began to use gold coins. Bokhara also minted silver coins. It was not long before gold and silver coins found their way from Bokhara into Turkestan.

Armenia, Georgia, and Azerbaijan in Transcaucasia used no Russian paper money, but printed their own. In Tiflis, however, it was the Turkish lira and the prerevolutionary Russian gold coins that were most important. The latter likewise played a most decisive rôle in Baku. Nor did Batum use Russian paper money to any great extent.

In the Crimea and in Odessa, gold coins began to dislodge paper money. The same phenomenon could be observed in the provinces adjoining Poland, where both Polish and prerevolutionary Russian gold and silver coins were displacing paper rubles.

This movement did not confine itself, however, merely to the

[78] For this latter purpose the use of an index is quite indispensable. If properly administered it tends to prevent a diminution of the real wages paid to workers, which if permitted to go on is sure to lead not only to a grave social injustice and to an undermining of the productivity of labor, but to serious political difficulties as well.

borderline provinces and republics. These places carried on trade with the interior and it was but natural that the use of metallic coins and foreign exchange should likewise spread to other points.[79]

In Petrograd and Moscow, for instance, gold, silver, and foreign exchange were used as a store of value, or, as Sokolnikov wittily observed, as "capitalist insurance against socialist finance." [80] But more than that, in Moscow these began to penetrate into circulation. The national economy, it seemed, was determined in one way or another to break the deadly grip of the paper ruble that was choking it. True, in a country where most important enterprises are government or quasi-government institutions that would not be likely to disobey the law because of the profit motive, the danger of the displacement from circulation of a depreciating currency is not so great as in other countries, where enterprises are privately owned. And yet there were instances when even state enterprises resorted to the actual gold ruble.[81] The government could not afford to overlook such a potential threat to the paper ruble, upon the revenue from which it still depended. Partly because it was apprehensive of this danger and partly because it was convinced that progress was not possible without a stable currency, the government decided to attempt the introduction of a new monetary unit even though the budget could not as yet be balanced.[82] Accordingly it authorized the State Bank to issue banknotes in units that were designated "chervontzy."

The manner in which this was done as well as the success that attended it are discussed in the next chapter.

[79] Contraband trade, too, was responsible for such infiltration.

[80] Sokolnikov, *Monetary Reform* (Moscow, Commissariat of Finance, 1925), pp. 23-24.

[81] *Ibid.*

[82] The importance that Lenin attached at that time to the stabilization of the ruble can be seen from the following statement made by him in November, 1922: "What is really important is the question of the ruble's stabilization. Our best minds are at present concentrated on that problem, and it is to that problem that we ascribe decisive economic importance. Should we succeed in stabilizing the ruble, at first for an extended period of time and later forever, then our victory is assured." Lenin, *loc. cit.*, XVIII, Pt. 2, 91.

VII

THE CHERVONETZ IN 1922–24

The State Bank acquires the right of note issue.—We have seen that when it became evident that under a regime of hyper-inflation the development of credit operations and consequent economic recovery were almost impossible, and, further, when the paper currency was in danger of being boycotted and forced out of circulation, the government instructed the State Bank to issue banknotes.

The first issue of banknotes took place on November 28, 1922.[1] The decree that was responsible for that issue was signed by the Council of People's Commissars on October 11, 1922.[2] That decree, however, was an almost exact repetition of a decree that had been issued by the same body on July 25[3] but upon which no action had been taken. The reason for withholding the right of note issue from the bank at the time of its organization in 1921 explained why no action had been taken by the bank under the July decree. The hesitancy in both cases was due to the conviction that a new type of currency ought not to be introduced while the budget was unbalanced and while the government depended upon the issue of paper money for revenue. The risk of bringing forth a new type of currency under those conditions and at a time when the public had little or no confidence in the issuer's ability to maintain its stability was great. Should the attempt prove abortive and the new currency become discredited, future efforts would encounter greater difficulties. Therefore, it was felt that the right of note issue should not be used unless absolutely essential. The temporary halt in the ruble's depreciation during the summer months of 1922 engendered false hopes. In the fall, however, when the decline of the ruble's purchasing power became marked, the

[1] "The Jubilee of the Chervonetz," *Finance and National Economy*, No. 48 (56), November 27, 1927, p. 1.

[2] *Collected Decrees*, 1922, Decree 827.

[3] Decree 578. According to the decree of July 25, however, the banknotes were to be issued in units of 10, 25, 50, and 100 chervontzy, while according to the October 11 decree they were to be issued in units of 1, 2, 3, 5, 10, 25 and 50 chervontzy.

situation was quite different and it was felt that it was no longer safe to postpone a monetary reform. Hence, the decree of October 11 was issued at a time when the budget was still unbalanced, the balance of foreign trade still unfavorable, and the productive forces within the country, although showing a slight improvement, still at a low ebb.[4]

The purpose of that decree, as stated in its preamble, was to grant the bank the right to issue notes of its own so as to augment its resources, make possible an expansion of its commercial operations (without increasing treasury note issues on that account), and enable it to regulate the circulation of currency. By the terms of this decree the bank was also permitted to use its right of note issue to extend loans to the Commissariat of Finance (that is, to the treasury).[5] These latter loans were to be secured by

[4] Several other solutions (besides the issuance of banknotes) to the problem of how to procure a stable currency under such conditions, were suggested to the government. Of these, one called for the establishment within the country of a foreign bank of issue. It was maintained that its notes, secured by gold on deposit in foreign banks would command respect. Although the scheme specified that a certain portion of the issue be turned over to the Soviet government, the latter rejected it, because it feared that such notes would displace Soviet paper currency, and that it would render the government dependent upon a foreign institution. Besides it was believed that such an institution would have ulterior motives. For similar reasons the government rejected an offer from abroad to extend to its railroads a large loan, provided it gave those railroads permission to issue currency and the lenders the right to regulate such issue. Sokolnikov, *Financial Policy of the Revolution,* I, 120-21.

[5] Shortly after the decree of October 11 had been published, the Commissariat of Finance issued a special *Nakaz* (of October 19) to the bank in which it defined with greater clearness the purposes for which banknotes may be issued. The two broad purposes laid down by the October 11 decree—to wit, to strengthen the bank's working capital that was to be employed in connection with its commercial operations, and to grant short-term loans to the Commissariat of Finance—remained, of course, inviolate. In so far as the first category, that is, commercial operations, was concerned, the Nakaz stated that banknotes may be issued for the following purposes:

(a) To enable the bank to buy and sell (for its own account) gold and precious metals in the form of bullion or coin, Soviet and foreign currency, foreign bills of exchange, and also securities.

(b) To grant time and demand loans for a period not exceeding six months against the security of such items as mentioned in (a) and against commodities and commercial documents (invoices, bills of lading, and so forth).

(c) Discount of commercial paper that is based upon commercial transactions, that has not less than two signatures, and that matures within six months. See S. L. Pevzner and I. B. Drisin (compilers), *Banking Affairs: a Manual for Bankers* (Kharkov, The Ukrainian Commissariat of Jurisprudence, 1927), II, 208.

50 percent in precious metals and 50 percent in interest-bearing treasury obligations.[6]

The notes were to be issued in units of 1, 2, 3, 5, 10, 25, and 50 chervontzy, one chervonetz being equal to ten rubles of the former Russian coinage (that is, to one zolotnik and 78.24 dolias, or to 119.4792 grains of fine gold).[7] They were to be fully secured: by precious metals and stable foreign currency, equal to not less than 25 percent of their amount outstanding; the balance of the security was to consist of easily marketable goods, short-term bills, and other short-term obligations.[8] The notes were not convertible but the decree states that the date upon which convertibility might begin was to be fixed by a special act of the government.[9]

Although not specifically legal tender, they were to be accepted, according to their face value, in payment of all sums due to or charged by the state (such as customs, taxes, railway charges, and so forth) in all cases where payments by law had to be effected in gold.[10] Besides, a market for them was created by that provision in

[6] Decree 827, Article 8.

[7] *Op. cit.*, Article 2. *Chervonetz* is singular; *chervontzy* is plural. The word *chervonetz* is not of recent origin. We are told that "from the time of Ivan the Terrible there developed the custom of distributing medals for distinguished military service, and that at first foreign gold coins . . . were used for that purpose (these were fastened to one's hat or sleeve), and later imitations of *chervontzy, the minting of which began in Moscow.* There are chervontzy that were minted by Feodor Joannovich, Boris Godunov, Vasili Shuisky, and others. . . ." The chervontzy of that period had no nominal price, however, and could hardly be regarded as coins in the real sense of that word. It would be more proper to date their functioning as coins from 1730, in which year their weight and fineness were fixed by a ukase. The weight of a chervonetz was set at 78 6/59 dolias of which 75 39/59 dolias were to be pure gold. Their nominal value then was 2 rubles 20 copecks. Their fineness and nominal prices, however, underwent changes in later years.—I. I. Kaufman, *The Silver Ruble in Russia from Its Beginning to the End of the XIX Century* (St. Petersburg, 1910), pp. 129, 130, 156 ff. Historically, therefore, the ruble is older, for it dates from the XIV century.

[8] Article 3.

[9] Article 5. Soviet Russia did not set a precedent for inconvertible banknotes *ab initio*. The Austro-Hungarian Bank, for instance, had been freed from the obligation of redeeming its notes from the very date of its organization in 1878. Max Sokal and Otto Rosenberg, "The Banking System of Austria" in *Foreign Banking Systems*, H. Parker Willis and B. H. Beckhart, editors, pp. 101-2.

[10] Decree 827, Article 6. By order of the People's Commissariat of Finance, dated February 3, 1923, banknotes were made acceptable not only in payment of all state taxes and duties, but of local taxes and rates as well, hence, in cases where payments were generally being effected in Soviet paper money.—*The State Bank of the U.S.S.R., 1922–25*, p. 16.

the decree which empowered the bank to demand that all credits which were granted or expressed by it in banknotes be repaid in that currency.

An analysis of the October decree.—As stated in the above provisions of the decree, 25 percent of the security behind the banknotes was to consist of *precious metals.* Silver, therefore, could be included in the metallic reserve. The decree, however, does not specify what proportion of the metallic reserve may consist of silver.[11] Still the Soviet Union is one of the world's leading gold producers. This, together with the appreciation by the Soviet government of the advantage of maintaining a sizable gold reserve, can be relied upon to prevent the inclusion in the bank's reserve of a disproportionate amount of silver.

A question may be raised as to whether a 25 percent metallic cover can be considered adequate reserve, especially when it is borne in mind that no legal reserve is required for the bank deposits, and that strong efforts were being made from the very beginning to develop the latter type of bank credit. Other important countries require proportionately larger reserves.[12] There are reasons, nevertheless, why a country like the Soviet Union does not have to imitate such practice. Demands for gold arising out of panics cannot possibly occur in a country where the banks are in the hands of the state and where an increasingly important number of holders of bank credit (notes and deposits) belong to the so-called *socialized sector* which is not likely to do anything of

[11] Since the days when the silver and bimetallic standards were given up, the holding of silver as security against notes has not been large. The Bank of England, for instance, between the years 1861 and 1928 made no use whatsoever of the right to use silver as security against notes. It was only in 1928, when the treasury and banknote issues were amalgamated, that the Bank of England made use of its right and had included a limited amount of silver in its metallic cover.

In the case of the Bank of Poland, the Bank of Spain, and the Bank of Japan (countries the statutes of which permit the inclusion of silver in the metallic reserve against notes), the amount is strictly limited.—Sir Cecil H. Kisch and W. A. Elkin, *Central Banks: a Study of the Constitutions of Banks of Issue, with an Analysis of Representative Charters* (London, Macmillan and Co., 1932), pp. 93, 330, 376, 412.

[12] On June 27, 1933, however, a subcommittee (the committee on gold) of the World Economic Conference declared itself in favor of restricting central bank gold coverage to a 25 percent maximum. It also favored the withdrawal of gold from general circulation.—The *New York Times,* June 28, 1933.

which the state does not approve. In such a country the question of metallic reserves and of liquidity of bank assets cannot be said to be so important as in capitalist countries. Besides, the Soviet Union maintains no gold in circulation, and the banknotes themselves are inconvertible.

Furthermore, the communist philosophy places greater reliance on planning and management than in automatic control. If so, one may ask why a gold reserve had been set up at all, and, in fact, why the chervonetz had been tied to gold? If, under a capitalist economy, gold is expected to serve as an "automatic" safety device which performs the work of brakes in the complicated credit machine and which keeps the domestic price level in line with that of other nations,[13] it certainly can neither be expected nor desired to perform the same service under a planned national economy, in part because in the latter prices are regulated by governmental agencies and in part because it would render economic planning difficult, if not impossible, if those prices were to be made dependent upon international prices. Besides, what makes it possible for gold to bring about a harmony of price levels is the fact that when prices of one country are lower or higher than world prices (by more than what it would cost that country, figuring freight, insurance, tariff, and other charges, to place commodities for sale in other countries or for other countries to sell in that country), a consequent increase in exports or in imports, as the case may be, will set in motion forces that will tend to bring those prices into international equilibrium. Under the Soviet planned economy, however, imports and exports are regulated by plan and the government has a monopoly of foreign trade and of foreign exchange.[14] "Automatic" adjustment has no place in such economy. The difference between the service that gold can render in this

[13] Professor Schumpeter speaks of it as being a brake that is applied to the credit machine. See his article "Die goldene Bremse an der Kreditmaschine (die Goldwährung und der Bankkredit)," Fritz Beckmann et al. *Die Kredit-wirtschaft* (Leipzig, 1927), Pt. 1, pp. 80-106.

[14] For the advantages of planning foreign trade, see G. D. H. Cole, "Planning International Trade," *International Conciliation* (Carnegie Endowment for International Peace, April, 1934), No. 299, pp. 104-16, or *Foreign Affairs*, XII, No. 2, January, 1934.

respect under a capitalist and under a soviet economy is, it should be observed, one of degree rather than of kind. For even under a capitalist economy the gold standard is incapable of bringing an equilibrium in international prices when its work is hampered by protective tariffs, restrictive quotas, exchange control, and the like.[15]

But the work of the gold reserve and of the gold standard is not restricted to this one function. It may be readily seen that gold can be utilized for the purpose of regulating foreign exchange, settling unfavorable balances of international payments, in case of war, and for other emergencies (famine, and so forth).

Not among its least important uses was the confidence which it was expected to engender at home and abroad towards the bank and the chervonetz (among other things it was hoped that the tying of the chervonetz to gold would help to win for it recognition in international exchange). There were at play also other important forces which were instrumental in influencing the decision to set up a gold reserve and to link the banknote to a given weight of gold. Imitation had its part here too. It is no mere coincidence that much of the early banking and currency practice in Soviet Russia resembled the practices of such institutions as the old Russian State Bank, the Bank of England, and the Reichsbank. Furthermore, when the re-establishment of banking and currency was taking place there existed, it must be remembered, no such thing as a detailed set of ready principles for the guidance of banking practice and currency circulation under a regime which was neither socialistic nor capitalistic, but which was a peculiar combination of both. Those who wanted counsel on currency matters could turn either to Marx, or else to the works of nonsocialistic writers. Paradoxical as it may seem, those who turned to Marx's *Capital* (which, it will be recalled, is a study of the economic system of a *capitalist* society) and those who relied upon nonsocialistic authorities carried away with them the same impression, namely, that gold constituted a vital part of the country's monetary

[15] For a discussion of exchange control and its effect, see Charles R. Whittlesey, "Exchange Control," *The American Economic Review* (December, 1932), XXII, No. 4, 585-604.

system,[16] a circumstance that could not fail to produce a most profound effect upon the shaping of the Soviet monetary policy.

Thus far we have dealt with the metallic reserve only. Let us now turn to the remaining 75 percent of the security against notes, or, to the bank cover, keeping in mind, however, what has been said above about the relative importance of bank liquidity in a soviet and in a capitalist country.

The bank cover, as we have stated, was to consist of easily marketable goods, short-term bills, and of other short-term obligations. The objections that are generally raised against commodities as security underlying bank credit (of which the banknote is but one form) have already been discussed and need not be repeated here. The bank, in fact, not only lent credit against commodities, but also sold and bought such commodities.

With respect to the remainder of the bank cover, it may be said that the inclusion of short-term bills as security against banknotes meets with universal approval, provided, of course, that they are bona fide short-term bills, that is, that they are given in connection with commercial rather than investment credit and that their

[16] The position that Marx takes with respect to gold in a monetary system may be inferred from the following of his statements:

"The chief function of money is to supply commodities with the material for the expression of their values, or to represent their values as magnitudes of the same denomination, qualitatively equal, and quantitatively comparable. It thus serves as a *universal measure of value*. And only by virtue of this function does gold, the equivalent commodity *par excellence*, become money."

"It is not money that renders commodities commensurable. Just the contrary; it is because all commodities, as values, are realized human labor, and therefore commensurable, that their values can be measured by one and the same special commodity . . ." (p. 106).

Again (p. 144): "Paper-money is a token representing gold or money. The relation between it and the values of commodities is this, that the latter are ideally expressed in the same quantities of gold that are symbolically represented by the paper. Only in so far as paper money represents gold, which like all other commodities has value, is it a symbol of value . . ."

"If the paper money exceed its proper limit, which is the amount of gold coins of the like denomination that can actually be current, it would, apart from falling into general disrepute, represent only that quantity of gold, which is required . . . If the quantity of paper money issued be double what it ought to be, then . . . £1 would be the money name, not of ¼ of an ounce, but of ⅛ of an ounce of gold . . ."

Of course, this applies to inconvertible paper money issued by a state. But then as to banknotes, Marx says: "money based upon credit implies on the other hand conditions which from our standpoint of the simple circulation of commodities are as yet totally unknown to us . . ."—*Capital*, I, 143.

maturities coincide with the time required for the consummation of the respective transactions. In the last analysis, it is the "goodness" of the underlying transactions that is wanted. If those transactions are of the commercial, so-called "self-liquidating" type, no better security could be desired. The commercial paper merely serves to evidence the transaction. (It is worthy of mention that the banknote may be, in a sense, regarded as commercial paper of the highest order that businessmen find advantageous to substitute for their own less known paper.)

The bank, however, was authorized to include in its bank cover not only short-term bills, but "other short-term obligations" as well. Since the bank was authorized to extend to the treasury loans that were secured to the extent of one-half by "interest-bearing treasury obligations" (the other half of the security consisting of precious metals), it may be assumed that "other short-term obligations" included treasury bills. The practice of including treasury obligations as a basis for note issue is commonly considered to be fraught with danger. The state, despite the fact that it owns the bank, and therefore could be said to be entitled to "borrow" from it, placed a limitation upon the amount of loans that the latter might advance to the treasury by requiring that one-half of the security against such loans consist of precious metals. A more direct limitation upon the amount of treasury bills was placed by the People's Commissariat of Finance, that is, by the treasury itself, when it ruled (in its Nakaz of October 19, 1922) that at least two-thirds of the bank cover must consist of commercial bills.[17] In this respect, then, the Soviet state followed the practice to which other countries resort,[18] the purpose of which is to proclaim to the nation and the world that the state means to safeguard its central

[17] Pevzner and Drisin, *op cit.*, II, 209, Article 6.

[18] Kisch and Elkin, *op. cit.*, pp. 35-37. In Germany, for instance, the Reichsbank was authorized to grant such loans to the state, provided they were for a short period of time and did not exceed a certain limit. No such loans were to be outstanding at the end of the fiscal year. In Holland such loans are limited to 15,000,000 gulden. In Esthonia they are not to exceed one-sixth of the estimated state revenue of the year and are to be repaid not later than at the end of the quarter following the close of that fiscal year. Restrictions upon loans to the treasury are also found in the statutes of the central banks of Bulgaria, Czechoslovakia, and of some other countries.

bank from becoming a mere adjunct to the treasury, and thus to remove one of the important causes of note overexpansion. Of course, such provisions are to be regarded more as declarations of principles, as acknowledgments of the fact that the state is aware of the danger that will follow when it abuses its right to borrow from the bank and that it means to guard against it, than as a promise not to set aside such limitations when a real emergency arises. Rarely does a state violate such provisions in normal times, and equally rarely does it observe them in times of stress.

Thus, the new State Bank was required to observe a number of limitations that are generally employed by countries for the purpose of guarding against an overissue of banknotes. In at least one important respect these limitations differed from similar limitations that other countries impose upon their central banks. They lacked the provision for the redemption by the State Bank of its notes. Redemption or convertibility is acknowledged in capitalist countries as one of the recognized mainstays for protection against an overexpansion of note issue. It had been left out of the statutes of the State Bank, of course, for no other reason than that the gold reserve was too small, and the general situation was such that even a much larger reserve would not have enabled the country to continue the payment of specie for any length of time. Irrespective, however, of what one may think of the part played by redemption in securing a sound and stable currency in other countries and of the consequent advisability of maintaining gold in circulation there, one is likely to agree that in the Soviet Union, where economic life is planned and strictly regulated, such devices are not essential. The planning of economic life in general and of credit and public finance in particular there take the place of "automatic" devices for control. Planning, to be sure, has not the power of a magic wand. Much depends upon the ability and willingness of those who plan to differentiate between commercial and investment credit and to confine the issue of notes and the creation of deposits to the former.[19] A balance must be maintained between

[19] In practice it is by no means easy to differentiate between commercial and investment operations. Take, for instance, the following cases upon which the Federal Reserve Board of the United States rendered its ruling: a corporation furnishing motor transportation borrowed funds for the purpose of purchasing motor

the rate of saving and the value of new capital investments if credit inflation is to be avoided.[20]

That the banknotes were not endowed with legal tender status was due to the fact that it was important to reserve that privilege for the treasury ruble (sovznak) which was being issued for fiscal purposes. Owing to the same reason the lowest banknote unit—one chervonetz—was made to equal ten imperial gold rubles, a rather high denomination. It was being argued at the time that in other European countries, where the standard of living and the per capita national income were in nowise lower than in Russia, marks, francs, and similar currency of low denomination constituted the monetary unit, and even in England it was the shilling rather than the pound that the majority of people found convenient to use. It is clear, however, that the government had no choice in the matter. Inasmuch as it was not as yet able to balance its budget, it could ill afford to set up competition for the sovznaks. It was only in 1924 that it succeeded in furnishing a stable currency of a low denomination. Besides it must not be forgotten that *banknotes* are not supposed to be issued in small denominations; the reason being that notes of a smaller denomination have a tendency to remain in circulation; while those of a higher denomination tend to return to the banks as soon as their function is completed.

Early difficulties.—It has been stated that the chervonetz (ten rubles) was too high a monetary unit for a country so poor at the time. Even so, the number of notes in circulation of the denomination of one chervonetz was very small indeed during the early period of its existence. On January 1, 1923, e.g., these constituted but 1.3 percent of the total value of chervontzy in circulation. The bulk was made up of five-chervontzy (50 rubles) notes (53.7 per-

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trucks, giving in acknowledgment of the debt its promissory note. It was held by the Board that such notes did not constitute commercial paper (to the corporation in question the trucks constituted a fixed investment). When, however, such notes are given by the transportation company to the producer or seller of those trucks, the paper in the hands of the latter as if by magic is converted into commercial paper and becomes eligible for rediscounting. See H. Parker Willis and William H. Steiner, *Federal Reserve Banking Practice* (New York, D. Appleton and Co., 1926), Bankers' Edition, p. 155.

[20] See John Maynard Keynes, *Treatise on Money* (Harcourt, Brace and Co., 1930), II, 220.

cent) and ten-chervontzy (100 rubles) notes (44.7 percent). The balance (.3 percent) consisted of three-chervontzy notes. Apparently the peasantry, the most numerous class of the population, could not very well avail itself of these banknotes and so escape the burden of depreciation entailed by the use of the Soviet rubles. The government, however, was far from being anxious that the chervonetz meet the requirements of the entire economy. Indeed, as we have seen, it was apprehensive all the time lest a better currency cause the displacement of the treasury notes (sovznaks) from circulation, thereby destroying its important source of revenue. Nevertheless, it is not at all certain that the natural conservatism of the peasantry, which expressed itself in a mistrust of a new Soviet currency, would not operate in the same direction even though the denominations of the chervontzy were much smaller. At any rate infiltration of the banknotes into circulation, as shown by Table 21, proceeded at first very slowly.

Of the 1,118,000 chervontzy that had been transferred by the issue department of the bank to the banking department on January 1, 1923, only 356,250 chervontzy, that is, slightly less than one-third, had been absorbed in circulation. By March 1 the amount of banknotes in circulation, although they had undergone an absolute and relative increase, still amounted to only a trifle more than one-half of the total banknotes transferred to the banking department. Meager as these results appear, it nevertheless required very strong stimulative measures to produce them. With some of these measures, such as the authorization given to the bank to demand that loans granted by it in chervontzy be repaid in the same currency, or the instruction of the Commissariat of Finance to its local offices to accept chervontzy in payment of all taxes and charges, we are already familiar. In addition to these, pressure was being brought to bear upon the clients of the bank in order to induce them to pay a part of the workers' wages in chervontzy and otherwise to use banknotes for the purpose of effecting payments.

Notwithstanding these efforts, it could hardly be said that the banknotes during this early period served as a medium of exchange. Their chief use was rather as a store of value. When not so used their holders would present them at the bank to be exchanged

TABLE 21

THE PENETRATION OF BANKNOTES INTO CIRCULATION

(*In chervontzy of ten rubles each*)

Date (First of the Month)	*Amount of Chervontzy*			
	Transferred to the Main Office (Banking Department) of the State Bank [a]	In Actual Circulation [b]	Ratio (%) Between the Amount of Notes in Actual Circulation and the Amount Transferred to the Banking Department	Monthly Increase in the Amount of Chervontzy in Actual Circulation
1923				
January	1,118,000	356,250	31.9	498,340
February	1,930,000	854,590	44.3	749,390
March	3,000,000	1,603,980	53.5	962,710
April	4,500,000	2,566,690	57.0	1,187,490
May	6,000,000	3,754,180	62.6	994,170
June	8,000,000	4,748,350	59.3	2,251,790
July	9,600,000	7,000,140	72.9	4,120,340
August	13,500,000	11,120,480	82.4	5,295,310
September	18,400,000	16,415,790	89.2	4,320,160
October	23,500,000	20,635,950	88.2	1,742,290
November	25,450,000	22,478,240	88.3	123,100
December	26,776,000	22,601,340	84.4	1,114,550
1924				
January	28,000,000	23,715,890	84.7	2,203,750
March	32,800,000	28,688,350	87.5	2,768,710 [c]

[a] The issue department of the bank, apparently in emulation of English practice, was organized by order of the Commissariat of Finance on October 19, 1922 (in the *Nakaz* to which reference has already been made). The figures in this column were taken from *Our Monetary Circulation*, p. 131.

[b] It is possible that these figures are not quite exact. *Ibid.*, p. 138.

[c] For the month of February.

for Soviet rubles, which could be then used to pay the workers' wages and the peasantry (who for some time did not accept any chervontzy) for whatever was bought from them. Little by little, however, the use of chervontzy as a medium of exchange increased, and by July 1, 1923, almost three-quarters of the steadily increasing amount of banknotes transferred to the banking department remained in circulation. By the beginning of September that figure reached almost 90 percent. At this latter time their use as a medium of exchange extended from the large centers into the villages. Among the factors which aided that process were the growing confidence in the new currency, the quickening of the depreciation of the sovznak and hence the flight to a better currency, as well as the appreciable increase in the proportion of the one-chervonetz notes from the low of 1.3 percent of the total value of chervontzy in circulation on January 1, 1923, to 16.7 percent on April 1, to almost 24 percent on September 1, and to 30 percent by the end of 1923.[21]

The security behind the chervontzy.—Despite the rapidly expanding volume of banknotes in circulation, the State Bank was careful to comply with the reserve requirements. Apparently, the goal that it had set for itself was much higher than the legal minimum (25 percent) prescribed for it. This can be seen from the fact that between the time when the banknotes were first issued and until some months after the Monetary Reform of 1924 had been completed, the firm cover (stable foreign currency included) was close to 50 percent—a record which the bank was either unwilling or unable to maintain in the later years. Table 22 shows the composition of that reserve.

The purchasing power of the chervonetz in terms of foreign exchange and gold.—Irredeemability of the currency, which proved helpful in enabling the bank to maintain as security behind the chervontzy an amount of precious metals and claims to them in excess of the minimum reserve prescribed by law, at the same time prevented that reserve from being useful in the capacity of an automatic regulator of the purchasing power of the chervontzy. The Commissariat of Finance and the State Bank made,

[21] *Our Monetary Circulation*, p. 136.

TABLE 22

THE STATE BANK OF THE U.S.S.R.

FIRM AND BANK COVER 1922–24 [a]

(In thousands of chervontzy and percent of total cover)

Date	*Gold Bullion and Coin*	*% of Total (Firm and Bank) Cover*	*Silver Bullion and Coin*	*% of Total Cover*	*Platinum (Bullion)*	*% of Total Cover*	*Foreign Currency*	*% of Total Cover*	*Foreign Bills of Exchange*	*% of Total Cover*	*Discounted Commercial Paper*	*% of Total Cover*	*Other Secured Obligations*	*% of Total Cover*	*Total (Firm and Bank) Cover*	*Total %*
November 28, 1922.	406.5	79.0	....	....	....	..	108 1	21.0	..	....	..	....	....	.. .	514.6	100
January 1, 1923..	506.5	33.7	....	....	....	. .	586.1	39 0	410 1	27.3	. .	....	....	....	1,502 7	100
April 1...	2,710.9	53.4	....	....	....	..	78 7	1.5	304 6	6.0	830 3	16.4	1,139.6	22.7	5,064.1	100
July 1....	4,959.1	46.0	62.7	0.6	....	..	291.5	2.7	438 3	4.1	2,309.5	21 5	2,700.0	25.1	10,761.1	100
October 1.	8,486.4	35.7	73.0	0.3	....	.	3,407.9	14.4	522 6	2.2	6,995.4	29.4	4,269.3	18.0	23,764.6	100
January 1, 1924..	8,753.2	31.2	110 6	0.4	....	. .	5,485.0	19.5	445.9	1.6	6,719.7	23.9	6,571.9	23.4	28,086.3	100
July 1....	9,269.3	23.0	110.6	0.3	742.7	1.8	10,007.2	24 9	342 6	0.9	13,782.7	35.0	5,994.9	14.1	40,250.0	100
January 1, 1925..	14,195.5	23.7	....	....	1,298.4	2.2	9,867 0	16 6	375.6	0 6	29,142 7	48 8	4,870.8	8.1	59,750.0	100

[a] Based on the figures given in *Our Monetary Circulation*, pp. 131-34.

It should be noticed that the percentages were calculated with respect to the "total firm and bank cover." The "total firm and bank cover," however, exceeded "the amount of chervontzy transferred to the Main Office (banking department)" and these in turn exceeded "the amount of chervontzy in actual circulation." If taken with respect to "the amount of chervontzy in actual circulation," the firm cover as a percentage would be appreciably higher.

nevertheless, full use of whatever services such reserves are able to render when managed. They could be used, among other things, for the purpose of intervening in the market so as to stabilize the purchasing power of the chervonetz either at a certain level or, if this proved impossible, then to prevent its fall to the low points that it might reach when unaided.

Under the conditions then prevailing these reserves lent themselves more readily to influencing the purchasing power of the banknotes in terms of foreign exchange and gold than in terms of everyday commodities. The reason for this is not difficult to see. Possessing supplies of gold and foreign exchange which could be offered in exchange for chervontzy at predetermined rates and aided by special legislation, the nature of which is explained in what follows, the bank could not fail to score a victory over rates and prices of foreign exchange and gold in the domestic market. This procedure, however, could hardly be used to affect the general price level, for the supply of gold and foreign exchange was not large enough to make possible, in the absence of loans, a running policy of large-scale purchasing of consumers' goods abroad so as to increase the volume of goods offered within the country. The government, therefore, could not very well influence commodity prices from this side.[22]

Again, having decided that it was essential to build up Russia's industries speedily, even though savings at home were practically nonexistent and foreign loans unobtainable, the authorities could not very well curtail the issue of banknotes to a larger extent than they did. Without, however, a sufficient increase of the supply of consumers' goods or an adequate diminution of the volume of banknotes in circulation, it was impossible to stabilize at a high level the purchasing power of chervontzy in terms of commodities. The government, of course, could fix prices but, in view of the high costs of production, this had to be done with discretion in the socialized sector, and, in view of the phenomenal shortage of goods, its use in the private sector (mostly retail trade) threatened to make bad matters worse.

[22] To be sure the government did buy consumers' goods abroad. The quantity so bought was, however, too negligible a factor to influence prices.

Since it was impossible to stabilize at a high level the purchasing power of the chervonetz in terms of commodities, the bank concentrated its efforts on the attempt to stabilize it in terms of foreign exchange. As a result, the index showing the banknotes' depreciation in terms of commodities is not as favorable as that showing its depreciation in terms of foreign exchange and gold. Let us first take up the banknotes' depreciation in terms of foreign exchange and gold.

As shown by Table 23, the rate of dollars in terms of chervontzy-rubles approached parity in March and April, 1923. The pound sterling, however, the purchasing power of which had declined in those days at home and on the various foreign exchanges, was being quoted below its par. In May, when the volume of banknotes in circulation underwent a too rapid increase, and when political relations with England had become tense, the rates of the dollar and other foreign currencies had risen to the highest point for the period. The relative stabilization of the rates of foreign currencies that is observable from the middle of 1923 was interrupted by a new advance and, therefore, improvement of their rates of exchange in the closing months of 1923 and in the beginning of 1924. In April, 1924, that is, after the Monetary Reform had been concluded, dollars began to be quoted at parity of exchange. This policy was not followed with respect to the pound sterling, which by that time underwent a further depreciation at home and on the world exchanges.

The depreciation of chervontzy in terms of gold was not proportionate to their depreciation in terms of foreign currency, partly because (in view of the illegality) the demand for gold coin was not too great and the government's resources were quite sufficient for that purpose, and partly because the government, knowing who the speculators were, could compel them to exchange their hoards for paper money.

Gold coins commanded a higher price than the same amount of gold in the form of bullion. That was, of course, because the demand for them was relatively higher in respect to their supply than the demand for bullion in respect to its supply. This preference was undoubtedly due to the fact that gold as money

TABLE 23

RATES ON DOLLARS, STERLING AND GOLD COIN IN CHERVONETZ-RUBLES [a]

Date	*Dollars* (*The then Par = 1.943 Rubles per Dollar*)		*Sterling* (*The then Par = 9.458 Rubles per Pound*)		*Ten-Ruble Gold Piece* (*"Free" Market*)
	Official Quotation [b]	"Free" Market (Moscow)	Official Quotation [b]	"Free" Market (Moscow)	
1923					
January 1	....	2.57	....	11.83	13.37
February 1	2.08 [c]	2.39	9.38 [c]	10.62	12.68
March 1	1.92	1.93	8.85	8.88	11.54
April 1	1.92	1.90	8.56	8.89	13.38
May 1	2.23	2.39	9.67	10.20	15.54
June 1	2.59	2.77	11.38	11.53	17.33
July 1	2.14	2.13	9.80	9.88	14.66
August 1	2.11	2.12	9.65	9.87	13.91
September 1	2.07	2.07	9.51	9.59	12.23
October 1	2.05	2.07	9.39	9.41	12.81
November 1	2.06	2.20	9.15	9.48	13.65
December 1	2.18	2.20	9.47	9.40	13.49
1924					
January 1	2.20	2.23	9.40	9.44	13.85
February 1	2.17	2.19	9.24	9.35	14.10
March 1	2.11	2.11	9.07	9.12	12.80
April 1	1.945	1.91	8.36	8.10	10.65
May 1	1.945	1.95	8.52	8.52	10.60
June 1	1.944	1.90	8.38	8.35	9.90
July 1	1.945	1.94	8.41	8.40	9.48

TABLE 23—*Continued*

RATES ON DOLLARS, STERLING, AND GOLD COIN IN CHERVONETZ-RUBLES [a]

Date	*Dollars (The then Par = 1.943 Rubles per Dollar)*		*Sterling (The then Par = 9.458 Rubles per Pound)*		*Ten-Ruble Gold Piece ("Free" Market)*
	Official Quotation [b]	"Free" Market (Moscow)	Official Quotation [b]	"Free" Market (Moscow)	
1924					
August 1	1.945	1.94	8.55	8.54	10.20
September 1	1.945	1.94	8.73	8.70	9.80
October 1	1.945	1.95	8.67	8.65	9.60
November 1	1.945	1.94	8.79	8.78	9.55
December 1	1.945	1.94	8.98	8.99	9.60

[a] *Our Monetary Circulation*, pp. 222-23, for official quotations; *The Economic Bulletin of the Institute for the Study of Economic Conditions*, 1925, No. 1, pp. 4-5, for "free" market and gold quotations.

[b] The official quotations are those of the Securities Department of the Moscow Produce Exchange. The Securities Department was opened for the first time (under the Soviet government) on February 15, 1923. It will be recalled, that the stock exchanges in Russia were closed in July, 1914, and that official rates of foreign exchange were introduced on January 25, 1916, by a special department at the Credit Chancellery of the Ministry of Finance. Under the Provisional government the Petrograd Bourse, although open for some time, did not quote foreign-exchange rates. The produce exchanges together with their securities departments were abolished in 1930 (Decree 120). In the same year there was established at the Main Office of the State Bank a Quotations Commission which fixes the rates of foreign exchange as well as bond prices. Up to December 1, 1923, the Securities Department of the Moscow Produce Exchange quoted foreign exchange in Soviet rubles; after that in chervonetz-rubles. All of the above figures are expressed in chervonetz-rubles.

[c] February 15.

performs its functions best within a country when in the form of coins, and since such coins were no longer minted they were bound to command a premium.

In the last analysis, the price of foreign exchange and gold in the Soviet Union during those years, as before, was being determined by the interaction of their supply and the demand for them. In that respect the Soviet Union in nowise differed from other countries. But the conditions influencing the supply of,

and the demand for, foreign media of payments and gold in the Soviet Union were seldom if ever encountered in peacetime elsewhere. The isolation of the Russian market from world markets, as has been explained, destroyed, *inter alia,* the fine interdependence between rates and prices of foreign media of payment and gold in the Soviet Union and abroad. This in itself served to give local conditions of supply and demand a greater weight than they otherwise would have had, and made the manipulation of rates and prices far simpler. The monopoly of trade that the state had retained made it possible furthermore to plan the country's imports and exports, and, therefore, the supply of, and the demand for, foreign exchange and gold for legitimate purposes. Moreover, by legal enactments the government made possible the "management" of foreign exchange by the State Bank. It is to these acts that we shall now turn.

The first act of importance is that of October 20, 1922.[23] Under this act the Council of People's Commissars gave the Council of Labor and Defense authority to organize, upon the recommendation of the People's Commissariat of Finance, securities exchanges, and, upon the joint recommendation of the latter and that of the Commissariat of Commerce, securities branches at the produce exchanges. The securities exchanges and branches were permitted to deal in (a) foreign media of payment, (b) banknotes, (c) government bonds approved by the Soviet government, (d) stocks and shares of joint-stock companies and the like, the statutes of which were approved by the Soviet government, and finally (e) precious metals in bullion. It should be noticed that this act did not authorize the purchase and sale of imperial gold coins. In

[23] Decree 858; also D. A. Loevetzky, *Valuta Policy of the U.S.S.R.* (Moscow, Commissariat of Finance, 1926), pp. 23 ff. By an earlier act of April 4, 1922 (Decree 318) the Council of People's Commissars repealed those provisions of the earlier decrees which required the surrender of all precious metals—whether in coin, bullion, or in the form of articles—as well as of precious stones and of foreign exchange, to the government. Moreover, by the act of April 4, 1922, it became legal to buy and sell precious metals in the form of bullion and articles as well as precious stones. The State Bank, at the same time, was given the monopoly of trade in gold, silver, and platinum coins and in foreign exchange. It was also authorized to receive deposits in gold and silver in coin and bullion, and in foreign media of payments subject to repayment of the principal in the same metal or foreign currency, while the interest was to be paid in Soviet currency. See Loevetzky, *op. cit.,* p. 20.

fact, by a later act, of February 15, 1923, the government specifically forbade the giving and receiving of such gold coins in any kind of payment.[24]

The latter act likewise forbade the making and receipt of payment in foreign media of exchange, except in the case of transactions necessarily involving foreign currencies. The object of these provisions undoubtedly was to secure for Soviet currency, and particularly for the chervontzy, exclusive right to serve as a medium of exchange within the country. The act of February 14, however, did not stop there. It further directed all state and co-operative establishments to place on deposit with the State Bank or other credit institutions whatever foreign media of payment they happened to have within the country.[25] Nor were private persons and enterprises wholly free from this requirement. The State Bank was endowed with the right of a preferential buyer of all foreign exchange received as a result of *export operations* by any establishment or person, whether state, co-operative, or private. To ensure that right the law required that even private persons and establishments turn over to the bank all foreign media of payment obtained from export operations. Private persons and establishments, though, were not forbidden by this act from buying and selling foreign exchange in general, the above limitations applying only to the proceeds from export trade. They were, however, required to execute all such purchases and sales on the securities exchanges or at credit institutions. It should be observed that only members of the securities exchanges had a right to engage freely in the purchase and sale of foreign media of payment; others wishing to buy exchange could do so provided they obtained the permission of a special so-called Valuta Council for each individual transaction.[26]

These conditions ideally suited the State Bank's purpose of

[24] Decree 189; Loevetzky, *op. cit.*, pp. 26 ff.

[25] Credit institutions, too, were required to transfer to the State Bank for deposit whatever foreign media of payment they had in their possession.

[26] The members and permanent traders at these exchanges—in addition to the representatives from various credit institutions, the State Bank, the Commissariat of Finance and the like—consisted only of such approved State and co-operative establishments as engaged in foreign trade. Private persons and establishments, whose license fees exceeded a certain sum, too, could qualify for membership.

stabilizing the chervonetz in terms of foreign exchange and gold. This is how Sokolnikov, Commissar of Finance at the time, described the victory of the chervonetz over gold and foreign exchange: [27]

We had concentrated among the reserves of the treasury and the State Bank a volume of gold and foreign exchange and with their aid we were able to fight the black exchange. Each one of the speculators at a given point proved weaker than the state. True, when the black exchange was legalized great fear was created. Some were saying: We are lost, can you not see that the end is coming, it is necessary to destroy the black exchange by means of the GPU, etc. Nevertheless, we went into this arena of fight, that is, we said: We are engaging small business in a battle and we are fighting it with its own weapons, in its own regulatory organs—on the black exchanges, the principal importance of which consisted in that they were organs for the regulation of the small free trade turnover. Having given them "liberty" that is, having legalized them to a certain extent, we went there and had to try to vanquish them not by administrative measures, but by economic means. . . .

Valuta intervention was likewise carried out with respect to foreign media of payment, since here too we were superior and could overcome the resistance of the holders of foreign exchange. . . .

Hence the artificiality of those high quotations.

It must not, however, be imagined that the government threw large supplies of gold and foreign exchange upon the markets for that purpose. Much had been accomplished in that direction, particularly before fall, 1923—that is, before the depreciation of the currency assumed exceedingly dangerous proportions—by buying and selling chervontzy for *sovznaks* in the open market. The sovznaks, therefore, paradoxical as it may seem, although in general they undermined the purchasing power of chervontzy, were at the same time being employed for the purpose of stabilizing that power.

The chervonetz and the price level.—Upon making its appearance at the end of 1922 the chervonetz had been, so to speak, endowed with a purchasing power over commodities and services approximately equivalent to ten pre-war rubles. This was accom-

[27] Sokolnikov, *op. cit.*, III, 142.

plished by fixing the current rates at which chervontzy and Soviet rubles exchanged, so that one chervonetz commanded in exchange an amount of Soviet rubles which had the purchasing power of approximately ten pre-war rubles. Its high purchasing power, however, was of an ephemeral nature and soon the price indices, calculated in chervontzy, began to advance. The approximate extent of the advance in the price level and of the concomitant decline in the purchasing power of the chervonetz is shown by Table 24. It appears from the figures given there that the decline of its purchasing power, although pronounced even in the early months of 1923, had become aggravated in the summer, and that the improvement that followed in the autumn months was succeeded in December of the same year by a fresh decline, which by March 1, 1924, that is, at the time of the Monetary Reform, brought its purchasing power to the lowest for the entire period.

Measured in terms of the revised wholesale price index of the State Planning Commission (Gosplan), the value of the chervonetz, as compared with what it had been on January 1, 1923, is seen to have declined by 43 percent by January 1, 1924, that is, within one year, and by 50 percent or one-half, by March 1, 1924. That the decline of the chervonetz' purchasing power when measured by this index was not greater is explained, of course, by the fact that the state owned or controlled wholesale establishments. Nevertheless, contrary to all expectations it appears that in the retail sector the extent of that decline, according to the revised index, between the dates mentioned was even smaller—41.2 percent and 44.6 percent respectively. It will be noticed, however, that whereas in the wholesale sector the initial purchasing power of the chervonetz (on January 1, 1923) was above par, in the retail sector it was already at a low level—6.99, according to the "old" index, or 8.13, according to the "revised" index. By January 1, 1924, as shown by the same table, its purchasing power in retail trade, measured by the old index, dropped to 4.18 and on March 1 of the same year to as low as 3.87 (or 4.78 and 4.50, respectively, according to the revised index); while in the wholesale trade its purchasing power on the two respective dates was 7.93 and 6.94,

TABLE 24

THE PRICE LEVEL AND THE PURCHASING POWER OF THE CHERVONETZ

PRICES OF 1913=1

Date (First of the Month)	*Wholesale Price Index of the Gosplan*		*Purchasing Power of Chervonetz (Ten Rubles) Calculated on the Basis of the Wholesale Price Index*		*Retail Price Index of the Institute for the Study of Economic Conditions*		*Purchasing Power of Chervonetz Calculated on the Basis of the Retail Price Index*	
	Old Index [a]	Revised Index [b]	On the Basis of the Old Index	On the Basis of the Revised Index	Old Index [a]	Revised Index [b]	On the Basis of the Old Index	On the Basis of the Revised Index
1923								
January...	0.90	0.96	11.11	10.42	1.43	1.23	6.99	8.13
February..	0.98	1.04	10.20	9.62	1.47	1.23	6.80	8.13
March.....	1.09	1.16	9.17	8.62	1.59	1.32	6.29	7.57
April.....	1.05	1.15	9.52	8.70	1.55	1.35	6.45	7.47
May.....	0.98 [c]	1.09	10.20	9.17	1.49	1.28	6.70	7.81
June.....	1.10	1.26	9.09	7.93	1.79	1.65	5.58	6.06
July.....	1.29	1.45	7.75	6.90	2.09	1.84	4.78	5.43
August....	1.36	1.58	7.35	6.33	2.27	1.91	4.40	5.23
September.	1.38	1.57	7.25	6.37	2.08	1.91	4.81	5.23
October...	1.37	1.57	7.30	6.37	1.91	1.65	5.23	6.06
November.	1.25	1.49	8.00	6.70	2.23	1.92	4.48	5.21
December .	1.26	1.57	7.93	6.37	2.08	1.83	4.81	5.43
1924								
January...	1.26	1.69	7.93	5.91	2.39	2.09	4.18	4.78
February.	1.42	1.87	7.04	5.35	2.57	2.22	3.89	4.50
March....	1.44	1.93	6.94	5.18	2.58	2.22	3.87	4.50
April.....	....	1.81	....	5.52	2.52	2.21	3.97	4.52
May.....	....	1.75	....	5.71	....	2.24	....	4.46

TABLE 24—*Continued*

THE PRICE LEVEL AND THE PURCHASING POWER OF THE CHERVONETZ

PRICES OF 1913=1

Date (First of the Month)	*Wholesale Price Index of the Gosplan*		*Purchasing Power of Chervonetz (Ten Rubles) Calculated on the Basis of the Wholesale Price Index*		*Retail Price Index of the Institute for the Study of Economic Conditions*		*Purchasing Power of Chervonetz Calculated on the Basis of the Retail Price Index*	
	Old Index [a]	Revised Index [b]	On the Basis of the Old Index	On the Basis of the Revised Index	Old Index [a]	Revised Index [b]	On the Basis of the Old Index	On the Basis of the Revised Index
1924								
June.....	....	1.66	....	6.02	....	2.24	....	4.46
July.....	....	1.69	....	5.91	....	2.21	....	4.52
August....	....	1.75	....	5.71	....	2.35	....	4.25
September	....	1.73	....	5.78	....	2.36	....	4.24
October...	....	1.64	....	6.10	....	2.20	....	4.54
November.	....	1.64	....	6.10	....	2.19	....	4.57
December .	....	1.68	....	5.95	....	2.20	....	4.54

[a] *Economic Bulletin of the Institute for the Study of Economic Conditions*, N. D. Kondratiev, ed. (Moscow, Commissariat of Finance, 1924), No. 4, p. 5.

[b] *Ibid.*, 1925, No. 1, pp. 4-5. In the revised wholesale price index the price level in the socialized sector appears to have been raised and, consequently, the purchasing power of the chervonetz lowered. Conversely, in the revised retail price index the price level was lowered and the chervonetz' purchasing power, in consequence, increased. The lowering of the price level, as reflected by the revised retail index, was accomplished by a change in the methods used for compiling it. Important among those changes were: the reduction of the number of included commodities from 98 to 60; the revision of certain basic (1913) prices so as to make allowance for the change in the grades of goods; the substitution of the geometric mean and the employment of the link method, instead of the former arithmetic mean; and, finally, the assignment of weights to the various *groups* of commodities (the old index was unweighted). See the *Economic Bulletin* . . . 1924, No. 4, pp. 12-13.

[c] In the *Bulletin* 1.98 is given as the figure for the month. Judging, however, by the movement of other indices, that is a misprint and the figure 0.98 is the one which should have been included instead.

according to the old index (or 5.91 and 5.18, according to the revised figures).

It will also be observed that the decline was particularly sharp during the first half of 1923 and that thereafter the purchasing

power of the chervonetz displayed a degree of relative stability.

The circumstances surrounding the decline of the chervonetz' purchasing power in 1923–24.—Broadly speaking, the forces which during this period contributed to the rise of prices as expressed in chervontzy can be divided into two groups, those originating on the side of commodities, and those whose origin lay on the side of money and credit.[28]

The badly organized and managed enterprises lacked working capital and did not operate at their capacity, a circumstance which accounted for a high per unit overhead cost. This, together with the general inefficiency and waste in production, could not but lead to a higher cost of production and consequently to higher prices.

Meanwhile the credits granted by the State Bank continued to expand rapidly and this reflected itself in a rapid increase in the volume of banknotes (chervontzy). Had the expanding credit and banknote issue been confined to true short-term credits, such expansion could not have led to the depreciation of the chervonetz. Because of scarcity of savings and the consequent inability of the credit system to meet fully the need of business enterprises for long-term investment funds, the borrowers not infrequently used the short-term credit obtained at the State Bank to buy machinery, for plant expansion and for other purposes requiring long-term financing.

The fact that the bank was granting such loans for short periods of time, renewing them from time to time, could not, of course, change the inflationary character of such credits. There followed, besides, during the early part of 1923 and particularly during the summer months of that year, a substantial increase in strictly commercial loans. But summer months in the Soviet Union, as elsewhere, are seldom noted for an increase in business activity, the height of such activity being reached in the fall. Under free competition this latter factor is likely to contribute to lowering rather than to raising prices. Free competition, however, is seldom if

[28] See S. A. Falkner, *Problems in Theory and Practice of Currency Emissions* (Moscow, 1924), p. 220; see especially, D. Kuzovkov, *Basic Moments in the Disintegration and Rehabilitation of the Monetary System* (Moscow, Communist Academy, 1925), pp. 311-49.

ever encountered anywhere, least of all in the Soviet Union, where the enterprises enjoy *monopoly* privileges and where they are encouraged to earn profits. There the expansion of credits during a slack period was bound to result in those early years (when the planning and the methods employed were very crude), even to a greater extent than in a capitalist country, in the holding out for higher prices. Apparently, the association of the two—the marked increase in banknotes in circulation as a result of credit expansion during the spring and summer of 1923, and the sharp decline of their purchasing power—is not purely coincidental. Especially, when we notice that in the autumn months of 1923, when business activity increased, a contraction of bank credit, and hence a decrease in the volume of banknotes issued, was accompanied by an increase in their purchasing power, and conversely in the winter, when the volume of bank credit was once more expanded, the increase in the volume of banknotes issued was accompanied by a new drop in their purchasing power. The overissue of banknotes was, therefore, an important factor in their depreciation.

There was yet another factor on the means of payment side which was undoubtedly to some extent responsible for the depreciation of the banknotes, the sovznaks. Issued by the treasury in large volume and depreciating rapidly, these could not fail to affect adversely the purchasing power of the chervonetz, even though it is impossible to measure quantitatively the extent of such influence.

The "scissors" crisis.—Armed with liberal credits furnished by the State Bank—principally against commodities as security—the monopolistic trusts and syndicates were able to withhold their goods from the market. Thus they created scarcity within scarcity [29] and were able to bring about a substantial rise in the prices of many necessaries of life.[30] Operating in the same direction was the rigorous credit policy adopted by the bank, in conformity with

[29] The per capita consumption at that time of such commodities as cotton goods or sugar was about one-fifth of what it was in 1913.—J. Kuperman, "The Effectiveness of the Policy of Commodity Price Regulation," *Vestnik Finansov*, 1925, No. 1.

[30] See S. Kiselev, "The Rise of Market Prices and the Reasons," *Vestnik Finansov*, 1923, Nos. 36 and 37, p. 37; also articles by Professor Weinstein, Commissar Vladimirov, and Professor Kondratiev in the *Economic Life* for September 12, 13 and 26, 1923.

the general policy of the government, towards *private* traders. Unable to procure ample credit at the bank, the latter turned to private lenders whose interest charges were very high, a circumstance which caused prices to advance in the so-called private sector of the national economy.

As a result of the rise of prices of manufactured goods, the peasants, whose receipts from the sale of their produce underwent no such corresponding increase, found that the commodities which they were accustomed to purchase in the towns were no longer within their reach.[31] The fact that the peasants were paid in *sovznaks,* of which they frequently were unable to dispose at once to escape the burden of depreciation, greatly aggravated the matter. An idea of the seriousness of the disparity between agricultural and industrial prices can be obtained from a comparison of the respective official indices.

As shown by Table 25, on August 1, 1922, when the wholesale price index of the Gosplan, calculated in chervontzy, stood at 2 (with 1913=1), the agricultural price index stood at 2.1 and the industrial price index at 1.9. This situation, though favorable to the peasantry, did not last very long, for one month later the agricultural and industrial index numbers were respectively 1.4 and 1.6. Thereafter, the disparity tended to become more and more pronounced. On October 1, 1922, e.g., the respective figures were 1.1 and 1.4; on January 1, 1923, 0.8 and 1.2; on April 1 of that year, 0.8 and 1.6; on July 1, 1.0 and 2.1; and on October 1

[31] It was not unnatural that agricultural and industrial commodities should exchange at this time in a ratio different from that of 1913. Industry, it will be remembered, suffered more during the World War, revolutions, and the stormy period of War Communism than did agriculture, and even though somewhat improved in 1923, that improvement was still insufficient to permit (in a free market) an exchange of agricultural and industrial commodities on the basis of the 1913 ratio. According to V. G. Groman, the total pre-war net production of Russian agriculture and industry (for one year) amounted to 7,900,000,000 rubles, of which agriculture was responsible for 5,600,000,000 and industry for 2,300,000,000. In other words, before the World War, agriculture was responsible for 71 percent and industry for 29 percent of the total net production. In 1922–23, however, the total net production amounted to but 4,900,000,000 pre-war rubles (calculated on the basis of the official index), of which agriculture was responsible for 4,200,000,000 or almost 86 percent of the total, industry for but 14 percent. See A. Kaktyn, *New Economic Policy and the "Scissors," Contemporary Problems in Economic Policy* (Moscow, 1924), pp. 51-54.

TABLE 25

THE DISPARITY BETWEEN AGRICULTURAL AND INDUSTRIAL PRICES OR THE "SCISSORS" [a]

PRICE INDICES CALCULATED IN TERMS OF CHERVONTZY

1913=1

Date	*Wholesale Price Index of Gosplan*			*The Extent of the Disparity ("the Opening of the Scissors")*
	1 General	2 Agricultural	3 Industrial	4 Column (3) divided by column (2)
1922				
August 1....	2.00	2.11	1.90	0.9
September 1 .	1.50	1.44	1.56	1.09
October 1....	1.23	1.07	1.41	1.31
1923				
January 1....	0.96	0.77	1.20	1.56
April 1.....	1.15	0.83	1.58	1.90
July 1.....	1.45	1.02	2.07	2.03
October 1....	1.56 [b]	0.89	0.76	3.10
1924				
January 1 ...	1.69	1.24	2.29	1.84
February 1 ..	1.86	1.53	2.27	1.48
March 1.....	1.93	1.70	2.19	1.28
April 1.....	1.81	1.56	2.09	1.33
October 1....	1.64	1.36	1.99	1.46
1925				
January 1..	1.72	1.52	1.94	1.27
July 1.....	1.88	1.86	1.90	1.02

[a] *Our Monetary Circulation*, p. 252. In Soviet literature this disparity went under the name of "scissors," inasmuch as, when plotted, the curves of the industrial and agricultural indices resemble a pair of scissors. The opening of the scissors is described by the quotients (as percentages) that are obtained when the figures of the agricultural index are divided into those of the industrial index.

[b] The Institute for the Study of Economic Conditions reported 1.57 as being the Gosplan index number for the month. See Table 24.

they were 0.9 and 2.8. In other words, if the ratio of interchange between agricultural and industrial goods in 1913 is taken as 1:1 then on October 1, 1923, this ratio, according to official data, stood at about 3:1. But the official price index was based largely upon prices prevailing in the socialized sector. The peasants, as a matter of fact, had to buy whatever manufactured goods they needed from private traders whose prices were considerably higher. It may be supposed, therefore, that in reality the disparity was much greater.[32]

The monopolistic trusts and syndicates were apparently hoping that after the autumn harvest they would be able to dispose of their commodities in a seller's market at even higher prices.

But what they failed to consider was the resistance which the peasants, as consumers, could offer, and in the fall of 1923 they found themselves faced with what amounted to a consumers' strike. By taking proper steps and introducing changes, the government was able to avert great danger and prevent a recurrence of this in the future. Before dealing with these steps and changes, it is necessary, however, to delve further into the evils of inflation of that period.

[32] See Maurice Dobb, *Russian Economic Development since the Revolution* (New York, E. P. Dutton and Co., 1928), pp. 226 ff. Cf. Calvin B. Hoover, *The Economic Life of Soviet Russia* (New York, The Macmillan Co., 1931), p. 77.

VIII

THE "BIPAPER" STANDARD AND HYPER-INFLATION

The chervonetz and the treasury notes from the end of 1922 to March, 1924.—The "scissors" crisis or the disparity between agricultural and industrial prices, which in turn was instrumental in causing a diminution of the trade turnover and contributing to the depreciation of the banknote, was doubtless aggravated by the simultaneous existence and circulation in the Soviet Union of two types of currencies side by side. One—the *treasury notes* (also referred to as *Soviet rubles* or *tokens,* or *sovznaks*)—was being issued by the state treasury in relatively small denominations easily accessible to the large mass of people and convenient for retail trade. The other—the banknotes or chervontzy—was being issued by the State Bank in large denominations, as a result of credits extended to its customers, and was intended for use in wholesale trade, and in general in connection with large transactions. The treasury rubles were legal tender; the banknotes, although enjoying many privileges, were not given such right. Being issued in large quantities for the purpose of enabling the government to cover its budgetary deficits, the very rapidly depreciating treasury rubles constituted one of the most unstable currencies imaginable. The banknotes, on the other hand, were relatively stable, especially from the second half of 1923.

The most unusual and interesting feature of this circulation of two paper currencies—of a relatively stable or "good" currency, and of a sharply depreciating or "bad" currency—lay in the fact that the law neither established a *fixed* relation between the two, nor made their exchange on the part of the State Bank, or some other governmental agency, obligatory.[1]

Since, however, the purchasing power of the two differed sharply, it became necessary to use some sort of rate at which these currencies could be interchangeable. For even when pay-

[1] The State Bank did carry on such exchange. It was not, however, required by law to do so, and in fact it not infrequently turned down requests to exchange one currency for the other.

ments were intended to be made in chervontzy, it often proved necessary to use at the same time treasury rubles, inasmuch as chervontzy were being used in tens of chervontzy-rubles or multiples thereof. If, for example, it was necessary to pay out 103 chervontzy-rubles,[2] 100 chervontzy-rubles could be paid in chervontzy, while the balance had to be made up of such an amount of treasury rubles as was considered to be equivalent to three chervontzy-rubles.

At first such rates were set by the various local exchanges; later (from October 17, 1923), by order of the Central Executive Committee, the quotations of the Securities Branch of the Moscow Produce Exchange began to be used throughout the Union and thus acquired an official character. There were also free market rates which often differed from the official quotations. Both of these—the market and official quotations—were current rates which kept on changing. To repeat, there existed no *fixed* relation between the banknote and the treasury ruble.

Because of the absence of a fixed ratio between those two currencies, some writers refer to them as a system of two "unrated" paper currencies and attempt to draw an analogy between that system and the bimetallic standard.[3] Apart from the fact that in one case we deal with paper currencies which as such can have no intrinsic value, and in the other with metallic currencies having intrinsic value, there are other difficulties in such an analogy. Under the conventional (rated) bimetallic standard, for instance, there is free and unlimited coinage; both metals enjoy legal-tender privileges and can be exchanged for one another, not only in the market at whatever rates happen to prevail there, but also at the mint *at a fixed ratio* established by law. It would seem, therefore, that the system of paper currencies in the Soviet Union in 1923–24 differed from the bimetallic standard described above in at

[2] "Chervontzy-rubles" should not be confused with "chervontzy." One chervonetz may be said to contain ten chervontzy-rubles.

[3] See e.g., L. N. Yurovsky, *Currency Problems and Policy of the Soviet Union* (London, 1925), pp. 111-14, where the above-described system of two inconvertible paper currencies is called "unrated," and where an analogy between it and the unrated bimetallic standard is drawn. Other writers (e.g., Katzenellenbaum, *Russian Currency and Banking 1914–24*, pp. 117 ff.) refer to the above system as being a system of two *parallel* paper currencies.

least one important respect: the law established no fixed and unchanging ratio between the banknote and the treasury ruble. This apparently caused some writers to conclude that the "unrated" inconvertible paper currencies of that period could best be compared with an *unrated* bimetallic standard, rather than with the "conventional," rated, type.

Now under an *unrated* bimetallic standard, the two metals, although accorded free and unlimited coinage as well as legal-tender privileges, need not be placed by law in any definite, fixed relation to one another—their exchange is supposed to be carried out on the basis of more or less fluctuating market rates. Because they can be so exchanged and because there is no official rate (the difference between which and the market rate is likely to make profitable at any one time the use of one currency rather than the other), the two unrated metals can conceivably circulate side by side.

This, however, was not the case with the Soviet "unrated" paper standard, for in the Soviet Union there existed not only market rates at which banknotes and treasury rubles could be interchanged, but also official rates which most often did not coincide with the market rates. As a result of the discrepancies between the official and market rates it became profitable, whenever the former lagged behind the latter, to make payments which were expressed in chervontzy, not in this latter currency but in the depreciating legal-tender Soviet notes at official rates of exchange. One's unspent margin or reserves could, in fact, be held in the form of the more stable banknotes, but as soon as an obligation matured, or, in general, when money was to be paid out for the purchase of goods and services, treasury notes could be purchased at the speculative market, and the payment made in them at the official rate, which, being changed only once a day, was bound to be lower during the day than the market rate. This, in fact, is what was happening, and as a result treasury rubles were threatening the position of chervontzy as a medium of exchange.

Naturally, the depreciating rubles could not threaten the position of chervontzy as a measure of value or as a store of value. Competition in the latter fields could come only from gold itself

or from stable foreign currencies, although it may be doubted whether enough of these existed in Soviet Russia to satisfy the needs of the population, even if the economic and political set-up of that country were not such as to make a large section of the national economy obedient to the wish of the state.

The position of chervontzy as a means of payment, however, was less secure than their position as a measure of value or a store of value. It is true, of course, that within a certain prescribed field the chervontzy enjoyed exclusive rights as a medium of payment. It will be recalled, for instance, that the bank had the right to demand of its clients that all loans expressed by it in terms of chervontzy be repaid in that currency. In addition, according to the decree of the Council of People's Commissars of July 31, 1923, chervontzy were accorded this privilege in the case of all commercial paper drawn in chervontzy, no matter who the payee might be.[4] But numerous transactions, even besides those for which a currency of smaller denomination than the chervonetz was required,[5] fell outside of the sphere in which chervontzy enjoyed

[4] *Collected Decrees,* 1923, Decree 882.

[5] In addition to chervontzy and paper rubles, there were in circulation in the Soviet Union in 1923–24 so-called "transportation certificates" of the denomination of *five* (gold) rubles each. They were issued on the strength of the July 27, 1923, decree of the Council of Labor and Defense (Decree 859) and of subsequent decrees authorizing additional issues on November 23, 1923, on December 8, 1923, and on March 26, 1924. (*Collected Decrees,* 1924, Decrees 120, 154, and 445, respectively). Their total authorized issue amounted to 24,000,000 gold rubles. Their actual issue began in September, 1923. The highest amount outstanding was that at the end of April, 1924—21,276,800 gold rubles (*Our Monetary Circulation,* p. 139). They had to be turned in not later than July, 1924. Issued as non-interest bearing short-term obligations of the Commissariat of Transportation (and guaranteed not only by the former but also by the Commissariat of Finance) for the purpose of enabling it to cover the deficit arising from the operation of railroads and other means of transportation, and, incidentally, of lightening the burden of the state budget, they soon began to be used as currency. It might be asked what caused their being drafted into circulation when there seemed to have been an excess of currency. Had there been a superior security behind them, the reason would be apparent; the only security, however, behind them was the pledge of the income of the transportation system, and the guarantee of the Commissariat of Finance. This, though, should not have made those certificates more attractive than the Soviet rubles. First, because the transportation system operated at a loss, and so the pledge of its revenue was not a valuable asset. Secondly, Soviet paper rubles, too, had the guarantee of the Commissariat of Finance. Their attractiveness, as one writer (T. Engeev, "State Treasury Notes," *Vestnik Finansov,* 1924, No. 2, p. 16) rightly remarks, lay in the fact that (a) they had stability (there was estab-

monopolistic rights. In such cases treasury rubles were given preference as a means of payment.

Although the principles which underlie the circulation of metallic currency are not generally applied to the circulation of paper currency, yet it is worth noticing that the phenomenon of the displacement from circulation of an officially undervalued currency by one which is officially overvalued is commonly associated with the *rated,* rather than the *unrated,* bimetallic standard. Apparently in this respect the Soviet paper standard of 1922–24, that is, the type which admits of two sets of rates, official and market, can more appropriately be likened to the rated bimetallic standard. Indeed, the term "unrated" when applied to paper currencies of the above variety is a misnomer. The official rate of the "unrated" paper standard accomplished very much the same as would the fixed, legal ratio under the rated bimetallic standard. It could, in fact, be assumed that there did exist a "fixed" relation between the chervonetz and the treasury ruble, but that the rapid depreciation of the ruble necessitated frequent changes in that relation, instead of changes at the end of so many years, as was the case under the rated bimetallic standard (in the United States, for instance the fixed, legal ratio of 15 to 1, established in 1792 was changed to 16 to 1 in 1834–37).[6]

Close analogies, to be sure, can hardly be expected in a case so unique as to have no precedent in the monetary histories of nations, and no place in the theoretical speculations of writers on currency questions. There have been instances when of two currencies circulating side by side one was a depreciating *paper* currency. Such an instance is found in Russia's history. In Russia, for example, for about thirty years (from 1810–12 to 1839–43 when the system was reorganized) there circulated side by side a depreciating paper currency, the "assignat," and a silver currency, with

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lished a definite rate of exchange for them; they were redeemable in the equivalent of five gold rubles each); (b) their denomination was *five rubles,* something that the chervontzy did not furnish and that the population required.

[6] In fact, originally the rate of the sovznak was fixed for a duration of three months, later it was changed to once every month, then once fortnightly, and finally once daily. See Sokolnikov, *The Monetary Reform* (Moscow, People's Commissariat of Finance, 1925), pp. 10-11.

the privilege given to the people of settling all their private transactions either in silver or in assignats at the market rate of exchange. The existence of a depreciating paper currency, also named "assignat," side by side with a metallic currency took place, to a greater or less degree, in France during the memorable years 1790–93 and 1795–96. It remained, however, for Soviet Russia to furnish history with an example of a new standard under which *two paper currencies,* one of which is relatively stable and the other sharply depreciating, circulate side by side. A fitting name for such standard is *bipaper standard.*

Position of treasury notes with respect to banknotes, gold, and foreign exchange.—With the size of the issues and the extent of the depreciation of the chervontzy we have already dealt. Let us now analyze the position of the Soviet rubles or treasury notes during 1923–24 with respect to banknotes, gold, foreign exchange, and the price level. On January 1, 1923, as shown by Table 26, treasury notes, or rubles, in the "free" market exchanged for chervonetz-rubles in the ratio of 16,700,000 : 1. By April 1, 1923, the ratio changed to 30,600,000 : 1 and by May 1 of the same year to 46,200,000 : 1. Thereafter as the note circulation kept on expanding, the "free" market was offering more and more of them in exchange for chervonetz-rubles. By the end of the year the ratio had advanced to 3,075,000,000 : 1 and by March 1, 1924 to 32,800,000,000 : 1.

In terms of chervonetz-rubles the sovznak (treasury note), therefore, between January 1, 1923, and April 1, 1923, lost 45.4 percent of its value; while between the former date and the end of the year it lost 99.46 percent. By March 1, 1924, it had lost 99.95 percent of the value that it had on January 1, 1923.

It should be observed that the rates at which sovznaks exchanged for chervonetz-rubles on the "free" markets lagged at times behind the official rates. On June 1, 1923, for instance, this lag in Moscow amounted to .5 percent; on July 1, to 1.1 percent; while on August 1 the two rates coincided. In other cities the lag amounted to 10 percent and more.

The basic reason for the lag (or premium on sovznaks) doubt-

less lay in the rapid increase in the amount of chervontzy in circulation, and the consequent disproportion between their volume and that of sovznaks or "small currency," a phenomenon that went under the name of "small change crisis" or "small change famine."

The small change famine soon, however, gave way to a different phenomenon, the lag of official rates behind "free" market rates. The rapid expansion of the sovznaks' circulation and the flight from them led to an increasing demand for chervontzy, hence, beginning with the fall months of 1923, chervontzy began to command a premium on the "free" market. In Moscow this latter lag (or premium on chervontzy) did not exceed 4 percent, but in other cities it not infrequently exceeded 10 percent.

In so far as the exchange of sovznaks for gold rubles was concerned the situation was as follows: the official rate of exchange between gold rubles and sovznaks until June, 1923, as shown by Table 26, had been kept below the rate at which sovznaks exchanged for chervonetz-rubles. On June 1, 1923, for instance, a ten-ruble gold piece of the Czarist mintage (of 1899 and later) commanded, according to the official rate, 560,000,000 Soviet rubles (or 560 rubles of the 1923 pattern), while a chervonetz commanded 580,000,000 rubles. After that date, however, the official rate at which the gold coins and the chervontzy exchanged for sovznaks did not differ.

Despite the intervention of the government on the "free" market, the latter placed a considerably higher valuation on gold than did the governmental agencies. That lag became particularly wide beginning with the fall of 1923, when the flight from sovznaks caused the demand for gold rubles to increase. The government apparently thought it inadvisable to use up its gold stock in an attempt to stem the tide when it was at its height. On November 1, 1923, for example, the "free" Moscow market quotations exceeded by 42.77 percent the official quotation.

On January 1, 1923, on the "free" Moscow market, treasury notes exchanged for gold rubles in the ratio of 22,500,000 : 1. By April 1, 1923, the ratio changed to 40,500,000 : 1. By the end of the

TABLE 26

RATES OF CHERVONTZY, DOLLARS, STERLING, AND GOLD

DECEMBER, 1922–MARCH, 1924

(In millions of treasury notes) [a]

Date	*Chervonetz*		*Dollar*		*Sterling*		*Gold Ruble*	
	Official [b]	Free Market [c]	Official [d]	Free Market [e]	Official [d]	Free Market [e]	Official (Special Commission on Quotations)	Free Market [e]
1922								
December 1	117	177	23.00	28.00	100.00	111.00	11.00	13.30
1923								
January 1	175	167	32.25	45.50	143.50	204.00	17.40	22.50
February 1	212	209	40.30	50.00	166.00	222.00	20.20	26.60
February 15	233	....	48.55	....	218.50	....	22.50	....
March 1	240	240	46.00	46.25	212.50	213.00	23.50	27.90
April 1	302	306	58.00	58.75	258.50	262.00	27.30	40.50
May 1	457	462	102.00	111.00	442.00	469.00	43.00	73.50
June 1	580	577	150.00	160.00	660.00	665.00	56.00	100.20
July 1	760	752	163.00	167.00	745.00	750.00	76.00	114.50
August 1	1,150	1,150	243.00	244.00	1,110.00	1,135.00	115.00	155.00

September 1.....	2,050	2,060	425.00	427.00	1,950.00	1,975.00	205.00	250.00
October 1.....	4,100	4,120	842.00	845.00	2,850.00	3,870.00	410.00	512.50
November 1	7,100	7,380	1,460.00	1,624.00	2,500.00	7,005.00	710.00	1,014.70
December 1.....	14,600	14,600	3,090.00	3,212.00	13,450.00	13,800.00	1,420.00	1,971.00
1924								
January 1.....	30,000	30,750	6,600.00 [f]	6,888.00 [f]	28,200.00 [f]	28,981.87 [f]	3,000.00 [f]	4,320.37 [f]
February 1.....	86,000	88,800	19,062.00	19,447.20	79,464.00	83,028.00	8,600.00	12,520.80
March 1.....	330,000	328,000	69,930.00	69,208.00	299,136.00	299,136.00	33,000.00	41,984.00
March 8.....	450,000	....	....	....	....	....	....	....

[a] Based upon *Our Monetary Circulation*, pp. 220, 222, 223, 227.

[b] As quoted by the Securities Branch of the Moscow Produce Exchange.

[c] In Moscow.

[d] The official dollar and sterling rates for the first three months in the above Table are those of the Special Commission on Quotations. On February 15, 1923, when the Securities Branch of the Moscow Produce Exchange opened, the Commission discontinued the publication of foreign exchange rates (as well as of precious metals). Accordingly, the remaining figures in the respective columns are those of the Securities Branch of the Moscow Produce Exchange. This latter body published foreign exchange rates in sovznaks only until December 1, 1923; after that date the published quotation of foreign exchange were expressed in chervonetz-rubles. It, however, continued to quote chervontzy in sovznaks.

[e] The figures for the first month are those of the Institute for the Study of Economic Conditions (Konjukturnyi Institut). The rest are those of the Currency Administration of the People's Commissariat of Finance of the U.S.S.R.

[f] This and the other figures for 1924 were obtained from quotations expressed in the official source in chervonetz-rubles by converting the chervontzy into rubles at the rates prevailing on the respective dates in the respective markets.

year the ratio had advanced to 4,320,370,000 : 1, and by March 1, 1924, to 41,984,000,000 : 1.

In terms of gold rubles the sovznak, therefore, between January 1, 1923, and April 1, 1923, had lost 44.5 percent of its value; by the end of the year the loss had increased to 99.48 percent and by March 1, 1924, to 99.95 percent. Thus, during the period of January 1, 1923, to March 1, 1924, the sovznak depreciated to almost the same extent in terms of gold as of chervontzy.

In terms of American dollars, as quoted on the "free" Moscow market, the sovznak between January 1 and April 1, 1923, had lost only 22.5 percent of its value, but by the end of the year the loss had increased to 99.34 percent, and by March 1, 1924, to 99.93 percent.

As will presently be shown, the depreciation of the sovznak in terms of everyday commodities was greater than that in terms of chervontzy, gold, or foreign exchange.

Treasury notes and the price level in 1923–24.—It has been seen that by the end of 1922 the volume of treasury notes in circulation had reached a colossal figure that was close to 2,000,000,000,000,000.[7]

During 1923 the volume of notes in circulation became augmented by further gigantic issues, so that by the end of the year the total swelled to 225,637,374,401,420,000 paper rubles, an amount that was 113 times, or 11,210 percent, greater than that at the beginning of the year.

Now it is interesting to observe that the volume of notes in circulation at the end of 1922 was 114 times as high as that at the end of 1921, and that the increase for the year amounted to 11,270 percent. But in 1922 this rate of increase of the volume of notes in circulation was accompanied by an increase in the

[7] According to official records, the volume of notes in circulation at the end of 1922 amounted to almost 2,000,000,000 rubles, and not 2,000,000,000,000,000 as stated here. Similarly, other items pertaining to the amounts of notes issued and in circulation appear one million times smaller in the official records. That, of course, is due to the fact that those amounts were expressed in rubles of the 1923 pattern, each of which equaled 1,000,000 rubles of the 1921 and pre-1921 issues (or to 100 rubles of the 1922 pattern, each of which in turn equaled 10,000 rubles of earlier issues).

To present a more realistic picture the present writer carried out all computations as though the six zeros were never cast off.

price level that was some 73 times, or 7,275 percent, higher than at the beginning of the year, whereas in 1923 the price level increased 256 times, or 25,590 percent.

Apparently, an important change was taking place. Once more the rate of increase of the price level was outstripping that of the volume of notes in circulation. And as shown by Table 27 the increase in the volume of notes and in the price level was more pronounced in the second half than in the first half of 1923. Up to July, for instance, the monthly increase in circulation had been kept below 2,000,000,000,000,000 rubles, but beginning with that month the issue had sharply risen. Thus in July the total volume of notes amounting to some 9,000,000,000,000,000 rubles had been augmented by another 3,400,000,000,000,000 rubles, or by more than one-third (37.9 percent) of its own huge volume, and the price level during that one month had risen by as much as 65.7 percent.

In August approximately 4,400,000,000,000,000 rubles had been issued, again an amount in excess of one-third (35.3 percent) of the volume of notes in circulation on the first of the month, and this was accompanied by a 72.1 percent increase in the price level. These colossal issues, however, soon became eclipsed by an even more imposing and staggering array of figures.

In September, for instance, with a volume of notes in circulation amounting to 16,800,000,000,000,000 rubles, there were issued 12,900,000,000,000,000 rubles of fresh notes, or more than three-quarters (76.5 percent) of the total note circulation, and the ever increasing price level almost doubled itself (rose by 96.8 percent) within that month.

The month of October far surpassed this record. In that month to a total volume of notes in circulation amounting on the first of the month to 29,700,000,000,000,000 rubles there had been added more than 39,000,000,000,000,000 rubles (131.7 percent), so that the amount of notes issued during that one month exceeded all that had been issued up to that time. The price level at the end of that month showed, however, no such proportionate increase. Its rise amounted to 67 percent, or almost one-half the rate at which the volume of currency had increased. That October

TABLE 27

SOVIET NOTES OR RUBLES IN 1923–24 [a]

Date	1 *Volume of Soviet Notes in Circulation (In Millions of Rubles on the First of the Month)*	2 *Index of Notes in Circulation (July 1, 1914 = 1)*	3 *Amount of Notes Issued during the Month (In Millions of Rubles)*	4 *Rate of Monthly Increase in the Volume of Notes in Circulation (Column 3 to Column 1 as a %)*	5 *Price Index (All-Union Index of the Department of Labor Statistics) on the First of the Month 1913 = 1*	6 *Monthly Rate of Increase in the Price Level*
1923						
January	1,994,464,453.75	1,223,579.8	633,677,519.33	31.8	21,242,000	30.4
February.....	2,628,141,973.08	1,612,357.0	607,389,981.24	23.1	27,700,000	11.9
March.....	3,235,531,954.32	1,984,988.9	1,246,161,174.38	38.5	31,000,000	26.6
April.....	4,481,693,128.70	2,749,505.0	1,594,142,568.02	35.6	39,260,000	39.4
May.....	6,075,835,696.72	3,727,506.6	974,422,268.09	16.0	54,741,000	41.7
June.....	7,050,257,964.81	4,325,311.6	1,981,104,524.48	28.1	77,549,000	51.6

July.....	9,031,362,489.29	5,540,713.2	3,424,195,960.99	37.9	117,569,000	65.7
August.....	12,455,558,450.28	7,641,446.9	4,399,814,476.72	35.3	194,834,000	72.1
September....	16,855,372,927.00	10,340,719.6	12,898,315,593.84	76.5	335,365,000	96.8
October.....	29,753,688,520.84	18,253,796.6	39,190,451,298.64	131.7	659,838,000	67.0
November....	68,944,139,819.48	42,297,018.3	46,720,269,657.07	67.8	1,101,700,000	110.1
December....	115,664,409,476.55	70,959,760.4	109,972,964,537.87	95.1	2,314,800,000	135.7
Total....	....	....	223,642,909,560.67	....	....	....
1924						
January.....	225,637,374,014.42	138,427,836.8	223,537,345,292.6	98.6	5,457,000,000	198.9
February.....	448,174,719,307.05	274,953,815.5	361,450,497,360.2	80.6	16,310,000,000	279.6
March.....	809,625,216,667.25	496,702,886.9	47,316,874,500.0	5.8	61,920,000,000	....
April.....	762,308,342,167.25	467,673,829.5	22,576,108,000.0	3.0	....	....
May.....	739,732,234,167.25	453,823,456.5	676,196,650,252.9	....	....	....

[a] *Our Monetary Circulation*, pp. 152-53, 204, 206, 248.

was the only month, over a year's period from April, 1923, to March, 1924, within which the rate of increase of prices failed to outstrip the rate of increase of the volume of currency, was probably due to an increased demand during that month for treasury notes. The increased demand came from the peasants, who, as a result of the Tax Reform of 1923, were accorded the privilege of substituting payments in money for those in kind that they had theretofore paid to the government. Inasmuch as the cash equivalent of the tax in kind had to be determined in advance, while the ruble was depreciating rapidly, the peasantry learned that it was more profitable to pay taxes in sovznaks than in kind. Accordingly, they were bringing to the market enough grain to realize the required sovznaks, which they then paid over to the government.

Although in itself a 67 percent rise in a price level that is already too high is nothing to be cheerful about, many saw in the fact that the increase of prices during that month lagged behind the increase in the volume of currency a sign of improvement in the monetary situation, and expected the government to take advantage of that situation to stabilize the sovznaks. The government, however, did not find this possible. It will be recalled that by this time the purchasing power of the banknotes had been considerably reduced, so that further issues would have had to be made with great caution, lest the banknotes meet the fate of the sovznaks. Accordingly, the government used the discredited sovznaks, rather than the chervontzy, for the required autumn financing of grain purchases, as well as for other credit purposes. Hence the tremendous issues and the annihilation of the sovznaks in the following months.

During November, 1923, for instance, the note issue amounted to about two-thirds, or 67.8 percent of the total volume of notes on the first of the month, thereby raising the total figure to 115,600,000,000,000 rubles. Prices soared upward and by the beginning of December the price level more than doubled itself, registering a 110.1 percent rise. The dwindling of the purchasing power of the sovznaks caused the injections into their body,

which by now was writhing in agony, to become stronger and stronger.

Within the next month, December, 1923, the volume of note issue almost equaled (95.1 percent) the huge amount that was already weighing down the channels of circulation, and by the beginning of 1924 the volume of notes in circulation, therefore, jumped to some 225,000,000,000,000,000 rubles. Prices during December rose by 135.7 percent, that is by more than two and one-third times.

In January, 1924, the dose was raised to almost 225,000,000,000,000,000 rubles, the increase amounting to 98.6 percent of the total volume of notes in circulation on the first of the month, and the total volume of notes jumped by the end of the month to 448,000,000,000,000,000 rubles. The depreciation of the ruble was becoming more and more accelerated, and prices during January rose by 198.9 percent, or almost trebled.

During the first half of February[8] the dose was raised to 361,400,000,000,000,000 rubles, the increase amounting to 80.6 percent of the total in circulation on the first of the month, and the price level rose by 279.6 percent, almost quadrupling itself. The total volume of notes by the end of the month, therefore, jumped to 809,625,216,667,250,000 rubles. This, however, was the last jump. Strictly speaking, it was not the last dose which terminated the agony of the sovznak. That agony could have continued yet for some time at least, if it had not been for the coup de grâce delivered by the Monetary Reform of 1924.

The steady and rapid decline of the ruble's purchasing power necessitated an increase in its denominations. Accordingly, the government by a series of decrees and instructions ordered the introduction of five-thousand,[9] ten-thousand,[10] fifteen-thousand,[11]

[8] On February 14, 1924, the Central Executive Committee and the Council of People's Commissars had decreed the termination of the printing and issue of sovznaks, to take effect beginning with February 15, 1924.

[9] *Collected Decrees*, 1923, Decree 1024 of the Council of People's Commissars of September 29, 1923.

[10] By order of the People's Commissariat of Finance of November 30, 1923.

[11] *Collected Decrees*, 1924, Decree 169 of the Central Executive Committee and of the Council of People's Commissars of December 18, 1923.

and twenty-five-thousand-ruble notes [12] of *the 1923 pattern,* which in reality, therefore were five, ten, fifteen and twenty-five-*thousands of millions* ruble notes.[13]

Since the rate of the increase of the ruble's depreciation was greater than the rate of increase of notes in circulation, the purchasing power of the total volume of treasury notes, particularly beginning with the second half of 1923, underwent a serious decline. As shown by Table 28, the purchasing power of the note circulation, which on January 1, 1923, amounted to about 94,000,000 (pre-war) rubles fell by March 1, 1924 (at the time of the Reform, when the total note issue amounted to 809,625,216,667,250,000 rubles), to as low as 13,000,000 pre-war rubles. At this latter date it took on the average some 62,000,000,000 Soviet rubles to buy what one Czarist ruble bought in 1913.

It has been intimated above that the depreciation of the treasury ruble had been considerably greater when measured in terms of the price level than in terms of gold or foreign exchange. Thus, between January 1 and April 1, 1923, it had lost 45.9 percent of its purchasing power over commodities. Between January 1, 1923, and January 1, 1924, that is within one year, the loss amounted to 99.996 percent, and between the former date and March 1, 1924, to 99.99966 percent. Now it will be recalled that the ruble's decline on the foreign exchange (Moscow) market when measured in terms of American dollars was but 22.5 percent between January 1 and April 1, 1923; 99.34 percent for the entire 1923 year; and 99.93 percent between the first day of 1923 and March 1, 1924. The reason for this difference has already been stated.

Revenue from note issue.—The government during 1922–24 tried, not without some success, to cover the budgetary deficits at least in part by proceeds from loans; not solely by means of note issue as before. From October, 1922, to October, 1923, for instance, the budgetary deficit amounted to 461,300,000 pre-war rubles, of which 375,200,000 rubles, or more than 80 percent, had been

[12] *Ibid.,* Decree 294 of the two above-mentioned bodies of February 7, 1924.

[13] 250, 500, and 1,000-ruble denominations of *the 1923 pattern* were decreed by the People's Commissariat of Finance as early as February 9, 1923 (*Collected Decrees,* 1923, Decree 157).

TABLE 28

CIRCULATION OF 1922–24 EXPRESSED IN PRE-WAR (1913) RUBLES[a]

(In thousands of rubles)

Date	1922	1923				1924				
First of Month	Purchasing Power of Total Volume of Paper Money	Sovznaks	Banknotes or Chervontzy	Transportation Certificates	Total	Sovznaks	Banknotes or Chervontzy	Transportation Certificates	Treasury Notes	Total
January	60,900.1	93,892.5	2,944.2	....	96,836.7	41,348.2	130,307.1	5,261.3	....	176,916.6
February	54,638.9	94,878.8	6,377.5	....	101,256.3	27,478.5	130,249.4	6,248.4	....	163,976.3
March	42,094.0	104,036.4	12,338.3	....	116,374.7	13,075.3	139,263.8	9,326.6	11,471.5	173,137.2
April	32,163.3	114,154.2	19,743.8	....	133,898.0	7,326.4	139,196.6	9,988.9	32,556.4	189,068.3
May	31,116.8	110,992.4	31,284.8	....	142,277.2	6,975.3	139,132.1	10,031.5	51,198.6	207,337.5
June	42,019.2	90,913.6	34,914.3	....	125,827.9	....	139,869.8	10,229.4	81,479.9	231,579.1
July	55,211.4	76,817.5	45,162.2	....	121,979.9	....	142,032.8	1,576.9	90,456.1	234,065.8
August	84,951.5	63,929.1	63,910.8	....	127,839.9	....	136,185.0	....	104,239.5	240,424.5
September	116,120.4	50,259.8	97,713.0	....	147,972.8	....	154,896.2	....	125,001.8	279,898.0
October	115,974.8	45,092.4	125,672.4	151.5	170,916.3	....	180,656.5	....	146,336.2	326,992.7
November	94,757.3	62,579.8	143,173.5	2,657.6	208,410.9	....	190,085.1	....	158,414.9	348,500.0
December	89,976.8	49,967.3	133,735.7	2,957.7	186,660.7	....	201,703.2	....	163,483.6	365,186.8

[a] The pre-war (1913) purchasing power was obtained by dividing the currency circulation by the Department of Labor Statistics Price Index for the respective dates.

covered by revenue from note issue, and the balance by loans.[14] But during the first quarter of 1922–23 the revenue from note issue covered 95.8 percent of the deficit of that quarter; during the second, 89.7 percent; during the third, 83.5 percent; and, during the last quarter, 54.2 percent, a distinct improvement. The budgetary deficit for 1923–24 (that is, from October, 1923 to October, 1924) amounted to 375,200,000 rubles, of which 150,700,000 rubles, or 40.1 percent, were covered by note issue; 29,700,000 rubles, or 8 percent, by issue of subsidiary metallic currency; and the balance by loans. During the months of October, November, and December, 1923, the revenue from the note issue covered only 41 percent (45,500,000 rubles) of the deficit for that quarter (110,900,000 rubles). During January, February, and March, 1924, however, the revenue from the note issue served to cover 63.5 percent (or 59,900,000 rubles) of the deficit for the quarter (94,300,000 rubles). But during the months of April, May, and June, 1924, following the Monetary Reform, the revenue from note issue covered but 46.7 percent of the budgetary deficit for that quarter. Within the last quarter of 1923–24 (that is, during July, August, and September, 1924) note issue did not figure as a means of covering budgetary deficit. The government during that quarter obtained 40.7 percent (or 29,700,000 rubles) of the budgetary deficit (73,000,000 rubles) from the issue of metallic currency.[15]

As shown by Table 29 the treasury note issue since November, 1917, had yielded the government in excess of 2,365,000,000 prewar rubles.

[14] The above figures do not include the obligations of the Central Treasury Office (Tzentrokassa). These were six-month and one-year 6 percent obligations issued for the purpose of raising revenue in anticipation of collection of taxes and in general for the purpose of enabling the treasury to meet extraordinary expenditures. During 1922–23 their issue amounted to 57,100,000 and during 1923–24 to 203,400,000 rubles; of these a total of 19,000,000 rubles was redeemed during the former period and another 192,800,800 rubles of such obligations were redeemed during the latter period, so that by the beginning of 1924–25 the amount outstanding was 48,700,000 rubles.—Sokolnikov and Associates, *Soviet Policy in Public Finance*, pp. 269-70.

[15] *Our Monetary Circulation*, pp. 31-37; cf., *Vestnik Finansov*, January, 1925, No. 1, p. 161.

TABLE 29

REVENUE YIELDED BY TREASURY NOTE ISSUE DURING 1917–24 [a]

(*In pre-war rubles*)

1917 (November and December)	675,431,400
1918	536,241,900
1919	224,638,600
1920	122,014,800
1921	149,029,200
1922	296,501,600
1923	327,791,500
1924 (January and February)	33,829,900
Total yield	2,365,478,900

[a] These figures were obtained by adding monthly yields. The monthly yields were obtained by dividing the treasury note issue during a given month by the monthly average price index (of the All-Union Index of the Department of Labor Statistics) for that month. The above figures presuppose an equal yield by all types of currency. This, as has been explained, was not the fact. It is further assumed that the notes issued during a given month were expended during the same period, which was not always the case. The figures given above nevertheless give a rough idea of revenue from note issue. Calculated on the above basis the banknote issue in December, 1922, amounted to 2,692,500; and in 1923, to 153,346,600 pre-war rubles. The transportation certificates brought in 5,879,000 pre-war rubles in 1923 and 5,824,400 in 1924.

By way of comparison it may be pointed out that the Provisional government obtained within *eight months* (March–October, 1917) from the emission of currency a total of 1,735,600,000 pre-war rubles. In other words, within the course of less than a year it obtained from the emission of 6,400,000,000 paper rubles almost three-quarters of what the Soviet government obtained over a period of six and one-third years from the emission of currency of stellar magnitudes.[16]

The evils of inflation under the "bipaper" standard.—We have seen that the disparity between agricultural and industrial prices

[16] The revenue yielded by note issues to the Imperial government from July, 1914, to March, 1917, amounted to 5,400,000,000 rubles. (For 1914–15 the yearly average index was used; for all other years, the monthly average.)

led to what was known as the "scissors" crisis. Prices for manufactured goods being beyond their reach, the impoverished peasants were compelled to curtail demand for those goods. This tended to produce a number of undesirable results. Traders, for example, found themselves unable to dispose of their wares while peasants began to show a disinclination to bring their produce to the towns.

The situation demanded a correction in the form of freeing the peasants from the burden which inflation under the "bipaper" standard placed upon them. This the government for fiscal reasons was as yet unable to do. Towards the end of 1923, however, the peasants began to resort increasingly to a method which served to speed the annihilation of the sovznaks and to render the revenue from their issue almost insignificant. The method was a very simple one. Instead of bringing to the town all of their produce, they brought only a little at a time. Before disposing even of that little they would first inform themselves of the prices set upon the commodities which they intended to purchase that day, and would then sell no more than was absolutely needed in order to obtain the necessary price.[17] As the supply of agricultural products diminished, their prices rose rapidly, or, to put it the other way around, the purchasing power of the sovznaks underwent a rapid decline. Finally, the peasants began to refuse to sell grain to the government for sovznaks, demanding chervontzy.

The workers, too, were paid mostly in sovznaks and so could not escape "exchange" losses.[18] Their condition, however, was, to some extent, ameliorated by the fact that the state raised their wages, accorded them preferential treatment in every respect, and, finally, early in 1923, opened savings banks in which the small depositor's funds were protected against depreciation through the device of converting the deposited sovznaks on the books of the bank into

[17] Yurovsky, *Towards a Monetary Reform*, p. 96.

[18] In a circular letter sent by the Central Committee of the Communist Party in the spring of 1924 to party organizations, the "exchange losses" of workers on the eve of the Reform were placed at 20 to 30 percent of their earnings. "Letter of the Central Committee of the Communist Party," in Sokolnikov, *Monetary Reform*, pp. 169-72.

fixed currency at the rate of the day of deposit, and upon withdrawal making payment (in sovznaks) at the rate of the day of withdrawal.[19] To the extent that the state so insured the earnings of the workers against depreciation, the burden was, of course, shifted back to the state budget and this necessitated the issue of more sovznaks.

Industry (in its broadest sense), transportation, and trade, also could to a certain extent protect themselves from losses on account of the depreciation of the sovznak. This they could do by reducing to a minimum the amount of sovznaks that had to be kept on hand and by opening "chervonetz-standard" accounts at the State Bank wherein to deposit the sovznaks that were bound to be received during the day. Under the latter arrangement, it will be recalled, clients depositing sovznaks in the bank were being actually credited with chervontzy at the current rate of exchange,[20] and paid when making withdrawals either in chervontzy or, as generally was the case, in sovznaks at the rate of the day of withdrawal. Whatever losses were sustained by the bank were by it directly or indirectly shifted to the state.

The various enterprises, however, could not escape substantial "exchange" losses. For reasons which have already been stated they were not able to avoid the receipt of sovznaks. In addition to being legal tender they were used by the treasury to make disbursements, and, as has been pointed out, the bank, too, not infrequently paid in that currency. True, those payments were being made at the current (official) rate of exchange,[21] but even an immediate conversion of the sovznaks into chervontzy involved a considerable loss on the transaction, for in order to obtain cher-

[19] *Collected Decrees*, 1923, Decree 12, December 26, 1922.

[20] The bank tried to avoid opening such accounts. Once opened, however, it generally applied to deposits in sovznaks "next day's" rate of exchange. The difference between the rates on the day of deposit and on the following day was of course the depositor's loss. Having received the sovznaks, the bank would try its best to get rid of them as quickly as possible (paying them out to its clients) in order to shift the burden to others. The "chervonetz-standard" device described above could not be employed for the purpose of transferring funds from one place to another—the bank refused to absorb the loss on those transactions.

[21] By the end of 1923 most prices were being quoted in chervontzy, but the actual payment was made in the depreciating legal-tender sovznaks at the official rate of exchange.

vontzy one had to pay for them at the market rate of exchange, which was higher than the official rate at which one was obliged to receive sovznaks. The real losses were far greater than the mere difference between the two rates. Unless business establishments could carry out conversions at the free market simultaneously with every receipt of sovznaks, they were bound to sustain additional losses on account of the depreciation of the currency.

In retail trade, for instance, the storekeeper would necessarily find himself at the end of a day with some sovznaks, the conversion of which into chervontzy had to be postponed until the following morning. He therefore bore a two-fold loss: (a) on account of the overnight depreciation of the currency; and (b) on account of the difference between the official rate at which he had accepted the sovznaks and the market rate at which he converted them into chervontzy. To avoid this loss, he would estimate at the beginning of a business day the loss on the exchange of sovznaks that he was likely to sustain within the next twenty-four hours and mark up the prices of his wares proportionately.[22] This method of raising prices in anticipation of future depreciation was instrumental in bringing about an acceleration of the sovznak's rate of depreciation, and in that manner, created difficulties for the state treasury.

When, for one reason or another, the burden of the emission "tax" [23] had not been shifted to the consumer, the loss was borne in the first instance by the business itself, and was shifted by it, in one way or another, to the state budget. It is, for instance, estimated that between October, 1923, and February, 1924, the state-

[22] Yurovsky, p. 95.

[23] The employment of the word "tax" for the purpose of expressing the burden imposed upon the users of paper currency during an inflation cannot be said to be sanctioned by general use. Horace White (*Money and Banking*, p. 103), for instance, considers such use inappropriate in view of the fact that the word is derived from the Latin *taxare*, "to value" or "to appraise." "It presumes," he says, "a methodical arrangement of the taxable persons so that justice shall be done and each shall know what he has to pay." It may be said, however, that if the qualities mentioned by him are present, then the tax is a just, good tax, and when they are lacking the tax is an unjust, bad tax. Indirect taxes generally fall heavily upon the poorer classes and, furthermore, those upon whom they fall do not know in advance the amount that they will be called upon to pay out, and yet the word "tax" is generally employed there.

owned and subsidized railways alone, notwithstanding the fact that they carried chervonetz-standard accounts, lost on the exchange of sovznaks over 10,000,000 gold rubles, a very substantial sum in those days.[24]

By the end of 1923 calculation of costs, prices, and, in fact, bookkeeping itself became exceedingly involved. The flight from the sovznak was then entering a new, advanced stage, and as everyone strove to make payments in that currency, in order to get rid of it, but hoarded (or speculated in) chervontzy, the "good" chervontzy became displaced from circulation as a medium of exchange by the "bad" sovznaks.[25] Accordingly, prices, although quoted in chervontzy, had to be converted at the *official* rate of exchange into sovznaks in which they were payable. Further calculations and computations followed upon the sovznaks' being exchanged for chervontzy at the *market* rate of exchange. Accounts had to be entered in terms of both currencies with a final conversion into chervontzy. Special records of the exchange transactions had to be maintained, and at least some method devised to make it difficult for employees to manipulate such transactions.

[24] Katzenellenbaum, *Russian Currency and Banking 1914–24*, p. 125. According to Yurovsky (*op. cit.*, p. 97), the combined monthly exchange losses of the Commissariats of Finance, of Transportation, and of Posts and Telegraphs exceeded 7 to 8 million rubles.

[25] Compare Dr. Alexander Schick, *Das Sowjetbankwesen und die Rolle der Banken in der Sowjetwirtschaft* (Ost-Europa Verlag, Königsberg, 1932), p. 33. Dr. Schick, in commenting on the downfall of the Soviet ruble (sovznak), makes the following interesting statement: "So verdrängte allmählich der 'gute' Tscherwonetz die "schlechten" Sowjetrubel, wobei, wie so manches im Sowjet-Russland, auch in diesem Falle die bisher bestehenden Gesetze der Nationalökonomie anscheinend umgeworfen wurden, indem das Gresham Gesetz auf den Kopf gestellt wurde." Dr. Schick apparently meant to emphasize the fact that the introduction of the chervonetz and the adoption of the method of calculating in "stable" chervontzy hastened the depreciation of the sovznak and doomed it to extinction, and that eventually when hyper-inflation reached its peak, threatening to disrupt the national economy, the "bad" sovznak was removed from circulation and the "good" chervonetz survived and remained the principal currency. As previously stated, Gresham's Law applies to metallic and not to paper currencies. Nevertheless, it is an incontrovertible fact that by the end of 1923 the "bad" sovznak had displaced the "good" chervonetz as a medium of exchange, the "good" chervonetz being used as a store of value. Accordingly, even if Gresham's Law be applied to the "bipaper" standard as it had operated at the end of 1923 and at the beginning of 1924, one sees no justification for the statement that the above law had been overthrown. See Finance—Economic Bureau, *Review of the Work of the Commissariat of Finance during October 1, 1923, to April 1, 1925* (Moscow, 1925), p. 188.

It will be recalled that the placement of the various economic units on a commercial, profit-making basis constituted one of the major aims of the New Economic Policy. That aim was now being defeated, for operating on a paying basis presupposes the ability to calculate accurately one's cost, something that the conditions mentioned were rendering impossible.

As a matter of fact, the devising of ways for the prompt riddance of sovznaks in those days was by many considered more important than cost calculation. Indeed, an hour's difference in the purchase or deposit of chervontzy meant a gain or a loss as high as five percent or even more. Speculation in currency, whether on the official or semi-official exchanges or even on street corners, expanded to a point where it could be said to have become nation-wide. This was, on the one hand, prompted by the disparity between the official and market rates—a characteristic which, as we have seen, is as true of the "bipaper" standard as it is of the bimetallic; and on the other, by the existence of a time interval between any two consecutive official quotations during which holders of currency anticipate an upward revision of that rate—a characteristic which is peculiar to the "bipaper" standard as it existed in Soviet Russia. The fact that small towns lacked facilities for such exchange and that as a result various enterprises and organizations located in them were sending their men for that purpose to large centers, such as Moscow, could not but intensify the speculative activities in such centers.

As had been stated before, the losses suffered on account of the depreciation of the currency by the various state-owned enterprises and institutions were being shifted by them to the state treasury and this served to cause a diminution in the latter's revenue from the emission tax. Furthermore there appeared to be a serious diminution in the yield from the state's chief source of revenue, the agricultural tax. This was due to the fact that the peasantry, who had the option of paying that tax either in kind or in currency, found it more profitable to pay it in the latter. Although, beginning with November, 1923, the government began to fix the cash equivalent of the agricultural tax in chervontzy, the tax itself, in order that a demand might be main-

tained for the sovznaks, was made payable in the latter currency. Inasmuch as there was a lapse between the time at which the sovznaks were collected in the remote villages and the time when they actually reached the central office, the government was bound to sustain an appreciable loss on the revenue it thus collected. An investigation by three commissariats (the Commissariats of Workers' and Peasants' Inspection, of Supplies, and of Finance) into the causes for the diminution of revenue from the agricultural tax disclosed that by the time the sovznaks reached the central office their purchasing power had already undergone a depreciation of 20 percent and even more.[26] The loss, of course, did not terminate there, for the receipt of revenue by the government did not necessarily synchronize with its expenditure. Besides this loss, which was serious enough in itself, the government had yet additional cause for alarm, inasmuch as those conditions prevented the accurate planning of the budget.

Moreover, if, by allowing the peasantry to substitute taxes in money for those in kind, the government had hoped to arrest the catastrophic decline of the sovznak's purchasing power through the resulting increased demand for paper currency, it was now quite clear that these hopes failed to materialize. For, although the demand for the sovznaks did increase as a result of such policy, the gain was of little or no consequence, inasmuch as the users of that currency, especially by the end of 1923, began to take measures to eliminate the costly lag between its receipt and expenditure, and in that manner caused the velocity of its circulation to increase spectacularly.

If it be also remembered that the chervonetz, the relatively stable currency on which so much was staked, had already depreciated considerably and was showing unmistakable signs of further weakness, it becomes patent that the monetary outlook of the Soviet Union by the end of 1923 was dark indeed.

[26] Kuzovkov, *op. cit.*, pp. 243 ff.

IX

THE MONETARY REFORM OF 1924

The eve of the Monetary Reform.—By the end of 1923 dark clouds began to gather once more over the financial and political skies of the Soviet Union. The peasants, caught between the upper and the nether stones of hyper-inflation and price distortion ("scissors"), began to refuse to accept the sovznaks and to limit to a minimum exchange transactions with the towns. This served, on the one hand, to step up most catastrophically the rate of the sovznak's depreciation, thus threatening the usefulness of the printing press as a source of revenue for the state, and, on the other, to undo the very thing which Lenin hoped to accomplish through the adoption of the New Economic Policy, namely, the promoting of a close tie (*smychka*), or a *rapprochement*, between the villages and the towns. The chervontzy, the stability of which the government considered very important, showed unmistakable signs of further weakness. All this boded the national economy no good.

Experience with various palliatives during the preceding years convinced the government that measures of a more fundamental character were needed, measures that would *eliminate* the "scissors" crisis and the instability of the currency rather than *mitigate* their evils. The measures adopted, as well as those which were rejected, were, of course, shaped by the postulates and preconceptions of their authors.

In dealing, for example, with the "scissors" crisis, the government proceeded with measures which were intended to facilitate a decline in industrial and a rise in agricultural prices. The decline in industrial prices was brought about by: (a) the tightening of credits granted to industry by the State Bank; (b) the creation of a new agency, a Committee of Domestic Trade with powers to set maximum prices; [1] and, finally (c) the importation of manu-

[1] Particularly beginning with 1924.

factured goods from abroad at lower prices, thus by underselling the trusts and syndicates compelling them to reduce prices. The government, however, could not make full use of the latter weapon. The stabilization of the currency necessitated the creation of a favorable balance of payment, hence imports had to be reduced to a minimum. Besides, it was necessary to import machinery and raw materials.

To bring about a rise in agricultural prices the government proceeded to grant more liberal credits to the grain-purchasing agencies, to pay higher prices for grain, and to stimulate the export of grain.

These measures, as shown by the official index numbers, proved effective in closing the blades of the "scissors." On October 1, 1923, when the agricultural price index calculated in chervontzy stood at 0.9, the industrial price index, it will be recalled, registered 2.8. On November 1 of the same year those indices stood at 0.9 and 2.4, respectively. On January 1, 1924, they stood at 1.2 and 2.3; on February 1, at 1.5 and 2.3; on March 1, at 1.7 and 2.2; and on January 1, 1925, at 1.5 and 1.9. By the middle of 1925 the two stood almost 1.9 to 1.9, but thereafter industrial prices once more took the lead.

The official approach to this problem was met by a strong opposition movement on the part of an influential minority group within the Communist Party. Affiliated with this group were such men as Trotsky, the economist Preobrazhensky, Ossinsky, and Piatakov. They denied that the "scissors" crisis was caused by a combination of such forces as the enjoyment of monopoly privileges by the industrial enterprises, together with the granting to them by the State Bank of liberal credits against commodities as security and the consequent withholding of commodities from the market. According to them the chief cause of the crisis was the underdevelopment of industry. To solve the problem, they argued, it was, therefore, necessary to rehabilitate and to expand industry. To accomplish this they would grant larger credits and subsidies to industry and would improve the system of economic planning. Furthermore, they held that it was necessary to permit the industrial enterprises to charge high prices so as to enable them to

accumulate the capital needed for their expansion.[2] They consequently opposed the government's policy of aiding the peasantry by means of raising agricultural and depressing industrial prices. Believing that the Commissariat of Finance was responsible for the official point of view, members of the minority proposed that control over the granting of credits and the allocation of budgetary subsidies and grants to industry should be transferred from it to the State Planning Commission (Gosplan), a number of members of which were in agreement with their views. It was proposed that the State Bank become a bankers' bank and that the long-term financing, as well as the short-term crediting, of industry should be transferred from the State Bank to the Industrial Bank which was under the jurisdiction of the Supreme Council of National Economy, in whose hands lay control over industry. The State Bank, as a matter of fact, had been denounced by the "industrialists" on a number of previous occasions as being "autocratic" and "dictatorial." It was, in fact, in response to the demand from the industrialists who were dissatisfied with the conservative credit policy of the State Bank (the latter made strenuous efforts to protect its notes from depreciation and so was not eager to exercise its right of issue for the purpose of providing industry with basic working capital or with fixed capital) that the Industrial Bank had been established a year earlier—in October, 1922.

It is not difficult to see why the government resolved to act as it did, and why Trotsky and others in the minority group sought to oppose those acts. The difference of opinion, as has earlier been intimated, was the result of a difference between the postulates and preconceptions of the two groups. Lenin, for example, believed that the workers could not retain power without the support of the lower and middle strata of the peasantry. His followers, accordingly, realizing that the situation was intolerable and knowing from the past that the peasants' fountain of patience was not inexhaustible, lost no time in urging the introduction of necessary correctives. Trotsky, on the other hand, was the author of a

[2] In general they maintained that the inordinately high price level could be brought down by closing all enterprises that were in deficit and by importing commodities from abroad. The commodity famine and lack of gold rendered such advice impractical.

theory known as "permanent revolution." According to that theory, to build socialism in a country, the proletariat upon seizing power must keep on waging a class struggle not only against the bourgeoisie but against the "broad masses of peasantry" as well. Its success in a single country (particularly in a backward, agricultural country like old Russia) is possible only on condition that similar victorious revolutions take place in the more advanced countries.[3] Another prominent member of the opposition, Preobrazhensky, the economist of the opposition movement, stated in his *Fundamental Law of Socialist Accumulation*[4] that in a backward, proletarian country the position of state industry amid private enterprises is very much like that of an islet surrounded by a vast sea. Its existence is threatened unless its size can be substantially increased. To change the metaphor, if state industry is to command an impregnable position (and without that the building of socialism is impossible), a substantial increase of its size is imperative. That, of course, requires capital. Barring loans from abroad, the accumulation of capital in Soviet Russia could come from surplus production of industry and from the "exploitation" by the latter of the private sector of the national economy. And so we have a picture of the "metropolis" (state industry) exploiting the "colonies"—the peasantry and the rest of the private sector.

Apparently, then, this group was not expected to favor the peasantry. In fact, they held that the ratio of interchange between agricultural and industrial commodities had to be, for the time being at least, such as to favor the trusts.

While in general not devoid of logic, the reasoning of the opposition, when applied to the situation then at hand, was anything but objective. Applied in the "short run" it would have proved disastrous, for there can be no doubt that the peasantry would refuse to part with present goods in return for a promise of compensation when industry would have become more prolific. The

[3] Leon Trotsky, *The Permanent Revolution* (New York, Pioneer Publishers), *passim;* Bertram D. Wolfe, *The Trotsky Opposition* (New York, Workers Library Publishers, 1928), pp. 7-40.

[4] *The Herald of the Communist Academy,* VIII; Dobb, *Russian Economic Development since the Revolution,* pp. 260 ff.

thirteenth Party Conference (which assembled in the middle of January, 1924) rejected the opposition philosophy and approved the official policy of lowering industrial prices. This was not enough. As has been explained, the peasantry began to refuse to exchange their produce for the sovznaks and this served as a catalyst in hastening the already too speedy process of their depreciation with all the consequent dangers. The Commissar of Finance, Sokolnikov, on December 5, 1923, warned the country of the danger of postponing the change to a stable currency:

> The chief danger with which we are confronted at present does not lie in the fact that we shall lose the sovznak, but in the fact that we may not find in ourselves enough wisdom and strength to renounce it in time. . . . Should we fail to do it, the disintegration of the currency circulation will be such as to make it considerably more difficult for us to extricate ourselves. Then we will no longer have the consolation that our currency circulation consists in part of a stable currency, for the instability and agony of the sovznak will lead to such distortion of prices and to such perturbation in all the market price relations as directly to put a stop to the use of the method of calculating prices in terms of gold; and the cessation of calculating in terms of gold, the formation of all kinds of lags between the official calculations in terms of gold and the real gold values, between real chervontzy [that is, the real value of chervontzy.—Author] and the rates at which they are quoted, etc., will result in the delivery of a most vital blow to the chervonetz itself.
>
> I am not going to dwell on the reasons which make it advisable to renounce the sovznak in time, the example of Germany is before us. Germany went so far in the matter of depreciating her paper currency as to render extremely difficult any attempt to get out of that situation even from a purely financial point of view, let alone political and economic factors.[5]

Sokolnikov thought that only a thoroughgoing monetary reform could remedy the situation. The re-establishment of a stable currency, however, necessitates such measures as the balancing of the budget and the striking of a favorable balance of international payments. The former, so as to obviate the necessity of using the printing press as a source of revenue; and the latter, so as to pre-

[5] Sokolnikov, "From the Monetary Token to a Stable Currency," *The Monetary Reform,* pp. 11-12.

serve and build up the gold reserve of the country. The application of these measures, however, is by no means a painless process. The balancing of the budget generally involves a reduction of state expenditures and outlays and a burdensome increase in taxation, while the favorable balance of payments generally means a reduction of imports. Applied to state industry, it threatened at least a temporary curtailment, or even complete elimination of state subsidies and grants, a restriction of credit, and a reduction in necessary raw materials which were being imported from abroad.

Plans for balancing the budget and for pulling the country out of the inflationary quagmire had been offered by Sokolnikov a year earlier (in December, 1922, at the tenth Soviet Congress) and had come to grief on account of the opposition to the proposed measures.

It should not be surprising, therefore, that his proposals in 1923 for the re-establishment of a stable currency evoked a great deal of criticism. Particularly if one remembers the tenets of the "opposition" philosophy. The piling up of gold in the coffers of the State Bank and of the Commissariat of Finance, it was argued, was a luxury which the Soviet Union could not and should not afford. Gold should be used for the purpose of building up industry and not for the purpose of piling up reserves. A favorable balance of trade, it was said, would injure industry, and foreign trade and, in fact, the whole problem of currency stabilization had better be subordinated to the interests of state industry. That foreign trade policy and plans for currency stabilization should be shaped so as to promote the best interests of the economic system is a platitude requiring no proof. In general, however, the opposition's stand on this question was quite unsound. The opposition failed to grasp that a sound currency was a prerequisite for the rehabilitation of that system, and that the sacrifices which the establishment of such currency demanded would be well rewarded in the end.

The Central Committee of the party at the opening of 1924 gave its approval to the official point of view. In its resolutions in a section fittingly entitled "Practical Conclusions" is found a

demand for the "transition to a stable currency; discontinuance of the issue of unstable sovznaks; the issue, not later than in the spring, in connection with the reform of the agricultural tax, of a stable currency in denominations lower than the chervonetz as well as of silver coins." [6] And in the middle of January, 1924, Sokolnikov submitted to the Central Committee of the party a memorandum in which he had charted the course of a proposed reform of the currency. It contained the following points:

1. The treasury is to issue notes in denominations lower than the chervonetz.

2. Their value is to be fixed in gold on the basis that one gold ruble is equal to one-tenth of one chervonetz.

3. The above parity (one gold ruble equaling one-tenth of one chervonetz) is to be established and maintained by banking measures.

4. The issue of treasury notes is to be kept within limits that are prescribed by the usual ratio between notes of a larger denomination (of one chervonetz and over) and those of a smaller one (below one chervonetz) in circulation. This ratio is to be fixed by the law as being two-thirds and one-third, respectively.

5. Treasury notes of higher denominations are to be introduced first, preferably in the course of changing chervontzy for such notes.

6. To supply the need for currency of denominations of one ruble and less, there are to be issued silver coins the legal parity of which is fixed in the following manner: one ruble in silver equals one ruble in gold.

7. Silver coins of 10, 15, and 20 copecks are to be introduced first; these are to be followed by 50-copeck pieces and, finally, by silver rubles.

8. The total of silver coins that are to be placed in circulation by January 1, 1925, is to be fixed at the minimum of 100,000,000 rubles. Should technical difficulties prevent the minting of such amount by that time, paper tokens ("bons") of equal denominations and within the above limitations are to be employed, but these latter are to be redeemed upon demand after January 1, 1925, in silver.

9. To supply the need for still lower denominations, there are to be issued coins in the denominations of 1 to 5 copecks. At first their place is to be taken by paper tokens.

10. The curtailment of the emission of sovznaks is to begin as soon

[6] *Economic Life,* January 10, 1924.

as treasury notes are placed in circulation. Those emissions are to be entirely discontinued as soon as treasury notes amounting to 25–30 million rubles are placed in circulation (which will exclude the possibility of a small-change crisis).

11. The rate at which the sovznaks are to be redeemed is to be fixed after the silver coins are issued and the "silver count" adopted by the free retail trade.

12. The redemption of the sovznaks is to be carried out in two ways: (a) through the retention by the Commissariat of Finance and by other institutions of whatever sovznaks they get, and the employment by those institutions of the new type of currency for whatever payments they have to make; (b) through the direct exchange of the sovznaks for the new currency on the basis of the established redemption rate, when the former are presented for that purpose by the public.

13. The commodity ruble as a standard of payment is to be discontinued. Only those agreements and transactions which are expressed in gold (chervontzy) are to be considered valid.

14. The issue of silver coins and treasury notes for the purpose of defraying budgetary deficits must not exceed the set limit of 15,000,000 rubles per month.

15. The regulation of commodity prices is to be achieved by means of price-fixing measures, as well as by means of the concerted steps of the commercial and industrial organs directed towards the stabilization of normal prices.[7]

These points were enacted into law. But before we turn to the laws, let us ascertain the extent to which the premises underlying a successful currency reform had been realized in the Soviet Union at that time.

First, with respect to the budget. This continued to be unbalanced and there was no hope of balancing it in 1923–24 without the aid of the printing press. The Commissariat of Finance estimated that the note issue required during that year for fiscal purposes would amount to 180,000,000 gold rubles (which constituted 10.6 percent of the total estimated revenue, and 47 percent of the estimated deficit). The budget, however, was showing signs of steady improvement. It will be recalled that during the fiscal year 1922–23 (that is from October 1, 1922, to September 30,

[7] Sokolnikov, *The Monetary Reform*, pp. 173-75.

1923) the budgetary deficit amounted to 461,300,000 gold rubles and that this deficit had been covered by note issue to the amount of some 375,000,000 gold rubles (or 81 percent of the deficit), and by public credit to the extent of the difference. But, whereas at the beginning of that year 95.8 percent of the deficit had been covered by note issue and but slightly more than 4 percent by loans, towards the end of the year only 54 percent of the deficit was covered by note issue, and about 46 percent by loans. During 1923–24 the budgetary deficit amounted to 375,200,000 gold rubles and this had been met by note issue to the extent of 150,700,000 (or 40.1 percent of the deficit), by loans to the extent of 194,800,000 (or 51.9 percent of the deficit), and by the issue of subsidiary coins to the extent of 29,700,000 (or 8 percent of the deficit).

The improvement of the budget was made possible by the gradual improvement of general economic conditions over the few years following the introduction of the New Economic Policy. Thus, coal production, which in 1913 amounted to 28,900,000 tons and in 1921–22 was only 9,600,000 tons, rose to 16,000,000 tons in 1923–24. The production of crude oil, which in 1913 amounted to 9,200,000 tons and in 1921–22 to 4,500,000 tons, climbed in 1923–24 to 6,100,000 tons. The output of iron ore, which in 1913 amounted to 9,200,000 tons and which in 1921–22 was but 179,000 tons, increased in 1923–24 to 947,000 tons. The production of pig iron, which in 1913 was 4,200,000 tons and but 173,600 tons in 1921–22, advanced to 653,000 tons in 1923–24. The production of steel, which in 1913 amounted to 4,247,000 tons and in 1921–22 to 316,100 tons, rose to 991,000 tons in 1923–24. The production of cotton yarn, which in 1913 was 262,000 tons and in 1921–22 but 50,000 tons, rose to 102,000 tons in 1923–24. The production of finished cotton cloth, which in 1913 amounted to 2,238,000,000 meters and in 1921–22 to but 337,000,000 meters, rose to 836,000,000 meters in 1923–24. The average daily freight-car loadings, which in 1913 amounted to 33,000 cars and in 1921–22 to but 9,600 cars, rose to 13,500 cars in 1923–24. The increase in freight-car loadings reflected the increase

in the output of the basic industries, consumers' goods, and a consequent increase in trade turnover.[8]

The economic situation at the time of the Reform, as seen from the above picture, was pitiable. It held out hope, however, inasmuch as the situation showed signs of steady improvement. These were of no small importance in emboldening the Commissariat of Finance to carry through a currency reform while the budget was still unbalanced. As we have seen, the Commissariat planned to cover the budgetary deficit for the fiscal year 1923–24 in part by an issue of paper money equal in value to 180,000,000 gold rubles. It felt that, although in a static society such an expansion of the volume of currency would exercise an inflationary influence and, therefore, constitute a danger, this was not likely to be the case in the Soviet Union, where the expansion of industries and trade—particularly when stimulated by the introduction of a sound currency—would serve to create a demand for the additional currency and in that way eliminate its menace. A widening of the demand for currency was also expected to come as a result of the Agricultural Tax Reform of 1923–24, which, among other things, was to abolish, beginning with January 1, 1924, all taxes in kind and substitute in their stead money payments, at the same time transferring the collection of such taxes from the Commissariat of Food Supplies to the Commissariat of Finance.[9] It was also felt that the confidence which the new measures were bound to engender would cause a decrease in the velocity of currency circulation and consequently create an additional demand for currency. Finally, it may be added that the Commissariat of Fi-

[8] The above figures were taken from the following sources: *Works of the Central Statistical Bureau* (Moscow, 1922), VIII, Section III, 64 ff.; *Compiled Statistical Information for 1918–23* by the same Bureau (Moscow, 1924), p. 203; and its *Statistical Yearbook* for 1924 (Moscow, 1926), X, Pt. VIII, Section 1, 192 ff. Also *The State Bank of the U.S.S.R., 1921–26* (Moscow, Financial and Economic Research Bureau of the State Bank of the U.S.S.R., 1927), pp. 6 ff.; and the *Economic Conditions of the U.S.S.R. and World Economic Conditions in 1925–26,* by the Institute for the Study of Economic Conditions, N. D. Kondratiev, ed. (Moscow, The People's Commissariat of Finance, 1927), tables following p. 256. The figures given in the various sources differ somewhat.

[9] P. P. Hensel, *Taxes in the U.S.S.R.* (Moscow, The People's Commissariat of Finance of the U.S.S.R., 1926), p. 75; also *Collected Decrees,* 1924, Decree 158.

nance was convinced that the increase in the tempo of economic recovery, which was likely to come as a result of the stabilization of currency, would serve to create additional revenue for the state and so help to balance the 1924–25 budget.

Foreign trade being a state monopoly in the Soviet Union and controlled by plan, the Commissariat of Finance figured on a favorable balance for 1923–24. By restricting imports and increasing exports the Soviet Union, as may be gleaned from Table 30, was able to create in that year a favorable balance of 139,700,000 (gold) rubles.

TABLE 30

FOREIGN TRADE OF THE U.S.S.R.
1918–1927/28 [a]
(*In millions of rubles*)

	1913	*1918*	*1919*	*1920*	*1921*	*1922*
Exports	1,520	8.1	0.1	1.4	20.2	81.6
Imports	1,374	105.2	3.2	28.7	210.7	269.8
Balance	+146	−97.1	−3.1	−27.3	−190.5	−188.2

	1923–24	*1924–25*	*1925–26*	*1926–27*	*1927–28*
Exports	373.2	577.8	703.3	806.8	791.6
Imports	233.5	723.4	756.3	713.6	945.5
Balance	+139.7	−145.6	−53.0	+93.2	−153.9

[a] Chief Department of Customs, *Foreign Trade of the U.S.S.R. for 1918—1927–28 Statistical Review* (Moscow, 1931), pp. xvi-xvii.

Although the hopes of the Commissariat of Finance, as shown by the march of later events, fully materialized, the risk was great and predictions of failure were not lacking. The government was cautioned to postpone the Reform at least until the fall months (of 1924) when the crops would be moved, the 1923–24 agri-

cultural tax would be paid in money, the trade turnover would increase, and when the demand for currency, therefore, would widen. It is undeniable that, all other things being equal, the fall months were better suited for the introduction of the Reform than were the spring months. Such advice, however, postulated a state of affairs where the government had much choice in the matter. The chairman of the Council of Labor and Defense, Kamenev, was most explicit on this point when addressing, on February 29, 1924, a joint meeting of the Moscow Central Committee of the party and of representative party workers. "We can not wait weeks," he declared, "let alone months. The peasantry refuses to sell grain to the state for sovznaks. The sovznak is depreciating with catastrophic rapidity." [10]

At the time of this address, however, the Monetary Reform was already in full swing. Let us, therefore, acquaint ourselves with the legislative measures involved.

The Introduction of the Monetary Reform of 1924

The issue of new treasury notes. The decree of February 5, 1924.[11]—Of a series of decrees promulgated by the government in 1924 and looking toward a monetary reform, that of February 5, 1924, was the first. By its terms the Central Executive Committee and the Council of People's Commissars of the U.S.S.R. ordered the introduction into circulation of a new paper currency, *state treasury notes* (*gosudarstvennye kaznacheiskie bilety*), in the denominations of one, three, and five "gold" rubles. The new treasury notes were accorded the right of legal tender. Their amount in circulation was to be governed by the requirements of trade. As a precaution against overissue and inflation, their amount on the first of any month could not exceed one-half of the total amount of chervontzy in circulation on the same date (after deducting the debt of the treasury to the State Bank).[12] As an additional precaution it was ordered that the determination of

[10] *Economic Life,* March 1, 1924.

[11] Decree 288.

[12] By later decrees this law was amended to permit the volume of treasury notes in circulation to equal at first 75 percent and then 100 percent of the volume of banknotes (chervontzy) in circulation.

the size of each separate issue of treasury notes should rest with the Council of Labor and Defense. The People's Commissariat of Finance, the agency entrusted with the issue of those notes, was required to publish monthly statements on the amounts of notes so issued.[13]

The decision to fix the ratio between the volume of treasury notes and chervontzy at 1 to 2, or, what is the same, at 33 1/3 percent to 66 2/3 percent, was influenced by the relationship in circulation then existing between denominations below and above ten rubles.[14] In pre-war years the volume of money in denominations below ten rubles constituted approximately 40 percent of the total money in circulation. The rise in the price level since that time justified to a certain extent the tipping of the scales in favor of the higher denominations.

The link between the treasury note and the banknote.—Uncertain of the outcome of the Reform and anxious to protect the good name of the chervontzy, the government in its decree of February 5, 1924, made no mention of the relation between the latter and the new fiduciary currency. But a few days after the publication of that decree, on February 9, the State Bank instructed all of its branches to exchange chervontzy for treasury notes freely and gratuitously, on the basis of one unit of the former to ten rubles of the latter. It further ordered the accept-

[13] Beginning with 1925 the State Bank assumed the issue of those notes as well as of coins (in addition to its own banknotes). It is carrying out those functions, however, merely as an agent of the treasury and in the latter's name.

[14] By February 15, 1924, the total amount of means of payment was estimated (in chervonetz-rubles) to equal 403,900,000 rubles. Its composition was as follows: banknotes, 268,900,000 rubles (or 66⅔ percent of the total); sovznaks, 39,600,000 (9.8 percent); treasury notes, 10,600,000 (or 2.6 percent); transportation certificates, 17,300,000 (or 4.2 percent); treasury obligations, which were used as money, 67,500,000 (or 16.7 percent). See Zheleznov, "The Course of the Monetary Reform," *Vestnik Finansov,* Nos. 4 and 5, 1924, p. 2. In carrying out those calculations the government statisticians failed to take into consideration the velocity of circulation of the various types of money. The sovznaks, however, circulated with a far greater velocity than the other types of money. Because this factor was ignored, the resulting figures could not be regarded as representing the real relative importance of the sovznaks in circulation. S. G. Strumilin, in an article entitled "Velocity of Sovznaks" in the *Economic Life* of March 30, 1924, declares that as compared with pre-war norms the velocity of the banknote (chervonetz) was normal and that of the sovznak four times as high, and that the 40,000,000 sovznaks were therefore doing the work of 160,000,000 rubles. He does not show how he derived his figures. It was probably guesswork on his part.

ance of treasury notes, on the same basis, in payment of all obligations due it, and, in fact, in connection with all its transactions.[15] In a later circular (on February 27), the bank made it clear to its branches that they were to exchange not only chervontzy for treasury notes but also treasury notes for chervontzy, making certain that neither discounts nor premiums developed in the process of those exchanges.[16] It was in this indirect manner that the government had established a relation between the banknote and the treasury note.

Cessation of printing and of issuing Soviet tokens (sovznaks). The decree of February 14, 1924.[17]—By a further decree of February 14, 1924, the Central Executive Committee and the Council of People's Commissars ordered that "in view of the introduction into circulation of treasury notes . . . as well as on account of the contemplated issue of silver coins, the printing of Soviet monetary tokens (sovznaks) that are not expressed in stable units must cease, and their further issue by the Currency Department and the local offices of the Commissariat of Finance be discontinued beginning with February 15, 1924." Old supplies of notes, whether at the government printing shops, in the Currency Department, in the special funds of the local offices of the Commissariat of Finance, or in those of any state or private organization or enterprise, retained their legal-tender rights and were permitted to circulate until such time as the Council of People's Commissars published a decree relative to the redemption of that currency.

The minting and issue of silver and copper coins. The decree of February 22, 1924.—The next step with respect to the introduction of the Monetary Reform was taken on February 22 when the Central Executive Committee and the Council of People's Commissars instructed the Commissariat of Finance to begin to issue silver coins in denominations of 10, 15, and 20 copecks as

[15] Circular No. 10 of the State Bank, dated February 9, 1924. *Vestnik Finansov,* Official Section, Number 18, February 26, 1924.

[16] *Vestnik Finansov,* Official Section, Number 26, March 18, 1924.

[17] Decree 308. It is interesting to note that barely a week before this, on February 7, the Central Executive Committee and the Council of People's Commissars published a decree (294) ordering the issue of sovznaks of the 1923 pattern in the denominations of *25,000 rubles* (or 25,000,000,000 old rubles) *each.*

well as of half-rubles and rubles, and copper coins in the denominations of 1, 2, 3, and 5 copecks. To maintain parity between the new treasury notes and the metallic currency, one ruble in the latter currency was declared to be equal to one ruble in the former. Although the pay offices (kassy) of the Commissariat of Finance were instructed to accept these coins without any restriction as to their amount, their legal tender with respect to all other transactions was fixed in the following manner: in the case of silver coins of the denomination of one and one-half rubles the limit was fixed at 25 rubles, while in the case of all other silver coins, as well as in the case of copper coins, the legal limit was fixed at 3 rubles. Their weight and fineness remained the same as in the respective coins of the Czarist mintage.

In the matter of coinage and of regulation of metallic currency (save for the design, which was new, and for certain minor changes such as the omission of 5 and of 25 copeck pieces, etc.), there was, therefore, no difference between the rules laid down by the Soviet government and the corresponding statutes of the preceding regime.

The Commissariat of Finance was instructed to speed up the mintage of silver and copper coins with a view to increasing the amount in circulation by January 1, 1925, to not less than 100,000,000 rubles. Anticipating the difficulty which the Commissariat of Finance was likely to encounter in fulfilling that task, the decree empowered it to issue paper substitutes ("bons") in denominations of from 1 to 50 copecks in lieu of the metallic coins in case it proved impossible to supply the country with the needed amount of the latter. Such paper substitutes, however, could not be issued without the approval of the Council of Labor and Defense, and in any event had to be redeemed in coin, beginning with January 1, 1925. In order to emphasize that the treasury meant to maintain the amount of coin issued at a level determined by the needs of circulation rather than by the needs of the treasury, the Soviet government introduced a principle not contained in the Czarist coinage statutes, namely that the amount of silver and copper coin issued was to be regarded as a part of the

total fiduciary issue which the treasury was permitted to have by virtue of the law of February 5, 1924.

It was also provided that silver, and not paper, money was to be used to cover the anticipated budgetary deficit of 1924–25. Although the overissue of silver coins would ultimately produce an inflation no less intense than an overissue of paper money, yet it was felt that if silver alone could be issued for fiscal purposes, the cost of the metal would serve as a deterrent to overissue.

Despite the desire for a speedy introduction into circulation of a sufficient amount of subsidiary metallic currency, the above decree categorically proscribed the use of the old Czarist coins, of which large amounts were being hoarded within the country. This served to protect the treasury against loss from competition.[18]

The population, which for years had lived under a regime of depreciated paper money, at first took to hoarding the newly issued metallic coins. These coins, in consequence, kept on disappearing from circulation. It took some time before the people became convinced that the metallic coins were to be a permanent institution and before they began to pass the specie from hand to hand.

The redemption of sovznaks. The decree of March 7, 1924.[19]— Although the further issue of sovznaks had been stopped, they continued, nevertheless, to circulate in the meantime as legal tender. Usually, it is found advisable to stabilize prices at a desirable level first and only then to proceed with fundamental monetary reforms. That, however, was not the course followed in the Soviet Union. There, as has already been shown, the Reform had been undertaken while the budget was still unbalanced, a circumstance which rendered impossible the stabilization of the price level. It was, of course, possible to begin the Reform with the announcement of the rate at which the redemption of sovznaks would be carried out. Indeed, the government was urged by some to do so. It was maintained that once the rate of their redemption was declared and the holders of them thus protected against further loss, the velocity of their circulation would decrease and

[18] The importation of Czarist silver coins from abroad was prohibited by a later decree of May 19, 1924 (Decree 643).

[19] Decree 433.

their further depreciation would be arrested. Among the advocates of this procedure were representatives of state industry and trade who were anxious to put a stop to their losses on the exchange of the sovznaks. One reason why the Commissariat of Finance followed a different course was that it believed that its task of introducing a *new* paper money would be materially lightened by the presence of the unstable, troublesome sovznaks. Indeed, the people in their flight from the sovznaks were not long in overcoming their mistrust of a new treasury issue. Another reason why the announcement of the rate at which the sovznaks were to be redeemed came some time after the appearance of the new treasury notes rather than simultaneously with it is that the treasury was desirous to impress the people that this was not a repetition of the former devalorization "reforms." Then, too, the treasury, prompted by considerations of economy, wished to allow the sovznak to sink somewhat lower before it would undertake to redeem it.

Within the month following their introduction, the new treasury notes successfully penetrated into circulation. The treasury's confidence in its ability to raise revenue by means of the new currency increased. It was now ready to dispense with the sovznaks. Accordingly there followed the enactment of one more decree—that of March 7, 1924. Together with the three earlier decrees published in February this constituted what is commonly known as the Monetary Reform of 1924. By the terms of the decree, the Council of Commissars "in view of the penetration into circulation of stable currency and in order to bring about a complete cessation of the losses borne by the laboring masses and the national economy on account of the depreciating Soviet monetary tokens," ordered the removal of all unstable currency from circulation. The sovznaks, to be sure, were not removed at once. According to the terms of the decree they were to retain their legal-tender qualities until April 11, 1924, and the Commissariat of Finance and the State Bank were to continue receiving them in payment and for exchange until May 1, 1924. And by a subsequent decree of March 22, 1924, the Council of Commissars ordered that "in view of the shortage of currency of smaller

denominations, as well as in view of the fact that the people of the U.S.S.R. were insufficiently informed as to the dates on which the acceptance of paper money of the 1923 pattern as a means of payment and in exchange for new currency was going to cease," the legal tender of the sovznaks be prolonged until May 11, and their acceptance by the Commissariat of Finance and the State Bank in payment of obligations and in exchange for new currency, until June 1, 1924. The two latter institutions were instructed to cease reissuing the old currency so accepted by them beginning with April 25, 1924.[20]

The rate at which sovznaks were to be redeemed was fixed at 50,000 sovznak rubles of the 1923 pattern, or, what is the same (since a ruble of the 1923 pattern equaled 1,000,000 pre-devalorization or pre-1921 rubles), at 50,000,000,000 pre-1921 rubles for one ruble of the new paper money. The redemption was to begin on March 10, 1924. The 500-ruble note of the 1923 pattern was the smallest single note that could be presented for redemption, but even notes smaller than the above could be so presented provided they came in aggregates amounting to not less than the above amount. When so presented, the 500-ruble note of the 1923 pattern—the equivalent of 500,000,000 old rubles—entitled its bearer to the receipt of one copeck in coin. At this rate the three-quarters of a quintillion sovznaks in circulation on April 1, 1924 (762,308,342,167.25 rubles of the 1923 pattern or 762,308,342,167,250,000 old rubles) had a value of but 15,200,000 rubles in the new treasury notes.

The sovznak was in agony until March 7, 1924, the day on which the rate of its redemption was announced. Thereafter it might be said to have lapsed into a state of coma and expired without regaining consciousness.[21]

[20] Decree 434. A further extension was ordered for the benefit of foreigners when the government decreed on June 17, 1924 (Decree 761), that the State Bank through its foreign correspondents continue to redeem such notes, when presented by foreigners, until August 1, 1924.

[21] Speaking of the continental money of the American Revolution, David Ramsay (*History of the American Revolution*, II, ch. 17) says: "Like an aged man expiring by the decays of nature, without a sigh or a groan, the paper money gently falls asleep in the hands of its last possessor." Such description was probably intended for "gentle readers." If the paper money (continental currency and sovznaks) can

By June 1, 1924 (when the Commissariat of Finance and the State Bank stopped accepting them in payment and for exchange), the sovznaks, to use Sokolnikov's expression, "passed into the realm of history." It is to be regretted that copies of that history, with the moral "let that be a lesson to you" emblazoned in the boldest type possible on the front page, had not been sent to the four corners of the earth.

The sovznaks did not leave this world unsung. There were the usual funeral orations with words of praise by those who make virtue of necessity. Commenting on the "very good" deeds accomplished by the "very bad" money, Sokolnikov said:

> . . . Really, the "sovznak regime" of currency circulation meant the retention of the printing press in the capacity of a miraculous remedy which, at the expense of a permanent deterioration of the state of currency circulation, was permitted to cure open wounds and to stop up scores of holes in the state apparatus and economy.
>
> During the first years of the revolution "poor finance" was indeed a necessary condition to a "good revolution." . . .
>
> But at present . . . the financial strengthening of the Soviet state is, naturally, a necessary condition to a firm rule, to an ability to insure the defense of the country, keep up an administrative machine, provide for the cultural needs. . . . The strengthening of a currency at a given moment becomes a necessary condition to the strengthening of power.[22]

Other measures.—The above legislative measures, it will be noticed, incorporated the basic measures outlined in Commissar Sokolnikov's memorandum. That memorandum made mention of certain other auxiliary measures, such as the discontinuation of the use of the "commodity ruble" and the regulation of commodity prices.

The discontinuation of the "commodity ruble."—There were

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be said to have aged, it aged prematurely because of a very unhappy life, and the analogy with an aged man expiring by the decays of nature is, therefore, unreal. Too, there were plenty of "sighs" and "groans," figuratively speaking, on the part of the paper money, and most certainly on the part of its users. While the paper is still "alive" it is being thrown by the people in their flight from it from one hand to another with such rapidity that it is not given a chance to breathe, let alone to fall asleep "gently." It is difficult to conceive of this as constituting a peaceful end.

[22] Sokolnikov, *The Monetary Reform*, pp. 87-88.

several reasons for recommending the discontinuation of the "commodity ruble." To begin with, the "commodity ruble" owed its existence in the Soviet Union to the highly unstable currency. It had been introduced, it will be recalled, in an effort to mitigate the stifling effect of the disintegrating currency upon the national economy. It was, therefore, associated, in the minds of the people, with bad money. Its elimination, then, was important for psychological, if for no other reasons. In addition, it was maintained that its use served to disguise inflation and obscure the importance of a stable currency, and that, besides, it made accounting difficult. At any rate, the Council of Labor and Defense by its ordinance of February 29, 1924, prohibited, beginning with March 1, 1924, the employment of that device in connection with contracts, agreements, and the fixing of prices and rates.[23] By a special order issued on the same day, the Council of Labor and Defense laid down the rules that were to be followed in changing the basis of wage agreements from the "commodity ruble," in terms of which they had been drawn since the day when it was introduced, to the gold (that is treasury note) ruble.

Stabilization of the price level.—When a country, which for a time has lived under a regime of depreciated paper currency, wishes to return to a stable metallic currency it must decide upon the metallic content of the new monetary unit upon which its currency is to be based. Is it to contain as much gold as the old unit had, or less? Now, this problem is not as simple as it may seem at first.

In order to uphold its prestige and to promote confidence in its financial stability, a country will, of course, be tempted to restore the old unit.[24] Let us assume that it does so and that the old mint par is, therefore, re-established. The level of prices in a country which has lived under a regime of depreciated paper

[23] Decree 341; also Yurovsky, *Currency Problems and Policy of the Soviet Union*, pp. 135-36.

[24] Speaking of the post-war stabilization of the monetary system in England, R. G. Hawtrey (*Currency and Credit*, 1923, p. 389) says: "If our currency is again restored, as in 1819, to its ancient gold value, this settlement will command more confidence than any other. If its gold value were changed once it might be changed again. A return despite difficulties to the former parity is a pledge of stability."

money is likely to be higher than in a country or countries on the gold standard. The relatively high prices make that country a good place for the sale of foreign merchandise and services and a bad place for the purchase of commodities and services by foreigners. But this would lead to an unfavorable balance of payments and unfavorable exchange rates, and as a result the country would be drained of gold, the reserves would become depleted, and control would be lost over the external and internal value of the monetary unit. It is plain that this problem is closely interlaced with the problem of relating internal prices to prices in a gold-standard country. If a country wishes to restore the old unit it consequently must stand ready to lower or deflate its prices to a level which will insure an equilibrium between these prices and the prices in a gold-standard country or countries. Deflation and falling prices, however, result in a diminution or elimination of profit margins, and this in turn leads to a decrease of business activity, depression, unemployment, the impoverishment of the wage-earning and salaried classes, the saddling of the taxpayers with a heavy burden by requiring them to pay off in units of a much higher purchasing power a war debt which had been raised in units of a low purchasing power, and, in general, to an unjust distribution of wealth and income.[25]

The Soviet Union was not the only major country in the post-war period to face this problem. Such countries as England, France, Germany, Italy, and Austria, too, had to find solutions to this problem. All of them did not follow the same path.

England was one of the countries which re-established a monetary unit with the same gold content as the pre-war unit. In England, however, there was a relatively mild inflation.[26] After

[25] Drawing a comparison between inflation and deflation, Keynes says that inflation is unjust and deflation is inexpedient. Of the two (barring exaggerated inflation as in Germany, etc.), he considers deflation as being the worse because it is worse to provoke unemployment than to disappoint the rentier. He adds, of course, that both are evils and are to be shunned and that what is needed is a stable measuring rod of value. See his *Monetary Reform*, ch. 1.

[26] The peak of it was reached in April, 1920, when the *Statist* index of wholesale prices registered 313 (1913 = 100). By December, 1921, it fell to 157. Even in the U. S. the price index in May, 1920, stood at 247. The latter too underwent a drastic decline and by December, 1921, fell to 140.

a period of careful preparation, during which England achieved a balanced budget, reduced her floating debt considerably, funded her long-term debt to the United States, decreased the volume of currency and bank credit, and so forth, the gold standard was restored in that country in the spring of 1925.[27] The exchange rate, reflecting in part confidence in England's ability to restore the gold standard, climbed after the passage of the Gold Standard Act in May, 1925, from $4.25, where it had stood at the beginning of 1924, to $4.85, or almost to its pre-war parity.[28] The relative increase in the cost of sterling made English goods and services costlier to foreigners and so her exports shrank. Since the pound sterling now commanded more of the foreign currency in exchange and the holders of sterling could buy foreign goods more cheaply than before, her imports increased. At the time of the pound's stabilization, however, the price level in England did not equal that in the United States. The difference amounted to 10 percent, that is, a pound sterling bought in England about 10 percent less than $4.85 did in the United States, a circumstance that served to intensify the *adjustment crisis* by making purchases in that country by foreigners still less advantageous.[29] As a result there followed a decrease in business activity and an increase in unemployment. In their struggle for trade British exporters began to slash export prices. There followed drastic wage cuts. Since all prices are interrelated, domestic prices too fell. The wholesale

[27] The standard adopted in that country in 1925 was really a gold bullion standard rather than a gold standard. Only those possessed of an amount of notes to entitle them to the receipt of *at least 400 ounces* of gold bullion could obtain gold at the bank.

[28] To insure the stability of the exchange rates, arrangements were made by the British government with J. P. Morgan and Co., and by the Bank of England with the Federal Reserve authorities for the placement at their disposal of credits of $100,000,000 by the former and of $200,000,000 by the latter. Also the discount rate at the Bank of England was kept at 5 percent or 1 percent above the New York rate in order to protect the gold reserve. The high discount rate, however, served to swell costs of production and discourage business.

[29] On the other hand, in Germany at the time of stabilization the internal value of the reichsmark was considerably greater than its external value. Germany, in consequence, became a good market in which to buy and a poor one in which to sell; it experienced, in other words, a *stabilization boom*.—F. Cyril James, *The Economics of Money, Credit and Banking* (New York, The Ronald Press Co., 1930), pp. 88-89. D. H. Robertson, *Money* (Harcourt, Brace and Co., 1922), chs. vi, viii.

index, which in April, 1925, stood at 163, was 144 in March, 1926 (1913 = 100). The wage cuts, nevertheless, threatened to reduce wages by a larger percentage than that by which commodity prices were reduced. This, together with the increasing unemployment, served to embitter the workers against the employers and led to such events as the famous coal and general strikes of 1926. England, it would seem, therefore paid a high price for the privilege of restoring its currency from a depreciated value of $3.18 in 1920 to its pre-war par.[30]

A country which has undergone a relatively moderate form of inflation may instead select a different course of action when stabilizing its currency. Instead of *restoring* its currency to the old mint par and *deflating* its prices to the level prevailing in gold countries, it may decide to stabilize the currency at a level that is close to the value of its paper unit at that time. Thus, when Italy returned to gold in December, 1927, the new lira was given a gold parity of only 5.26315 cents (as compared with a pre-war parity of 19.3 cents), and the depreciated paper was redeemed not at par but at the rate of 3.67 old lire for one new lira. It was consequently unnecessary to deflate Italian prices all the way down to the level of American prices. The index of wholesale prices which during 1926 was in that country close to 700 (1913 = 100) was brought down to 535 in the last quarter of 1927.[31]

A course similar to Italy's was followed by France. When the franc was officially stabilized (in June, 1928), its new par of exchange was fixed at 3.92 cents as against the old mint par of 19.3 cents. The French index of wholesale prices during 1928 stood at 611 during the first quarter of the year; at 625 during

[30] Edie, *Money, Bank Credit and Prices*, chs. xvi and xvii; T. E. Gregory, *The First Year of the Gold Standard* (London, E. Benn Ltd., 1926). Gregory, *The Return to Gold* (London, E. Benn Ltd., 1925). H. A. MacCrosty, "Inflation and Deflation in the United States and the United Kingdom," *Journal of the Royal Statistical Society*, XC (1927), 45-135.

[31] The index figures are those of Professor C. Ottolenghi. See Royal Economic Society, *Report on Current Economic Conditions in Europe*, Memorandum No. 45 (London, February, 1934), p. 15. According to Bachi the index stood at 558.2 at the beginning of 1927 and at 463.5 at the end. See *Handbook of Labor Statistics*, 1929 edition (Washington, 1929), p. 614.

the second, at 618 during the third, and at 620 during the last quarter.[32]

The change from a depreciated to a stable currency may be effected by a method that differs from the one that was employed in England (*restoration* of the currency to the old value) as well as from that which was employed in France and Italy (*devaluation* of the old monetary unit to a level fixed by its existing internal and external value).[33] The third method—*repudiation* of the existing currency—is destructive of financial prestige and is, therefore, likely to be eschewed by countries having another way out.[34] In Germany and in the Soviet Union, as we have seen, the depreciation of the currency was such that its value shrank to an infinitesimally small magnitude. It was impossible to redeem the depreciated paper at par. To be sure, the re-established monetary units in those countries were based upon the same metallic content

[32] The wholesale index is that of the *Statistique générale de la France*. The external value of the franc was fixed at a somewhat lower figure than that which expressed its internal value, a circumstance which proved to be of benefit to the country. See J. H. Rogers, *The Process of Inflation in France, 1914–1927* (Columbia University Press, 1929), *passim*. See also E. L. Dulles, *The French Franc, 1914–1928* (New York, The Macmillan Co., 1929), *passim*. France is sometimes cited as a country exemplifying the advantages of inflation. It is generally overlooked that a great deal of the increased industrial activity in France between 1919 and 1926 was due to the rebuilding of devastated regions, plants, destroyed machinery, and so forth.

[33] In general devaluation can be carried to any point between the existing value of the currency and its former value.

[34] The difference between devaluation and repudiation is really one of degree. Under the latter the currency may be said to be permitted to depreciate to a far greater extent than under the former. Devaluation, too, may be said to involve a certain degree of repudiation (of the difference between the former value and the value at which the currency is stabilized). And on the other hand, repudiation is nothing but an *extreme devaluation*. One may, in fact, question the suitability of the term "repudiation." In Black's *Law Dictionary* "repudiation" is defined as the refusal on the part of a state or government to pay its debts, or its declaration that its obligations, previously contracted, are no longer regarded by it as of binding force. But do states, in fact, regard the outstanding means of payment as constituting a *legal debt* or *obligation* on their part? No matter how desirable it is that a state should maintain the price level within certain bounds, is it legally obligated to do so? Is not the holder of money presumed to know that the state has a right to suspend specie payment, and to change the metallic content of the monetary unit, and that the state will avail itself of that right when faced by an emergency? The term "nullification" that is sometimes used instead of "repudiation" is not quite accurate, inasmuch as the depreciated paper has some value, however small, at the time of its stabilization and is redeemed for value.

as the respective pre-war units; the German reichsmark was stabilized at the old parity, 23.82 cents, and the Soviet chervonetz, containing 10 rubles, at $5.146 (the old parity of the ruble equaled 51.46 cents). The price levels of those countries were, however, phenomenally high. The price indices reached stellar heights. Those levels were so far above the price level in the United States that an equilibrium between them could not be established by a mere restriction of credit and the like; deflation from so high to so low a price level would have proved disastrous. This difficulty, as we know, had been overcome in Germany by redeeming the depreciated paper at the rate of 1,000,000,000,000 marks to one reichsmark, and in the Soviet Union at the rate of 50,000,000,000 depreciated rubles to one ruble of the new issue.

On March 1, 1924, a week before the redemption of the sovznaks was announced, the All-Union Price Index of the Institute for the Study of Economic Conditions had stood at 6,094,500,000,000 and the wholesale price index (of the Gosplan) at 5,790,000,000,000. Translated into chervontzy, the retail price index on March 1, 1924, was 203 (1913 = 100) and the wholesale price index was 193.[35] In the United States at the same time the retail food index stood at 143.7 and the wholesale index at 149.9.[36] The Soviet price level was (on the basis of the wholesale price indices), therefore, 28.7 percent higher than the American level. Applying the same reasoning as has been used above, such a state of affairs should have caused the Soviet Union to become a good market in which to sell and a poor one in which to buy—with the familiar results. Because the monopoly of foreign trade was in its hands, the government was able, as we have seen, to keep imports and exports within the desired limits. But the shortage of commodities in general, the relatively high prices, and the forced omission of certain luxury items for which there was a demand from the list of imports, led to the development in the Soviet Union of contraband import trade on a considerable

[35] *Our Monetary Circulation*, pp. 250-52.

[36] U. S. Department of Labor, Bureau of Labor Statistics, *Handbook of Labor Statistics 1924-26* (Washington, 1927), pp. 495, 522.

scale.[37] To pay for such goods the smugglers of course needed gold or foreign exchange. These they obtained through purchase on the "black" exchanges and through the export of chervontzy abroad, where the latter used to be converted into gold. Gold was, therefore, leaving the country.

What was the situation with respect to exports? Inasmuch as the Soviet Union did not control world prices, it had to sell in foreign markets at the relatively lower prices prevailing there. Obviously, the Soviet exporting agencies were sustaining losses.[38]

The disequilibrium between prices within the Soviet Union itself, and between Soviet prices and those of foreign countries, as well as the desire to make the stabilization of the currency a success, all these considerations suggested the necessity of lowering the price level. Such lowering of the price level could, of course, be accomplished by a policy of deflation involving a restriction of credit and a decrease in the note issue. It was vital, nevertheless, not to throttle the budding industries. The Commissariat of Finance therefore applied credit restriction with great caution and only to a very limited extent. As shown by Table 31, the banknote issue, which during the months of January and February, 1924, amounted to 22,000,000 and 27,700,000 rubles, respectively, dropped in March, the month of the Monetary Reform, to a mere 2,800,000 rubles. This moderation was apparent also during the months immediately following the Reform. But, then, it must be remembered that during the spring months business activity is at a low point. The months of August, September, October, and November, when the crops are moved and credit is required for that purpose, witnessed a steady increase in the amount of banknotes issued. By the end of 1924 the circulation became surfeited with them and in January, 1925, the bank retired some 45,000,000 rubles of those notes. During 1925 there was a steady growth of their volume and by the end of the year

[37] See Loevetzky, *Valuta Policy of the U.S.S.R.*, pp. 69, 84-88.

[38] It is important to remember that prices of exportable commodities were considerably lower in the Soviet Union than its wholesale price index seems to indicate. Soviet exports, at that time much the same as pre-war Russian exports, consisted of some 70 percent agricultural products. The agricultural price index, however, stood lower than the general wholesale price index.

TABLE 31

BANKNOTE (CHERVONTZY) ISSUE IN 1924–25 [a]

(*In rubles*)

	1924		1925	
	Total in Circulation on the First of the Month	Issued during the Month	Total in Circulation on the First of the Month	Issued during the Month
January	237,158,900	22,037,500	410,832,000	−45,740,100
February	259,196,400	27,687,100	365,091,900	11,776,400
March	286,883,500	2,784,700	376,868,300	25,519,000
April	289,668,200	5,430,900	402,387,300	6,233,500
May	295,099,100	−12,002,700	408,620,800	9,199,200
June	283,096,400	11,479,600	417,820,000	42,310,200
July	294,576,000	− 3,684,900	460,130,200	45,240,100
August	290,891,100	21,224,700	505,370,300	61,254,000
September	312,115,800	34,383,400	566,624,300	85,345,200
October	346,499,200	23,786,600	651,969,500	67,277,600
November	370,285,800	28,683,200	719,247,100	19,038,900
December	398,969,000	11,863,000	738,286,000	−11,646,400
Total	....	173,673,100	....	315,807,600

[a] *Our Monetary Circulation*, pp. 154-55.

their amount in circulation was 726,639,600 rubles, an amount more than three times that recorded on January 1, 1924.

Meanwhile the amount of other types of money in circulation, too, underwent an increase.

As shown by Table 32, between the beginning of 1924 and the end of 1925 the total amount of currency in circulation had almost quadrupled and the total means of payment had increased by more than three and a half times. All increase in means of payment, however, is not necessarily inflationary. An allowance

TABLE 32

THE VOLUME OF MEANS OF PAYMENT IN 1924–25 [a]

(In millions of rubles on the first of the month)

	Sovznaks (in Terms of Stable Currency)	*Banknotes*	*Transportation Certificates*	*Treasury Notes, and Metallic Currency*	*Total Currency in Circulation*	*Bank Deposits*	*Total Means of Payment*
1924							
January.....	75.2	237.1	9.6	....	321.9	336.8	658.7
March.....	27.0	286.9	19.2	23.6	356.7	475.3	832.0
April.....	15.2	289.7	20.8	67.7	393.4	426.7	820.1
July.....	....	294.6	3.3	187.6	485.5	461.7	947.2
October.....	....	346.5	....	280.7	627.2	508.0 (475.3)	1,135.2
1925							
January.....	....	410.8	....	331.8	742.6	642.1	1,384.7
April	....	402.4	....	363.3	765.7	770.7	1,536.4
July.....	....	460.1	....	386.0	846.1	842.0	1,688.1
October ...	....	652.0	....	490.9	1,142.9	1,173.5 (1,132.4)	2,316.4
1926							
January ...	....	726.6	....	542.7	1,269.3	1,112.7	2,382.0

[a] The figures pertaining to currency circulation were taken from *Our Monetary Circulation*, p. 155; those pertaining to bank deposits, from the *Vestnik Finansov*, 1927, No. 6, pp. 228-29. The latter represent the deposits of the eight most important banks, with the exception of the data for the month of October (in 1924 and 1925), which are more complete and were taken from Chapter XI. These, rather than the *Vestnik Finansov* October figures (which are shown in parenthesis), were included in the totals in order to make the latter comparable with later data.

must be made here for an increased trade turnover, the widening of the sphere in which means of payment were used (due to the disappearance of barter and other vestiges of the "natural" economy, that hangover from the period of War Communism), and for the decreased velocity of currency circulation, which was being

promoted by a growing degree of confidence resulting from the introduction of a stable money. The increase in the trade turnover, however, was much more important than the other items in furnishing employment to the additionally created purchasing power. Still, a comparison of the percentage increase of goods produced, sold (trade turnover), and shipped (carloadings) during 1924 and 1925 with the percentage increase of currency in circulation over the same period reveals unmistakable signs of inflation.

Table 33 shows that whereas the volume of means of payment

TABLE 33

RELATIVE INCREASE OF MEANS OF PAYMENT, OUTPUT OF LARGE-SCALE INDUSTRY, TRADE TURNOVER, AND CARLOADINGS 1924–26 [a]

	Increase between January 1, 1924, and 1925 in %	*Increase between January 1, 1925, and 1926 in %*
Volume of means of payment	110.2	72.0
Gross output of large-scale industry (deflated)	57.0	39.2
Trade turnover of 162 state agencies (deflated)	63.0	28.0
Trade turnover of the Moscow and 70 country produce exchanges (deflated)	84.6	22.5
Average daily carloadings	24.2	51.0

[a] The large percentage increases are misleading. It must be remembered that the New Economic Policy found economic conditions at a very low ebb. The percentages were computed on the basis of data given in S. M. Vinokur, "Currency Circulation after the Reform," *Vestnik Finansov*, 1926, No. 4, p. 4.

had increased between January 1, 1924, and January 1, 1925, by 110.2 percent, and between the latter date and January 1, 1926, by 72 percent, trade turnover and carloadings increased during those years by a much smaller percentage.[39]

[39] As a result of an investigation of the state of currency circulation and of the supplies of commodities, the Special Commission at the Institute of Economic Research of the Commissariat of Finance reported along the following lines: in the fall of 1925 there were seen sharp inflationary phenomena. These phenomena were the result of a disproportion between the rise in the income of the urban

A glance, however, at the price indices (in Table 34) shows that the government was quite successful in its attempts to stabilize the price level and, consequently, the purchasing power of the monetary unit. This it was able to accomplish by means of a policy of *price regulation and "intervention"* on the commodity markets.[40] There were created two special commissions at the Council of Labor and Defense. One was known as the Commission of Domestic or Internal Trade (*Komissiia Vnutrennei Torgovli pri STO,* abbreviated *Komvnutorg,* and subsequently reorganized as the Commissariat of Internal Trade), the other as the Commission of the Council of Labor and Defense (*Komissiia STO*) to Combat High Prices.[41] The former was authorized to regulate the prices of all commodities sold within the Union in wholesale or retail trade by state, co-operative, and private business enterprises. The latter, in addition to its general power to regulate state agencies and enterprises, was furnished with supplies of com-

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and rural populations and of commodities placed on the markets. The increase in the money income of the urban population was due to the financing of industry which led to an increase in the number of workers employed, a rise in their wages, etc., as well as to the increased income of private traders. The rise in the money income of the rural population was due to the excessive credits granted for the purchase of grain at a time when the peasantry had no incentive to offer such grain for sale. As a result of the inflationary process there followed a deep derangement of economic relations which internally expressed itself in the sharpening of the commodities famine, a sharp cleavage between wholesale and retail prices in general, and between regulated and free prices in particular. Externally, it affected the Soviet Union by rendering its exports unprofitable.

The Commission recommended the policy of refraining from granting excessive credits to *state* and *co-operative* enterprises, and of encouraging *private* trade and abandoning the attempt to force industrial expansion by means of printing paper money. See Zheleznov in *Vestnik Finansov,* 1926, No. 4, pp. 11 ff. The communists, although realizing the danger of inflation, felt that the recommended course would lead to capitalism and not to socialism, that is, that the cure offered was worse than the ailment, hence they did not follow it. It must also be added that the communists believed these findings to be not so much the result of impartial research as of bourgeois ideology, and of a desire to restore capitalism in the country.

[40] *Collected Decrees,* 1924, Decree 385 on the regulation of the retail price of coal and oil (Regulation of February 20, 1924, by STO); Decree 332 on the establishment of price limits (Regulation of February 22, 1924, by STO); Decree 338 on the publishing of retail prices (Regulation of February 29, 1924, by STO); and Decree 532 on the registration of the commercial transactions that are carried out by state agencies and enterprises in places other than produce exchanges (Regulation of April 11, 1924, by STO).

[41] The Commission of the Council of Labor and Defense was a temporary agency. It functioned during February and March. The actions of both were co-ordinated.

TABLE 34

WHOLESALE AND RETAIL PRICE INDICES

1924–25 [a]

(1913 = 100)

	1924						1925					
	Wholesale			*Retail*			*Wholesale*			*Retail*		
	General	Agricultural	Industrial	General	Agricultural	Industrial	General	Agricultural	Industrial	General	Agricultural	Industrial
January ..	169.0	124.5	229.3	180.0	134.0	239.0	172.0	152.5	193.9	205.0	177.0	235.0
February	186.5	153.3	226.9	201.0	159.0	253.0	178.0	164.4	192.6	208.0	185.0	232.0
March ..	193.0	170.3	218.7	203.0	159.0	255.0	183.3	176.3	190.6	211.0	193.0	229.0
April....	180.8	156.5	208.9	207.0	172.0	242.0	194.5	197.9	190.6	217.0	208.0	227.0
May.....	175.2	150.9	203.4	213.0	187.0	238.0	196.6	202.5	190.8	221.0	217.0	225.0
June....	165.8	136.8	201.3	206.0	173.0	243.0	191.4	193.1	189.8	219.0	217.0	222.0
July	169.0	141.4	202.1	210.0	179.0	245.0	188.0	186.2	189.8	218.0	217.0	219.0
August...	175.4	151.3	203.2	225.0	103.0	248.0	175.1	161.0	190.3	210.0	199.0	221.0
September	172.5	148.1	200.9	219.0	192.0	248.0	172.7	151.8	192.7	208.0	190.0	227.0
October .	164.3	136.0	198.6	206.0	172.0	243.0	174.2	155.6	194.9	215.0	192.3	238.8
November	163.6	135.2	198.0	203.0	167.0	244.0	175.3	156.3	196.4	217.0	191.0	245.0
December	168.2	144.8	195.2	205.0	174.0	240.0	179.3	162.6	197.6[b]	224.0	199.0	251.0[c]

[a] *Our Monetary Circulation*, pp. 250, 252. The wholesale index is that of the Gosplan, and the retail is that of the Institute for the Study of Economic Conditions.

[b] On January 1, 1926: General Index (Wholesale), 183.3; agricultural, 169.4; industrial, 198.2.

[c] On January 1, 1926: General Index (Retail), 226.0; agricultural, 204.0; industrial, 248.0.

modities with which it was to undersell business enterprises and in that manner compel the lowering of prices. There was produced in consequence a very interesting phenomenon, a lowering (or prevented increase) of commodity prices at a time when there was a shortage of consumers' goods (a "commodity famine"), that is, at a time when the demand for commodities exceeded their supply

many times over.[42] A policy of this kind, other things being equal, should have led to a still further increase in the demand for goods and services relative to their supply. It should, in other words, have intensified the shortage of commodities. Other things, however, did not remain equal: the lowering of commodity prices justified a lowering of wages. The lowering of wages meant, of course, the lowering of the costs of production, and the latter (ignoring the disparity between demand and supply) was considered a justification for the lowering of prices.

It was, then, the policy of price regulation rather than deflation that helped to produce a comparatively stable price level. Inflation under a regime of regulated prices apparently cannot be judged by the *height* of the index number of prices no matter how carefully computed. There enters a new factor—the extent of the unsatisfied consumers' demand.

A very interesting query may, as a matter of fact, be posited. If the price level was comparatively stable, what justification can there be for saying that there was "inflation" in the Soviet Union? Indeed, if we define inflation as a good many authorities on the subject generally do, namely, as *a condition resulting in a rise in the price level that is caused by an increase in the volume of purchasing power not accompanied by a corresponding increase in the volume of goods and services available for distribution,* then there was no inflation in the Soviet Union. This and similar definitions of inflation, however, were not meant to apply to a regime of regulated prices. They were meant for economies in which "free" prices prevailed. And yet "an increase in the volume of purchasing power that is not accompanied by a corresponding increase in the volume of goods and services offered for sale," which really is the quintessence of inflation, may take place not only where "free" prices prevail, but, as has been shown, also in economies where prices are controlled. Obviously, if we want to have a definition of inflation that is universally applicable, it will read as follows: *Inflation is a condition caused by an in-*

[42] The supplies thrown on the markets by the government could not materially increase the total supply of commodities in view of the fact that they were relatively small. The government could not afford to carry out such policy on a large scale. For a criticism of this policy, see Kuzovkov, *op. cit.*, pp. 389-416.

crease in volume of purchasing power that is not accompanied by a corresponding increase in the volume of goods and services available for distribution.[43] It may be added further that this condition may result in a fall of the value of money and, therefore, in a higher price level in countries in which "free" prices prevail, and in a shortage of commodities (which may or may not be accompanied by a fall of the value of money) in countries in which prices are controlled or regulated. Since the term "inflation" is used throughout this book in the sense in which it is defined above, it is advisable to bear this definition in mind.

The stabilization of the exchanges.—The stabilization of the price level was paralleled by a stabilization of the exchanges. The dollar, which on January 1, 1924, was quoted by the Securities Department of the Moscow Produce Exchange at 2.20 (old parity: one dollar = 1.934 rubles) dropped to its parity on April 1, 1924, when it was quoted at 1.945. Thereafter, it was held at that level.

The pound sterling which on January 1, 1924, was quoted by the same agency at 9.40 rubles (parity: 9.4576) stood on April 1, 1924, at 8.36, but by October 1 of that year reached 8.67. By June 1, 1925 (as a result of the pound's stabilization in England), it reached and even slightly exceeded parity. In the second half of 1925, however, it lost some of its ground. The "free" market, reflecting the same guidance, showed but a slight variation from the official rates.

The Czarist ten-ruble gold piece (of 1899 and later mintage), which was quoted on January 1, 1924, on the "free" Moscow exchange at 14.05 chervonetz-rubles, began to lose grace steadily and by May 1 of the same year was quoted at 10.60. On June 1, 1924, it sold at 9.90 and on July 1 its price dropped to 9.47—that is, it "circulated" at a discount. Except for short periods of time, it continued to be quoted in 1924 and until November,

[43] A definition somewhat similar to this was offered by Prof. Walter E. Spahr, in an article entitled "Currency Inflation: Its Nature and Implications" in *The American Economic Review*, XXIV, No. 2, June, 1934. It reads as follows: "Inflation is a condition resulting from an extension of purchasing power either in the form of money or credit which is not secured by a sufficient amount of reserves or commodities to liquidate it."

1925, below its parity. From November 1, 1925, to the end of that year it was quoted either at par or slightly above par.

The favorable balance of payments, together with the intervention by governmental agencies in the domestic exchanges, could not fail to accomplish the above results. Particularly since with the stabilization of the currency the demand for foreign exchange as a store of value had fallen off considerably (in fact the country experienced a *"foreign exchange inflation"*).[44]

The shortage of notes of low denominations.—The "shortage of commodities" was not the only shortage that the Soviet Union suffered in those days. The Monetary Reform brought with it an additional shortage, a shortage of small change and, in general, of notes of small denominations. This latter shortage was so acute during the month of March that in Odessa notes of small denominations commanded a premium (as compared with the chervonetz) as high as 20 percent; in Kiev, 18 percent; in Vologda and Omsk, 30 percent; Vinnitza, 24 percent, and so forth.[45] How did this shortage come about? In carrying out the Reform the Commissariat of Finance, as has been explained, postponed the fixing of the rate at which the sovznaks were to be redeemed. Their depreciation therefore continued. On February 15, 1924, for instance, when their issue (but not their circulation) was discontinued, they were quoted by the Securities Department of the Moscow Produce Exchange at 14,000 rubles of the 1923 pattern (or 14,000,000,000 pre-devalorization rubles) to one stable ruble, and on March 10, 1924, as we know, their further depreciation led to the fixing of their *redemption* rate at 50,000 to 1. It was this steady shrinkage of their value coupled with a discontinuance of their further issue that was in part responsible for the shortage of small change and of notes of low denominations.[46]

[44] The phenomenon of "foreign exchange inflation" cannot very well exist under *free trade* because an excess of the supply of foreign exchange relative to the demand for it will under that regime bring about a drop in the rates making imports profitable, and hence will cause a readjustment in the supply and demand.

[45] Zheleznov, "The Course of the Monetary Reform," *Vestnik Finansov,* Nos. 4 and 5; April–May, 1924, p. 10; also *Economic Bulletin* of the Institute for the Study of Economic Conditions, No. 4, 1924, p. 17.

[46] It may also be supposed that as soon as the rate of their redemption was fixed, the velocity of their circulation had diminished and that this in turn created a need for additional notes of low denominations.

But why did not the new treasury notes, the issue of which had commenced on February 5 of that year, together with the metallic coins that were issued later, satisfy that demand? In regard to metallic coins it may be said that they were not brought out in sufficient quantity and, therefore, kept on disappearing from circulation. It was of course to be expected that, following a prolonged regime of inflation, currency having an intrinsic value would disappear from circulation if introduced in small doses. As to the treasury notes, it must be remembered that not all of the early issues constituted a net addition to the total amount of money in circulation. Some of them merely displaced sovznaks and chervontzy.[47] Inasmuch as it is impossible to determine on the basis of existing data the velocity with which the various kinds of money circulated in the Soviet Union, it therefore cannot be stated with certainty whether or not a given number of treasury notes, which took the place of the retired sovznaks, were able to accomplish the work of the latter. An interesting and telling picture, however, is furnished by the figures showing the distribution of the treasury notes in circulation according to their denominations (see Table 35).

It is seen from Table 35 that the Commissariat of Finance was placing in circulation only a relatively small amount of the one-ruble notes. It may be said that, inasmuch as the part played by one-ruble notes in the total circulation before the Revolution

[47] On March 1, 1924, for instance, 98.4 percent of all the treasury issues were for the purpose of providing an exchange fund with which to redeem banknotes, and 1.6 percent for the purpose of retiring sovznaks. On June 1, 1924, the respective percentages were 67.6 and 4.5. The balance, 27.9 percent, were used for the purpose of covering budgetary deficits. The term "Exchange Fund" which one encounters in post-Reform bank statements may appear puzzling and, therefore, requires an explanation. Originally the treasury (the Commissariat of Finance), when supplying the bank with treasury notes and coins with which to meet the demand for currency of a low denomination, used to take back as security an equivalent amount of chervontzy, hence, the name "Exchange Fund." Realizing that such procedure was but a waste of energy, inasmuch as it (the treasury) was not allowed to reissue the chervontzy so held for fiscal purposes, the treasury dispensed with the "security" requirements. As a result of the change the bank began to enter the notes and coins transferred to it by the treasury "for the purpose of satisfying the demand of trade" in an account known as "Special Exchange Fund of the Commissariat of Finance." Such deposits of course partook of the nature of additional note issue by the bank. See *The State Bank of the U.S.S.R., 1921–26*, pp. 34-35.

TABLE 35

ABSOLUTE AND RELATIVE DISTRIBUTION OF TREASURY NOTES IN CIRCULATION BY DENOMINATIONS[a]

1924–25

(*In thousands of rubles and percents*)

	One Ruble		*Three Rubles*		*Five Rubles*		*Total Treasury Notes*		*Silver Rubles*		*Total Silver*	
	Absolute	%	Absolute	%	Absolute	%	Absolute	%	Absolute	%	Absolute	%
1924												
March 1.....	326.6	1.6	3,462.7	17.7	15,820.0	80.7	19,609.3	100	....	...	3,812.0	100
April 1.....	3,857.7	7.1	16,660.3	30.5	34,123.7	62.4	54,641.7	100	....	...	9,964.9	100
May 1.....	9,349.1	11.0	25,497.5	29.9	50,382.7	59.1	85,229.3	100	334.9	2.7	12,720.9	100
June 1.....	21,060.3	16.1	39,242.9	30.0	70,506.3	53.9	130,809.5	100	807.5	4.6	17,555.7	100
1925												
March 1....	51,196.9	21.7	70,071.3	29.7	114,662.2	48.6	235,930.4	100	2,860.2	3.1	91,559.5	100

[a] *Our Monetary Circulation*, p. 146.

was not prominent, there was a justification for not giving such notes a more prominent part in 1924. But then it must be remembered that in the pre-war days the silver ruble was quite conspicuous. On January 1, 1914, for instance, Russia had in circulation silver coins to the amount of 225,800,000 rubles (out of a grand total of 2,402,800,000 rubles). And of this amount 84,300,000 rubles (or 37.3 percent of the total silver in circulation) was represented by one-ruble coins. Although it must be recognized that the monetary needs of the Soviet Union differed from the monetary needs which existed in old Russia, nevertheless it is patent that the shortage of such currency was in part due to the failure of the Commissariat of Finance to place a sufficient amount of small money in circulation. The crisis was, moreover, intensified by the slow and uneven distribution of those notes and coins in the various centers.

The steady increase of the volume of notes of lower denominations and of silver rubles in circulation helped to overcome the crisis. It lasted some three months and was over in June.

An appraisal.—The Reform as carried out in the Soviet Union in 1924 differed radically from the reforms which had taken place in Imperial Russia under Kankrin and Witte as well as from a good many of those which had taken place in other lands. The Reform of 1924 was introduced at a time when the budget was still unbalanced, and, consequently, when it was known that the new currency would have to be used for the purpose of covering budgetary deficits. Then, too, contrary to the accepted views, the Reform of 1924 dispensed with such preliminary requirements as the stabilization of the old depreciated notes before the new ones were issued. Clearly the Reform had not been carefully prepared and could have easily come to grief. These are the strongest points that one could offer in criticism of it.

The treasury, as we have seen, was aware of the fact that it was departing from the traditional and safe path. It claimed, however, that inasmuch as the depreciated paper contributed to the disorganization of the budget, both problems—the stabilization of the currency and the balancing of the budget—had to be tackled

at the same time as well as possible.[48] At any rate it had been compelled by circumstances to introduce the Reform at a time when the conditions were not fully ripe for it. The steady expansion of productive forces saved it from a fate of culminating in nothing more than a mere substitution of a new depreciating paper money for an old, and in discrediting the government and rendering future attempts at stabilization more difficult.

The Reform has been criticized because of the too high parity which was established under it between the ruble and the dollar.[49] As we have seen, there was considerable difference between Soviet and world price levels at the time the old parity had been re-established. It was, therefore, asserted by critics that, since the external value of the ruble had been fixed and maintained at a considerably higher level than its internal value justified, exporters were sustaining losses; furthermore, that such losses were not counterbalanced by the windfall profits made by importers, in view of the fact that such policy served to destroy the incentive to export commodities. After the Reform some of the critics, in fact, proposed a devaluation of the ruble so as to stimulate exports and build up a large gold reserve.

There can be no doubt that the ruble was fixed at too high a level. It had been done presumably with the intention of pro-

[48] It may not be uninteresting to read the lines on the interdependence of a balanced budget and a stable currency from the opinion of the First Committee of Experts under the Dawes Commission:

"The currency of a country cannot remain stable unless its budget is normally balanced, for if expenditure continually exceeds receipts there will in time be no alternative to the printing of new notes to meet the excess; and the inflation will inevitably involve depreciation. On the other hand, the task of balancing a budget, unless the currency is relatively stable, is an impossible one, for a falling currency makes calculations both of receipts and expenses unreliable, and in particular causes a continual loss to the taxing authority through the necessary interval of time between assessment and collection [and one may add: between collection and expenditure.—Author]. While, therefore, in the nature of things it is necessary that the two problems should in the first instance be studied separately, their interdependence must be consistently borne in mind." Quoted by Edie, *op. cit.*, pp. 339-40.

[49] See, for example, A. Yugoff, *Economic Trends in Soviet Russia* (New York, Richard R. Smith, 1930), p. 240; also S. Vinokur, "The Basic Lines of a Valuta Policy," *Financial Problems of a Planned Economy*, 1930, No. 3, p. 24; Loevetzky, *op. cit.*, pp. 97-108.

ducing a desirable effect at home and abroad. It must be remembered, however, that no matter at what point the parity is fixed there is likely to develop a new disequilibrium between Soviet and world prices. Planned economy, as has been explained, puts a stop to "automatic" regulation of the price level. Naturally, if the Soviet Union wished it could plan and pursue a policy leading to the establishment and to the maintenance of an equilibrium between its own and world price levels. But at what price? It would have to subordinate all other plans to the "price level plan." Today, for example, Soviet prices are planned with a view of allowing business enterprises to earn certain profits which can be used for the purpose of expanding production to a certain point. Obviously, if the Soviet Union sets before itself the task of bringing its prices into harmony with foreign prices, it will thereby place a very serious limitation upon its planning.

Furthermore, it is not at all certain that a devaluation or depreciation of the external value of a monetary unit leads to increased exports. It cannot be denied that the lowering of the external value of a monetary unit by a country would make it advantageous for other countries to buy there, provided, of course, that the lowering of the external value is not offset by an internal depreciation of the currency. But does not experience teach us that other countries may either do the same with their currencies, or else raise tariffs, or apply quota restrictions? Let us, however, suppose that other countries will not retaliate and that exports will increase. Will the country in question (not the individual sellers) benefit from such increase in exports? Assume that before the devaluation of the currency is carried out the country exports a certain quantity of commodities in order to pay for the needed imports. If it devaluates its currency by 50 percent, it will have to export *double* that quantity in order to pay for the same imports. But can a country enrich itself by giving away its material wealth? Quite the contrary, such policy would lead to its impoverishment, to its being drained, as the Germans used to say, of its "economic substance." [50] Still, a country whose monetary unit

[50] This expression was employed in Germany during the post-war inflationary period. See Robert Eisler, *Stable Money* (London, 1933), p. 192.

is fixed at too high a level is at a disadvantage when trading with other countries. During 1924–25, however, its very weakness compelled the Soviet Union to display signs of strength. Since then conditions have changed. In recent years the Soviet Union, scoring important victories on all fronts, was able to take its place among the leading countries of the world. So when other countries revalued their currencies, it adopted a similar policy.[51]

Some critics have also maintained that if conditions were really ripe for the stabilization of the currency, then it was the sovznak that should have been stabilized and that new currency should not have been introduced. An answer to this was given by Yurovsky.[52] He pointed out that, since the monthly budgetary deficit necessitated the issue of an amount of sovznaks equaling 15,000,000 rubles in gold, and since the losses sustained by the Commissariats of Finance, the Railways, and the Post and Telegraph necessitated a further issue of about half of the above amount at a time when the gold value of the entire mass of the depreciated sovznaks was below 40,000,000 gold rubles (at the beginning of 1924), one could not expect the purchasing power of the sovznaks to become stabilized under those circumstances. Besides, the retention of the sovznaks would mean the further continuance of the evils which the government sought to abolish.

In justice to those who had advocated the stabilization of the sovznak it must be said that their opinion had been voiced chiefly in the early part of 1923. The appearance of the chervonetz led to a discussion of its and the sovznak's future, concerning which two major trends of opinion developed. One opinion was that the chervonetz' sphere of action should be restricted to large transactions, and to its use as a store of value. It was to serve as a supplementary and not as a basic currency. The latter rôle was to be assumed by the paper ruble, and steps therefore had to be taken toward stabilizing it. Accordingly, the balancing of the budget and the discontinuance of note issue for that purpose were recommended.

Another trend of opinion favored the displacement of the

[51] See Chapter XIV.

[52] *Currency Problems and Policy of the Soviet Union,* pp. 124-25.

sovznak by the chervonetz and the issue of chervontzy of small denominations.[53]

According to Kuzovkov [54] it was the first trend that gave orientation to the official policy until August, 1923. He sees a corroboration of this opinion in the fact that on July 7, 1923, the Central Executive Committee ordered that, beginning with May 1, 1923, the monthly issue of sovznaks must not exceed an amount equivalent to 30,000,000 rubles in gold (calculated as of the first of the month on the basis of the official rates), and, beginning with August 1, 1923, such issue must not exceed the equivalent of 15,000,000 rubles in gold.[55] As we have seen, the depreciation of the banknote made it necessary in the fall months to give it a temporary respite, which meant that much larger issues of sovznaks had to be brought out; this stepped up the latter's depreciation to a point where even its most ardent supporters recognized that it was impossible to stabilize it.

Once inflation reaches such gigantic proportions as it did in Soviet Russia, Germany, or Austria, it becomes impossible to stabilize the existing currency—devaluation is the only solution then. The only question is the extent to which the devaluation will be applied: is it going to be 1,000,000,000,000 to 1 as in Germany, 50,000,000,000 to 1 as in Soviet Russia, 10,000 to 1 as in Austria, or some other ratio?

Considerable criticism was also leveled against the regulations

[53] It will be recalled that before the Revolution all paper money in Russia was being issued by the State Bank. The paper money was known as "credit notes" (*kreditnye bilety*) and was convertible into gold upon demand.

[54] *Op. cit.*, Pt. II, 225 ff.; see also Diachenko, "Stability of the Monetary Circulation . . ." *Financial Problems of a Planned Economy*, No. 5, 1930, pp. 45 ff.

[55] Sokolnikov's speeches and writings, however, do not entirely bear out the correctness of Kuzovkov's assertions. As a case in point the following excerpt from Sokolnikov's speech in October, 1922, before the Second All-Union Conference of "Financiers" is illuminating. Explaining the rôle that the banknotes were to play in Soviet Russia, he said: ". . . The payment functions of the banknotes will gradually increase, and if, at the same time, we succeed in overcoming our budgetary deficit, if our tax apparatus begins to work satisfactorily, then simultaneously with it can be discontinued the issuance of paper money and we will be able to change entirely to a paper valuta [i.e., banknotes.—Author] of the State Bank."—*Financial Policy of the Revolution*, I, 259-60; see also Sokolnikov, "The Quinquennial of the Monetary Reform," *Vestnik Finansov*, 1929, No. 4, p. 4.

pertaining to the issue of treasury notes. One writer,[56] for instance, points out that the limitation set upon their issue is a very flexible one (originally not to exceed 50 percent of the amount of banknotes in circulation), since under it their amount may be increased whenever an increase takes place in the volume of banknotes. This, of course, is true. But then the volume of the banknotes, which serves as a regulator of the volume of treasury notes, is itself limited by the requirement of a firm cover of 25 percent.

Despite its lack of perfection, the Monetary Reform of 1924 constituted a great achievement for the country. Unaided by outside help the Soviet Union succeeded in extricating itself from the inflationary morass which threatened to swallow it. It required heroic effort to accomplish that. It would be a mistake to think that success was achieved merely as a result of the legislative steps taken in February and March, 1924. The foundation for this Reform began to be laid in 1921, when the compulsory requisition and expropriation of agricultural products was brought to an end and free trade ushered in, in short, when the New Economic Policy was introduced. It brought with it, as we have seen, the realization of the fact that the country could not get along without money and, what is more, without a stable money. There followed the gradual introduction of pecuniary taxes, the placement of state enterprises on a commercial footing, the encouragement to private initiative, the creation of new sources of revenue and the improvement of the taxing machine in general, the curtailment of state expenditures, the development of public and banking credit, and so forth. The introduction of the chervonetz (in the fall of 1922) which by many is regarded as the *first stage* of the Monetary Reform, was really but one of the important links in the chain of events the forging of which had begun in 1921.

The Reform and the *unification of the currency circulation* [57]

[56] H. J. Seraphim, *Die russische Währungsreform des Jahres 1924* (Leipzig, 1925), p. 47; see also M. V. Bernatzky, *Soviet Russia. . . .* (London, 1924), pp. 123-24.

[57] The "unification" of the currency had begun in January, 1921. That date marked the beginning of the retirement from circulation of all local paper currency in

TABLE 36

UNIFIED STATE BUDGET OF THE U.S.S.R.

1924–25—1927–28 [a]

(*In millions of rubles*)

Revenues	*1924–25*	*1925–26*	*1926–27*	*1927–28*
1. Tax revenue	1,327.7	1,791.2	2,490.6	2,962.0
2. Non-tax revenue	1,475.9	2,095.7	2,558.8	2,922.3
3. State loans (industry, transport, etc.)	130.5	146.0	319.2	726.4
4. Other sources	68.1	5.7	6.7	3.7
(Including revenue from issue of money)	(33.0)	(5.7)	(6.7)	(3.7)
Total revenues	3,002.2	4,038.6	5,375.3	6,614.4
Revenue carried over from previous years	....	27.6	15.3	56.0
Total	3,002.2	4,066.2	5,390.6	6,670.4
Total expenditures	2,969.5	4,050.9	5,334.6	6,465.0

[a] Central Administration of Economic Accounting of the Gosplan of the U.S.S.R., *Socialist Construction of the U.S.S.R., Statistical Yearbook* (Moscow, 1935), pp. 644 ff.

gave the country a unified and comparatively stable currency, helped to put an end to the evils which existed under the "bi-paper" standard, improved the position of the treasury, exercised a salubrious effect upon the development of trade and industry, made possible the development of a credit system, and served

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Turkestan and the substitution for it of Soviet notes of the 1919 pattern at the rate of ten Turkestan rubles to one Soviet ruble. In Bokhara and Koresm the retirement of local paper issues and the substitution for them of Soviet notes (at the rate of 3 to 1 in the former, and 1 to 1 in the latter) took place in 1923.

In that year an attempt was made to supplant the Japanese yen and other metallic currency having circulation in the Far East with the depreciated sovznaks, which for obvious reasons proved unsuccessful. Following the Reform, however, Soviet currency met there with a better reception. March 1, 1925, was fixed as the final date for the redemption of the Czarist silver coins in Soviet currency.

In Transcaucasia the reform of the currency took place in 1924. July 31, 1924, was fixed as the final date for the redemption of local currency in Soviet notes.

to enhance the prestige of the government at home and abroad. It served as a turning point in the history of the Soviet Union. It may be added that Stalin's rise to leadership, the victory of his views over those of his opponents in the years following 1924, made it quite certain that the Soviet Union would strive to maintain a stable currency. As may be seen from Table 36, the budgets for the years 1924–25 to 1927–28 were free from note issue as a source of revenue.

It has been said above that the Monetary Reform of 1924 made possible the development of a banking system in the Soviet Union. It is with that development that the next chapter is going to deal.

X

THE STATE BANK, 1924–1928

The credit operations of the State Bank, 1924–1928.—The Monetary Reform of 1924 introduced order into a chaotic economic system, thus paving the way for an increase of production which by 1927–28 reached and exceeded the 1913 level in a number of important industries.[1] It imparted stability to all economic relations and particularly to those between lenders and borrowers. It also helped to simplify the work of the banks, reduce their operating cost, and end their losses. Similarly, it enabled borrowers to calculate their costs and plan their operations in advance. As a result, the credit granted by the State Bank expanded rapidly. From a total of 312,300,000 rubles on October 1, 1923, its loans and discounts mounted to 598,500,000 rubles on October 1, 1924, and to 1,425,000,000 rubles on October 1, 1925. The credit continued to expand, and by October 1, 1928, it amounted to 3,054,700,000 rubles.[2]

The bulk of the loans and discounts in the years following the stabilization of the currency was represented by discounted commercial paper. On April 1, 1928, e.g., the outstanding credit at the State Bank, for its own account, amounted to 2,822,400,000 rubles, of which 1,825,400,000, or two-thirds, was represented by discounted commercial paper.[3] Of the total loans and discounts about 98,000,000 rubles represented long-term loans granted by the bank, for its own account, to credit institutions. In addition, the bank granted 625,000,000 rubles of long-term loans for the account of the Commissariat of Finance.

Of the total bank credit outstanding on April 1, 1924, the state

[1] For data see *The Five-Year Plan of National Economic Construction of the U.S.S.R.* (Moscow, Gosplan of the U.S.S.R., 1929), Second edition, I, 16, 144 ff.

[2] See Table 37.

[3] The balance included loans of 326,300,000 rubles against commodities, bills of lading, etc.; 21,200,000 rubles against securities, foreign currency, and precious metals; 206,700,000 rubles in special loans to industry; and 292,200,000 rubles for financing grain operations.—*Vestnik Finansov*, 1929, No. 1, pp. 166-67; see also Katzenellenbaum in *Foreign Banking Systems*, H. Parker Willis and B. H. Beckhart, editors (Henry Holt and Co., 1929), p. 948.

enterprises received 56.0 percent; the co-operatives, 25.2 percent; and the credit institutions, 10.5 percent. Four years later, on April 1, 1928, the respective percentages were 73.3, 15.7, and 10.1. Inasmuch as the bank dealt directly with business enterprises its loans to other credit institutions were relatively small. That the relative shares of the state and co-operative enterprises changed by 1928 in favor of the former could, of course, be attributed to a desire to strengthen the purely state enterprises. It must, however, be borne in mind that co-operative enterprises were also served by co-operative credit banks and that the latter developed some strength between 1924 and 1928.

Private individuals and private enterprises received in 1924 4.4 percent of the total bank credit. As a result, however, of a determination to stamp out private traders, their loans and discounts dropped in 1928 to a mere 0.1 percent of the total.[4]

The discount rate and the discount policy.—When the bank began to grant credit in 1923 in terms of chervontzy, it lowered its discount rate from 18 percent per month to from 8 to 12 percent per annum.[5] After the currency stabilization of 1924 the rates were lowered still further. From March 22, 1927, the bank charged state and co-operative enterprises from 8 to 10 percent per annum. Its rates remained the same until 1934.[6]

These rates, considering the demand for short-term credit and its supply, were not at all excessive. In fact, the bank itself paid its depositors from 7 to 8 percent on time and 6 percent on demand deposits. The interest rates were not, however, the result of the interaction of the supply of and the demand for credit,

[4] *Vestnik Finansov,* 1927, No. 4, pp. 168-69; No. 12, p. 180; 1929, No. 7, p. 158.

[5] *The State Bank of the U.S.S.R., 1921–26,* p. 43. The above rate applied to state and co-operative enterprises. Its discount rate, including its commission charge in the case of private individuals and firms, stood during the same period at 10 to 15½ percent per annum.

The custom of collecting a "commission charge" in addition to the discount when granting credit was introduced in Soviet Russia at the time when the currency was depreciating very fast. After the stabilization of the currency it was retained only with respect to private borrowers. See Dezen, *The System of Bank Credit,* pp. 53-54; also N. D. Silin, "The Discount Policy of the Gosbank in Present-Day Conditions," *Vestnik Finansov,* 1925, No. 6, pp. 30-32.

[6] See G. Roginski and J. Rubinshtein, *Credit and Settlements* (Moscow, Finance Press, 1932), p. 31. Also G. Schwartz, "Strengthening the Ruble . . ." *Economic Life,* June 30, 1936.

TABLE 37

BALANCE SHEETS OF THE STATE BANK OF THE U.S.S.R.

1923–28 [a]

(*In millions of rubles on October 1 of each year*)

	1923	*1924*	*1925*	*1926*	*1927*	*1928*
Assets						
Cash	22.5	62.2	125.1	96.2	72.3	54.0
Bullion, coin, precious metals and foreign currency [b]	144.8	297.2	298.1	253.4	302.9	291.0
Securities	14.7	47.7	87.6	64.0	280.4	276.6
Investments [c]	17.1	14.3	89.8	52.9	5.9	....
Loans and discounts [d]	312.3 (298.7)	598.5 (598.5)	1,425.0 (1,425.1)	1,902.5 (1,902.5)	2,174.2 (2,359.0)	3,054.7[e]
Special loans to trade and industry on account of Commissariat of Finance	121.3	186.6	213.9	176.5	626.3	250.2
Special loans to agriculture	....	....	....	....	119.3	190.3
Other assets	32.7	47.3	62.1	167.3	207.1[f]	254.6
Total assets	665.4	1,253.8	2,301.6	2,712.8	3,788.4	4,371.4
Liabilities						
Capital	50.0	100.0	100.0	100.0	250.0	250.0
Reserve fund	....	7.9	15.0	33.0	99.9	99.9
Special reserves	....	....	....	45.4	9.4	6.1
Undivided profits	15.7	33.6[g]	72.1	91.9	97.7	14.5
Banknote issue	235.0	521.9	756.6	856.8	1,026.6	1,090.0
Deposit and current accounts [h]	178.9 (157.9)	361.2 (308.1)	988.7 (742.8)	1,200.8 (762.7)	1,378.3 (869.8)	1,553.1 (1,302.5)

TABLE 37—*Continued*

BALANCE SHEETS OF THE STATE BANK OF THE U.S.S.R.

1923–28 [a]

(*In millions of rubles on October 1 of each year*)

	1923	*1924*	*1925*	*1926*	*1927*	*1928*
Liabilities—(Continued)						
Govt. funds for loans to industry and trade	109.0	160.1	211.3	178.5	624.9	249.4
Commission and interest. ...	0.8	2.5	8.7	11.9	9.9	242.9
Offices, branches and agencies	....	....	4.2	....	3.3	170.0
Other liabilities	76.0	66.6	145.0	194.5	288.4	695.4
Total liabilities	665.4	1,253.8	2,301.6	2,712.8	3,788.4	4,371.4

[a] The figures for 1923, 1924, and 1925 were taken from *The State Bank of the U.S.S.R., 1921–26* (Moscow, 1927), pp. 31-32; the figures for 1926–28, from *The State Bank of the U.S.S.R. Economic Survey* of March 14, 1928, III, No. 10; and of October 7, 1928, III, No. 34.

The figures as given herein differ from figures given by certain other writers and source books. The difference is due to the fact that Soviet institutions issue preliminary balance sheets, which are later revised and refined. Planning and centralization make necessary the issuance of *estimates* before adjustments are made and final figures can be issued. Then again, it is a matter of classification. Some writers, for example, lump together all loans and discounts, others divide them into separate categories. Similarly with deposits, some exclude the deposits of the treasury, while others include them in the total deposits. Take, for example, the account entitled "Banknote Issue." Some writers state under this heading the amount of notes *transferred* to the bank by the Issue Department, while others include only those notes that were *actually issued* by the bank. In the *Vestnik Finansov*, for instance, the banknote issue in millions of rubles on October 1, 1923, 1924, 1925, 1926, and 1927 is given as 235; 521.9; 946.6; 1,172.6 and 1,471.0 respectively. (See *V.F.* 1927, No. 2, pp. 172-73; No. 4, pp. 168-69; No. 6, p. 216; No. 12, pp. 173-86.)

[b] At home and with correspondents abroad.

[c] According to the *Vestnik Finansov, loc. cit.*, the State Bank's investments in commodities in 1923, 1924, 1925, 1926, and 1927 were (in millions of rubles on October 1 of each of those years) 15.5, 15.8, 37.6, 46.6, and 1.1 respectively.

[d] In parenthesis are the figures given in *Vestnik Finansov, loc. cit.*

[e] Included in "other assets."

[f] Of which 64,600,000 rubles represent the debit balance of the Commissariat of Ways and Communications.

[g] Before losses had been written off; after that the balance amounted to 28,600,000 rubles.

[h] The upper row represents the summarized figures published by the State Bank itself. The figures in parenthesis were taken from the detailed, analytical statements printed in the *Vestnik Finansov* (1927, No. 2, p. 172; No. 4, pp. 174-75; No. 12, p. 180; 1929, No. 7, p. 158).

The rather substantial difference between the two sets of figures is apparently due to the fact that the State Bank had used a different classification.

but were fixed quite arbitrarily with a view to enabling the bank to earn a sufficient profit to meet its operating expenses and to build up its resources.

The discount policy of the State Bank differs very sharply from that of other central banks. Central banks, as we have seen, attempt to guide their discount policy in such a way as to influence the internal and external purchasing power of the monetary unit over which they stand guard.[7] It will be recalled, for example, that the raising of the discount rate on the part of the banks will tend to cause a falling off in the demand for credit and a lowering of prices (or the raising of the internal purchasing power of money) through the forced sales of goods on the part of marginal businessmen, and that, furthermore, it will serve to increase the country's exports in relation to its imports and to attract foreign capital, thus improving the foreign exchange rate of the monetary unit in question. Of course tariffs, restrictive quotas, the fact of being off the gold standard, and so forth, may not permit those tendencies to work themselves out. Nevertheless, under favorable conditions the results would be as outlined above.

In the Soviet Union the discount rate cannot, and is not intended to, accomplish these things. For example, if it is raised by the State Bank, the lowering of prices does not necessarily follow. On the contrary, higher rates would make for higher costs and, consequently, for higher prices (inasmuch as the enterprises are monopolies). Higher prices would discourage, and not encourage, exports. If it is desired to lower prices, the government will issue an order to that effect and the proper commission will carry out that order without resorting to indirect methods. If it is desired to increase the exports in relation to the imports, the government's monopoly of foreign trade can be relied upon to bring that about. To bring about the contraction of the note issue or of the credit outstanding, it is not at all necessary to employ any such devices as the discount rate; the credit plan will provide for that.

[7] Although, as Dr. Eisler says (*Stable Money . . .*, p. 272), central banks as they are constituted at present are primarily concerned with the maintenance of the stability of the exchanges so as to protect their gold reserves.

Conversely, the lowering of the discount rate by the State Bank would not necessarily lead to an expansion of credit or to higher prices. The expansion or contraction of credit in the Soviet Union is governed, as has been said above, by credit plans. The lowering of the rate would reduce costs and thus make possible the lowering of prices. Besides, the expansion of credit in the Soviet Union is likely to enable producers to cheapen their costs of production in general and thus may lead to still lower prices. Nor would the lowering of the discount rate stimulate the flow of capital from the Soviet Union to foreign markets where the rates may be relatively higher, inasmuch as the banknotes are inconvertible and must not be exported or imported, and the foreign exchange rates are fixed by the government.

The capital of the bank.—It has been previously shown that the original capital of the bank was formed through a budgetary grant (of 2,000,000,000,000 paper rubles). As a result of additional budgetary grants as well as of the ploughing in of its profits its capital continued to grow until by October 1, 1928, it amounted to 250,000,000 rubles.[8] In addition, it had on that day a reserve fund and special reserves of 99,900,000 and 6,100,000 rubles, respectively.

The deposits of the bank.—With the measures and devices which were employed during the first years of the State Bank's life with a view to increasing its deposits, we are already familiar. It had been estimated that by the end of 1922 its total deposits, when converted into stable currency, amounted to 37,300,000 rubles, of which 11,300,000 rubles belonged to the Commissariat of Finance. By October 1, 1923, the deposits rose to 157,900,000 rubles. The increase came mainly as a result of the bank's practice of "insuring" deposits against depreciation. This it did by crediting the depositor of depreciated rubles in terms of stable units, and paying him upon withdrawal in sovznaks at the then current rate (or in banknotes, if the bank so chose). On October

[8] In its new statutes of June, 1929, its capital is stated to be 400,000,000 rubles. Its balance sheet of October 1, 1929, still carried, however, the old amount (250,000,000 rubles). Thereafter, it was increased and in the balance sheet of October 1, 1930, it appears as 400,000,000 rubles. Its authorized capital was raised in 1932 to 600,000,000 rubles

1, 1924, the deposits amounted to 308,100,000 rubles. On October 1 of 1925, 1926, 1927, and 1928 they were 742,800,000, 762,700,000, 869,800,000, and 1,302,500,000 rubles, respectively.

On the basis of these figures the increase of 1924 deposits over those of 1923 amounted to 95.1 percent, and of 1925 deposits over 1924, to 141 percent. Thereafter the tempo of increase diminished very sharply; the increase in deposits in 1926 over those in 1925 amounted to but 2.7 percent.[9] The increases over the preceding year for 1927 and 1928 were 14 percent and 49.7 percent, respectively. It was, of course, natural for the early years to register substantial relative increases, inasmuch as the starting figure was very low.

The absolute increase in the State Bank deposits over these years, it will be observed, was quite substantial—from 157,900,000 rubles in 1923 to 1,300,000,000 rubles in 1928. Its predecessor, the Czarist State Bank, on January 1, 1914, had deposits amounting to almost 1,300,000,000 rubles.[10] Those rubles, however, differed materially from the 1928 rubles. Converted on the basis of the Soviet official retail index number into pre-war rubles, the deposits of 1928 would amount to about one-half of those in 1914.[11] Since the deposits at the State Bank of the U.S.S.R. on October 1, 1928, were more than double those of all other Soviet banks on that day, it appears that the total deposits of 4,655,000,000 rubles of all of the Czarist banks (except savings banks) on January 1, 1914, were about five times as large as the total deflated (according to the Soviet index) deposits of all of the Soviet banks (except savings banks) in 1928. Why this difference? For one thing, because the Soviet economy differs drastically from that of the pre-war economy. Certain transactions which formerly resulted in bank deposits were completely eliminated. Concentration in industry and trade was growing apace under the Soviet regime. The huge syndicates and the co-operative centers, embracing as they did numerous producing and trading units, found

[9] The loans and discounts in 1926 as compared with those in 1925 showed a 33 percent increase.

[10] Its outstanding loans and discounts on that day amounted to 1,100,000,000 rubles.

[11] An allowance would have to be made for the change in territory. The above is intended merely to give a rough idea.

it expedient to develop certain "banking" functions of their own. Intra-syndicate transactions, for instance, began to be cleared without the aid of outside banks.[12] This served to decrease bank deposits. Besides, the continuous and rapid expansion of industrial and trading activities, which is so characteristic of present-day Russia, is not conducive to the maintenance of large balances in the banks. In fact, commercial and industrial deposits were, relatively speaking, not very large during those years.

As shown by Table 38, the bulk of deposits belonged to the treasury, to various state administrative agencies, to credit institutions, and to the Ways and Means of Communication. In 1924, for instance, state industry and trade, agriculture and the co-operatives together owned but 71,100,000 rubles or 23.7 percent of the total deposits. The Commissariat of Finance alone owned 106,100,000 rubles, or 32.6 percent, of the total deposits. The heavy participation of the treasury in the formation of deposits by no means diminished during the succeeding years: its share of the total deposits in the State Bank amounted to 47.5 percent in 1925; to 45.5 percent in 1926; and to 44.1 percent in 1927.

In 1928 the state and local budget funds constituted more than one-half (54.4 percent) of the total deposits in the bank.[13] In that year the share of state industry, trade, agriculture, flour mills, and co-operatives in the total deposits of the bank amounted to 22.3 percent, the balance (except for 21,900,000 rubles or 1.7 percent of the total deposits which belonged to private individuals) constituted either budget funds or funds of railroads, post and telegraph, banks and various public and administrative organizations. It will be further observed that those who contributed the bulk of the deposits borrowed but little from the bank, while the state industry and trade and the co-operatives which maintained thin deposits were at the same time the heaviest borrowers.

[12] Lupandin, *The Problems of Bank Credit in the U.S.S.R.* (Moscow, State Finance Press, 1930), pp. 78-79.

[13] The above figures do not include the special funds loaned to industry, trade, and agriculture for the account of the Commissariat of Finance. As has been pointed out already the State Bank acted merely as an agent for the treasury in these transactions. The movement of these transactions is shown on the debit side of the bank's balance sheet by the account entitled "Special Loans," and on the credit side by the account "Government Funds for Loans . . ."

TABLE 38

THE STATE BANK'S DEPOSITS AND LOANS AND DISCOUNTS

1924–28 [a]

(*In millions of rubles on October 1 of each year*)

	1924	*1925*	*1926*	*1927*	*1928*
I. State enterprises					
A. State industry	47.4 (279.3)	116.5 (620.5)	108.1 (971.3)	105.7 (1,246.2)	188.7 (2,021.8)
B. State and "mixed" trade	15.0 (58.1)	31.6 (319.3)	16.6 (164.6)	20.4 (204.8)	26.3[e] (232.7)
C. Transport	11.9 (24.0)	49.0 (68.3)	24.9 (173.5)	39.1 (189.2)	50.7[f] (146.4)
D. Agricultural economy	0.5 (1.0)	0.6 (1.5)	0.4 (1.4)	....	3.1 (3.0)
Flour mills and grain trade	....	....	....	....	6.9
E. Other state administrative and economic organizations[b]	76.7 (6.6)	105.1 (20.8)	153.5 (46.2)	227.9 (60.1)	107.3 (45.8)
Total state enterprises	151.5 (369.0)	302.8 (930.4)	303.5 (1,357.0)	393.1 (1,700.3)	383.0 (2,499.9)
II. Co-operatives	8.2 (141.5)	23.7 (242.4)	24.3 (245.9)	31.3 (299.9)	65.6 (401.7)
III. Private individuals and firms	8.8 (11.2)	19.2 (32.0)	18.7 (23.2)	19.8 (15.9)	21.9 (11.4)
IV. Other enterprises and organizations	....	7.8 (0.7)	23.4 (1.4)	[d]	.... (5.2)
Undistributed among I–IV	0.8 (3.5)	.... (6.1)	.... (28.2)	8.4 (16.4)	4.7 (23.4)
Credit institutions	32.7 (73.3)	36.0 (213.5)	45.6 (246.8)	33.1 (326.5)	76.0 (321.1)
Deposits of the Commissariat of Finance	106.1	353.3	447.2[c]	384.1	....
State and local budget	....	....	....	....	709.1[g]

TABLE 38—*Continued*

THE STATE BANK'S DEPOSITS AND LOANS AND DISCOUNTS

1924–28 [a]

(*In millions of rubles on October 1 of each year*)

	1924	*1925*	*1926*	*1927*	*1928*
Trade unions, party, etc. organizations	....	....	....	....	42.2
Total deposits.....	308.1	742.8	762.7	869.8	1,302.5
Total loans and discounts.....	(598.5)	(1,425.1)	(1,902.5)	(2,359.0)	(3,262.7)

[a] Adapted from the *Vestnik Finansov, loc. cit.* The figures outside parenthesis represent the *deposits*, those in parenthesis, *the loans and discounts* on the corresponding dates, except in 1928 where the July figures are given. Of the total 1,251,000,000 rubles on deposit in the State Bank on July 1, 1928, state enterprises and organizations were responsible for 609,200,000 rubles, of which state industry owned 159,000,000; state trade, 21,100,000; flour mills and grain trade, 17,500,000; ways and means of communications, 40,100,000; agricultural economy, 3,300,000 and "other" state organizations, 368,200,000 rubles. The deposits of the Commissariat of Finance amounted to 529,900,000 rubles; of co-operatives, 48,900,000; of private individuals, 21,000,000; of credit institutions, 38,600,000 rubles.

[b] Such as state and social insurance, various political administrative units, etc.; in short it is composed to a large extent of other than purely economic units.

[c] Apparently a misprint and should probably read 347,200,000 rubles. If it is correct, then the total deposits for that year equal 862,700,000 rubles.

[d] Included under Group E.

[e] State trade.

[f] Ways and means of communication.

[g] A new classification. As a matter of fact the deposits of the Commissariat of Finance for previous years also included "budgetary" items (such as taxes, etc.) which the State Bank collected as the fiscal agent of the state. The State Bank receives and disburses all funds under the Unified State Budget. The deposits of the treasury, therefore, represent the receipts minus the expenditures. Their turnover, as well as that of other deposits, as a result of the rapid unfolding of the national economy is rather rapid; much more so than it used to be in Czarist Russia.

The deposits of private individuals played a very insignificant part in the total deposits. In 1924 they amounted to 2.8 percent, and in 1928 to but 1.7 percent (despite the absolute increase) of the total deposits.

Savings of the wage- and salary-earning classes did not find their way into the State Bank except indirectly through the deposits of the Commissariat of Finance. They went primarily to the savings banks (whose deposits increased from 11,300,000

rubles in 1924 to 314,800,000 rubles in 1928) or were invested directly in government bonds (the gross revenue from which increased from 366,700,000 rubles in 1925 to 1,422,100,000 in 1928 and 2,613,100,000 in 1929).[14]

In its attempt to increase deposits, the bank, as we have seen, allowed interest on them. In the years following the Monetary Reform such interest rates were from 7 to 8 percent on time deposits and 6 percent on demand deposits. In more recent years, the rates varied from 5 to 6 percent, although from August 1, 1932, the bank paid the "collective" farmers 8 percent on their demand deposits and 12 percent on time deposits left for three months or longer.[15] As a rule, banks of issue pay no interest on deposits. Not merely because they do not wish to compete with other banks and take advantage of their superior position (note issue), but because such practice would tend to impede the workings of the official discount rate and of its open market operations. The desire to employ the deposits profitably would interfere with their functions as central banks and banks of issue. Inasmuch as the nature of the State Bank of the U.S.S.R. differs from that of central banks in capitalist countries, the payment by it of interest on deposits did not interfere with any of its other functions. It did produce, however, during the early years, undesirable competition between itself and other banks. The various banks, anxious to attract deposits, either exerted pressure to that effect upon applicants for credit, or else tried to influence the commissariats, which headed prospective "customers." These commissariats began to publish regulations as to where the subordinate organizations were to deposit their funds.[16] To stop that practice the Commissariat of Finance in 1924 ruled that each enterprise and organization had the right to deposit its funds with a bank of its own choosing. The wrangling among the banks, nevertheless, continued until the State Bank emerged victor.

The note issue.—In the preceding sections we dealt with two

[14] *The State Bank of the U.S.S.R. Economic Survey*, December 31, 1928, III, No. 45, and November 30, 1929, IV, No. 38.

[15] Roginski and Rubinshtein, *op. cit.*, p. 31. For more recent changes, see Chapter XV.

[16] Dezen, *The System of Bank Credit*, pp. 27-28.

of the resources of the bank, its capital and its deposits. It has been shown that the treasury participated heavily in the formation of both of them.

The bank had in addition a third, and very important, resource, the right to issue notes. The expansion of its note issue is seen from Table 39:

TABLE 39

TOTAL CURRENCY IN CIRCULATION AND BANK COVER

1924–28 [a]

(*In millions of rubles on October 1 of each year*)

	Banknotes Transferred to the Bank	*Banknotes in Actual Circulation*	*Treasury Notes and Coins*	*Total Currency in Circulation*	*Firm Cover with Issue Department*			
					Gold in Coin and Bullion	Platinum	Foreign Currency and Exchange	Total Firm Cover
1924	518.9	346.5	280.7	627.2	131.4	7.4	103.7	242.5
1925	756.6	652.0	490.9	1,142.9	184.8	31.8	48.5	265.1
1926	856.8	780.6	521.8	1,302.4 [b]	153.3	30.6	53.1	237.0
1927	1,026.6	989.8	638.5	1,628.3	173.6	20.7	77.3	271.6
1928	1,090.1	1,063.7	907.7	1,971.4	148.1	47.1	87.0	282.2 [c]

[a] *Vestnik Finansov*, 1927, No. 10, p. 156; 1928, No. 12, p. 161; also *Our Monetary Circulation*, pp. 132, 133, and 155.

[b] According to *Vestnik Finansov*, 1927, No. 10, p. 156, the amount of banknotes in circulation on October 1, 1926, amounted to 780,600,000; in No. 12, p. 168, it is given as 769,500,000 and the total, therefore, is given there as 1,291,200,000 rubles.

[c] Compare *The State Bank of the U.S.S.R. Economic Survey*, December 31, 1928, III, No. 45.

From October 1, 1924, to October 1, 1928, banknotes in circulation increased from 346,500,000 to 1,063,700,000 rubles—an increase of over 200 percent.

The expansion between 1924 and 1928 of its note issue by some 720,000,000 rubles, of its deposits by about 1,000,000,000 rubles, and of its capital and reserves by an additional 300,000,000 rubles enabled it, as we have seen, to expand its loans and discounts over the same period by 2,456,200,000 rubles.

Inasmuch as the firm cover behind the banknotes did not experience in these years a parallel growth, its ratio to the ever expanding volume of banknotes steadily declined—from 46.7 percent in 1924 it dropped to 35 percent in 1925; to 27.7 percent in 1926; to 26.5 percent in 1927, and, finally, to 25.9 percent (the statutory minimum being 25 percent) in 1928.

Of aid in the matter of financing the national economy were likewise the treasury notes. The Commissariat of Finance, it will be recalled, was transferring to the bank "government funds" for loans to industry, trade, and agriculture (mostly as long-term loans or grants), and, of course, it was making deposits in the bank besides. The increase of treasury circulation during this period amounted to 627,000,000 rubles (from 280,700,000 rubles in 1924 to 907,700,000 rubles in 1928).[17]

On October 1, 1928, the total banknote and treasury circulation reached almost 2,000,000,000 rubles.

As may be seen from Table 40, the credit and currency policy pursued during 1926–27 was a fairly cautious one. For example, although the trade turnover in 1926–27 exceeded that in 1925–26 by 17 percent, the increase in the means of payment during that year amounted to but 6.6 percent. In 1927, however, the means of payment underwent another rapid expansion. And before the swelled streams of circulation had an opportunity to recede to their normal levels, there followed a further expansion of their volume. Thus, on October 1, 1928, the total means of payment registered a 25.8 percent increase over October 1, 1927, although the trade turnover in 1928–29 showed but a 13 percent increase over that in 1927–28. A large part of the additional means of payment, as during the earlier part of this period, was used for the building and the enlargement of plants, factories, workshops, and so forth—all with a view to expanding the production of producers' goods. Since the volume of consumers' goods did not increase in proportion to the increased purchasing power in the hands of the workers engaged in the durable-goods

[17] The ratio between treasury notes and banknotes in circulation moved up during this period from 59.2 to 66.8 percent.

industries, the familiar commodity famine phenomenon continued to exist.

Because of the deepening of price control during those years, the price indices which are given in Table 40 do not show the effect of overissue upon commodity prices. Besides, the retail price index underwent another revision in those years. From October 1, 1924, to October 1, 1926, it climbed from 206 to 230 (showing

TABLE 40

TOTAL MEANS OF PAYMENT, TRADE TURNOVER, PRICE INDICES IN 1924–28

(*In millions of rubles on October 1 of each year*)

Date	*Total Bank-note and Treasury Circulation*	*Total Bank Deposits*[a]	*Total Means of Payment*		*Yearly Increase in Trade Turnover in %*[b]	*Retail Price Index 1913 = 100*[c]	*Wholesale Price Index 1913 = 100*
			In Millions of Rubles	Yearly Increase in %			
1924	627.2	508.0	1,135.2	125.9	44	206	164.3
1925	1,142.9	1,173.5	2,316.4	104.0	51	215	174.2
1926	1,302.4	1,167.7	2,470.1	6.6	17	230 (207)	178.8
1927	1,628.3	1,233.4	2,861.7	15.8	7	198	170.0
1928	1,971.4	1,629.7	3,601.1	25.8	13	211	176.1

[a] The total bank deposits are based upon data given in Chapter XI.

[b] Central Administration of Economic Accounting of the Gosplan of the U.S.S.R., *Socialist Construction of the U.S.S.R., Yearbook* (Moscow, 1934), pp. 362-63.

[c] The index numbers were taken from *The State Bank of the U.S.S.R. Economic Survey*, October, 1926, I, No. 4, and December 31, 1928, III, No. 45.

a drop in the purchasing power of the chervonetz from 4.85 to 4.35 rubles). The latter index number, however, as a result of the revision had been lowered to 207 [18] and a new series of numbers was begun.

Financing of foreign trade.—Although there exists in the Soviet

[18] The revised index numbers for October 1, 1926, were as follows: private trade, 224; state trade, 200; co-operative, 197. These were added and divided by 3.

Union a special Bank for Foreign Trade, the State Bank is a very important factor in the matter of financing foreign trade. In 1923–24, for example, the credits granted by the bank to exporters amounted to 43.3 percent of the total value of all exports, and those granted to importers, to 64.1 percent of the total value of all imports.[19] On October 1, 1928, the State Bank was directly responsible for 78 percent of the total foreign trade credits.

The settlement of international balances.—In view of the state's *valuta* (or foreign exchange) monopoly, the credit that is granted to importers and exporters is given them in the form of Soviet currency. The settlement with foreign sellers and buyers constitutes quite a separate category of transactions.

The credit granted to importers enables them to buy foreign exchange with which to pay foreign exporters, and the sale of the imported commodities provides the funds with which their indebtedness to the banks is paid. The credit granted to exporters is paid by the latter with the valuta obtained from the sale of their commodities abroad.

The settlement with foreign sellers and buyers is effected as in most countries through the mediation of banks. The right to carry on such transactions was given to the State Bank, the Bank for Foreign Trade, the Far Eastern and the Mid-Asiatic banks, the last two being restricted to their respective territories. As we have seen, the State Bank plays the most important part. It may be added that, of a total turnover of about 5,400,000,000 rubles in the "correspondents" accounts of the banks of the Soviet Union in 1928–29, the State Bank was responsible for 5,000,000,000 rubles. Furthermore, settlements with foreign sellers and buyers are effected by banks other than the State Bank only with the approval of the latter.

The method of settlement before 1930 was as follows: the Soviet exporter or importer sold or bought goods abroad through Soviet trading agencies established for that purpose in foreign coun-

[19] N. G. Tumanov, *The Valuta and Credit Policy of the Gosbank* (Moscow, Commissariat of Finance, 1925), p. 82.

tries.[20] Each Soviet trading agency when executing an importer's order settled by means of negotiable commercial paper. It drew at the same time against the Soviet importer so as to be placed in funds when its own obligation matured. The Soviet importer, having obtained permission from a special valuta council, would negotiate the transfer of valuta to the Soviet trading agency and the latter would settle the indebtedness. In so far, however, as the Soviet Union was concerned, the settlement with foreign countries under the above method was taking place when the Soviet trading agency was paid.

This method proved undesirable because the agency abroad, in order to make sure that it would be placed in funds in due time, used to arrange the maturities of the bills that it drew upon Soviet importers in such a way as to have them fall due ahead of the maturities of the bills drawn against it by foreign banks or firms. Thus valuta was being tied up unproductively. Moreover, the method involved separate deals with numerous importers. Then again the trading agency would find itself at times in difficulties inasmuch as it used to combine smaller orders into one larger order covered by a single obligation that matured at a given date despite the fact that, when drawing against the various Soviet importers, it had to comply with the time specifications mentioned in the licenses granted to the latter.

Accordingly after 1930 a different method was devised. Under the new method the settlement with foreign countries was considered to be taking place when the foreign and not the Soviet agency was being paid. Soviet credit institutions were to supply with valuta only those who came in direct contact with foreign banks and firms.[21] Remittances were no longer made in each case separately. The State Bank being the central agency for making international payments is able to plan them in advance and it or the Bank for Foreign Trade makes arrangements with foreign correspondents for the payment of the various obligations which

[20] The latter are agencies of the People's Commissariat of Trade.

[21] This ruling did not apply to foreign branches of Soviet banks and to foreign banks in which Soviet capital participated. Settlements with them were regarded as settlements abroad. Otherwise their resources could not be replenished.

are to fall due within a given month. This method enables the bank to conserve foreign exchange, time, and energy.[22]

It has been stated above that Soviet exporters and importers were required to deal with foreign countries through trading agencies established for that purpose in foreign countries. On July 27, 1935, however, the Council of People's Commissars authorized the Commissariat of Foreign Trade (Decree 367) to allow exporting, importing, and transporting combinations which come under its jurisdiction to enter into transactions with foreign firms whether in the Soviet Union or abroad in their own name, and issue and receive in connection therewith bills of exchange. The activities of these combinations, it will be noticed, continue to be circumscribed by their approved plans.

Foreign exchange policy.—The State Bank is thus faced with the problem of providing sufficient foreign exchange to enable the settlement of international indebtedness. The problem is an important one. The bank must guard its metallic reserves and yet must be in a position to make possible the prompt payment of all such debts, inasmuch as the failure of a single Soviet importer to honor his obligation would tend to impair the credit standing of the Soviet state.

In capitalist countries the task of providing a sufficient supply of foreign exchange is normally left to "natural" or "automatic" forces. Under free trade those forces operate through the international balance of payments. When the demand for foreign exchange increases relatively to the supply, the rates go up; higher exchange rates, normally, tend to stimulate the export of goods, the sale of services by that country, and the flow into it of foreign capital, at the same time discouraging its import trade. As a result of the shift from the debit to the credit items in its international balance of payments, the country's supply of exchange expands. If there is too much of it and the rates go down, opposite forces will tend to bring about a decrease. This constant balancing tends to adjust the supply of foreign exchange to the demand for it. Given free trade, the natural or automatic

[22] J. R. Bliakhov and A. A. Levin, *International Settlements and Foreign Work of the Banks in the U.S.S.R.* (Moscow, State Finance Press, 1931), pp. 8, 9, 27-31.

forces tend to operate not only under metallic standards but even under a paper standard, albeit under the latter to a more limited extent. Under a paper standard too, it will be observed, an increase or decrease in the demand for foreign exchange relative to its supply will tend to cause the rates to rise or fall and thus bring into play forces which help to produce the needed change. But the paper standard is very often resorted to during revolutions, devastating wars, and the like, when the productive powers of the country are crippled and when exports, therefore, however profitable, cannot be increased, and when foreign capital, owing to lack of confidence abroad, cannot be attracted. If this be the case, there will follow a steady sinking of the rates and the natural forces will fail to provide the needed cure.

In the Soviet Union, however, the monopoly of foreign trade by the state precludes the operation of natural or automatic forces. It may be said of course that the supply of foreign exchange in the Soviet Union too is provided automatically, that is, once the "export-import plan" has been drawn up. In a sense that is true, but it must be remembered that during a given period international payments will have to be made against debts contracted at an earlier fiscal period, foreign credits will be obtained, new gold will be mined, and so forth.[23] Hence, to give effect to all of that and at the same time to avoid the depletion of the metallic reserves of the country, it is necessary to draw up a "foreign exchange plan."

Although crude "export-import plans" were used as early as 1921–22, the "foreign-exchange plan" came into being as late as 1925, partly because planning in general received its impetus in the Soviet Union at that time, and largely because the increasing imports made it necessary to watch the metallic reserves.

The execution of the "foreign-exchange plan" is entrusted to the State Bank, in which resides the monopoly of foreign ex-

[23] The "foreign-exchange plan" in fact is based not only upon the "export-import plan" but also upon the "credit plan," which encompasses the credits obtained abroad and the payments due there, as well as upon the "firm-cover plan" (i.e., the planning of an increase in it commensurate with the projected increase of banknote issue). It also takes into consideration the changes in the treasury resources, reserves (or balances) abroad, and the like. There are annual, quarterly, and monthly plans.

change (delegated by the state).[24] The bank is particularly suited for that purpose, inasmuch as the gold and foreign exchange of the country are concentrated in its hands.

Once the foreign exchange plan is adopted all banks are required to comply with it and to render to the State Bank at regular intervals detailed reports of their operations in that field. The foreign exchange policy of the Union underwent certain changes during 1924–28.

Before 1924 foreign exporters and importers, as well as foreign concessionaires, when transacting business with the Soviet Union were obliged to follow the official Moscow exchange rate. The chervonetz at that time was not quoted on foreign exchanges. With the stabilization of the currency an attempt was made to "internationalize" the chervonetz. The chervonetz began to be quoted in Rome, Milan, Riga, and other foreign centers. There naturally arose the problem of protecting the chervonetz on foreign exchanges. A capitalist government, as we know, has several devices at its disposal for that purpose. Through its tariff policy, for example, it can bring about a diminution in the volume of its imports and thereby cause a decrease in the supply of foreign bills of exchange drawn against it abroad (or, what is the same, a decrease in the demand for foreign exchange at home). Through its policy of raising loans abroad it is able to increase the flow of capital in its direction and thereby to cause an increase in foreign demand for exchange on its country. Besides, the discount rate of its central bank can be raised in order to stimulate the flow of foreign capital and investments into the country. In addition to these indirect ways, a government's foreign exchange policy may call for direct intervention on the markets. In such cases it must be ready to buy bills drawn against banks in its own country and to sell bills drawn against banks in other countries. The smaller the confidence in that country's stability, the larger the fund needed for such operations.

The Soviet government believed that its monopoly of foreign trade and, particularly, the planning of imports and exports were

[24] The foreign exchange monopoly was reaffirmed by the state in 1923, when it ordered that exporters deposit all of their foreign exchange with banks authorized to deal in it, and that all banks in turn deposit it with the State Bank.

in themselves sufficient to assure the stability of the chervonetz on foreign exchanges. Although such assumption was logical, certain circumstances, not previously taken into consideration, upset its plans. It has already been mentioned that the shortage of commodities, the high prices in the "free" market, and the inability of the government to lay greater emphasis upon consumers' goods in its import schedules led to the development of contraband trade. In payment for purchases abroad the dealers in contraband goods began to export not only gold, which was more difficult to get, but also large quantities of chervontzy. That, of course, served to increase the supply of exchange on the Soviet Union. To maintain the stability of the external purchasing power of the chervonetz, the State Bank had to remove this excess supply from the foreign markets. In other words, it was necessary to stand ready to redeem these notes in gold (or foreign exchange). The very limited supplies of precious metals, obviously, compelled the bank to refrain from such operations. Hence, the government on July 9, 1926, issued an order forbidding the export of chervontzy. The bank thereupon discontinued the redemption of its notes abroad and the chervontzy there began to be regarded as contraband goods. The career of the chervonetz on foreign markets was consequently short-lived.

The edict against the export of chervontzy did not, however, put a complete stop to dealings in it. Foreigners, whether concessionaires or visitors, found it advantageous to buy them from speculators and in that way obtain better values in the Soviet Union. To the extent that this was being done the Soviet Union was the recipient of less foreign exchange than it could otherwise have gathered in. Accordingly the government, by a further order of March 21, 1928, prohibited not only the export but the import of banknotes as well. It also prohibited the transfer of funds by any other means than those of credit institutions.

Thus, the banknote became a purely internal currency. It is not being quoted, sold, or bought abroad, except illegally. The exchange rates quoted in the U.S.S.R. are determined by a Quotations Commission at the State Bank. The rates are based primarily upon the parities of exchange (that is, upon the rela-

tive metallic contents of the statutory chervonetz and of foreign currencies).[25] Corrections are then made for the changes in the value of foreign currencies as reflected by the appraisal of the principal world exchange markets. Furthermore, once determined, it is not at all difficult, as Table 41 shows, to maintain them at home. The planning and the licensing of imports, the limitations upon all other transfers of funds to foreign countries, the forcing, if necessary, of exports would tend to accomplish that even if forces otherwise were given free play. An increase in the

TABLE 41

MOSCOW FOREIGN EXCHANGE RATES [a]

On:	*Parity*	*January, 1928*		*December 31, 1928*
		Highest	Lowest	
New York	1.943 Rubles per Dollar	1.945	1.943	1.943
London	9.458 Rubles per Pound	9.474	9.46	9.4375
Paris	7.616 Rubles per 100 Francs	7.64	7.56	7.61
Berlin	46.294 Rubles per 100 R. M.	46.33	46.22	46.31

[a] *The State Bank of the U.S.S.R. Economic Survey*, for the respective dates.

demand for exchange relative to its supply does not lead under Soviet conditions to a rise in rates. It simply results in the refusal to grant a license for the import of goods.[26]

Other activities of the bank.—One of the most important and conspicuous functions of the bank is that connected with its

[25] In pursuance of the decrees of November 14, 1935, and February 29, 1936, the ruble was revalued on the basis of 1 ruble = 3 francs. The exchange on the United States, England, and other countries off the gold standard will depend upon what their currencies command in terms of francs. See Chapter XIV.

[26] Bliakhov and Levin, *op. cit.*; Lupandin, op. cit., p. 120; P. Morgunov, "The Straightening of the Basic Lines of the Valuta Policy," *Financial Problems of the Planned Economy*, 1930, No. 6, pp. 87-88; Loevetzky, *op. cit.*, pp. 95-97.

duties as the fiscal agent of the treasury. From its very re-establishment, the State Bank served as a depositary for whatever funds the treasury chose to place with it, a circumstance which, as has been previously pointed out, enabled it to expand its lending operations. In time it was decided to make it possible for the bank to utilize every free copeck of the treasury. Accordingly, as a result of a regulation published by the Council of People's Commissars on September 1, 1925, the People's Commissariat of Finance and the State Bank of the U.S.S.R. entered into a five-year agreement under which, beginning with October 1, 1925, all of the funds of the treasury offices (*Prikhodo-raskhodnye kassy*) were transferred to the bank. The offices (643 in number at the time) were authorized to perform simple banking operations. All of the revenue received by them on behalf of the treasury was to be credited on the books of the bank to a single non-interest-bearing current account of the Commissariat of Finance. All expenditures made by them in connection with the state budget were to be debited to that account.[27] Thus a fusion of the resources of the treasury with those of the bank was brought about.

By a further directed agreement of September 10, 1928, the bank undertook to collect all of the revenue and to make all of the expenditures appertaining to the state budget and to the local budgets throughout the Union, wherever it had or was to have branches or offices. All the treasury offices (kassy), with minor exceptions, were discontinued.[28]

The bank is also active in the matter of distributing government bonds and obligations. This it does in co-operation with the Commissariat of Finance.

Branches, offices, and agencies.—The branches, offices, and agencies with the aid of which the bank carried on all of that work grew from 116 on October 1, 1922, to 486 four years later. During 1927 some of them were discontinued in accordance with the policy at that time of eliminating unnecessary overhead expenses.

[27] Pevzner and Diisin, *loc. cit.*, Pt. II, pp. 176-78; also *The State Bank of the U.S.S.R., 1921–26*, p. 45.

[28] *Collected Decrees*, 1928, Decree 481.

On October 1, 1927, they numbered 417, but a year later their number jumped to slightly less than 600.[29]

The relation of the bank with other banks. The Committee of Banks of 1924.—During the early years of the bank's existence there developed, as has been shown, an unwholesome competition between it and other banks. Deaf to the pleas of the other banks that it remain a central bank, a bankers' bank, the State Bank was fighting them, and not without success, for "lucrative" clients. True, the banks did not seek profit for its own sake, they were merely anxious to present a good showing, but nevertheless the competition led to excesses and wastes, such as the opening of more branches than business justified. There was a need for leadership. It was necessary to bring the various credit institutions into a credit *system*.

The first step in this direction was taken on June 24, 1924 (as a result of the regulation of the Council of People's Commissars of that day), at which time there was formed at the State Bank a body known as the *Committee of Banks*. Its membership—in addition to the chairman of the State Bank's board (or his representative), who was also the chairman of the Committee—included the chairmen or representatives of the boards of other banks, all these with a decisive vote, and, besides, representatives from the Commissariat of Finance of the U.S.S.R., from the Supreme Council of National Economy of the U.S.S.R., from the Commissariats of Foreign Trade, of Internal Trade, and, finally, from the State Planning Commission—this latter group with a deliberative vote.[30]

As stated in the regulation, the object of the Committee was to co-ordinate the activities of the credit institutions and to cope with general problems pertaining to the regulation of bank credit. With a view to that the Committee was instructed to consider questions pertaining to the general credit policy, to the distribution of credit among the various branches of the national economy, co-ordination of interest rates, expansion of the credit sys-

[29] According to *The State Bank of the U.S.S.R. Economic Survey*, VI, No. 2 (February, 1931), its branches on October 1, 1928, numbered 588. *The National Economy of the U.S.S.R. Statistical Manual for 1932* (Moscow, State Social-Economic Press, 1932), p. 602, on the other hand, states it to have been 599.

[30] Pevzner and Drisin, *loc. cit.*, p. 76.

tem, and the like. Its decisions were to be transmitted to the Commissariat of Finance, and, if approved by the latter, either adopted or recommended for enactment.

With great avidity and assiduity the Committee began to discuss various important issues. A number of important resolutions were made. So pleased was the Committee with its work that it decided to organize local bank conferences at the branches of the State Bank in the more important cities where there were not less than three banks. This activity, however, lasted but a few months. The many resolutions were not lived up to by the members of the Committee. Nothing of importance was accomplished. The Committee's work thereafter was confined to the drawing up of credit plans.[31]

The burning problem of how to eliminate the overlapping activities of various "independent" banks was not solved. True, the Commission (headed by Smirnov) which was entrusted with solving it recommended the apportionment of clients among the banks, but no legislative steps were taken.

The Laws of June 15, and June 20, 1927, delimiting the activities of the banks.—It was not until 1927 that the government took a really decisive step in that direction. In that year, on June 15, the Central Executive Committee and the Council of People's Commissars of the U.S.S.R., "in order to achieve unity in the work of the credit system and to secure to the State Bank of the U.S.S.R. a leading rôle with respect to all other banks," published a decree entitled "principles underlying the structure of the credit system.[32] As a result of that decree the State Bank achieved leadership over the country's banking system. It was empowered to participate, through its representatives, in the councils and auditing committees of all credit institutions which received their capital from the state. It was also given the right to supervise the expenditure of the credit granted by it to other banks, as well as to make certain that it was distributed by them among the branches of the national economy in accordance with the government's instructions. The State Bank was, furthermore,

[31] J. Kuperman, "The Problem of Regulating the Present Bank System of the U.S.S.R.," *Vestnik Finansov*, 1926, Nos. 5-6, p. 9.

[32] *Collected Decrees*, 1927, Decrees 363 and 364.

empowered to demand from all credit institutions financial statements and information with respect to credits opened for individual clients and to the indebtedness of the latter, as well as to the deposits of state agencies. To strengthen the financial relations of the bank with all other banks it was necessary, according to the decree, to increase the size of the bank's ownership of their stock. Accordingly the Commissariat of Finance was instructed to turn over all such stock owned by it to the State Bank. The banks were directed to deposit their free reserves with the State Bank. The size of such deposits was to be determined by the Committee of Banks. The bank on its part was required, when extending credit to them, to take into consideration the general economic and financial situation, the strength of the individual bank, as well as the growth of the borrowing bank's operations.

In the matter of deposits the decree specified that the State Bank was to serve as a depositary for the funds of the state budget, savings banks, state and social insurance, state alcohol monopoly, and state playing cards monopoly, subject to certain qualifications. The funds of organizations that were covered by local budgets could be deposited in either the State Bank or in local municipal or agricultural banks.

The bank was also provided with a definite borrowing clientele. The approved list included: (a) credit institutions; (b) transactions in grain, transactions in raw materials (with certain exceptions); (c) ways of communication; (d) state trading enterprises of an All-Union or republican importance (engaged in domestic trade) as well as their local establishments, and joint-stock trading enterprises in which state capital predominated (with certain exceptions); (e) the largest industrial enterprises and combinations of an All-Union or republican importance and their local establishments in whole or in part; (f) the largest co-operative organizations of an All-Union, republican, regional, district, provincial, or county importance in whole or in part as per agreement between the State Bank on the one hand, and the co-operative banks and the Central Agricultural Bank on the other; and, finally, (g) local state industry and trade, in whole where there

are no municipal banks or branches of the respective specialized central banks, and in part (by agreement) where municipal banks are found.

The "specialized" credit institutions (such as the Industrial Bank, the Agricultural Credit System, the Municipal Credit System, and others) were to grant *long-term credit* within their own fields if they belonged to the long-term credit type and also short-term credit within the same fields in cases where the clientele was not secured to the State Bank. The decree directed that as a general rule clients must obtain short-term credit from no more than one bank, on the principle of one client—one bank.

Finally, the decree ordered the broadening of the activities of the Committee of Banks, as well as of the Bank Conferences, in order to "co-ordinate the work of the banks, rationalize their operations, lower costs, and so forth." The Committee was attached to the Commissariat of Finance of the U.S.S.R. under the chairmanship of the Commissar of Finance.

The execution of the above decree was entrusted to the Commissariats of Finance and of Workers' and Peasants' Inspection. Accordingly the Commissariats issued on June 20, 1927, instructions and regulations embodying the provisions of the above act as well as giving effect to an earlier decree (of May 17, 1927) of the Council of People's Commissars concerning the crediting of foreign trade.[33]

So important was this legislation at the time that many writers referred to it as the new charter or constitution of Soviet banks. Its importance lay in the fact that it had put an end to the agitation for a banks' bank, that it definitely established the State Bank's leadership in the banking *system,* and brought about the concentration of the bulk of the short-term credit business in the bank's hands.

The reason for placing the leadership in the State Bank is clear and need not be explained. The concentration of short-

[33] The decree of May 17, 1927, specified which exports or imports were to be financed by the State Bank and which by the Bank for Foreign Trade. The two Commissariats were assisted in this work by a "Central Commission for the Delimitation of Banks" which was formed in May, 1927. See *Finance and National Economy,* 1927, No. 32 (40), p. 19.

term credit in the bank needs, however, a word of explanation.

Inasmuch as bank deposits did not show any considerable growth during this period, note issue was the main source for short-term credit. Hence the decision to let the bank which enjoyed the monopoly of note issue grant short-term credit without the aid of intermediaries. On the other hand, it must be remembered that socialist philosophy always stressed the importance of economic concentration in general and of banking concentration in particular. This no doubt influenced the decision. At any rate it was an important step towards making the State Bank "the one and the largest." [34]

In the years that followed, more and more of the short-term credit business was being concentrated in the hands of the bank until it became almost the sole dispenser of it.[35]

Comparison between the Imperial State Bank and the State Bank of the U.S.S.R.—Inasmuch as 1928 is considered the year in which production in the Soviet Union reached the pre-war level, it may not be uninteresting to compare the balance-sheet items of the Czarist State Bank and of the State Bank of the U.S.S.R. True, the radical change in the economy, the fact that those two banks did not cover the same territory, and the changed purchasing power of the ruble prevent anything but a rough comparison. But even so, a comparison of this kind will accentuate the changed nature of the State Bank. Let us examine Table 42.

[34] Lenin's expression.

[35] On February 14, 1928, all the short-term credit business of the Industrial Bank was transferred to the State Bank. In the same year it was resolved that the State Bank was also to grant short-term credit to agricultural organizations, with the understanding, however, that it would carry out such operations through the agricultural credit associations. When the Credit Reform of 1930 was enacted, the All-Russian and the Ukrainian Co-operative Banks were ordered to liquidate their branches. Without them, however, these banks could not carry on short-term credit business; and so they remained long-term credit institutions. But even before that the State Bank came to an understanding with the Bank for Foreign Trade, whereby the latter lost the right to grant short-term credit in connection with the *production* of exportable goods. The mutual-credit societies which granted commercial credit to private individuals and firms were eliminated. Of the municipal banks only the local banks retained that right but the volume of business handled by them in this connection was quite insignificant. The Central Municipal Bank was deprived of the right to grant such credit. See A. Kaktyn, *Basic Questions of the Credit Reform,* Second Edition (Moscow, State Finance Press, 1930), pp. 7-10.

TABLE 42

COMPARISON BETWEEN THE BALANCE SHEETS OF THE IMPERIAL STATE BANK AND OF THE STATE BANK OF THE U.S.S.R. [a]

JANUARY 1, 1914–OCTOBER 1, 1928

	January 1, 1914		*October 1, 1928*		
	In Millions of Rubles	As a % of its Balance Sheet Total	In Millions of Rubles	As a % of its Balance Sheet Total	Column 3 Deflated [c]
	1	2	3	4	5
Assets					
Cash, precious metals, foreign exchange	1,866.3	59.2	345.0	7.9	163.5
Securities	107.9	3.5	276.6	6.3	131.1
Loans and discounts [b]	1,072.0	34.0	3,054.7	69.8	1,447.7
Miscellaneous	104.7	3.3	695.1	16.0	329.4
Total assets	3,150.9	100.0	4,371.4	100.0	2,071.7
Capital and Liabilities					
Capital	55.0	1.8	356.0	8.1	168.7
Note issue	1,775.0	56.3	1,090.1	24.9	516.6
Time and demand deposits	1,228.2	39.0	1,302.5	29.8	617.3
(a) Treasury deposits	(951.2)	(30.2)	(709.1)	(16.2)	(336.1)
(b) Other deposits	(277.0)	(8.8)	(593.4)	(13.6)	(281.2)
Miscellaneous	92.7	2.9	1,622.8	37.2	769.1
Total capital and liabilities	3,150.9	100.0	4,371.4	100.0	2,071.7

[a] *Economic Conditions of the U.S.S.R. and World Economic Conditions in 1925–26* (Moscow, Commissariat of Finance Press, 1927), pp. 188-96. Also Table 37, *supra*.

[b] The loans and discounts account of the Czarist Bank on the assets' side and its time and demand deposits account on the liabilities' side include transactions with correspondents at home. The respective accounts of the State Bank of the U.S.S.R. do not include them. They are listed by the latter separately, but have been merged here in the miscellaneous groups.

[c] With the aid of the Soviet Retail Price Index for that date (211).

The first striking difference is found in the very first item on the assets side. The Czarist State Bank had on January 1, 1914, 1,866,300,000 rubles in cash, precious metals, and foreign exchange, whereas the Soviet Bank on October 1, 1928, had only 163,500,000 rubles (deflated).[36] The relative weight of that item in the balance sheet of the former bank was 59.2 percent, and in the balance sheet of the latter, 7.9 percent. This was, of course, due to the fact that the metallic reserves of the old State Bank were very much larger than those of the State Bank of the U.S.S.R. in 1928. The Czarist Bank needed a larger reserve: its note issue was larger and was convertible into gold.

Another striking difference is found in the loans and discounts of the respective banks. On January 1, 1914, these amounted to 1,072,000,000 rubles and constituted 34 percent of the balance-sheet total whereas on October 1, 1928, they reached 1,447,700,000 rubles (deflated) and represented 69.8 percent of the balance-sheet total of that day. Why this difference? The old bank was operated as a bank for banks; it did not compete with other banks. The State Bank of the U.S.S.R., on the other hand, pursued a diametrically opposite policy. It proceeded to expand its own "commercial" transactions, and all short-term credits came to be concentrated in that bank.

The capital of the new bank is much larger. The nature of its operations, however, necessitate a larger capital. The note issue of the old bank on January 1, 1914, was 1,775,000,000 rubles and formed 56.3 percent of the balance-sheet total as against 516,600,000 rubles (deflated) or 24.9 percent of the balance-sheet total on October 1, 1928. The balance sheets of the two banks seem to indicate that the Czarist bank employed the note issue principally to acquire precious metals, whereas the Soviet bank used only a small part of its notes for that purpose; the rest it used for the purpose of extending credit to the national economy. When comparing the size of the issues an allowance, however, must be made for the fact that the Czarist currency shown above included all paper currency, whereas the Soviet banknotes constitute but a

[36] For purposes of comparison the deflated figures will be used in this section.

part of the total paper money in circulation. When deflated, the total of paper currency in the Soviet Union on October 1, 1928, amounted to 934,300,000 rubles. But even so there seems to be a wide difference. This difference was undoubtedly due to the changed economic system which eliminated a number of transactions that previously required money. It was probably also due, at least to some extent, to the fact that a substantial part of the old currency was being hoarded by the peasantry.

The reasons for the difference in deposits (1,228,200,000 rubles on January 1, 1914, and 617,300,000 rubles on October 1, 1928) has already been explained. The old bank, it may be added, paid no interest on deposits.

The treasury deposits in the new bank were smaller than they were under the old regime, presumably because the Soviet government used every available ruble for the building up of the national economy.

These, in short, are some of the important points of difference between the two banks that can be discerned when a comparison of their balance sheets is made.

The distinguishing characteristics of the State Bank and of Soviet banks in general.—The qualitative differences between the Czarist State Bank and the State Bank of the U.S.S.R., however, are not shown by their balance sheets. Both, for instance, were state-owned, but, whereas the clientele of the Czarist Bank was primarily composed of private individuals, private firms, private banks, and so forth, that of the State Bank of the U.S.S.R., owing to the changed economic and political order, is composed almost in its entirety of state agencies.

The new order eliminated a good many of the old institutions, and with them a number of the banking transactions that are peculiar to capitalist countries. For example, the speculative and investment activities in stocks and bonds, which used to create business for the old Russian banks, were entirely abolished. Under the old regime, business enterprises used to sell their securities or borrow against them from the banks, thus creating deposits, a feature which the new regime has eliminated. Dividends used to be

paid and deposited in the banks by the recipients. Loans used to be granted against real-estate mortgages, but here again with the abolition of private property these transactions entirely disappeared and with them another section of bank loans and bank deposits. Furthermore, price control and government regulation of the markets eliminated large-scale speculative operations in commodities, together with all the banking transactions that used to arise therefrom.

There are also other and very important differences between Soviet banks and the old Russian banks, or, what is the same, between Soviet banks and banks in capitalist countries. Soviet banks are not only *economic* institutions, they are *socio-political* institutions as well. They are used by the state as a means for the preservation of the dictatorship of the proletariat and for the building of socialism. For example, the *kulaks* (well-to-do peasants) and some private traders or speculators may be better able to meet a loan at maturity and could pay more for its use than the poorest peasants, or some state enterprises or collective farms, but because the state considers it socially and politically desirable to extinguish the former and to strengthen the latter, bank loans are denied to the *kulaks* and private traders.

The *yield* from the investment of funds or from the extension of credit does not at all influence Soviet banks. The charges that they make (*interest* or *discount rates*) are calculated to enable them to meet losses without an impairment of their capital and to provide for an expansion of their resources. The discount rate, as we have seen, is not the result of an interaction of the supply of credit and the demand for it. Nor does it serve as a regulator of the volume of credit. Regulation in the Soviet Union is sought through conscious planning and not through natural or automatic devices.

The banks not only help their clients to plan their business activities and particularly the expenditure of the loans, but also exercise control over them during the life of the loans. The loans are generally granted for specific purposes and must be so applied. The banks, therefore, attempt to guide and watch the application of the borrowed funds and to make sure that the borrower lives

up to the plan which was presented by him when the request for credit was made and which was incorporated into the general credit plan.

Control over the borrowers was exercised during the years under review not only through the banks, but also through such agencies of the state as the *Workers' and Peasants' Inspection,* the *State Financial Control Board,* various auditing committees of the trusts and other economic units, and, finally, through public opinion.

Soviet banks have no choice in the matter of selecting "customers." Credit granting, as will presently be shown, is governed by plans. Nevertheless, a Soviet bank need not continue dealing with an enterprise which fails to honor its obligations. If a given enterprise is in deficit because it is young, inexperienced, and so forth, but its output is needed, the state or the local budget will take care of it. If an investigation shows that its losses are due to inefficient, dishonest, or disloyal managers, steps are taken to remove them. It takes time, of course, before the discovery is made, and this is one of the reasons why not all loans are paid at maturity and some are never paid.

But failure to maintain liquidity under the Soviet regime, it must be understood, is not fraught with the same danger as under the capitalist regime. Under the former, financial panics and runs are quite impossible inasmuch as the borrowers and depositors are state agencies which obey the word of the same master that the banks do. If an obligation cannot be met promptly the doors of the bank need not be shut, the client will be instructed to call at some other time.

But Soviet banks are not at all oblivious to the importance of meeting obligations when they are due. If they were, they would wreck the elaborate apparatus of national planning; for how could a given enterprise furnish its quota of the planned output when the required credit for it was not furnished on time? As a matter of fact they attempt to estimate in advance the resources that will be at their disposal within a given period and try not to create more obligations than can be met. In other words, credit is planned in the Soviet Union. This *planning of credit* is also one of the most important characteristics of Soviet banking.

Credit planning.—Planning in general and credit planning in particular constitute the foundation stones of Soviet economy. It is, of course, a well-known fact that properly managed business concerns and properly managed credit institutions plan their activities also under a capitalist economy. There is, however, a vast difference between the two types of planning. The difference consists in the fact that in the Soviet Union the plans of the various economic units are co-ordinated and integrated into a unified plan for the entire country, whereas under the capitalist economy the plans of individual business enterprises (credit institutions included) are not co-ordinated, are not integrated, and do not form a unified plan for the entire country.

The first attempts at credit planning in the Soviet Union were made as early as the fall of 1922, when an annual plan was drawn up. Those attempts were due not only to the socialist philosophy but to the scarcity of funds as well. Inasmuch as the demand for credit exceeded its supply, it became necessary to apportion the available funds among the various claimants. Naturally the apportionment had to be carried out in such a way as not to leave out any essential branch of the economy—hence, planning. The early plans were very crude. Those of the State Bank, for example, were confined, so to say, to the distribution of its banknotes. With 1923–24, the credit plans of the bank took on a different aspect. The bank began to draw up quarterly plans. These plans were broadened to include its basic assets and liabilities accounts. Still, until October 1, 1924, such plans covered only the Main Office of the bank, its branches being included only in the form of a total balance. From that date its branches, too, commenced to draw up credit plans and the bank's plans began to embrace the separate plans of all of its links. In 1924 credit planning in the Soviet Union was already a well-established institution. All banks of national importance began to be required to draw up and present monthly and quarterly plans for co-ordination to the Committee of Banks. When so co-ordinated they were forwarded to the State Planning Commission (or Gosplan) and finally to the Council of Labor and Defense for approval. Gradually, too, the State Bank,

which until the end of 1924 was not infrequently confronted with a solid opposition on the part of all other banks that were apparently imbued with a desire to break up the bank's "hegemony," took an upper hand also in the matter of credit planning. Its monopoly of note issue won here too, and the bank commenced (on its own initiative at first) to draw up co-ordinated credit plans for the entire Union.

The distribution of credit was arranged in the credit plans by branches of economy and types of industry. This helped to secure to the banks a certain degree of leeway.

Credit planning, however, is not as easy as it may at first appear. All economic planning is difficult. After all, when you attempt to draw up plans for a nation's industries, for its trade, domestic and foreign, and for its agriculture, you deal with a great many unknowns which cannot be predicted with exactitude. But the planning of credit is even more complicated than the planning of any of the above-mentioned activities, because it is derivative planning. It is based upon all of those plans, and, therefore, incorporates all of the errors contained in them. And yet to be effective credit plans must be interlaced with the plans of the entire national economy.

Broadly speaking, the credit plans of the State Bank in their final form are divided into two sections: (a) resources and (b) channels into which they are to be directed during a given quarter of the year.

On the resources (or liabilities) side the bank, giving in each case the estimated balance of the account at the beginning of the quarter, the changes during the quarter, and the estimated balance at the end of the quarter, includes the following accounts: profit; deposits (itemized so as to show the movement of deposits of the state and local budgets, state and social insurance, trade unions, savings banks, and so forth); repayment of debts (also itemized and including the various commissariats, consumers' cooperatives, etc.); accounts of credit institutions (itemized); and "other" liabilities.

The loans and discounts (classified in the same manner as under

"repayment of debts" on the liabilities side) are shown on the other side.[37]

It is, of course, the "resources" (or liabilities) side that presents the difficulties. If the bank's estimates as to the repayment of previous loans and discounts by its clients are wrong, if their deposits fall below the estimates, the bank will have to resort to additional banknote issue (which may not always be feasible or advisable) or else curtail the projected loans and discounts. The latter step, however, will cause the flow of repayments and deposits into the bank to become still weaker (not to mention the disruption of the general plan). Whether or not the repayment of loans and discounts and the balance of deposits will approximate the amounts estimated by the bank, will, of course, depend upon the accuracy with which the plans of individual enterprises had been made up. For example, if those enterprises are unable to increase the productivity of labor or to lower the cost of production as instructed—to take but a few possibilities—the bank's credit plans are upset.[38]

These difficulties are reflected in the discrepancies between the estimated and the actual performance by the bank. The figures for 1926–27 and 1927–28 are shown in Table 43. The wide discrepancies are seen at a glance. The bank, in these early plans, was unable to foresee the movement of deposits, of the account with the Commissariat of Finance or of the financing of grain purchases—the latter depending upon crop conditions and, therefore, among other things, upon the weather.

Calculated over a longer period, its plans were somewhat closer to the actual performance. Thus, the figures for the entire 1927–28 period were:

	Plan	Actual
Note issue	+395	+338
Deposits	+100	− 72
Loans	−627.7	−818.5
Financing of grain	−160	− 82

[37] O. J. Efimov, *The Technique of Credit and Cash-Account Planning* (Moscow, State Finance Press, 1933), pp. 15-21.

[38] Lupandin, *op. cit.*, pp. 126-32.

TABLE 43

THE CREDIT PLANS OF THE STATE BANK AND THE ACTUAL PERFORMANCE [a]

	Year	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
		Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual
Note issue	1926–27	+100.8	+ 63.0	− 75.0	− 70.0	....	+135.7	+ 75.0	+208.6
	1927–28	+170.0	+ 39.5	−150.0	−149.5	+125.0	+178.6	+250.0	+269.8
Deposits of Commissariat of Finance [b]	1926–27	....	+ 4.5	....	+ 44.8	....	+ 62.2	+ 35.0	− 5.8
	1927–28	+ 37.0	− 18.3	+ 58.0	+141.9	....	− 43.5	+ 5.0	− 57.6
Other deposits	1926–27	....	+ 74.2	....	+ 53.7	....	− 16.7	....	....
	1927–28	+ 29.5	+ 42.5	+ 20.0	+ 26.8	− 62.0	− 30.8	− 35.0	− 15.0
Account with the Commissariat of Finance	1927–28	+136.0	+ 71.2	+126.0	+ 29.4	+ 90.7	+ 58.2	+ 39.8	+ 97.6
Loans and discounts	1926–27	−136.1	−155.6	− 52.0	− 6.2	−160.0	−306.6	− 80.0	−103.0
	1927–28	−236.7	−238.0	− 25.7	− 65.3	−226.5	−318.7	−139.3	−196.5
Financing grain purchases	1926–27	− 80.0	− 76.4	+ 25.0	+ 70.7	+ 65.0	+ 94.7	− 60.0	− 94.4
	1927–28	−140.0	− 12.2	− 10.0	− 63.4	+100.0	+139.5	−110.0	−146.5

[a] Lupandin, *op. cit.*, p. 137.

[b] In 1926–27 the deposits of the Commissariat of Finance and "other" deposits are shown jointly. The *plan* for that period did not include deposits.

The nearest approach to the actual is shown by the note issue, but as for the rest, the bank's estimates and the actual performance were wide apart even when the entire year's figures are included. Great accuracy was not achieved in the few years that followed.

In fact, during those years there raged a controversy in the Soviet Union as to the nature of planning in general and of credit planning in particular. One school held to the idea that planning can be nothing more than a mere prevision, or prognosis (and even then far from accurate) of phenomena and relationships which are bound to come as a result of a definite, causal development, as a result of an immanent economic process. The opposing school held that the function of planning was not to foresee what was bound to happen, but what could and should happen when the economic system strained its will power.[39] Needless to say, the official Soviet policy adopted (particularly since October 1, 1928) the latter philosophy.

From what has been said above, it must not be concluded that planning in general and credit planning in particular have no merit. The Soviet Union had at the time merely begun to amass the experience needed for accurate planning. The rapidity, the feverishness of the economic progress of that country, the kaleidoscopic changes in the following years continued to interfere with accurate planning. It is far easier to plan when economic conditions are normalized and when the economic tempo of one year does not differ materially from that of another than in the midst of a gigantic industrial revolution. But just the same, planning in the Soviet Union is steadily improving even though it has by no means been reduced to an exact science, and even in its imperfect state it has proved of inestimable value to the economy of the country.

The present planning apparatus and the planning methods employed today are far more scientific, far more complex than they were during the earlier years of their evolution. Inasmuch, however, as the scope of the present chapter does not reach beyond 1928, their treatment is reserved for later chapters.

[39] See Lupandin, *op. cit.*, p. 126; also S. Strumilin "On the Theory of Planning," *Planned Economy* (Moscow, 1928), No. 11.

XI

THE EVOLUTION OF A SYSTEM OF SPECIALIZED BANKS

A general view of the development of banks during 1922–28.— When, in response to the needs growing out of the New Economic Policy, the Soviet government had re-established the State Bank in 1921, it was intended that the bank remain the sole credit institution of the country. The communists, it will be recalled, regarded a giant monopolistic credit institution not only as no menace to a socialist order but, on the contrary, as a positive aid in its achievement. In the words of Lenin:

> Large banks constitute that "state apparatus" which we need for the realization of socialism and which we take ready made from capitalism; our problem is merely to cut away that which capitalistically cripples this excellent apparatus, to make it still larger, still more democratic, still more universal; quantity will change into quality; a single state bank of huge dimensions, with branches in every *volost*,[1] in every factory, is already nine-tenths of the socialist apparatus; it is a general state bookkeeping, a general state accounting of the production and distribution of commodities, it is, so to say, something in the nature of a skeleton of a socialist society.[2]

The unfolding of the New Economic Policy, the temporary detour from the socialist path to what some regarded as the path of state capitalism, created a demand for, and necessitated the introduction of, a good many institutions which would not have been tolerated earlier. Among the latter were a number of banking institutions.

The agitation for the creation of commercial and investment banks began soon after the re-establishment of the State Bank. It came as a result of the latter's inability to meet fully the demand of the various enterprises for credit. Its resources, considering the growing needs of the economy which it was to serve, were, as we have seen, quite moderate. Besides, it had to use a portion of

[1] A *volost* is a district embracing several villages.
[2] Lenin, *Collected Works*, Second edition, XXI, 260.

these resources towards the accumulation of a gold reserve. The dissatisfaction of those engaged in trade and industry became especially pronounced when the bank through its lending policy made it clear that it did not mean to use indiscriminately its right of note issue to provide long-term credits. As a result there followed the organization of a number of banks, each specializing within a given field and catering to a given clientele. They were mostly of the joint-stock type of organization.

The first to be organized (that is, after the State Bank) was the Consumers' Co-operative Bank (Bank Potrebitelskoy Kooperatzii) known, in its abbreviated form, as "Pokobank." Its statutes were approved on February 16, 1922, and on the twentieth of the same month it commenced operations. About a year later it was reorganized as the All-Russian Co-operative Bank (Vserossiiyskii Kooperativnyi Bank) or "Vsekobank." [3]

Several other banks were organized during the same year (1922): the Far Eastern Bank (Dalne-Vostochnyi Bank) or "Dalbank"; [4] a number of mutual-credit societies (Obschestva Vzaimnogo Kredita or "O.V.K.") of which the Leningrad Society, organized on June 1, was the first; also the Russian Commercial Bank (Rossiiskii Kommercheskii Bank) or "Roskombank," representing an unsuccessful attempt to found in Soviet Russia a bank with foreign (Swedish) capital, the statutes of which were approved on October 19 of that year, but which was reorganized in 1924 as the Bank for Foreign Trade (Bank dlia Vneshnei Torgovli) or "Vneshtorgbank"; and finally, the Industrial Bank (Promyshlennyi Bank) or "Prombank," the original statutes of which were approved on September 1, 1922. Shortly thereafter this last was renamed Commercial-Industrial Bank of the U.S.S.R. (Torgovo-Promyshlennyi Bank S.S.S.R.).

In 1923 there were opened a number of *municipal* or *city banks,* first among which was the Moscow City Bank (Moskovskii Go-

[3] The original statutes of the All-Ukrainian Co-operative Bank or "Ukrainbank," the main provisions of which resemble those of the Vsekobank, were approved on October 27, 1922.

[4] Established by the Far Eastern Republic; reorganized on March 24, 1923. There was also organized in April a South Eastern Commercial Bank (Yugo-Vostochnyi Kommercheskyi Bank) which did not, however, play an important part.

rodskoi Bank) or "Mosgorbank." From 1925 these were headed by the Central Municipal and Housing Bank (Tzentralnyi Bank Kommunalnogo Khoziaistva i Zhilischnogo Stroitelstva or "Tzekombank"), organized that year.

There were also opened in 1923 a number of agricultural credit societies (Obschestva Selsko-Khoziaistvennogo Kredita), and agricultural banks, which in February, 1924, came under the head of the newly organized Central Agricultural Bank of the U.S.S.R. (Tzentralnyi Selsko-Khoziaistvennyi Bank S.S.S.R.) or "Tz. S.-Kh. Bank." [5]

Among other banks organized in 1924 may be mentioned the Mid-Asiatic Commercial Bank (Sredne-Aziatskii Kommercheskii Bank), and among those organized in 1925, the Joint-Stock Bank for Electrification (Aktzionernyi Bank Po Electrifikatzii) or the "Electrobank." [6]

If we add to the above the savings banks, which date from 1923, and the pawnshops ("lombardy"), which date from 1922–23, we have a picture of the rapid unfolding of the credit system between 1922 and 1926. Thereafter, the numerical growth stopped and, in fact, some banks and branches were discontinued (see Table 44).

The quantitative growth of the banking units before 1924, that is before the Monetary Reform had been introduced, cannot be said to have been accompanied by a qualitative growth.

Continuous depreciation of a currency, as has been pointed out, is not at all conducive to the development of banking. To begin with, the steady annihilation of the value of the monetary unit in which repayment of the loan is to take place endangers the position of the lender. It will be recalled that it was under such

[5] In addition to the agricultural associations which had been organized earlier.

[6] The Electrobank was formed out of the All-Russian Joint-Stock Company for the Financing of Local Electrification ("Electrocredit"), which was established as early as 1922. The Electrobank's life, however, was short. In 1928, when the Commercial-Industrial Bank of the U.S.S.R. (Prombank) was reorganized as the Bank of Long-Term Credits for Industry and Electrification of the U.S.S.R. (Bank Dolgosrochnogo Kreditovania Promyshlennosti i Electrokhoziaistva S.S.S.R. or B.D.K.)—still referred to as Prombank—the assets and liabilities of the Electrobank, except those pertaining to short-term credit, were transferred to it. Its short-term assets and liabilities were transferred to the State Bank.

TABLE 44

THE DEVELOPMENT OF CREDIT INSTITUTIONS IN THE U.S.S.R.[a]

AT THE BEGINNING OF EACH FISCAL YEAR, THAT IS, ON OCTOBER 1

	1922		1923		1924		1925		1926		1927		1928	
	Main	Branches	Main	Branches	Main	Branches	Main	Branches	Main	Branches	Main	Branches	Main	Branches
State bank	1	116	1	271	1	390	1	458[b]	1	486	1	417	1	583
Prombank	...	...	1	35	1	72	1	82	1	88	1	33	1	6
Vneshtorgbank	...	...	1	2	1	4	1	9	1	9	1	4	1	...
Vsekobank	1	5	1	25	1	53	1	59	1	61	1	45	1	41
Agricultural credit system	...	...	...	...	49	103	66	130	71	140	78	129	76	111
Electrobank	...	...	...	...	...	...	1	2	1	3	1	...	...	...
Tzekombank	...	...	...	...	...	...	1	...	1	2	1	2	1	2

Mosgorbank	...	...	1	15	1	51	1	77	1	74	1	31	1	26
Municipal (city) banks	..	..	8	3	16	19	29	45	43	77	49	43	50	41
Dalbank	1	6	1	9	1	9	1	10	1	9	1	7	1	6
North-Caucasian bank	1	...	1	...	1	...	1	...	1	...	...	...	...	...
Mid-Asiatic bank	...	...	...	..	1	4	1	12	1	12	1	8	1	7
Ukrainbank	1	3	1	23	1	51	1	53	1	49	1	34	1	32
Mutual-credit societies	7	..	45	...	86	...	173	...	280	...	285	...	237	...
Total	12	130	61	383	160	756	279	937	405	1,010	422	753	372	855

[a] *Vestnik Finansov*, 1928, No. 7, p. 170; No. 10, p. 138, and Katzenellenbaum, "The Credit System of the U.S.S.R., and the Financing of the National Economy," *Vestnik Finansov*, 1927, No. 11, p. 139.

[b] On October 1, 1925, the treasury pay offices (kassy) were officially added to the list of branches of the State Bank. Their number on that day was 643; a year later, 650; on October 1, 1927, 557. Thereafter they were eliminated. They were functioning principally as depositaries and were, therefore, not included in the above table.

circumstances that the State Bank had suffered a dissipation of its resources during 1921 and 1922. Nor does such a state of affairs favor the development of another important function of a bank —deposits. Since at the time of withdrawal the latter are paid off in a depreciated unit, prudent people will not leave their funds with a bank. The adoption of various palliatives and the introduction of the chervonetz made it possible to avoid a large part of the losses which would have been sustained otherwise, but it did not and could not relieve the banks of all the losses caused by an unstable currency. It is in the following words that one writer describes the difficulties of the agricultural credit societies, a situation which may be regarded as typical in the Soviet Union before 1924:

> . . . Despite the chervonetz currency, the agricultural credit societies, when realizing on the twenty million rubles granted to them under the decree of December 21, 1922, had lost in the process of exchange some 30 percent of the amount. At the same time the work of the agricultural credit societies during 1923 had shown a number of distortions (the tendency to engage in commercial operations rather than in earmarked agricultural credits, the leaning towards functions of middlemen in commodities, and so forth), which are explained mainly by a desire to insure oneself against losses from the granting of agricultural credit in the environment of a depreciating currency. It was only with the final transition of the entire Soviet economy to a stable currency that there was created a real base for a broad development of agricultural credit. . . .[7]

It was, then, only after the introduction of the Monetary Reform that the various credit institutions were able to develop along more or less healthy lines.

But let us pass on from this bird's-eye view of the development of credit institutions in the Soviet Union between the years 1922 and 1928 to a more detailed study. We shall begin with the Prombank.

The Bank of Long-Term Credits for Industry and Electrification of the U.S.S.R. ("B.D.K.") or Prombank.—Around the problem

[7] P. Sevruk, *Agricultural Credit in the U.S.S.R., the Central Agricultural Bank of the U.S.S.R.* (Moscow, Press of the Presidium of the Central Executive Committee, 1928), p. 28.

of the establishment of an "independent" industrial bank, as we have seen, there were waged many spirited debates in the Soviet Union. Opponents of this scheme maintained that lack of free capital in the country would necessitate the issue of notes for its support, and, besides, that credit in the Soviet Union ought to be concentrated in one bank.

Chronologically, the steps leading up to its establishment were as follows: the question of the founding of such a bank had been raised by the Supreme Council of National Economy at the very beginning of 1922. The first draft of the proposed statutes were discussed by the Presidium of that Council on March 2, 1922. A little over a month later (on April 10) the question was taken up and favorably reported on by the finance and budgetary section of the Gosplan. The matter was further discussed at a joint conference of the Economic Council of the Supreme Council of National Economy and representatives of trusts, syndicates, and state trading agencies. The latter stressed the need for such a bank and, although they could ill afford it, offered to subscribe its capital stock in cash and commodities. The organizational committee which was formed at that conference prepared detailed statutes of the Industrial Bank and submitted them for approval.[8] Such approval was given by the Council of Labor and Defense on September 1, 1922.[9]

The bank was organized as a joint-stock company with an authorized capital of 5,000,000 rubles (which was paid up in commodities and cash). Its capital stock, however, was from time to time increased and at the beginning of 1928 was in excess of 100,000,000 rubles.[10] Although joint stock in form it was to all intents and purposes (and this was true of all other joint-stock banks in

[8] For the early history of the Prombank, see: "The Prombank and the Organization of Industrial Credit" in *Questions on Industry and Trade* (Moscow, 1923); the *Collected Materials by the Council of State Industry and Trade* (Moscow, 1924); *Review of the Prombank's Activities, November 1, 1922–May 1, 1923* (Moscow, 1923) and the *Reports of the Prombank* for those years; *The Economic Survey* (Moscow) for 1924, Nos. 1, 5, 19; also I. A. Kirillov, *Financing of Industry* (Moscow, 1926).

[9] Thereafter the statutes were changed and amended several times.

[10] This does not include its surplus (some 18,000,000 rubles), its reserves (about 14,000,000 rubles), and other capital accounts. *Vestnik Finansov*, 1927, No. 12, p. 174.

the Soviet Union) a state institution. Its stock was distributed among the Supreme Council of National Economy and its agencies, various state enterprises, state institutions, commissariats (Foreign Trade, Transportation, and so on). The number of shares in private hands was quite insignificant.

In addition to the usual operations connected with the granting of short-term commercial credit, the bank was permitted to grant "long-term (up to three years) industrial loans, as well as all kinds of 'specific purpose' (earmarked) industrial, transportation, and other loans, for a definite purpose and for a specified time or on demand, out of special funds. The specified special funds could be formed, when a general meeting of stockholders so decided, out of proceeds of long-term loans floated for that purpose, as well as out of sums given the bank for that purpose by the state." The bank was also given the right to buy and sell for its own account precious metals, foreign exchange, and *commodities.*[11]

The management and administration of the bank was placed in the hands of a Board of Directors (9 members) and of a Council (39 members). The former and 36 members of the latter were to be elected by the stockholders, while the 3 remaining members of the Council were to be appointed by the People's Commissariat of Finance of the U.S.S.R.[12]

As may be seen from Table 45, the bank's lending activities developed quite rapidly, from 44,400,000 rubles on October 1, 1923, to 163,600,000 a year later, to 328,300,000 two years later, and to 1,277,800,000 rubles on October 1, 1928, that is, after it was reorganized as the Bank of Long-Term Credits for Industry and Electrification. Its deposits within the first few years, too, experienced a rapid increase, which is quite natural inasmuch as a part of the borrowed credit was left on deposit with the bank. From 32,100,000 rubles on October 1, 1923, they increased to 103,700,000 a year later and to 224,100,000 rubles on October 1, 1925. They did not increase, however, sufficiently to support the

[11] This, as we have seen, served as an insurance against loss from the depreciation of the currency. This provision was subsequently omitted.

[12] As of June 26, 1926.

TABLE 45

PRINCIPAL ITEMS IN THE BALANCE SHEETS OF THE PROMBANK [a]

(In millions of rubles on October 1 of each year)

	1923	*1924*	*1925*	*1926*	*1927*		*1928*
					Department of Long-Term Credit (O.D.K.)		
Total loans and discounts	44.4	163.6	328.3	346.1	134.9	313.6	1,277.8
Loans against commercial paper	(26.2)	(117.5)	(231.1)	(237.3)	....	(240.7)	....
Loans against commodities	(15.3)	(40.0)	(65.7)	(57.2)	....	(52.2)	....
"Earmarked" loans [b]	....	(0.1)	(7.0)	(29.1)	(83.1)	(4.0)	....
Special loans for accounts of others	(1.5)	(2.0)	(4.2)	(3.3)	(51.8)	(7.1)	....
Miscellaneous	(1.4)	(4.0)	(20.3)	(19.2)	....	(9.6)	....
Total capital	18.5	43.8	85.8	130.9	60.6	139.5	180.0
Capital stock	(15.3)	(31.7)	(63.9)	(82.6)	....	(103.7)	....
Reserve capital	(0.5)	(2.0)	(7.9)	(12.3)	....	(14.8)	....
Special capital	....	(0.3)	(2.6)	(21.5)	(57.7)	....	....
Special funds	(0.6)	(1.2)	(2.7)	(2.8)	....	(2.8)	....
Profit	(2.1)	(8.6)	(8.7)	(11.7)	(2.9)	(18.2)	....
Total deposits	32.1	103.7	224.1	180.4	24.1	122.5	105.0

[a] The figures for the years 1923–27 were taken from *Vestnik Finansov*, 1927, No. 6, pp. 218-19; No. 12, pp. 174-75. Those for 1928, from Lupandin, *The Problems of Bank Credit in the U.S.S.R.*, p. 10.

[b] Loans granted for a specific purpose. Here, *long-term* credits.

loan structure and in 1925 it became quite apparent that the bank was overlending. From that year, although the loans continued their upward movement, the deposits, as shown in Table 45, experienced a decline.[13]

It was necessary to relieve the Prombank—and, for that matter, all the other joint-stock banks, for they were similarly affected—of the financial strain. As far as the Prombank was concerned, it was quite clear that its resources were entirely inadequate. The Prombank during these years was granting both short-term and long-term credit; it was therefore decided that a correct solution of this problem called for the finding of new ways in which to provide long-term credit.[14] It was in connection with this that on August 14, 1925, the government announced its decision to float "a loan for economic reconstruction." Each enterprise was required to subscribe for a given amount of bonds (bearing 10 percent interest). The underlying idea was, of course, to tap in that way the savings of the country. But although the subscribers did not have to pay the entire purchase price at once, the bonds, nevertheless, were entrusted to them. Moreover, they were given permission to borrow against them in the State Bank. In other words, the treasury sold them bonds on credit and permitted them to use these bonds as collateral for bank loans. The total issue of such bonds amounted to some 300,000,000 rubles.[15]

The attempt to procure long-term credit by means of borrowing proved, however, highly unsuccessful. The various enterprises,

[13] The drastic decline in the volume of deposits in 1925–26 was due largely to the decreed transfer of state insurance funds to the State Bank and, besides, to the "competition" set up by the latter. The State Bank did not readily rediscount paper for the joint-stock banks, preferring to deal with the borrowers directly. The right of note issue is, of course, a powerful weapon. See S. S. Mekler, "Currency Circulation, Credit and Banks in 1925–26," *Economic Conditions of the U.S.S.R. and World Economic Conditions in 1925–26* (Moscow, Commissariat of Finance Press, 1927), pp. 183-84.

[14] See A. A. Sokolov, "The Problem of Organizing Long-Term Credit in the U.S.S.R.," *Vestnik Finansov*, 1926, No. 7, pp. 18 ff.; also G. Nagler, "Questions Concerning Long-Term Credit to Industry," *Vestnik Finansov*, 1928, No. 9, pp. 13 ff.; "Prombank in the First Half of 1926–27," *Finance and National Economy*, 1927, No. 30 (38), pp. 21-22.

[15] See I. Reingold, "The New Economic Policy 1921–28," *Soviet Policy in Public Finance 1917–28*, by Gregory Y. Sokolnikov and Associates (Stanford University Press, 1931), pp. 267-68.

badly in need of capital, proceeded to "lombard" these bonds at the State Bank. As the loans at the latter bank matured, these enterprises (principally connected with "heavy" industries) failed to meet them.[16] And although, in order to meet the payments due the treasury, the subscribers drew heavily against their bank deposits (thus causing balances to diminish appreciably), the treasury found that the installments which it was receiving did not take care of the amounts paid out by it to redeem the bonds.

A little before the plan for the "economic reconstruction" loan was formulated, the Supreme Council of the National Economy brought forth (in November, 1924) a project which was worked out by its special commission for the rehabilitation of the basic industrial capital. The project was formulated as follows: "With a view to accumulating financial resources for a planned rehabilitation and expansion of the most important state enterprises and for the organization of new enterprises, there is formed, under the immediate supervision of the Supreme Council and under the general jurisdiction of the Council of Labor and Defense, an Industrial Fund of the U.S.S.R." The fund was to be formed out of the following resources: a portion of the profits set aside for this purpose by industries and turned over by them as a contribution to the fund; grants by the treasury (budget), sums realized from the disposal of immobile assets, and so forth. In addition to these non-returnable resources, the fund was also to draw upon so-called returnable resources, such as the reserves set aside by enterprises for depreciation, loans by the treasury, flotation of bonds and long-term loans granted by the State Bank and other credit institutions.[17]

This project, however, was not approved by the government,

[16] The transactions, in fact, took on the following character: Having received the bonds, the particular enterprise would present them to the State Bank. The latter would reduce the indebtedness of the enterprise substituting for it, so to say, the government bonds. The treasury would redeem the bonds, extinguish the debt, and would look to the subscriber for repayment. It had the effect of making the subscriber appear as a long-term borrower from the treasury.

On September 24, 1926, it was ordered that all accounts relative to the loan between the enterprises and the treasury be concentrated in the hands of the State Bank. See S. Rubinshtein and M. Tzypkin, *Soviet Credit*, Pt. III (Moscow, State Finance Press, 1933), p. 14.

[17] *Ibid.*, pp. 14-15.

partly because it was presented after the budget for 1925–26 had already been approved, and partly because of the method by which it was proposed to administer that fund. Instead, it was decided on March 17, 1926, to organize *within* the Prombank a Department of Long-Term Credit (Otdel Dolgosrochnogo Kredita or O.D.K.) with a balance of its own. Its operating fund was to come from the special capital funds possessed by the Prombank and from the sources suggested in the rejected "Industrial Fund" project. It was authorized to grant returnable long-term loans of from one to ten years' duration. In an attempt to enable it to expand its resources, the Council of People's Commissars on July 14, 1927, permitted the O.D.K. to draw also upon such additional sources as allocations from the profits of the Prombank set aside for the former's benefit by order of a decision of a general meeting of the stockholders of the latter, and upon such funds as reserves for depreciation, reserves for capital expansion and the like, which its clients were to entrust to it in the form of long-term and special deposits. It was at the same time provided that the O.D.K. was to operate on the basis of an annual financial plan that was to be prepared by the Supreme Council of National Economy and approved by the Council of Labor and Defense (S.T.O.). The amounts specified in the plans were to serve as "limits." The loans, on the basis of this latter regulation, were to be granted for a period of years not to exceed twenty-five.[18]

The rôle of this "bank within a bank" was, then, to redistribute the funds possessed by industry itself and to act as a distributor of budgetary funds. The budget helped the O.D.K. to reach accumulations by other layers of the national economy than industry itself. Inasmuch as the savings of the country were relatively small and foreign savings could not be reached by it, the O.D.K., through no fault of its own, failed in its mission to find "new" sources for long-term credit to industry. In a further attempt to improve the situation pertaining to long-term credit it was decided to reorganize the Prombank (Commercial-Industrial Bank) together with its O.D.K. as a Bank of Long-Term Credit for Industry and Electrification of the U.S.S.R. (Bank

[18] *Ibid.*

Dolgosrochnogo Kreditovania Promyshlennosti i Electrifikatzii S.S.S.R., or, B.D.K., or Prombank) to be placed under the jurisdiction of the Supreme Council of National Economy. The decree to this effect was promulgated by the government on June 27, 1928.[19]

The reorganized Prombank was to take over all of the assets and liabilities of the Electrobank, except those pertaining to short-term credit.[20] The latter, as well as the short-term assets and liabilities of the old Prombank, were transferred to the State Bank, following the policy announced in June, 1927, of concentrating the short-term credit of the country in the latter bank.

The reorganized Prombank was charged with the performance of the following functions: (a) granting of long-term credits for purposes of capital construction [21] to enterprises of state industries, syndicates, and joint-stock companies, and providing them with additional working capital; (b) raising the means necessary to carry out the above; (c) allocating funds (grants) for capital investments among the above-mentioned enterprises for the account of the state budget (Article 2).

Its authorized capital stock was fixed at 130,000,000 rubles. Its resources, in addition to the capital stock, were to consist of the following: (a) a *reserve capital* (to be formed by setting aside annually 10 percent of the bank's profit, until it reached half of the capital stock); (b) *special funds,* such as budgetary grants, sums transferred by the Supreme Council of National Economy and supreme councils of the republics (from the realization of assets of liquidated enterprises, and so forth); the portion of profits (10 percent) which state enterprises were required to pay into the

[19] Decree 377; see also *Collected Decrees,* 1929, Decree 272. For the approved statutes of the bank, see *ibid.* (Section II), Decree 201, signed July 12, 1929.

[20] The Electrobank was organized in 1924 for the purpose of developing and strengthening the electrification of the country. It financed the construction and equipment of electric power, telegraph, telephone, and radio stations together with their network; their reconstruction, repairs, additions, etc.; the change to electric power on the part of various economic units and so forth.

Its original capitalization was fixed at 7,000,000 rubles. It granted short-term credits up to one year, and long-term credits for a specific purpose, up to five years. It naturally leaned very heavily upon the state budget. The movement of its principal accounts is shown by Table 46.

[21] Except construction of dwellings.

bank for the expansion of the latter's capital funds, and the not less than 40 percent of its own profits which the bank was required to transfer annually to this account; [22] and (c) its deposits, particularly of its time deposits which were made up of one-half of the profits set aside by state enterprises for the expansion of their plants, a part of the amount set aside by them as reserves for depreciation, certain budgetary funds, and deposits by "others"

TABLE 46

MOVEMENT OF THE PRINCIPAL ACCOUNTS OF THE ELECTROBANK [a]

(In millions of rubles on October 1)

	1925	*1926*	*1927*
Total capital	9.4	16.8	37.6
Capital stock	(8.0)	(13.8)	(30.2)
Deposits	15.3	15.7	13.4
"Other funds"	11.5	32.3	107.6
Total loans and discounts	43.8	71.1	178.3
Loans against commercial paper	(24.4)	(19.6)	(24.4)
Loans against commodities	(5.1)	(4.1)	(2.6)
"Earmarked" loans	(3.8)	(11.5)	(39.4)
Special loans out of "other funds"	(10.4)	(32.3)	(107.6)

[a] The "other funds" came from the budget. Its deposits did not develop. Its short-term loans remained stagnant while its long-term loans ("earmarked" and "special loans") increased considerably. The figures were taken from the *Vestnik Finansov*, 1927, No. 6, p. 225; and No. 12, p. 177.

for a period of not less than three years. The peculiar nature (from a "capitalistic" point of view) of those sources is, of course, due to the peculiarities of the Soviet economy.

[22] At the time of the merger the capital stock of the two merged banks amounted to 130,000,000 rubles. The new bank also fell heir to the reserve capital and special funds of the two institutions amounting to 270,000,000 rubles. Before this reorganization took place the Commissariat of Finance used the State Bank as its principal agent for the allocation of budgetary funds. When the Prombank was reorganized and the above function was transferred to it, the balance of that account, amounting to 950,000,000 rubles, was also transferred to it.—G. Tochilnikov, *Finance and Industrialization* (Moscow, State Finance Press, 1929), pp. 72-73.

The bank was authorized to accept long-term deposits, to float (with permission of S.T.O.) loans, and to perform other long-term operations in the U.S.S.R. and abroad, by permission of the Commissariat of Finance.

Its long-term loans were to be granted for specific purposes and for a period not to exceed thirty years. Such loans (as well as grants made by it on behalf of the budget) had to be based upon projects and estimates submitted by clients, or upon a notification from the agencies administering them, to the effect that such documents were approved.

The extension of long-term credits and the transfer of budgetary grants to the various state enterprises were to be governed by the bank's *annual credit plan.* The latter was to be drawn up in conformity with the production-financial plan of industry ("promfin plan"). Such credit plan was to include the anticipated receipts from all sources (an additional 5 percent of this total was to be included as a reserve for contingencies), as well as the anticipated payments on account of advances and grants. To become effective such plan had to be approved first by the Supreme Council of National Economy and then by the Council of Labor and Defense. In addition to this plan the bank was required to present for approval to the agency having jurisdiction over the borrower—whether that be the Supreme Council of National Economy or the supreme councils of the constituent republics, or the respective People's Commissariats—a *list of expected borrowers.* When approved, a copy of it had to be sent to the People's Commissariat of Finance. It was by the approved credit plan and the list of borrowers that the bank was to be guided when making loans and transferring budgetary grants.[23]

The bank was also charged with the duty of exercising strict control over the expenditure of funds loaned or transferred by it in the form of a budgetary grant. It had to see that they were expended for the purpose and at the periods specified in the borrower's agreement. In case of breach of contract the bank was to

[23] The bank was authorized to grant loans and allocate budgetary funds not only directly, but through other banks as well. The bank, in fact, was deprived of its branches and carried on its business through the medium of the State Bank.

stop the further withdrawals of funds by the borrower and notify the Supreme Council of National Economy and the Commissariat of Finance of the Union or of the respective republic depending on where jurisdiction resided.

The management of the bank was placed in the general meeting of the stockholders and in a Board of Directors consisting of a chairman and four other members elected (for three years) by the former and approved by the Supreme Council of National Economy.

The general meeting was also to elect from among stockholders and outsiders an Auditing Commission (for a term of three years) of three members and two candidates to be approved by the Supreme Council of National Economy. In the hands of the latter body (the Supreme Council), as has been pointed out above, was placed the general supervision of the bank's activities.

Co-operative Credit (the Vsekobank)

The re-establishment in Soviet Russia in 1921 of the independence of the various co-operative institutions, in line with the general attempt to revivify trade and industry, led to the problem of co-operative credit. The establishment in February, 1922, of the Consumers' Co-operative Bank or "Pokobank" was the first attempt at its solution. Its original share capital was fixed at 1,300,000 (gold) rubles. By the end of 1922, however, the amount of shares outstanding exceeded 4,000,000 rubles. The shares were distributed among consumers' co-operative organizations, the Centrosoyuz, the State Bank, and so on. As its name indicates, the Pokobank was a *consumers'* co-operative bank.

Meanwhile, in 1922 there developed also various types of producers' co-operatives. To meet the demand of all types of co-operatives, a new bank—the All-Russian Co-operative Bank or "Vsekobank" was organized on January 27, 1923 (when the first general meeting of the stockholders was held). The assets and liabilities of the Pokobank, as well as its entire apparatus, were transferred as of January 1, 1923, to the new bank. On that day the balance sheet total of the former amounted to 43,199,573 rubles

of the 1923 pattern or (on the basis of the official rate for the banknote on that day, which was 175) to 2,460,000 chervonetz-rubles.[24] Among the organizers of the Vsekobank were the Pokobank itself, the Centrosoyuz, the Selskosoyuz, and a number of various other co-operative organizations. Its original share capital was set at 10,000,000 rubles, but from time to time this was increased until in 1929 it reached 40,000,000 rubles.

In addition to the usual commercial banking operations, its statute permitted it to engage in long-term operations. The latter took the form of "earmarked" loans granted either for one to three years or indefinitely and payable on call. It was also permitted to buy and sell foreign exchange, securities (those of course which were permitted to circulate in the country), and commodities, the latter two not only for the accounts of others, but for its own account as well.

The management of the bank was placed in the hands of a board of directors, and the general supervision in those of a Council, both of those bodies being elected by the shareholders.[25]

Stimulated by the economic policy of the state, the co-operative economy was growing too rapidly, like most other branches of the Soviet economy, to permit it to accumulate a sizable surplus of its own. The state, therefore, had to render it financial assistance. The financing of the co-operatives by the state was, however, carried out largely through the agency of other banks than the Vsekobank. These two circumstances, the meagerness of the resources possessed by the co-operative system itself and the routing of state funds intended for them through other banks, did not favor the development of the Vsekobank. It was always heavily indebted and, since it paid a relatively high rate of interest on the borrowed funds, credit at the bank was rather costly (especially when compared with the charges made by those banks

[24] N. Barou, *Russian Co-operative Banking* (London, P. S. King and Son Ltd., 1931), p. 16; also F. D. Livshitz, *The Banks of the U.S.S.R.* (Moscow, Commissariat of Finance Press, 1925), p. 16; A. Doroshenko, "The Banks in 1922–1923," *Vestnik Finansov,* 1923, No. 44, p. 41; A. Doroshenko, "On the Origin and the Work of the Credit Institutions," *Vestnik Finansov,* 1922, No. 38, p. 45.

[25] From the Statute of the All-Russian Co-operative Bank. *Collected Decrees,* 1923, Section 2, No. 3, Decree 16.

which operated with budgetary funds or, like the State Bank, had a right to issue notes).[26]

In spite of those obstacles, however, its balance sheet total swelled from 35,994,000 rubles on October 1, 1923, to 399,417,000 rubles on October 1, 1928. The number of its shareholders increased between these two dates from 1,008 to 12,835. The bank also increased the number of its branches, and by the end of 1928 these amounted to 39 as compared with 6 on October 1, 1923.

It is seen from Table 47 that its loans and discounts grew from

TABLE 47

PRINCIPAL ACCOUNTS OF THE VSEKOBANK

1923–28 [a]

(*In thousands of rubles on October 1 of each year*)

	1923	*1924*	*1925*	*1926*	*1927*	*1928*
Loans and discounts	26,227	47,804	70,599	94,774	174,814	257,888
Capital and special funds	6,364	12,948	16,636	21,841	28,037	37,035
Time and demand deposits	8,255	24,298	52,032	55,767	72,350	89,571
Borrowed funds	14,342	18,566	23,490	39,672	85,687	138,224

[a] Based upon Barou, *op. cit.*, pp. 18-19. These figures differ somewhat from those given in the *Vestnik Finansov*, 1927, No. 6, pp. 222-23; No. 12, pp. 176-77; and 1928, No. 7, pp. 159 ff. See also "The All-Russian Co-operative Bank," *The State Bank of the U.S.S.R. Economic Survey*, February 7, 1929, IV, No. 5.

26,200,000 to 257,900,000 rubles between October 1, 1923, and October 1, 1928. Of the total loaned and discounted on the latter date 192,300,000 rubles represented short-term credits, and the rest long-term credits. Consumers' co-operatives on that date were the recipients of 53.3 percent; agricultural co-operatives, of 27.8 percent; and peasants' crafts, of 17.2 percent of the total loaned and discounted.

The deposits increased from 8,200,000 to 89,600,000 rubles between those two dates. The account of the trade unions was an

[26] M. Valutin, "Vsekobank (Totals and Perspectives)," *Credit over Ten Years*, Supplement to *Finance and National Economy*, 1927, No. 45/53, p. 13.

important factor in that increase. On October 1, 1924, the trade unions had 6,300,000 rubles on deposit with the bank. Their balances, however, steadily increased and by October 1, 1928, amounted to 34,100,000 rubles or 38 percent of the total deposits. The loans from outside sources, mostly from the State Bank (in the form of rediscounts or rehypothecation of goods), and from the treasury (for the purpose of advancing long-term credits to co-operatives) grew apace.

The Vsekobank was not given monopoly rights in the matter of handling co-operative credit and deposits.[27] On October 1, 1928, for example, it held but 37.1 percent of the total deposits maintained by the various co-operatives in the five leading banks of the Union and was responsible for but 34.3 percent of the total credit advanced to the co-operatives by the "big five." The greater part of the credits obtained by the co-operatives as a matter of fact came from the State Bank. The Vsekobank, however, played a very important part in the matter of developing the co-operative system. It not only extended credits to it but counseled and guided it along sound paths. It also served as a clearing house for the various co-operatives. Furthermore, it was instrumental in developing their foreign trade. Its foreign banking business the Vsekobank carried on through the Moscow Narodny Bank, Ltd., in London, the Co-operative Transit Bank in Riga (the major part of whose shares it owned), and a number of correspondents in the various parts of the world.[28]

[27] From 1928, however, all co-operatives were required to set aside 10 percent of their profits annually to serve as a reserve. These funds were to be deposited with the Vsekobank. The latter was to invest 40 percent of these amounts in securities and to use the remainder for the purpose of short-term loans. *The State Bank of the U.S.S.R. Economic Survey, loc. cit.*, p. 3.

[28] The Moscow Narodnyi Bank (Moscow) opened in 1916 an agency in England known as the London Agency of the Moscow Narodnyi Bank, Moscow. In 1917 it was converted into a London Branch of the bank. In 1919 there was founded in London the Moscow Narodny Bank, Limited, having an authorized capital of £250,000. The Moscow Narodnyi Bank, Moscow, owned some 52 percent of the shares; the Centrosoyuz, about 12 percent, and other co-operative institutions, the balance. In 1923 the shares and, therefore, the control over the Moscow Narodny Bank, Ltd., passed into the hands of the Vsekobank and the co-operative organizations of the U.S.S.R. The Co-operative Transit Bank in Riga was established in 1923 for the purpose of facilitating the exports by co-operatives to the Baltic States. Its organizers were the Moscow Narodny Bank, Ltd., the Vsekobank, the Centro-

In addition to the All-Russian Co-operative Bank or Vsekobank there was also organized in 1922 an All-Ukrainian Co-operative Bank or "Ukrainbank" with a share capital of 120,000 gold rubles. On October 1, 1928, its total capital account (including reserves) amounted to 9,900,000 rubles, its deposits to 26,800,000 rubles, its loans and discounts to 52,900,000 rubles.[29] Its statute with minor exceptions resembled that of the Vsekobank.

Agricultural Credit

It has been shown in the preceding section that the change to the New Economic Policy caused the government to become interested in the development of consumers' co-operatives (Decree of April 7, 1921). The next step was the organization of peasants' craft and agricultural co-operatives. These were legalized by a series of decrees of May 17, July 7, and August 16, 1921. Mere decrees, however, were not enough. Cheap credit was needed for their development. It was with this in mind that the Ninth All-Russian Congress of Soviets (December, 1921) laid special emphasis in its resolutions upon the necessity of rendering "wide support to co-operative credit organizations." In compliance with the above decision the Council of People's Commissars published a decree on January 24, 1922, dealing with co-operative credit in the villages. It projected two types of institutions: credit associations and loan-and-savings associations. Their resources, according to the decree, were to be derived from membership fees and the sale of shares, from loans, and from credit granted by the state itself. The poverty of the peasants, their distrust of the new organizations and the depreciating sovznak hindered, however, the development of strictly credit associations. There sprang up instead (in addition to the poorly functioning village consumers' co-operatives) co-oper-

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soyuz, Selskosoyuz and other co-operative institutions.—Barou, *op. cit.*, pp. 36, 37, 50, 51. Besides these two banks, the Soviet Union had abroad a number of other banks, such as the Arcos Banking Corporation in London, the Garantie und Kreditbank für d. Osten ("Garkrebo") in Berlin and Hamburg, Swenska Economie Aktiebolaget in Stockholm, Nordiske Aktieselskab in Copenhagen, Russo-Persian Banking Office ("Russpers") in Teheran, Russo-Mongolian Commercial Bank in Urga, and the Far Eastern Bank in Kharbin.

[29] *Ibid.*, pp. 24-35.

ative associations of a *general* nature, and although they also performed credit functions these were but weakly developed.

To give strength and direction to the various village credit cooperatives, the government (by decree of December 21, 1922) ordered the organization of agricultural credit societies (or local agricultural banks). These issued shares of two types: *founders'* and *peasants'*.[30] The founders (obligatory) were: the Commissariat of Finance, the Commissariats of Agriculture, and the All-Russian Union of Agricultural Co-operation.[31] The co-ordination of the activities of these societies (or local agricultural banks) and the regulation of them was placed in the hands of a special sub-committee of the Central Executive Committee, known as the Committee for Co-operation with Rural Economy and Rural-Industrial Economy, which had general supervision over the organization of agricultural credit, and in the hands of the department of agricultural credit at the State Bank.[32] The latter had immediate supervision over that work. A good many of these early societies, however, were either "paper" organizations or else were engaged in trading.[33]

The adoption of a new policy of creating specialized banks for the various branches of the national economy could not fail to affect the course of the development of rural credit institutions. There were organized six republican agricultural banks (such as the Ukrainian, the first of the kind to be organized, in November, 1923; the Transcaucasian in April, 1924; the White Russian in December, 1924, and so forth).[34] They were joint-stock in form. Their statutes provided that not less than 51 percent of their shares had to be held by state institutions and enterprises. In them was placed the duty of co-ordinating and supervising the activities of the system of agricultural credit in the respective republics. To

[30] The distribution of peasants' shares was discontinued in 1927 (Decree of February 4th, 1927). There was sold up to January 1, 1927, a total of 10,000,000 rubles of such shares.

[31] *Collected Decrees*, 1924, Section II, Decree 31.

[32] The Committee for Co-operation was abolished when the Central Agricultural Bank of the U.S.S.R. was established.

[33] I. Palaschenko, "Activity of Agricultural Credit Societies," *Vestnik Finansov*, 1927, No. 4, p. 72.

[34] Later increased to seven.

them the government looked for the carrying out of the official policy.[35]

At the head of the entire rural credit system there was placed an All-Union bank, the Central Agricultural Bank of the U.S.S.R. The organization of the latter was decided by the Second All-Union Congress of Soviets on February 1, 1924. Its statutes were approved by the Central Executive Committee and the Council of People's Commissars of the U.S.S.R. on the fifteenth of the same month. Its original authorized capital stock was set at 40,000,000 rubles in gold.[36] The State Bank, however, at once concluded an agreement with the above bank undertaking to provide the latter with a line of credit equaling its (the Central Agricultural Bank's) authorized capital stock. In the beginning this, of course, amounted to an additional 40,000,000 rubles. As its capital stock increased it automatically became entitled to larger credits.[37] The bank was authorized to grant short- and long-term credits. The short-term credits were to be of a maturity not in excess of one year; the long-term, up to five years. The latter were to be given for a definite purpose ("earmarked") and in an amount not to exceed 75 percent of the total estimated expenditure. Since real estate was no longer privately owned there was, of course, no room for mortgage credit. Whatever long-term credits were granted were for the purpose of enlarging the cultivated area, for improvements, erection of various buildings (for industrial purposes), and the like. The loans were to be granted to the republican agricultural banks, to agricultural credit societies within the limits of the plans agreed upon by the republican banks, to other agricultural organizations and enterprises directly, when the loan was of an All-Union importance, or through the first two agencies in all other cases. The Central Agricultural

[35] Sevruk, *op. cit., passim.*

[36] Not less than 10 percent of the annual profits were to be set aside as a reserve.

[37] The C.A.B., however, could borrow that credit only against short-term paper, which excluded the possibility of its being loaned out to the peasantry for the procurement of fixed assets. The C.A.B. at first paid 5 percent on the borrowed funds; later the charge was reduced to 3 percent.—Sevruk, *op. cit.*, pp. 30-31. The C.A.B. itself charged from 6 to 8 percent on its long-term and from 10 to 12 percent on its short-term loans. *Ibid.*, p. 185. Compare Barou, *op. cit.*, p. 70.

Bank was given the right to inspect the books and accounts of its borrowers; this in addition to the requirement that they submit detailed statements with respect to their financial condition, disposal of the borrowed funds, and other pertinent information.

Its management was placed in the hands of the general meeting of stockholders, in a board of directors (of not less than five members) and in a council (eleven members). The latter two were to be elected by the stockholders.

Officially, the bringing of the various loose agricultural credit organizations into a system under the leadership and guidance of the Central Agricultural Bank dates from January 7, 1927.[38] On that day the government published a decree by the terms of which the Central Agricultural Bank was placed at the head of the entire agricultural credit system (consisting, besides the Central Agricultural Bank, of the republican agricultural bank; of the agricultural credit societies or local agricultural banks, and of the agricultural credit-co-operative organizations) [39] with authority to guide and direct it.

In reality, however, the Central Agricultural Bank tended to assume that rôle long before the publication of the above decree, not by usurpation of power but in conformity with the policy laid down by the Second All-Union Congress of Soviets at the time of its organization.

It may be seen from Table 48 that the deposits of the Central Agricultural Bank played an insignificant part in furnishing the resources for the credit operations. The state budget and the State

[38] See *Agricultural Credit System* (Moscow, Central Agricultural Bank, 1927) for important decisions and legislative acts pertaining to agricultural credit; see also Pevzner and Drisin, *loc. cit.*, where the statutes of all banks are given.

[39] Toward the end of the period under review the numerical strength of this organization in addition to the C.A.B. and the six (later seven) republican banks was as follows: 70 agricultural credit societies with 137 branch offices; 39 agricultural credit unions, and about 9,000 agricultural credit-co-operative associations. The two last mentioned actually performed multifold operations (such as, for example, buying of consumers' goods, selling of agricultural produce, and participating in local industry) besides engaging in *credit* business. The operations of an agricultural credit-co-operative association (the lowest link of the system) were confined to a very small section. The operations of a credit union, on the other hand, covered an entire county (okrug). The membership of a credit union was composed largely of "associations" and to a less extent of other co-operatives.

Bank were very important sources in that connection.[40] Its capital stock, too, it must be remembered, was contributed by state organizations. Of the total loans and discounts which on October 1, 1928, amounted to 461,700,000 rubles, 416,600,000 rubles were represented by long-term loans.[41] The amount of loans extended directly to the borrowers by the *entire* agricultural credit system is estimated (as of October 1, 1928) at 939,000,000 rubles of which 618,300,000 rubles was represented by long-term loans.[42]

The rural economy, in addition to borrowing from the agricultural credit system, relied very heavily upon the State Bank

TABLE 48

MOVEMENT OF THE PRINCIPAL ITEMS IN THE BALANCE SHEETS OF THE CENTRAL AGRICULTURAL BANK[a]

(*In millions of rubles on October 1 of each year*)

	1924	*1925*	*1926*	*1927*	*1928*
Loans and discounts	31.2	144.9	210.7	319.8	461.7
Capital	15.3	53.4	88.3	92.9	96.7
Deposits	....	11.3	6.4	10.1	17.0
Funds received from the state budget	4.7	20.5	47.5	85.9	151.0
Borrowed from the State Bank	13.7	70.9	75.6	31.8	108.5

[a] *Vestnik Finansov*, 1927, No. 6, pp. 224-25; No. 12, p. 179; also Barou, *op. cit.*, pp. 68-69.

and to a much less extent upon the co-operative banks. Its total indebtedness on the above date to the various credit institutions was distributed as follows: to the agricultural credit system, 53 percent of the total; to the State Bank (exclusive of the financing of the agricultural credit system), 42 percent, and to the co-operative banks, 5 percent.[43]

[40] L. Shanin, "Problems of Financial Guidance," *Vestnik Finansov*, 1928, No. 9, p. 8; G. Schwartz, "Evolution of Credit," *Vestnik Finansov*, 1928, No. 3, pp. 75 ff.; L. Yurovsky, "The Credit System," *Finance and National Economy*, 1927, No. 42/50, p. 13.

[41] A year later, on October 1, 1929, when the total loans and discounts amounted to 578,300,000 rubles, the long-term loans stood at 543,700,000 rubles.

[42] *The State Bank of the U.S.S.R. Economic Survey*, 1929, IV, No. 33, p. 3.

[43] *Ibid.*

If the aim of the Central Agricultural Bank was to weld the many loose agricultural credit agencies into a harmonious and efficient banking system which would tap the resources of the peasantry and provide it with cheap credit, it failed to achieve its aim. The "system" continued to remain unwieldy with entirely too many links between the borrower and the bank, a circumstance which served to increase the cost of credit extended to the villages. Furthermore, the system proved unable to attract peasant funds. Nor did it exercise efficient control over the funds loaned to the peasants. Once loaned, the funds had a tendency to remain in the villages. The latter circumstance was to no small extent the product of the communist program, which demanded that credit aid be extended to the poor and the middle-class peasants rather than to the "efficient" kulaks. The communists, although eager to encourage efficiency, were not willing to strengthen the hand of their enemy. They were convinced that the kulaks aimed at a restoration of capitalism.

The defects of the agricultural credit system were known to the government and attempts were made by it to remedy them in ways which would not impede the building of socialism in the country. In their decree of February 13, 1929, the Central Executive Committee and the Council of People's Commissars of the U.S.S.R., for example, following a thorough examination of the agricultural credit system by the Commissariat of Workers' and Peasants' Inspection, noted the following faults: [44]

> Complex and decentralized control and guidance . . . failure, in consequence of this, to insure the realization of the directives of the government . . . extraordinary complexity in the interrelations between the various links of the system; the slowness with which funds move to the ultimate borrower; the rise in the cost of credit; failure to come to an understanding with the Gosbank and the co-operative banks relative to the extension of credit to agriculture, and with the agricultural co-operative unions relative to the guidance of the credit associations; the weakness of credit discipline and the inadequacy of measures to collect debts when due; the very weak pull on peasant resources . . . poor supervision over the use of borrowed funds by the

[44] *Collected Decrees*, 1929, Decree 96.

respective links of the agricultural credit system as well as by the borrowers; a medley of interest rates.

To overcome this formidable list of defects the government decreed the strengthening of the guiding rôle of the Central Agricultural Bank, and defined the scope of the work of the republican agricultural banks, strengthening their supervision over the lower agricultural credit organizations. In accordance with the terms of the above decree, the Central Agricultural Bank was authorized: [45]

(a) To grant credit to enterprises and organizations of national importance, as well as to the republican agricultural banks.
(b) To regulate, plan, and control the activities of the entire agricultural credit system.

The functions enumerated in clause *a* require no comment. Those enumerated in clause *b* covered the following specific powers and duties: to prepare a consolidated credit plan for the entire system and to present it through the State Planning Commission to the Council of People's Commissars for approval; to issue rules governing the preparation of credit plans by the system; to control the work of the republican agricultural banks, among other things, the fulfillment by them of the credit plans and the use made of the resources; to fix the limits for interest rates. The Central Bank was also given the right to inspect the republican banks.

The republican agricultural banks, in addition to granting agricultural credit, were authorized:

(a) To prepare credit plans for the agricultural credit system.
(b) To build up agricultural credit systems within the respective republics.
(c) To guide and control the activities of the agricultural credit societies, as well as of the credit-co-operative associations.

The republican banks were also instructed to present reports to the Central Agricultural Bank on fixed dates. The agricultural credit system was permitted to grant both long- and short-term agricultural credit. To augment the resources of the Central Agri-

[45] *Ibid.*

cultural Bank, the government a little later permitted it to issue government-guaranteed 31-year bonds (to be realized through the State Bank) to the amount of 46,000,000 rubles.[46] The bank was also to set aside as reserves 10 percent of its profits.[47]

As is shown, however, in Chapter XV the sweep of the collectivization movement necessitated other and more radical changes.

Municipal Credit

At the end of 1922, when the new order was already well under way, housing in Soviet Russia was in a most deplorable condition: the construction of new dwellings had ceased in 1917, the old dwellings were not being repaired and were deteriorating. All this in the face of a fast growing urban population.

The return to normal life made apparent the need not only for such construction and repairs but also the need for schools, hospitals, street railways, water supply, sewerage, and, in short, for all those things without which civilized life is difficult. Most of these latter needs are usually cared for by the budgets of municipalities.

In those years, however, there was very little free capital in Soviet Russia that sought investment, and whatever could be raised in that manner was needed for the national budget.[48] The latter, needless to say, was at that time in no position to assist the municipalities. In 1923–24, for example, its total contribution towards their needs amounted to but 2,000,000 rubles.[49]

Attempts, of course, were made by the municipalities to utilize the resources of the State Bank and then of the Prombank, but it was soon decided that special municipal credit institutions were indispensable. Accordingly, the government in a decree published on January 18, 1923, charted the course of their development. By its provisions the provincial (*gubernskie*) executive committees,

[46] Decree 461. [47] Decree 504.

[48] An attempt made by the Moscow City Council to float a building construction loan was far from successful. F. D. Livshitz, "Basic Lines of Credit and Credit Policy in 1917–27," *Financial Policy of the Soviet Government for 10 Years* (Moscow, 1928), p. 81.

[49] E. D. Chernekhovsky, *Municipal Finance* (Moscow, Press of the People's Commissariat of Internal Affairs, 1929), p. 138.

upon proper authorization, were permitted to organize "mixed" joint-stock municipal banks in which they owned not less than 51 percent of the total capital stock. They were to be organized for the purpose of "aiding by means of banking operations the re-establishment and development of local economic life, and in particular: (a) rendering credit to the local, municipal economy; (b) granting credit to the various localities to enable them to meet their needs for municipal construction of all types; (c) furnishing short-term credit to the municipal government, co-operative and private enterprises." [50] By a regulation of November 23, 1925, there were adopted, along the lines promulgated in the above decree, model statutes for municipal banks. Under these they were authorized to perform the usual banking functions, to grant long-term credits for the restoration, construction, and expansion of municipal buildings and undertakings, as well as for the construction and the repair of dwellings and the like.

Of the various municipal banks organized the Moscow City Bank (Moskovskii Gorodskoi Bank or "Mosgorbank") was the first and the largest. It commenced its banking operations in January, 1923, with an initial capital stock of 2,500,000 rubles subscribed for by various governmental agencies and particularly by the Moscow Council (*Mossoviet*). Since the depreciating currency discouraged long-term loans, its activity during the early period centered around commercial rather than municipal operations. On October 1, 1924, for example, its total loans and discounts amounted to 75,200,000 rubles, of which 38,300,000 rubles were granted against commercial paper, and 18,100,000 rubles against commodities.[51] In other words, over 75 percent of its credits were granted for purposes other than those which it was intended to serve primarily, and, it may be added, in competition with banks whose function it was to grant such credits. Nor is it uninteresting to look into a more detailed distribution of its loans on that date. Of that total, 12 percent went to state trading enterprises; 46.6 percent, to industrial enterprises; 12.6 percent, to consumers' co-operatives; 8.1 per cent, to the "housing" co-operatives; 14.0

[50] *Collected Decrees*, 1923, Decree 82.
[51] *Vestnik Finansov*, 1927, No. 6, p. 226.

percent, to other types of co-operatives; 5.1 percent, to various Moscow organizations; and 0.2 percent, to private individuals.[52]

Its loans and discounts, as shown by Table 49, underwent a considerable growth. The growth of its own resources and of the deposits left with it (largely, municipal budget funds) enabled it to get along without appreciable borrowing from other credit institutions. Its interest rates towards the end of this period

TABLE 49

PRINCIPAL ACCOUNTS OF THE MOSGORBANK [a]

(*In millions of rubles on October 1 of each year*)

	1923	*1924*	*1925*	*1926*	*1927*	*1928*
Total loans and discounts.....	27.7	75.2	140.2	214.2	265.2	372.0
Capital stock	3.5	7.0	32.3	33.5	34.0	44.4
Special capital and funds.....	0.6	2.0	5.9	12.0	69.0	218.3
Time and demand deposits ..	20.3	54.1	89.9	114.1	95.0 [b]	95.7
Borrowed from other credit institutions.....	0.5	4.0	6.1	8.6	0.8	19.7

[a] The figures for 1923–27 were taken from the *Vestnik Finansov*, 1927, No. 6, pp. 226-27, and No. 12, p. 177; those for the year 1928, from *The State Bank of the U.S.S.R. Economic Survey*, 1929, IV, No. 3, and are not quite exact since they represent preliminary returns. Of the total loans and discounts on October 1, 1928, some 75 percent were long-term.

[b] The decrease in deposits was primarily due to the decreed (June 15, 1927) separation of banks into short-term and long-term institutions.

were, however, quite high—fluctuating between 8 and 14 percent for short-term loans, and between 9 and 11 percent for long-term loans.[53] It nevertheless constituted an improvement over the earlier period when municipal banks used to charge from 12 to 48 percent per annum.[54]

[52] F. D. Livshitz, *The Banks of the U.S.S.R.*, p. 21; A. G. Orlov, "The Quinquennial of the Mosgorbank," *Vestnik Finansov*, 1928, No. 2, pp. 91 ff.

[53] Orlov, *op. cit.*, p. 93; on deposits it allowed from 6 to 9 percent.

[54] Livshitz, *op. cit.*, pp. 21-22. In 1927 the municipal banks were instructed not to charge more than 10 percent on their short-term loans.

In addition to the Mosgorbank and its 26 branches [55] there were in the Soviet Union on October 1, 1928, 50 other municipal banks with 41 branches. The combined capital of the latter had increased from 3,200,000 rubles on October 1, 1923, to 54,100,000 on October 1, 1927; their deposits, from 3,600,000 to 95,800,000 rubles; and their loans and discounts from 9,700,000 to 254,500,000 rubles.[56] Like the Mosgorbank and for the same reason the provincial municipal banks turned to commercial operations during the early years of their existence. Their failure to follow the course charted for them in the decree of January 18, 1923, called for action. Accordingly, the Eleventh Congress of Soviets in 1924 appointed a special commission "to work out, and present to the Council of People's Commissars, a scheme for the organization and practical realization of co-operative construction of workers' homes and for the creation of a financial institution in which would be concentrated the financing of such work." [57] The commission recommended the creation of a *Central Municipal and Housing Bank.* Its recommendation was given official sanction on November 18, 1924. The statutes of the Central Municipal and Housing Bank (Tzentralni Bank Kommunalnogo Khoziaistva i Zhilishchnogo Stroitelstva) or "Tzekombank" were approved on January 17, 1925. It was joint-stock in form. Among its organizers were the People's Commissariats of Finance, of Labor, of Internal Affairs (of the various republics); the All-Union Soviet of Trade Unions, the Main Office of the State Insurance of the U.S.S.R., and the Mosgorbank. It was organized with an initial capital of 40,000,000 rubles with the right (as in the case of other banks) to increase it from time to time, but with the proviso that not less than one-half of its capital stock be placed in *long-term* loans. The familiar provision for reserve funds and special capital accounts is also found in its statutes.

[55] On October 1, 1926, it had 75 branches. The reduction in the number of its branches came as a result of a general policy which called for the elimination of unnecessary branch banks.

[56] Chernekhovsky, *op. cit.*, p. 139; B. B. Veselovsky, ed., *Credit: Housing, Municipal, Schools, Hospitals, Rural Buildings, Legislation* . . . (Moscow, Press of the Commissariat of Internal Affairs, 1928), pp. 11 ff.

[57] Chernekhovsky, *op. cit.*

It was also permitted to carry on short-term credit operations. It could deal either directly with the borrowers or with the municipal banks. It was at once besieged by a number of municipalities and enterprises clamoring for long-term credits to be utilized for the development of various fantastic projects. The wholesale refusals, however, had a sobering effect upon the applicants. The Tzekombank made it clear that it would grant long-term loans for specific purposes only, and on the condition that the revenue of the borrowing municipality be large enough to provide for the amortization and servicing of the debt.

As may be seen from Table 50, its total loans and discounts

TABLE 50

PRINCIPAL ACCOUNTS OF THE TZEKOMBANK [a]

(In millions of rubles on October 1 of each year)

	1925	*1926*	*1927*	*1928*
Branches	1	2	2	2
Total loans and discounts	35.4	146.8	308.4	543.7
Paid-in capital stock	36.2	40.0	43.2	52.3
Reserves, special capital and funds [b]	2.4	112.7	272.6	512.2
Deposits	1.3	6.6	8.9	7.4

[a] The figures for 1925–27 were taken from *Vestnik Finansov*, 1927, No. 6, p. 217; and No. 12, p. 178; for 1928, from *The State Bank of the U.S.S.R. Economic Survey*, 1929, IV, No. 3, January 21. Those for 1928 are *estimated* figures.

[b] These figures include funds placed at the disposal of the Tzekombank by others (e.g., the budget) to be loaned out to municipalities. In 1925 such funds amounted to 200,000; in 1926, to 102,400,000; and in 1927, to 169,200,000 rubles.

increased from 35,400,000 rubles on October 1, 1925, to over 500,000,000 rubles on October 1, 1928. Its deposits were very small and played a negligible part in providing the resources for the granting of loans. The resources came from its own paid-in capital and special capital fund accounts, particularly from the budget grants by the local councils (*soviets*). The bulk of its loans were represented by long-term advances. Inasmuch as its

participation in the capital formation of the various provincial municipal banks was small, it could not mold their activities.[58] The Tzekombank, however, had introduced an efficient method of control over the expenditure of long-term municipal and building credits granted by itself. Its policy at this time, as a matter of fact, was not only to control the expenditure of the funds loaned out, but to participate directly or through its correspondents, the provincial municipal banks, in the planning of the projects to be financed.[59]

An important step toward the co-ordination of municipal credit and the creation of a *system* under its leadership was taken by the Tzekombank in April, 1927, when it summoned an All-Union Conference of municipal banks at which the standardization of principles and methods pertaining to the granting of long-term credits was stressed.[60] This was not an attempt on its part to usurp power. The Tzekombank was intended to play that part when first organized. At any rate, the law of June 15, 1927, pertaining to the delimitation of the activities of banks stated specifically that the Tzekombank was to co-ordinate the activities of the municipal banks.

In a measure as the municipal banks were becoming more and more banks for long-term credit, their relations with the Tzekombank were becoming closer. Inasmuch as it was the lack of resources that hindered the development of the municipal banks into long-term credit institutions, the government adopted measures seeking to provide them with the necessary funds. Of great importance among these was the Workmen's Housing Construction Encouragement Act passed on June 15, 1927. It insured a steady flow of funds into the special capital accounts of the municipal banks. Such funds were to come from: (a) budgetary grants, union and local; (b) appropriations from the funds that

[58] In November, 1925, the municipal banks of the R.S.F.S.R. were ordered to send to the central authorities their quarterly credit plans for the purpose of being co-ordinated there with the plans of the central banks. It did not, however, work out successfully. S. Friedman, "Planning the Activity of Municipal Banks," *Finance and National Economy*, 1927, No. 48/56, November 27, p. 11.

[59] Lupandin, *op. cit.*, p. 99.

[60] "Activity of the Tzekombank," *Credit over Ten Years, Supplement to Finance and National Economy*, 1927, No. 45/53, p. 21.

the various enterprises were required to set aside for the improvement of the workers' living conditions; (c) appropriations from the net profits of state insurance; (d) a special apartment tax; (e) appropriations from the revenue of municipal councils (*soviets*) derived from the rentals paid by commercial and industrial enterprises; and (f) appropriations from the special "housing funds," when such exist, of the municipal soviets.[61] Another act was passed on January 30, 1929, to the same effect. Among other things, it required state industrial enterprises to set aside 7.5 percent of their net profits in a special "housing fund." The fund was to be deposited in the municipal banks and used for the building of homes for the employees of the respective enterprises. The banks were required to charge low rates on such loans.[62]

These measures proved successful in that they furnished the municipal banks with resources which made possible an expansion of their long-term credit operations (see Table 51).

The Bank for Foreign Trade

The Bank for Foreign Trade (Bank dlia Vneshnei Torgovli S.S.S.R. or "Vneshtorgbank") of the U.S.S.R. was set up on April 17, 1924, as a successor to the Russian Commercial Bank (Rossiiskii Kommercheskii Bank or "Roskombank").

Organized by a Swedish company (Swenska Economie Aktiebolaget) represented by Olaf Ashberg,[63] the Roskombank began its operations on December 12, 1922, not quite two months after its statutes were approved by the Council of Labor and Defense. It had a capital of 10,000,000 gold rubles. It was required to deposit with the State Bank, which had a representative on the Roskombank's board of directors, 25 percent of this capital as well as 10 percent of its deposits. It was also required to sell to the State Bank upon the latter's request up to one-half of its free foreign exchange (at the official rate).

The Roskombank was intended in general as a commercial bank and in particular as a bank for foreign trade. There was

[61] Veselovsky, *op. cit.*, pp. 90 ff.
[62] *The State Bank of the U.S.S.R. Economic Survey*, 1929, IV, No. 35, October 15.
[63] The Swenska Economie Aktiebolaget was really a *Soviet* enterprise.

TABLE 51

DETAILED ANALYSIS OF THE LOANS AND RESOURCES OF THE ENTIRE SYSTEM OF MUNICIPAL CREDIT [a]

(In millions of rubles on October 1 of each year)

	1926	*1927*	*1928*
I. Commercial loans and discounts	205.0	223.9	250.5
II. Specific-purpose loans	275.1	570.8	967.9
A. Long-term loans	(253.1)	(528.9)	(904.1)
Distributed as follows:			
(a) Housing	(166.9)	(374.5)	(648.3)
(b) Municipal	(39.6)	(75.3)	(110.4)
(c) Industrial	(25.9)	(40.9)	(105.4)
(d) Cultural (such as schools, cinemas, and the like)	(20.7)	(38.2)	(40.0)
B. Short-term loans	(22.0)	(41.9)	(63.8)
Distributed as follows:			
(a) Housing	(13.0)	(24.4)	(39.0)
(b) Municipal	(6.7)	(13.8)	(18.6)
(c) Industrial	(2.0)	(2.3)	(2.2)
(d) Others	(0.3)	(1.4)	(4.0)
III. Capital Funds	119.0	149.8	165.7
A. Capital stock	(107.4)	(128.6)	(134.4)
IV. Deposits	194.8	207.2	200.1
V. Special funds for specific-purpose loans	158.3	425.8	841.8
A. For housing and repairs	(124.5)	(332.9)	(635.8)
The special funds used for housing and repairs came from:			
(a) Budget	(93.0)	(186.5)	(327.4)
(1) State budget	(66.4)	(92.4)	(163.3)
(2) Republican budget	....	(3.1)	(5.4)
(3) Municipal budget	(26.6)	(91.0)	(158.7)

TABLE 51—*Continued*

DETAILED ANALYSIS OF THE LOANS AND RESOURCES OF THE ENTIRE SYSTEM OF MUNICIPAL CREDIT [a]

(*In millions of rubles on October 1 of each year*)

	1926	*1927*	*9128*
(b) State insurance and social insurance....	(23.6)	(108.1)	(219.5)
(c) Decreed appropriations.....	(6.1)	(23.1)	(51.2)
(d) "Fubr," fund for the improvement of workers' living conditions.....	(0.2)	(14.9)	(31.5)
(e) Miscellaneous.....	(1.6)	(2.9)	(6.2)
B. Specific-purpose loans to municipalities.....	(13.4)	(30.4)	(68.9)
Derived from:			
(a) State budget.....	(8.5)	(12.8)	(31.7)
(b) Republican budget.....	(1.7)	(3.6)	(4.9)
(c) Municipal budget.....	(3.2)	(7.8)	(21.1)
(d) Miscellaneous.....	....	(6.2)	(11.2)
C. Specific-purpose loans to industry.....	(13.3)	(37.3)	(81.4)
D. Specific-purpose loans for cultural purposes (schools, etc.).....	(0.5)	(9.9)	(30.2)
E. Miscellaneous loans.....	(6.6)	(15.3)	(25.4)
VI. Loans from credit institutions.....	30.0	33.3	40.3
A. Short-term loans.....	(29.0)	(27.6)	(34.6)

[a] From *The Perspectives for the Development of Local Finance of the U.S.S.R. in the Five-Year Plan* (Moscow, Gosplan, 1929), p. 50. It will be noticed that the totals given here differ somewhat from the totals which are obtained by adding the corresponding figures for the Mosgorbank, Tzekombank, and the provincial municipal banks. That is due to the fact that planning necessitates the publication of "preliminary" figures as soon as they can be produced. These are, generally, later revised, hence the resulting discrepancies.

apparently a belief that it could attract sufficient foreign capital to make possible a considerable expansion of trade between Soviet Russia and the outside world.

It was developing, however, rather too slowly; on April 1, 1924, its capital stood at the original 10,000,000 rubles, its deposits

amounted to 4,500,000 rubles, and its loans and discounts, to 12,200,000 rubles.[64] Hyper-inflation necessitated, of course, the placement of a considerable portion of the bank's capital in foreign exchange or abroad—to prevent its annihilation.

Of its total loans and discounts on that day but 17.4 percent were granted in connection with foreign trade, the remaining 82.6 percent were granted to enterprises engaged in internal trade, chiefly to private individuals and enterprises. It is, therefore, not surprising that the Soviet Union decided to put an end to this "private" institution. To some it may, in fact, seem more surprising that such an institution was even permitted to set itself up on Soviet soil. As to this, we must remember that it was done at a time when it was believed that concessions to foreigners would help to transform small Russian production to large scale, the latter being a prerequisite for the successful building of socialism.[65]

On April 17, 1924, as has been noted above, it gave place to the Bank for Foreign Trade or "Vneshtorgbank."[66] The latter began business with an authorized capital stock of 25,000,000 rubles, but by October 1, 1924, only 18,400,000 rubles of that was paid in. It was permitted to carry on all commercial banking operations. Its management and supervision were entrusted to the general meeting of stockholders, a board of directors (of not less than 5 members), a council (of not less than 7 members, with, in addition, a representative from the Commissariat of Finance), and an auditing commission. As in the case of other Soviet banks, it

[64] *Vestnik Finansov,* 1927, No. 4, p. 170.

[65] Lenin, *Complete Works,* XVII, p. 397; XVIII, 217, 222; also L. J. Eventov, *Foreign Capital in Russian Industry* (Moscow, State Socio-Economic Press, 1931), p. 98. It must further be remembered that at that stage of the Nep the country did not know how deep a plunge into capitalism would be made. At about the same time that the Roskombank opened its doors, for instance, the Council of Labor and Defense approved the statutes of a so-called "Credit Bureau," a "Moscow organization with a right to have branches at home and abroad." The "Credit Bureau" was given permission to act as expert accountants and "to furnish information as to the credit standing of private firms and persons, co-operative, public, and state enterprises and their combinations, as well as of institutions which receive credit or apply for it." (*Collected Decrees,* 1922, Pt. II, No. 19).

[66] The stock of the Roskombank was taken up by the Commissariat of Foreign Trade and by the State Bank.

was required by its statutes to set aside a part of its profits as reserve capital; another part, as an employees' fund.

The change from private to state ownership marked also a change in the nature of its operations. For example, whereas the Roskombank on April 1, 1924, had but 17.4 percent of its loans and discounts invested in transactions pertaining to foreign trade, those of the Vneshtorgbank, by the beginning of 1925, were divided as follows: 87.1 percent in connection with foreign trade, and but 12.9 percent in connection with internal trade.[67] Furthermore, unlike the Roskombank, it granted to private persons and firms but a negligible part of its total credit, the bulk (almost in its entirety) going to state (principally) and co-operative enterprises.[68]

As may be seen from Table 52, the loans and discounts of the

TABLE 52

PRINCIPAL ACCOUNTS OF THE VNESHTORGBANK [a]

(*In millions of rubles on October 1 of each year*)

	1924	*1925*	*1926*	*1927*	*1928*
Branches	4	9	9	4	0
Loans and discounts	37.8	89.6	96.0	107.2	80.1
Paid-in capital stock	18.4	30.0	38.9	42.6	43.2
Reserves and surplus	0.6	5.7	8.3	13.9	9.9
Deposits	17.8	36.8	26.0	17.3	12.5
Borrowed abroad	6.0	5.7	13.0	11.7	17.9

[a] The figures for 1924–27 were taken from the *Vestnik Finansov*, 1927, No. 6, pp. 220-21, and No. 12, p. 175; those for 1928 from the *Statement of Condition* for that year published by the Bank for Foreign Trade.

Vneshtorgbank experienced a growth between the years 1924 and 1927, but thereafter declined, and on October 1, 1928, amounted to 80,100,000 rubles. It was not a temporary decline;

[67] Livshitz, *op. cit.*, p. 13.

[68] *Vestnik Finansov*, 1927, No. 4, p. 170.

in the years that followed this amount dropped still further. On December 31, 1930, for example, it was 61,800,000, and on December 31, 1931, 69,900,000 rubles.[69] The decline was due to its being restricted to the granting of credit at one stage only, when the commodity is ready to be shipped abroad. The credit needed for the actual production of the exportable commodities was to be obtained from the State Bank.[70]

Its paid-in capital increased from 18,400,000 rubles on October 1, 1924, to 43,200,000 on October 1, 1928. Its deposits showed at first a rise but then declined, and on October 1, 1928, amounted to but 12,500,000 rubles.

The relative importance of the State Bank and of the Bank for Foreign Trade in the matter of financing foreign trade may be best understood from the following figures: on October 1, 1928, the total foreign trade credits granted within the country by both banks amounted to 457,500,000 rubles of which 375,100,000 rubles, or 78 percent of the total, was granted by the State Bank and 82,400,000 rubles, or 22 percent, by the Bank for Foreign Trade. On October 1, 1929, of a total of 623,200,000 rubles of such credits, their shares were 84 percent, and 16 percent, respectively.[71]

Although theoretically an independent bank, the Bank for Foreign Trade is in *reality,* at present, so to say, a department of the State Bank. It carries out the technical work pertaining to the financing of foreign trade and the making of settlements abroad.

Mutual-Credit Societies

Inasmuch as the New Economic Policy made it possible for private individuals to enter trade and industry, it was but logical that they should also be given an opportunity to obtain necessary bank credit with which to carry on their business. To be sure, private traders at that time had access to two sources of credit, the illegal private money market and banks. How important the

[69] Bank for Foreign Trade, *Statements of Condition for 1930 and 1931.*

[70] A. Orbelov, "Perspectives of Our Credit System," *Finance and National Economy,* 1930, No. 20/21 (184/185), p. 13; Kaktyn, *op. cit.,* p. 8.

[71] *The State Bank of the U.S.S.R. Economic Survey,* 1930, V, No. 1, January 15.

illegal market was as a source of credit is, for obvious reasons, impossible to tell. The cost of credit in that market was very high. In 1925, for instance, after the stabilization of the currency had been effected, the interest rates in the illegal Moscow market were 6 percent *per month,* in the provincial cities and towns, 8 to 10 percent and at times up to 20 percent *per month.*[72] Those high rates were influenced not only by the scarcity of funds but also by the fact that the creditors, in view of the illegality of the transactions, had no standing in the courts, and, therefore, included a charge for the risk involved. The second source, bank credit, was considered by the private traders to be entirely inadequate.[73]

To provide them with adequate credit facilities as well as to encourage the drawing of private capital accumulation into the economic sphere, the government sanctioned the organization of mutual-credit societies (Obschestva Vzaimnogo Kredita or "O.V.K.").

The Petrograd (Leningrad) Mutual-Credit Society which was organized in June, 1922, was the first to spring up in Soviet Russia. The numbers of mutual-credit societies increased quite rapidly, reaching 285 units on October 1, 1927.

Their capital took the form of membership fees. The membership fees, in accordance with the model statutes for mutual-credit societies, which were approved on September 2, 1922, were fixed at 10 percent (unless the membership chose to raise it up to 20 percent) of the loans allowed to individual members. The borrowing member was subject to a double liability, being responsible not only for the debt contracted by himself but for an additional amount equal to it.

The societies were permitted to discount for members acceptable two-name paper with a maturity not to exceed six months;

[72] *Vestnik Finansov,* 1925, No. 5, p. 192. In 1922 the *minimum* private discount rate amounted to 360 percent per annum. A. A. Dezen, *The System of Bank Credit* (Moscow, 1925), p. 11.

[73] The amount of credit granted to private individuals and firms by the State Bank and outstanding on October 1 of each year was as follows (in millions of rubles): 1923, 25.8; 1924, 11.2; 1925, 32.0; 1926, 23.2; 1927, 15.9; July 1, 1928, 11.4. Thereafter, declining and disappearing. See *Vestnik Finansov,* 1927, No. 4, pp. 168-69; No. 12, p. 186; 1929, No. 2, pp. 174-75.

to grant loans maturing within the same period as well as upon demand against commodities, warehouse receipts, bills of lading, government securities, foreign valuta, and precious metals,[74] and to grant loans for a period not to exceed nine months for the repair and improvement of buildings. They were also given the right to buy and sell commodities, machinery, merchandise, and so forth for others; to accept deposits; and to make transfers.

Of the profits made 10 percent was to be set aside as reserve capital. The societies were also required to maintain a cash reserve equal to 5 percent of their total deposits and indebtedness to others.

Their management rested with the general meetings of members, boards of directors, councils, and membership admission committees. Monthly and annual reports and statements had to be submitted, however, to the People's Commissariat of Finance.

Table 53 shows that their loans and discounts rose steadily

TABLE 53

THE GROWTH AND DECLINE OF THE MUTUAL-CREDIT SOCIETIES [a]

(*In millions of rubles on October 1 of each year*)

	1923	*1924*	*1925*	*1926*	*1927*	*1928*
Number of societies	45	86	173	280	285	237
Loans and discounts	4.8	9.3	31.1	51.7	31.1	22.8
Capital	1.2	3.3	7.8	15.9	13.9	11.1
Deposits	2.1	5.4	18.4	28.4	22.1	17.0

[a] Based upon *Vestnik Finansov*, 1927, No. 2, pp. 192-93; *The State Bank of the U.S.S.R Economic Survey*, 1930, No. 2. See also *Vestnik Finansov*, 1928, No. 3, p. 85.

from 4,800,000 rubles on October 1, 1923, reaching 51,700,000 rubles three years later. Thereafter a decline set in and by October 1, 1928, the loans and discounts outstanding amounted to but 22,800,000 rubles. Their resources came from their own capital, deposits left with them, and from whatever they could borrow at

[74] They had no right, however, to perform any other operations with foreign valuta or precious metals.

other banks, mostly at the State Bank. Their capital, between 1923 and 1926, had grown from 1,200,000 to 15,900,000 rubles. Their deposits during the same period increased from 2,100,000 to 28,400,000 rubles. The growth of these two would no doubt have been even greater had it not been for the instability of the currency during the early period as well as for the treasury's policy of looking into private accounts, whether for purposes of taxation or for any other reason.[75] To attract deposits, the mutual-credit societies paid a rate of interest much in excess of that allowed by other banks. In 1925, for example, although their reduction had previously been ordered by the Commissariat of Finance, the interest rates on deposits left with them varied from 0.5 to 3 percent *per month,* the bulk of the deposits drawing 1.5 percent per month, or 18 percent per annum, that is, three times as much as other banks paid. Hence the rates charged by them for the credit granted to borrowers were also high, approximately 36 percent per annum.[76]

Considering the size of their own capital and deposits, the credit that they obtained at other banks was rather substantial. On October 1, 1923, 1924, 1925, and 1926 it was 2,200,000; 2,600,000; 13,100,000, and 16,000,000 rubles, respectively.[77] The year 1926, which marked the peak of their development, also marked the beginning of their end. By October 1, 1927, their loans and discounts fell to 31,100,000 rubles; their capital, to 13,900,000, and their deposits, to 22,100,000 rubles. A year later these shrank further to 22,800,000; 11,100,000, and 17,000,000 rubles, respectively. Once they hit the toboggan slide they could not stop, and by 1930 there were left of them only pitiful remnants.[78] Why this change of fortune?

The mutual-credit societies, as we have seen, were intended to

[75] S. Friedman, *Development of Private Credit,* p. 21.

[76] *Vestnik Finansov,* 1925, No. 5, pp. 191-92. In 1927 the average rate of interest paid by the societies in the R.S.F.S.R. amounted to 10.1 percent, and the average rate charged by them for credit, to 33.2 percent (the minimum being 18 percent and the maximum 48 percent) per annum. *Finance and National Economy,* 1927, No. 46 (54), p. 21.

[77] *Vestnik Finansov,* 1928, No. 3, p. 85.

[78] Orbelov, *op. cit.,* p. 13; Kaktyn, *op. cit.,* p. 8. Needless to say the State Bank had discontinued giving them credit.

serve the *private sector* (that is, private trade). In 1922–23 that sector commanded a decisive position. Of the total trade turnover during that period, but 24.7 percent fell to the so-called *socialized sector* (to co-operatives 10.3 percent, and to state trading enterprises 14.4 percent), while the lion's share, 75.3 percent, fell to the private sector.[79] Naturally, this favored the development of the mutual-credit societies. They began to cater, particularly in the large centers, to "big" business, to the private wholesaler.[80] This policy they pursued even after 1924, despite the fact that the government made it quite clear in that year that it intended to eliminate from economic life the private wholesaler as a factor.[81] Indeed, as a result of the state policy, the socialized sector by 1924–25 already embraced 72.6 percent of the total trade turnover.[82] Undismayed by this, the mutual-credit societies continued to favor the "wholesaler" and in addition engaged in various irregular transactions.[83] In the summer of 1926 the government, however, began to stamp out the private middlemen who in one way or another would come into possession of commodities originally held in the socialized sector and then sell them to the public at exorbitant prices. A number of private traders failed. The repercussion of this was, of course, felt by the mutual-credit societies, and a number of them, particularly in Moscow, had to close their doors.[84]

[79] G. Schwartz, *Economic Life,* June 20, 1923.

[80] Hence of a combined balance-sheet total of 67,600,000 rubles on October 1, 1925, the Moscow and Leningrad societies were responsible for 33,200,000.

[81] See A. Kozyrin, "On Mutual-Credit Societies," *Vestnik Finansov,* 1927, No. 10, p. 97.

[82] *The Five-Year Plan,* p. 19; Butaev and Dzenis, *The Dictatorship of the Proletariat and the Building of Socialism in the U.S.S.R.* (Moscow, State Press, 1931), p. 201.

[83] In a circular of May 26, 1926 (No. 687), the Commissar of Finance pointed out that an examination of the societies (by the Commissariat of Finance) disclosed many violations of their statutes. Among those listed were: favoritism to large borrowers; lending in excess of the maximum (ten times the membership fee) allowed to one borrower; the credit granted was virtually long term inasmuch as borrowers kept on renewing their notes; stressing too much operations involving the purchase and sale of commodities for the account of others and for its own account, and so forth. *Bulletin of the People's Commissariat of Finance,* 1926, No. 32/33, p. 52.

[84] Of the eight societies on October 1, 1926 (with a membership of 7,434) in Moscow there remained only two (with a membership of 1,882) on April 1, 1927. A. Kozyrin, *op. cit.,* p. 99.

TABLE 54
PRIVATE TRADE,
1926–30 [a]
(*In millions of rubles*)

	Private Middlemen Trade	*As a Percentage of the Total Middlemen Trade Turnover*
1926–27	5,840	18.9
1927–28	4,375	11.3
1928–29	2,900	5.8
1929–30	2,035	3.3

[a] Segal, "The Ways of the Departing Private Capital," *Financial Problems of Planned Economy* (Moscow, Commissariat of Finance, 1930), No. 7/8, p. 90; the *Five-Year Plan of the National Economic Construction of the U.S.S.R.*, I, p. 19 (in Russian) or *The Soviet Union Looks Ahead—The Five-Year Plan for Economic Construction* (New York, Horace Liveright, 1929), p. 16 (in English); M. Livshitz, "How to Change the Private Sector," *Financial Problems of Planned Economy*, 1930, No. 6, p. 67; *Economic Life*, June 20, 1932, p. 3; Butaev and Dzenis, *op. cit.*, p. 201; *The Finances of the Three Years of the Five-Year Plan* (Moscow, State Finance Press, 1931), p. 28. The figures given in the above sources do not quite agree. Thus, the last-mentioned reference gives the share of the private sector in the trade turnover of 1928–29 as 10.7 percent. They point, however, in the same direction.

During 1926–27 the Commissariat of Finance, in order to compel a lowering of commodity prices, issued a number of circulars having as their purpose the curtailment or complete denial of credit to sellers of commodities the prices of which were adjudged to be too high.[85] Some of these were applied to all banks, a number to the mutual-credit societies, which were instructed on several occasions to grant credit to private borrowers only when the latter pledged that their selling or buying prices, as the case might be, would not exceed those of state and cooperative enterprises. This, together with a number of other regulations affecting their middlemen functions—the rate of interest paid on deposits, and the like—served to narrow their activities and diminish their resources. Meanwhile the socialized sector in the towns kept on expanding, threatening to engulf private trade (see Table 54).

[85] See, for example, *Vestnik Finansov*, 1926, No. 36, p. 2; also Pevzner and Drisin, *op. cit.*, pp. 31 ff.

The death knell of private trade was also the death knell of the mutual-credit societies; their fortunes were intermixed. Deprived of their clients, stripped of their erstwhile resources, subjected to increased taxation, they dwindled to nothing.

Savings Banks

When during the early part of the New Economic Policy banks began to be set up, there naturally was brought up the question of establishing savings banks. Some thought it inadvisable to set up such banks, for the reason that thrift by the individual is a bourgeois institution, and as such can have no place under a socialist regime where the individual is guaranteed the means of livelihood not only when he works, but even when he is ill, unemployed, incapacitated, aged, or, for any reason, he cannot work.[86] It is but logical, it was argued, that saving in such a society should be carried out by the state or the group and should come from the "surplus value" retained by it. Those who argued thus apparently overlooked the fact that Soviet Russia of that day had not as yet entered the socialist phase, and could not guarantee a full life even to those employed.

It was also urged that the earnings of the population were not high enough to permit saving; and that even if they were high enough, saving would not go on because of the depreciating currency; furthermore, the population, as a result of the bitter experience during the early years of Soviet rule, had no confidence in the credit institutions.

The government, however, took a different attitude, and the Collegium of the Commissariat of Finance on December 8, 1922, drew up a plan for the establishment of such banks. On December 26 of the same year the Council of People's Commissars approved the proposed plan and the statutes which were to govern their organization, administration, and operations. In the latter it was proclaimed that the government accepts complete responsibility for the sums entrusted by the people to the savings banks, and

[86] See Dr. Mark Soliterman, "Savings Banks in the U. S. Soviet Russia," *Savings Bank Association News Bulletin*, State of New York, December 12, 1930, XI, No. M-48; pp. 197-99; and December 19, No. M-49, pp. 202-6. Also A. T. Popov, *Thrift and Its Propaganda* (Moscow, 1928), p. 29.

that deposits will not be attached or confiscated without a court order. A pledge was also made that the savings banks would not divulge the balance of one's account to anyone save the owner or his agent and court authorities.

The savings banks were placed under the jurisdiction of the Commissariat of Finance and their administration was entrusted to one of its divisions—the Chief Department (Board) of State Labor Savings Banks (Glavnoe Upravlenie Gosudarstvennykh Trudovykh Sberegatelnykh Kass).

The first two savings banks, one in Moscow and the other in Leningrad, were opened on February 11, 1923. It was planned to have by fall of that year a thousand such banks in operation.

The inducement offered to the public by these banks was great indeed. The banks offered protection against inflation plus 6 percent interest on the deposits. The protection against inflation, as we have seen, consisted in crediting the depositor's account, whenever he would present sovznaks for deposit, with stable units in accordance with the prevailing official rate of exchange, but in paying him at the time of withdrawal in sovznaks according to the official rate of exchange on the day of withdrawal.

Partly because income was too low to permit saving and partly because the people still remembered what had happened to their old savings accounts,[87] the development of savings banks at first proceeded quite slowly. In August, 1923, there were in operation but 69 branches having 29,544 depositors, with the equivalent of about 1,250,000 gold rubles in deposits.

As a result, however, of an intensive campaign savings began to grow. By October 1, 1923, the country had 304 such banks with 59,583 depositors, and 1,773,415 rubles in deposits. As the ruble kept on depreciating and more and more workers sought

[87] It will be recalled that by the decree of April 10, 1919, the savings banks then existing were merged with the People's Bank (former State Bank). The assets and liabilities of the People's Bank, by decree of January 19, 1920, were transferred to the Central Budgeting and Accounting Administration. The latter opened accounts for the former savings banks depositors on the books of the local treasury branches. On June 17, 1920, the Commissariat of Finance set six months as the limit within which all such balances had to be withdrawn. On June 1, 1920, however, 100 rubles had the purchasing power of about one pre-war copeck, while by December, 1920, 1,000 rubles equaled about five pre-war copecks.

protection against inflation, the deposits of the savings banks kept on growing. At the time of the Monetary Reform, on March 1, 1924, there were already 2,566 savings banks with 768,764 depositors and 17,964,214 rubles in deposits.[88] All of that, however, did not represent savings in the real sense of the word. It was rather a fund made up of deposited earnings against which the depositors meant to draw at once. Hence, by July 1, 1924, when, in view of the accomplished stablization of the currency, the protection or insurance of earnings against inflation was withdrawn by the savings banks, their deposits shrank to 8,964,655 rubles.[89]

The protection of depositors against inflation was carried out by the savings banks at a cost of 2,069,067 gold rubles to themselves or, rather, to the treasury. As can be seen, this was a costly business. Naturally, the government could not possibly insure everybody against depreciation. But, then, all people did not seek such insurance. Even as late as October 1, 1925, the number of peasant depositors at the savings banks amounted to but 1.8 percent of the total depositors.[90] It served, however, to show the good faith of the government, to build good will, and to attract depositors. Above all, it gave the workers at least some protection against inflation.

It had been intended to serve also another purpose, to check the rate of the ruble's depreciation. Since one's holdings of sovznaks were insured against depreciation, it was figured, there was no cause for rushing to convert them into commodities. It is, of course, impossible to determine the net effect of the protection of deposits against depreciation upon the rate of the ruble's depreciation. It may be supposed, however, that it was not great, particularly if it is borne in mind that the loss arising from that

[88] V. Vvedensky, "Three Years of Work of the State Labor Savings Banks," *Vestnik Finansov*, 1926, No. 1, pp. 122-23.

[89] *Ibid.*, p. 124.

[90] K. Tufesko, "Savings Work in 1925–26," *Vestnik Finansov*, 1927, No. 1, p. 67. Of the total deposits on that day 36.4 percent were those of "legal entities," that is organizations of one kind or another; 31.4 per cent, employees; 9.2 per cent, workers; and 21.2 percent, "other individuals." On October 1, 1926, peasants' deposits represented 2.4 percent of the total.

transaction had to be made good by the issue of more paper money.

During those years the savings banks did not emphasize business principles as much as they should. An interesting comparison of the distribution of cost by the Soviet savings banks in 1924–25 with that of the pre-war savings banks is shown by Table 55.

The principle of "business accounting" was called to their attention on a number of occasions. In their new regulations of

TABLE 55

SAVINGS BANKS: DISTRIBUTION OF COSTS

1913 and 1924–25 [a]

In percents

	1913	*1924–25*
Interest on deposits	90.1	29.0
Administrative and business expenses	9.6	63.6
Amounts charged to loss	0.1	5.7
Loss sustained on the sale of securities	0.2	....
Loss on the difference in sovznak rates	....	1.7
Total	100.0%	100.0%

[a] K. Tufesko, "Savings Work in 1925–26," *Vestnik Finansov*, 1927, No. 1, p. 68.

November 27, 1925, the government, having granted them 10,000,000 rubles to be used as a reserve capital,[91] specified that expenses should be met out of profits, unless the latter were not large enough, in which case the reserve capital was to be used. Again, in the more recent regulations adopted on February 20, 1929, it was clearly pointed out that the savings banks must operate on a principle of "business accounting." But it was not

[91] According to the regulations of February 20, 1929, this was to be considered the initial capital of the banks, while the reserve capital was to be formed from the profits. The profit was to be divided as follows: 65 percent, to reserve capital account; 35 percent, to the treasury of the U.S.S.R., and 5 percent, to bank employees' welfare fund.

until 1932 that a beginning in that direction was made.[92] The savings banks, however, were not unique in this respect; the formative period meant waste and high cost in all branches of the economy.[93]

As may be seen from Table 56, the deposits had steadily mounted, reaching by October 1, 1928, 314,800,000 rubles. On that day there were 16,924 savings banks with 3,800,000 depositors.[94] A year later the deposits increased to 505,300,000 rubles,

TABLE 56

SAVINGS BANKS: MOVEMENT OF DEPOSITS [a]

1924–29

(*In millions of rubles on October 1 of each year*)

Year	*Amount*	*Year*	*Amount*
1924	11.3	1927	181.5
1925	33.5	1928	314.8
1926	90.5	1929	505.3

[a] *The State Bank of the U.S.S.R. Economic Survey*, November, 1929, IV, No. 38, and, October, 1930, V, No. 18.

the number of banks to 20,068, and the number of depositors, to 7,600,000.[95] Now, this represented a considerable growth. Of course, in 1913, when there were only some 8,000 such banks, the deposits amounted to 1,600,000,000 rubles and those rubles, according to official index numbers, had no less than twice the purchasing power of their 1928 namesakes. Still, conditions had changed considerably since 1913, and the Soviet government had good reason to be proud of its achievement. In various ways banks enabled it to carry out its gigantic projects with a smaller volume

[92] G. Gaido, "Business Accounting in the Savings Banks System," *Finance and Socialist Economy*, December, 1932, No. 35/36, p. 12.

[93] G. I. Bronshtein, *Analysis of the Financial Economy and Profitability of Savings Banks* (Moscow, State Finance Press, 1933), Second revised and enlarged edition, Chapter IV.

[94] *The State Bank of the U.S.S.R. Economic Survey*, July, 1930, V, No. 12/13.

[95] Included in the number of savings banks are so-called independent offices, offices established at various treasury agencies, post and telegraph offices, railroad stations, libraries, drug stores, factories, and so forth.

of paper money than would otherwise have been possible. They had invested their funds in government bonds and besides helped to distribute the various issues among the population. It may also be interesting to note that in 1928 the savings banks began to issue government-guaranteed *certificates* of five- and ten-ruble denominations. These were to mature in six years, at which time their holders were to receive double their face value.[96] Judging by the fact that they were of low denominations and enjoyed the privilege of circulating as money, the purpose behind their issue was not only to attract savings but to create a money substitute.[97] As will be shown in later chapters, the savings banks were also instrumental in introducing so-called "moneyless" payments, that is, payments by means of a debit to the payer's account and an equivalent credit to the recipient's account.

Miscellaneous Banks

In addition to the above, mention may be made of a few other, less important banks. Of these the Far Eastern Joint-Stock Bank (Dalne-Vostochnyi Aktzionernyi Bank or "Dalbank") was established on April 25, 1922, by the one-time government of the Far Eastern Republic. Its operations extended to both domestic and foreign trade of the Far Eastern region and Siberia. It served as municipal, commercial, and agricultural bank, financing the fishing industry, and trade with the Far East (particularly, with Japan).

In 1928 it had an authorized capital of 10,000,000 rubles. The loans and discounts granted on July 1, 1928, by the parent office and the seven branches amounted to 26,900,000 rubles. As in the case of all the other banks (except the private mutual-credit societies) only a small part of the total loans and discounts went to private individuals and enterprises, the bulk (26,700,000) went to state enterprises, municipal, co-operative, and agricultural or-

[96] *Ibid.*, October, 1927, II, No. 10. On their savings accounts the banks from August 1, 1925, paid the following rates of interest: on demand deposits, 8 percent; on time, 9 percent; and to "legal entities," 6 percent per annum. For recent changes see Chapter XV.

[97] The issue of these certificates was terminated in 1930.—B. I. Levik, *Operating Technique and Accounting in Credit Institutions* (Moscow, State Finance Press, 1933), Pt. I, p. 20.

ganizations. Its deposits on the same date amounted to 7,000,000 rubles.[98]

The Mid-Asiatic Commercial Bank (Sredne-Aziatskii Kommercheskii Bank) is another bank worthy of mention. It was organized in Tashkent on March 1, 1924, for the purpose of developing commercial relations between the republics of the U.S.S.R. and the countries in Middle Asia. Among its organizers were the People's Commissariat of Finance of the U.S.S.R., the governments of the Turkestan S.S.R., of the Bokhara Soviet Republic, of the Koresm S.S.R., and the Chief Cotton Committee. Its initial authorized capital was fixed at 7,500,000 rubles but was increased in October, 1927, to 10,000,000. It served the needs of the territory over which its activities were intended to spread. It financed trade with the above-mentioned countries and Persia; aided in the financing of such commodities as cotton, silk, wool, and karakul.

The loans and discounts of the bank together with its seven branches on July 1, 1928, amounted to 22,200,000 rubles; its deposits, to 5,000,000 rubles.

Still another bank, the South Eastern Commercial Bank (Yugo-Vostochnyi Bank) in Rostov-on-the-Don was established in April, 1922, with a small initial capital stock of 860,000 rubles. It was of a "mixed" character; slightly more than half of its stock was owned by the State Bank, the rest by private holders. Up to 1924 it catered to private trade but then, as the policy of the government changed, its operations took on a different aspect. Its loans and discounts as well as its deposits remained quite small.

The German-Volga Bank (Nemetzko-Volzhskii Bank) combined the activities of a municipal and agricultural bank in the German settlement along the Volga.

There were also pawnshops which were doing a thriving business. They began to be organized in 1922. In 1927 there were about 25 such institutions in the Union. Their own capital was quite small, but some of them obtained credit at the municipal banks. Their interest rates were quite high. In the R.S.F.S.R.

[98] On October 1, 1928, to 9,300,000 rubles. *Vestnik Finansov*, 1929, No. 2, pp. 173, 179; No. 7, p. 161.

their charges in 1927 on loans from 1 to 10 rubles were 1.5 to 3 percent; from 10 to 25 rubles, 2 to 6 percent; and above 25 rubles, 6 to 10 percent *per month*. The pre-war pawnshops charged from 1.5 to 2 percent monthly.[99]

[99] M. Banovich and G. Derchenkov, "The Present Position of the Pawnshop Business in the U.S.S.R.," *Finance and National Economy*, October, 1927, No. 40/48, pp. 10-12.

XII

THE STATE BANK AND THE CREDIT REFORM OF 1930

Rapid industrialization and socialization of the national economy beginning with 1928.—In 1928, when production in a number of her important industries reached the pre-war level, Soviet Russia set out to speed up the rate of the development of her productive forces. She was determined to bring about a rapid industrialization of the country, to effect a socialistic reconstruction of her national economy in general, and of her rural economy in particular, all of which would serve to secure self-sufficiency and to enable her to strengthen the defenses of the country.

To effect these ends, a plan charting the development of the national economy over a period of five years (1928–29 to 1932–33), and, therefore, known as the Five-Year Plan, was drawn up.[1] Altogether it called for an outlay of 86,000,000,000 rubles *net,* or 91,600,000,000 rubles *gross.*[2] Of the total gross outlay, 56,800,000,000 rubles (62 percent) were to be expended in connection with the financing of the national economy, and 21,400,000,000 rubles (23.4 percent), in connection with the social-welfare needs of the country (education, health, and so forth). The balance was to be taken up by administrative and defense costs and miscellaneous outlays.

Of the 56,800,000,000 rubles intended for the financing of the national economy, 22,000,000,000 rubles were to be directed into

[1] Russians commonly refer to it as "Piatiletka," or "Quinquenny."

[2] *The Five-Year Plan of the National Economic Construction of the U.S.S.R.,* 2d edition (Moscow, "Planned Economy" Press, 1929), I, 159; also *Results ("Itogi") of the Fulfillment of the First Five-Year Plan for the Development of the National Economy of the U.S.S.R.* (Moscow, Gosplan of the U.S.S.R., 1933), p. 271. The *net* figure was obtained by including merely the *difference* between the amount received from the population in the form of loans and social-insurance premiums and that paid out to it in the form of interest, benefits, etc. Figured on the basis of the *net* total (86,000,000,000 rubles) the investment in the national economy was to amount to 54,600,000,000 rubles (63.5 percent); in social welfare, 21,400,000,000 rubles (24.9 percent). Another 10,000,000,000 rubles (11.6 percent) was to be used for administrative expenses and defense.

industry and electrification; 7,300,000,000 rubles, into agriculture; and 10,200,000,000 rubles, into transportation and communication. Particular stress was laid on "heavy" industry and the production of means of production.

As compared with 1927–28 the output of the basic and most essential industries in 1932–33 was to increase as follows (in millions of metric tons): coal, from 35.4 to 75.0; petroleum and natural gas, from 11.7 to 21.7; iron ore, from 5.7 to 19.4; pig iron, from 3.3 to 10.0; steel ingots, from 4.0 to 10.4; rolled steel, from 3.2 to 8.0; grain, from 73.1 to 106.0. Cotton cloth was to increase from 2.5 to 3.6 thousands of millions meters; leather shoes, from 23.0 to 80.0 million pairs; electric power production, from 5.0 to 22.0 thousands of millions kilowatt-hours; railway lines, from 47.8 to 55.9 thousand miles, etc., etc.[3]

With this in view the country proceeded to expand the old, and to construct new, large, and well-equipped mines. It likewise proceeded to construct giant metallurgical works. The machine industry, which in old Russia occupied an insignificant place but without which economic autarchy is impossible, became one of the major centers of attention under the Plan. To make possible the projected economic growth there was ordered the development of a number of large power plants. Tremendous changes were likewise charted for agriculture. The *socialized sector,* i.e., the sector comprising the collective farms (or "kolkhozy"), and state farms (or "sovkhozy"), was to be expanded appreciably. To accelerate the change from small to large-scale production in agriculture, so-called machine tractor stations (or M.T.S.) were to be set up. These were intended to supply the socialized sector with tractors, harvesting combines, and other machinery, and to guide the peasantry technically and politically.

The means for financing this ambitious scheme were to come from the following sources: the budget was to yield 44,700,000,000 rubles (52 percent of the total net outlay);[4] the various enter-

[3] *The Monthly Statistical Bulletin of the Supreme Council of National Economy,* October, 1928–29, No. 1 (64) (Moscow, 1929), p. 14; also *The Five-Year Plan of the National Economic Construction of the U.S.S.R.,* I, pp. 144-47.

[4] The state budget was to yield 29,639,000,000 rubles, and the local budgets the balance.

prises themselves, around 19,000,000,000 rubles (22 percent); the social-insurance funds, 9,200,000,000 rubles (10.7 percent); the credit system, 6,600,000,000 rubles (7.7 percent); miscellaneous sources (foreign credits, share capital of co-operatives, and so on), 6,500,000,000 rubles (7.6 percent).[5]

The part that was to be played in this connection by the short-term credit system is reflected by the projected changes in its principal accounts. Thus, the short-term loans and discounts were expected to increase during the five years by 3,375,000,000 rubles.[6] An increase of 1,250,000,000 rubles in the banknote issue, of 1,700,000,000 rubles in time and demand deposits, and of 750,000,000 rubles in the capital account, was to provide the resources for the expansion of the loans and discounts.

The long-term credits were expected to expand by 9,300,000,000 rubles. Accordingly the credit plan provided for an increase in the resources of the Prombank by 3,800,000,000 rubles, in those of the agricultural credit system, by 2,000,000,000 rubles, and, finally, in those of the municipal credit system by 3,500,000,000 rubles. The expansion of their resources was to come in part from the growth of deposits, profits, and so forth, and in part from funds furnished by the budget itself. Thus, the state budget was to furnish the Prombank with 1,000,000,000 rubles to be used by it for the granting of *repayable* loans to industry; the agricultural credit system was to receive from the state budget 1,600,000,000 rubles; and the municipal credit system was to receive from the state budget about 2,000,000,000 rubles.

The actual performance differed, however, from the planned; in part because the conditions envisaged by the Plan failed to materialize. The 1931 crop, for example, was disastrous.[7] Then, too, the unfolding world crisis caused a terrific slump in international trade. As a result, between October, 1928, and the end

[5] *The Five-Year Plan of the National Economic Construction of the U.S.S.R.*, I, 159; also M. I. Bogolepov, *The Financial Plan of the Five-Year Plan*, 2d edition (Moscow, Gosplan of the U.S.S.R., 1929), pp. 54-55. The percentage distribution approximated that in 1927–28.

[6] The projected increase was in conformity with the experience of the preceding years.

[7] The gross production in the principal eastern grain districts was 10,700,000 metric tons below the 1927–30 average.—*Itogi*, p. 11.

of 1933 Soviet exports, as may be seen from Table 57, amounted to but 4,009,800,000 rubles, and its imports to 4,294,500,000 rubles, and not to 7,000,000,000 rubles and 6,180,000,000 rubles, respectively, as envisaged by the Plan. Instead of a *planned* favorable balance of 820,000,000 rubles, the country consequently sustained an unfavorable *(actual)* balance amounting to 284,700,000 rubles.

Besides, the growing acuteness of the Far Eastern situation demanded an acceleration of military preparedness, and the resulting

TABLE 57

FOREIGN TRADE OF THE U.S.S.R., 1928–34 [a]

(In millions of rubles)

	Export	*Import*	*Favorable (+) or Unfavorable (−) Balance*
1928 (October-December)	216.5	203.2	+ 13.3
1929	923.7	880.6	+ 43.1
1930	1,036.4	1,058.8	− 22.4
1931	811.2	1,105.0	−293.8
1932	563.9	698.7	−134.8
1933	458.1	348.2	+109.9
1934	419.3	232.4	+186.9

[a] Chief Department of Customs, *Foreign Trade of the U.S.S.R. during the First Five-Year Plan (1928 to 1933)* (Moscow, 1933), p. 2; also "Foreign Trade of the U.S.S.R. at the New Stage," *Economic Life*, May 1, 1935.

shift in the center of attention interfered to no small degree with the Plan.

Furthermore, the so-called qualitative indices (productivity of labor, cost of production, yield per acre) upon which, as a foundation, the whole Plan rested, were running all the time considerably behind the planned figures.

In general it may be added that scientific planning requires adequate data with respect to previous experience along the same lines, something which the Soviet Union lacked at the time.

The First Five-Year Plan was declared completed by the end of 1932 [8] rather than on October 1, 1933, as originally contemplated, that is, in four and a quarter years—a circumstance which serves to make comparisons difficult. By that time the total *gross* outlay reached 120,100,000,000 rubles (or 114,500,000,000 rubles *net*) as against the contemplated 91,600,000,000 rubles *gross* (or 86,000,000,000 rubles *net*), a difference of 31.1 percent. The *actual* revenue raised by the budget amounted to 72,800,000,000 rubles as against the *planned,* 45,000,000,000 rubles, a difference of 60 percent.[9] In fact, the actual 1932 budget exceeded the planned budget for 1932–33 by more than 160 percent, its revenue being 31,030,000,000 rubles as against the planned 11,820,000,000 rubles.[10]

The *actual* distribution of the *gross* total outlay of 120,100,000,000 rubles was as follows:

(a) Financing the national economy, 80,300,000,000 rubles (as against the planned 56,800,000,000 rubles). Of this amount 41,600,000,000 rubles (as against the planned 22,000,000,000 rubles) were directed into industry; 15,100,000,000 rubles (as against the planned 7,300,000,000 rubles), into agriculture; and 12,500,000,000 rubles (as against the planned 10,200,000,000 rubles), into transportation and communication.

(b) Financing social-welfare needs, 23,900,000,000 rubles (as against the planned 21,400,000,000 rubles).

(c) Administration and defense, 9,000,000,000 rubles (as against the planned 10,000,000,000 rubles).

(d) Miscellaneous, 6,900,000,000 rubles (as against the planned 3,400,000,000 rubles).

The actual output of the basic Soviet industries in 1932 was

[8] The practice of calculating the economic and fiscal year from the first of October to the end of September was discontinued, beginning with January 1, 1931, in favor of the customary calendar year, January 1 to December 31. The change necessitated the drawing up of special plans for the last quarter of 1930. *Collected Decrees,* 1930, Decree 510.

[9] *Itogi,* pp. 205, 272. The 72,800,000,000 rubles received by the budget were distributed as follows (in thousands of millions of rubles): 52.0, financing of national economy (of this 22.99, to industry; 8.54, to agriculture, and 10.4 to ways and means of communication); 4.61, for social-welfare needs (of this 4.12 for education); 6.95, for administration and defense; 10.16, for other expenditures.—*Ibid.,* p. 272.

[10] *Collected Decrees,* 1934, Decree 15.

as follows (in millions of tons): coal, 64.4; oil and gas, 22.3; iron ore, 12.2; pig iron, 6.2; steel ingots, 5.9; rolled steel, 4.2. The electric power output amounted to 13,400,000,000 kilowatt-hours. The railway lines covered 51,800 miles. The production of cotton cloth amounted to 2,400,000,000 meters; leather shoes, 81,900,000 pairs; grain, 69,900,000 tons.[11]

Although the actual output in 1932 fell short of the goal set by the Plan for 1932–33, the achievement, nevertheless, was tremendous. The Soviet Union laid during 1928–32 the foundation for a vast industrial structure to be operated by the most modern technique. There were set up new industries producing caterpillar tractors, cotton pickers, chemicals, airplanes, blooming mills, lathes, machine tools, precision instruments, linotypes, turbines, generators, locomotives, electric cars, and so forth, many of which were not even included in the original Plan. It must be understood, too, that a number of the new plants were either under construction by the end of 1932 or else had just begun to produce.

The socialization of the Soviet national economy proceeded apace. In industry the socialized sector was said to have embraced, in 1932, more than 99 percent of the total production.[12] In wholesale trade it covered 100 percent of the total turnover. In retail trade it covered the entire *stationary* retail network.

In agriculture, where the socialized sector in 1928 accounted for but 2.7 percent and the individual peasants for 97.3 percent of the total grain production, a rather drastic change took place. In 1932 the socialized sector's share in the total production of grain rose to 78 percent, and that of the private sector (individual peasants) dropped precipitously to 22 percent. By the end of that year the country had, in addition to 5,820 state farms (or *grain factories*), 210,000 collective farms holding 14,700,000 peasant families (or 61.5 percent of the total) and representing

[11] Molotov's Report at the Seventeenth Congress of the Communist Party. *Economic Life,* February 6, 1934. Also *Itogi, passim.*

[12] *Itogi,* p. 30. The estimate pertaining to the degree of socialization of industry apparently overlooked the "private" handicraft trades (shoemakers, dressmakers, etc.). It is officially estimated that *at present* the socialized sector of industry accounts for 98.5 percent of all goods produced, and the private sector (handicraft trades), for the remaining 1.5 percent.

75.6 percent of the entire grain cultivated area.[13] The machine tractor stations at the end of that year numbered around 2,500 and the tractors, 148,480.

Before the First Five-Year Plan was brought to a close, announcement was made of a Second Five-Year Plan (1933–37). Its financing is estimated to require 333,800,000,000 rubles as against 120,100,000,000 under the First Plan. Capital construction is expected to require 130,400,000,000 rubles (as against some 50,000,000,000 during October 1, 1928—December 31, 1932) to be divided as follows: heavy industry, producers' goods, 53,400,000,000 rubles (as against 21,300,000,000 rubles in 1928–32); consumers' goods, 16,100,000,000 rubles (as against 3,500,000,000 rubles in 1928–32); agriculture, 15,200,000,000 rubles (as against 9,700,000,000 rubles in 1928–32); transportation, 26,300,000,000 rubles (as against 3,900,000,000 rubles in 1928–32).[14]

The output of the basic industries is expected to reach, in 1937, the following levels (in millions of tons): coal, 152.5; oil and gas, 46.8; pig iron, 16; steel ingots, 17; rolled steel, 13. Electric power is expected to amount to 38,000,000,000 kilowatt-hours; automobiles, 200,000 (units); combines, 20,000; freight cars, 118,400. The trade turnover in 1937 is expected to increase by 150 to 200 percent as compared with 1932 (when it amounted to 31,900,000,000 rubles). The output of grain is expected to reach 110,600,000 tons; of cloth, 5,100,000,000 meters; of leather shoes, 180,000,000 pairs. Retail prices are to be lowered by 35 to 40 percent (as compared with 1933). The productivity of labor is scheduled to rise by 63 percent (as against an actual rise of 41 percent during 1928–32). The quality of the goods produced (which left much to be desired under the First Five-Year Plan) is to increase materially. According to the official figures given out from time to time the output of both producers' and consumers' goods is steadily pushing upward.[15]

[13] *Ibid.*, pp. 136-37.

[14] The State Planning Commission of the Council of People's Commissars of the U.S.S.R., *The Project of the Second Five-Year Plan for the Development of the National Economy of the U.S.S.R. (1933–37)* (Moscow, 1934), p. 403; also *Economic Life*, February 8 and 11, 1934.

[15] *Economic Life, passim.*

So much, in brief, for the change on the Soviet economic front since 1928. Let us now see how that affected the country's short- and long-term credit institutions and the currency. We shall deal first with the State Bank.

The State Bank's Statutes of 1929

As the First Five-Year Plan was getting under way the statutes of the State Bank of the U.S.S.R. underwent a revision. The new statutes, which were approved in June, 1929,[16] by the Central Executive Committee and the Council of People's Commissars of the U.S.S.R., reflected primarily the changes that had occurred in the preceding years rather than those which had taken place or were anticipated as a result of the inauguration of the First Five-Year Plan.

The purpose of the bank.—According to the 1929 statutes the purpose of the bank is "to regulate currency circulation and to grant short-term credit to industry, agriculture, trade, transport, and to other branches of the economy, in conformity with the general plan of the development of the national economy of the U.S.S.R." (Article 1). Thus, the allusion to long-term credit, which was present in its old statutes, was removed as inconsistent with the object of regulating currency circulation.

Capital and surplus.—The bank has an authorized capital and a reserve capital or surplus. The authorized capital was fixed by the 1929 statutes at 400,000,000 rubles.[17] Its increase may be sanctioned by the Council of People's Commissars of the U.S.S.R. (Articles 14 and 15).

The surplus is formed by transferring to it a part of the profits earned by the bank. The size of the surplus account may not exceed that of the authorized capital[18] (Article 16).

[16] *Collected Decrees,* 1929, Decree 332. Also the Statutes of the State Bank of the U.S.S.R. (Moscow, Gosbank, 1929).

[17] The bank's authorized capital in June, 1929, amounted to 250,000,000 rubles. The above is to be understood in the sense of a *permission to increase the capital* to 400,000,000 rubles. See *The State Bank of the U.S.S.R. Economic Survey,* June 30, 1929, p. 4.

[18] The excess net profit is to be used for the purpose of increasing the authorized capital and surplus or is to be credited to the treasury, depending on the decision of the Council of People's Commissars of the U.S.S.R. (Article 49).

The net profit of the bank is to be distributed as follows: (a) 50 percent, to the treasury; (b) 5 percent, to the bank employees' and workers' welfare fund; (c) not to exceed 0.25 percent, to the bonus fund; (d) remainder, to surplus (Article 49).

Relations with the state and treasury.—According to the 1929 statutes, the State Bank "is a legal entity operating on a commercial basis" (Article 2). It is not responsible for the debts of the state or of any political subdivision thereof unless it assumes such responsibility. Nor is the state or any of its political subdivisions responsible for the obligations incurred by the bank, with this exception, however: the authorized capital of the bank must not be reduced, and should the loss sustained by the bank during any given year exceed its surplus, the All-Union budget will make good the difference (Articles 3 and 4).

The State Bank, furthermore, "operates independently within the bounds of the present statutes" (Article 5). The meaning of this provision becomes clear when it is recalled that in the old statutes it was stated that the bank was being set up as a constituent part of the People's Commissariat of Finance (that is, of the treasury), and that it was directly subordinated to the Commissar of Finance. Apparently, in deference to good capitalistic banking theory, it was decided to lay emphasis on the fact that the bank was not an agency of the treasury and that its policies, therefore, were not influenced by the needs of the latter. However interesting from an academic viewpoint, such distinctions are of no practical importance in the Soviet Union. There the centralized authority directs the policy of both the treasury and the bank, and gives orders to both. Besides, the Commissariat of Finance and the bank continue to be closely related. The Commissar of Finance, for instance, fixes the limits of banknote issue (as directed by the Council of Labor and Defense), approves the list of members of the Board of Directors of the State Bank, as recommended by the latter's Council, approves the annual financial statements, the orders for the issue and withdrawal of notes, and the instructions to the auditing committee (Articles 5, 46, and 47). Moreover, the Commissar of Finance is the chairman

of the Council of the bank.[19] The Commissariat of Finance also exercises supervision over the activities of the bank in the same manner as it does over all other All-Union credit institutions (Article 5).

Fiscal operations.—The bank was entrusted with the receipt, holding, and disbursement of funds under the unified state budget of the U.S.S.R. and under local budgets. It was also to participate, on the basis of a special agreement with the Commissariat of Finance of the U.S.S.R., in the flotation of state loans of the U.S.S.R., its federated republics, and of treasury bills (Article 7).

Relations with other banks.—The free cash reserves of all credit institutions, except the credit co-operative organizations, must be maintained with the bank. The Commissar of Finance may exempt from this ruling also state labor savings banks and the agricultural credit system (Article 8).

Note issue.—Since the old statutes had been passed a year before the bank obtained the right to issue notes, they naturally contained no reference to note issue. The statutes of 1929 contain a special section entitled "The Issue of Banknotes," which is largely a repetition of some of the provisions of the Act of October 11, 1922, as well as of the more recent regulations.

Articles 17, 18, and 19 of this section enumerate the denom-

[19] In the Regulation of the Central Executive Committee and of the Council of People's Commissars of the U.S.S.R. of May 27, 1936, relative to the People's Commissariat of Finance of the U.S.S.R., the latter is described as performing, among others, the following functions: regulating the system of monetary circulation; preparing the All-Union budget, consolidating the latter with the republican budgets into a unified state budget, and submitting it to the Council of People's Commissars for approval; controlling the execution of the republican budgets. It submits to the Council of People's Commissars its recommendations relative to the financial plans of the various departments and institutions, as well as relative to the *credit plans of the State Bank* and supervises their fulfillment. It guides the work of the long-term banks; guides the savings banks system, and the system of state insurance. It maintains control and supervision over the activities of the State Bank and its branches; approves the rules and regulations pertaining to the credit and settlement operations of the bank (except those which are confirmed by the Council of People's Commissars); examines the reports and statements of the bank and submits to the Council last mentioned, its findings. It also formulates the rules governing the fulfillment by the branches of the State Bank of the state and local budgets, and examines them to that effect. See *Economic Life,* June 1, 1936.

inations (1, 2, 3, 5, 10, 25, and 50 chervontzy) of notes issued by the bank, and the security behind them, as well as the security behind notes issued for the purpose of extending loans to the treasury.[20]

The old declaration, that the date upon which the convertibility of banknotes into gold was to begin is to be fixed by a special regulation of the Council of People's Commissars of the U.S.S.R., was incorporated also in the new statutes (Article 20).

The section on the issue of banknotes also deals with the Issue Department of the bank, which supervises the issue of notes into circulation and their withdrawal and which scrutinizes the security offered by the bank (Article 22).

Finally, it deals with the Council on Note Issue, a body which is presided over by the chairman of the bank's Board of Directors, and which evaluates the recommendations of the Issue Department with respect to the security offered, etc. It also ratifies the statements of the Issue Department, inspects the vaults, and exercises general supervision over the issue into circulation and the withdrawal therefrom of banknotes (Articles 23 and 24).

Administration and management of the bank.—Under the old statutes general guidance of the policy of the bank was vested in the Commissar of Finance, and the management of its affairs, in the hands of a Board of Directors.[21] Under the new regulations the administration was divided between a Council and a Board of Directors (Article 50).

The Council exercises general guidance of the policy of the bank; ratifies important decisions; decides on the opening or closing of branches; nominates members of the Board of Directors and submits a list of them to the Commissar of Finance for approval; fixes the limits of unsecured specific-purpose credits, of overdrafts and current accounts; in exceptional cases approves credits in the form of guarantees and acceptances for terms longer than a year, and so forth (Article 52).

The Council is composed of the following: the Chairman (the

[20] See Chapter VII.

[21] See footnote 19, *supra*, relative to the control of the bank by the Commissariat of Finance.

People's Commissar of Finance of the U.S.S.R.), and members. Among the latter are included the chairmen of the boards of the State Bank, Prombank, Agricultural Bank, Tzekombank, Vneshtorgbank, and Vsekobank; persons appointed by the Council of People's Commissars upon the recommendations of the following administrative bodies and organizations, three from the Commissariat of Finance, one from the savings banks, one from the Board of State Insurance, one each from the People's Commissariats of Workers' and Peasants' Inspection, Heavy Industry, Light Industry, Supplies, Foreign Trade, Means of Communication, Waterways Transport, Agriculture, Grain and Livestock State Farms, Central Administration of Roads and Auto Transport, Central Administration of Civil Aviation, Centrosoyuz, Co-operative Industrial Council, Co-operative Industrial Forestry Union, the All-Union Central Trades' Union Council, and, finally, one representative from each of the affiliated republics, appointed by the latter (Article 51).[22]

The Board of Directors retained the functions which were specified in the old statutes and continued as an executive body to conduct and manage the business of the bank (Article 56). Its members (not less than seven), as has been explained, are nominated by the Council of the bank and are appointed by the Commissar of Finance. Its chairman and vice-chairman are appointed by the Council of the People's Commissars of the U.S.S.R. (Article 55).

Branches.—The bank has republic and regional offices, offices in large commercial and industrial centers, branches, agencies and sub-agencies (Article 61).

Operations.—To accomplish the purposes set forth in Article One, the State Bank was permitted to carry on the following operations (Article 25):

(a) To buy and to sell for its own account gold and other precious metals, foreign currency and exchange

(b) To discount commercial paper and also other time, non-interest-bearing obligations

[22] Article 51 was somewhat revised in 1933 and is given here in its revised form. *Collected Decrees,* 1933, Decree 250.

(c) To grant time loans and to open credit in the form of "on-call" (demand) overdrafts and current accounts

(d) To grant credit against commercial documents

(e) To grant special-purpose loans

(f) To guarantee payments at home or abroad, and to accept bills of exchange payable abroad

(g) To accept the following deposits: (1) current, (2) demand, (3) time [23]

(h) To obtain credit abroad, in particular, by means of rediscounts, issuance of commercial paper, as well as by rehypothecation of property hypothecated with the bank

(i) To make and to receive payments on behalf of others, to make transfers, etc.

(j) To effect settlements between clients upon their request

(k) To receive subscriptions for state bonds as well as for other approved bonds

(l) To buy and to sell securities on its own behalf and for others

(m) To buy and to sell on account of others gold and other precious metals, foreign currency and exchange

(n) To receive for safekeeping securities and precious metals; also to receive securities for safekeeping and management

(o) To receive goods for storage in warehouses and to rent vaults and safes

(p) To engage in other operations when permitted by the Council of the bank

To be eligible for discount, commercial paper had to have the signatures of not less than two persons. Its maturity could not exceed six months from the day on which it was offered for discount, except that in cases where such paper arose out of trade with remote localities a nine-months' maturity, and, if those remote localities were in the Asiatic part of the U.S.S.R., an eighteen-months' maturity, could be permitted (Article 26).

Special-purpose ("earmarked") credits and credits in the form of acceptances and guarantees were permitted for a term not to exceed one year (Articles 29 and 31). Credits in the form of time loans, overdraft accounts, current accounts, acceptances, guarantees, and the like, had to be secured by one of the following:

[23] The difference between *current* and *demand* deposits is that current deposits may be made from time to time and withdrawals of a part or of the entire balance may be made at any time, whereas in the case of the latter a *single* deposit is made which may be withdrawn at any time but only in its entirety. Time deposits are deposits left for stated periods.

government or other bonds, foreign or domestic, precious metals, foreign exchange, commodities, or commercial documents. Credits in the form of overdraft accounts and current accounts could also be secured by promissory notes or other obligations, and if granted within limits set by the Council, a single-name promissory note of the borrower sufficed (Article 27).

As will be seen presently, however, the Credit Reform of 1930 wrought fundamental changes in the credit operations of the bank.

The Credit Reform of 1930

Background.—The re-establishment in Soviet Russia during the early days of the New Economic Policy of a credit system along capitalistic patterns was being accompanied by a reintroduction of many of the capitalistic credit practices, particularly with respect to the methods and forms. As has been previously shown, Soviet banks were granting short-term credit against commodities, commercial documents, and commercial paper as securities. Each borrower had as many accounts in his bank as the number of types of security that he offered.[24] Of all the short-term credit operations performed by Soviet banks, those involving commercial paper with two or more names constituted the bulk.[25] Commercial paper, however, was used not only in connection with bank credit but also in connection with *manufacturing and mercantile credit.*[26] The latter played an important part. When a trust (composed of a number of producing enterprises) transferred its manufactured goods to a syndicate (which marketed the former's product and

[24] See V. S. Korobkov, *Settlements of Commercial Transactions without the Employment of Cash* (Moscow, Press of People's Commissariats of Trade of the U.S.S.R. and R.S.F.S.R., 1930), pp. 17, 18.

[25] The reports of the various banks seem to indicate that beginning with October 1, 1927, there was a relative diminution in the volume of operations involving commercial paper. These figures, however, are powerless to show the real weight of such operations, since the banks, following the instructions of the Commissariat of Finance, began in October, 1927, to group all credits granted for a certain specific purpose among "special-purpose (earmarked) credits," irrespective of whether they were secured by commodities, commercial paper, or anything else. See I. Averbakh, "Bank Operations Involving Commercial Paper," *Vestnik Finansov*, 1929, pp. 96 ff.

[26] Manufacturing and mercantile credit is used here in the sense of credit granted by producing or mercantile establishments as distinguished from credit granted by a bank or banks.

bought raw material for it), or when a syndicate sold the product to another syndicate or to the Centrosoyuz (central buying agency for the co-operatives), or, finally, when the Centrosoyuz sold it in its turn to a co-operative organization, manufacturing and mercantile credit was being granted by the seller against the written promise of the buyer to make payment so many months later. The commercial paper so obtained by the seller would be turned over to a bank in exchange for *bank credit.*

The national economy was, thus, being supplied with two streams of credit: one flowing from the bank, and another from industrial and mercantile organizations. The latter stream in fact was itself being fed largely by bank credit. The above method, it can be seen, is in no way different from the method employed in capitalist countries.

It was inevitable that the Soviet Union should in time turn away from this method of credit granting, not only because of the odium attached in the country to capitalist institutions and procedure but also for another very important reason, namely, that indirect credit granting was likely to complicate and hinder the scientific planning of credit. Indeed, with the deepening of economic planning, particularly after the adoption of the First Five-Year Plan, attention began to be centered upon this problem. At first the bank attempted to solve it by introducing "control" over the drawer of commercial paper. This it did by establishing for each of its clients a "limit" to the aggregate amount of paper that the latter could draw and issue within a certain period of time. The bank maintained in its files a record of the paper so issued. Still this cumbersome palliative did not eliminate the method of indirect credit granting. In consequence there developed considerable discussion, particularly under the auspices of the State Bank, centering around the question of the ineptness of indirect credit in the Soviet Union. The directorate of the bank discussed this question on a number of occasions and finally, on April 20, 1929, formed a special commission (under the chairmanship of one of its members, A. I. Morin) to make a more detailed study. On June 18–22, 1929, the special commission presented its recommendations at a conference of the bank's branch

managers. These recommendations, save for minor corrections and changes, were indorsed by the conference, as well as by the directorate of the bank.[27] In substance the bank proposed that the national economy be supplied with but one stream of credit, *bank credit,* and that the second stream of credit, flowing from the industrial and mercantile organizations, be stemmed and eliminated. The bank credit, according to the projected scheme, was to be granted to the *buyer* rather than to the seller.

If, for instance, enterprise B (a selling agency) buys goods from enterprise A (a manufacturer), bank credit is to be given to B, and the settlement between A and B takes place at once. A, it will be observed, under this scheme, is deprived of the right to sell to B on credit (whether in the form of "open book account," against commercial paper, or in any other way). It follows from this that B must not give promissory notes (or give its acceptance to a bill of exchange) to A and that the bank will not, except in certain special cases, grant the seller any credit against paper given by a buyer.[28]

Let us, however, continue our illustration. Most likely A (the manufacturer) borrowed from the bank at a previous period in order to pay for the raw materials, to meet the payroll while the goods were in process of being manufactured, and so forth. If so, A is now in a position to pay off the indebtedness to the bank.

Let it be further assumed that B (the selling agency) sells the goods to C (the *Centrosoyuz*). Again, the terms of the sale are "cash"; C obtains credit at the bank and pays off B. B, in turn, is now able to pay off its indebtedness to the bank. A similar procedure is followed when C sells the goods to D (one of the links of the co-operative system, e.g., the "regional union"), and D to others until the goods reach the stores from which they are sold to consumers. The "storekeepers," the last link in the distribu-

[27] See A. I. Morin, G. L. Piatakov, V. V. Sher, G. L. Piatakov, ed., *The Reform of Credit* (Moscow, State Financial Press, 1929), *passim.*

[28] It was not proposed that commercial paper *per se* be abolished. The bank, for instance, did not propose to discontinue the granting of *bank* credit against the borrower's own single-name promissory note. Nor was it proposed to forbid the sale of goods against commercial paper in the *private sector* (including foreign trade). The proposed reform covered only the socialized sector. See the "theses" of the directorate of the bank.—*Ibid.,* pp. 65-78.

tion chain, pay off their indebtedness to the bank with the proceeds from the sale of goods to consumers.[29]

It will be noticed that under this method, *credit follows the goods.* It is for that reason that it was referred to by some as the "conveyor method" of credit. Complete adherence to the principle that bank credit must be granted in no other way than *direct* to the enterprise needing it, the bank contended, demands that the functions of syndicates be restricted to planning, organizing the sales of the finished product, as well as buying for the trusts raw and other auxiliary materials. Their rôle as credit intermediaries must be definitely ended, and all settlements between them and the trusts are to take the form of cash settlements effected through the medium of the bank (as in the case of any other enterprises).[30]

The bank further proposed to open for each enterprise a single *conto corrento* (or "current account") in which would be concentrated the enterprise's own funds as well as its borrowed funds, and which could be debited with the sums due to other enterprises and credited with the sums due it.[31]

The bank's spokesmen claimed (and not without reason) that if adopted, the plan would eliminate the multiplicity of commercial instruments of credit against the same goods; the pyramiding of credit, and the consequent demand for more credit than was actually needed by the economy; the giving of accommodation paper, a practice that at times bordered on criminality; and the expense of handling commercial paper.[32] Above all, the elimina-

[29] As will be seen later, in actual practice (after the Reform had been enacted into law) the ideal pattern was not followed.

[30] Under the method which was followed at the time, the syndicates and the large co-operative centers used to borrow credit at the bank and reloan it to the enterprises composing them. They were thus performing banking functions and it looked as though trade and industry succeeded in their attempt to force the bank into the position of a "bankers' bank." This did not suit the bank, principally because it interfered with credit-planning. See K. Lupandin, *Problems of Bank Credit in the U.S.S.R.* (Moscow, State Finance Press, 1930), pp. 69-74.

[31] The Russian term "Kontokorrent" is derived from the Italian "conto corrento" or current account, and is not to be confused with the type of "current account" (a deposit account) described in footnote 23, p. 344.

[32] According to the computations of the Centrosoyuz the total cost attached to the handling of one note amounted to two rubles.—G. L. Piatakov, ed. *The Reform of Credit,* p. 11.

tion of all *indirectness* in credit granting and the concentration in the hands of the bank of a *real* monopoly of short-term credit would serve to make the country's credit transactions clear and transparent and so facilitate credit-planning and control over the direction and use of resources.

Preliminary steps.—The projected plan for a credit reform became the center of a heated discussion. As might be expected, it had not only proponents but also opponents. Among the proponents, besides the State Bank, was the People's Commissariat of Workers' and Peasants' Inspection; among the opponents, the Supreme Council of National Economy and the business enterprises.[33] The law-making machine, although taking heed of the issue, moved rather cautiously. As late as November 18, 1929, the Council of People's Commissars published a regulation concerning "the giving of commercial paper and the forbidding of making any advance payments in the socialized sector of the national economy." [34] By its terms the government restricted the employment of commercial paper to actual trade transactions, loans, and the giving of security. It also forbade the granting of money loans by one enterprise to another, as well as the making of advance payments, and the giving of deposits. There was no attempt whatsoever in that piece of legislation to outlaw "seller-to-buyer credit" or "buyer-to-seller commercial paper," but only to purge away some of the undesirable features of the old methods. True, by another regulation of the same date the government sought to eliminate the buyer-to-seller commercial paper and to substitute in its stead a clearing of claims between enterprises by means of *conto corrento* accounts (on their books).[35]

Meanwhile the point of view maintained by the State Bank and the Commissariat of Workers' and Peasants' Inspection was gaining ground. On December 5, 1929, the government published a regulation concerning the reorganization of industry.[36] The

[33] Lupandin, *op. cit.*, p. 51.

[34] *Collected Decrees*, 1929, Decree 694.

[35] An unpublished regulation. See A. O. Schwartzman, *Legislation on the Credit Reform: a Systematic Collection of Legislative and Departmental Material on the Credit Reform and Commentary* (Moscow, State Finance Press of the U.S.S.R., 1931), p. 31.

[36] *Ibid*, pp. 24-30.

principal feature of the reorganization was the grouping of factories and trusts of a given branch of industry into a combination (*obedinenie*).[37] The combinations took the place of the former syndicates. It was not, however, a mere change of terminology. The functions of the new organization became considerably widened and included planning production for the factories and trusts comprising it, planning and directing their capital construction, rendering them technical guidance, organizing the sale of commodities and the supply of raw material, directing their commercial and financial activities, taking up labor problems, training and distributing workers, and appointing and discharging the heads of the constituent units. Furthermore, the combinations were placed directly under the Supreme Council of National Economy and the so-called "main departments" (*glavki*) of the latter body, each of which exercised control over a specific industry, were abolished as superfluous.

The principal aim of the reorganization was the further strengthening of the principles of planning and of business management in industry. Now, it will be recalled that the proponents of a "credit reform" also had better planning as their aim. Indeed, there was a close connection between these two ideas. It is not surprising, therefore, that on January 30, 1930, the Central Executive Committee and the Council of People's Commissars of the

[37] Three types of combinations were created: (*a*) those embracing factories and trusts of an All-Union significance; (*b*) those embracing factories and trusts not only of an All-Union significance but also of republican and local significance; and finally (*c*) those embracing factories and trusts solely of a republican and local significance. Type *a* was to perform all the functions enumerated in the text above. Type *b* was to perform the same functions with respect to the factories and trusts of an All-Union significance. With respect to its other components, it was to perform the functions of the former syndicates plus planning production and capital construction, rendering technical guidance in connection with rationalization and reconstruction, as well as directing the training of the personnel. Type *c* was to perform syndicate functions, plus inter-republican planning of production and capital construction, and supervising rationalization and particularly technical reconstruction. The combinations were to have their own balance sheets, on the assets side of which were to be shown the resources of the factories and trusts composing them. The difference between the selling price and the cost of goods sold shows the profit of a combination (the combination buys the commodities from its constituent factories at cost of production). The trusts were ordered to concentrate their activities upon problems of technical guidance, rationalization, and reconstruction. As a rule they were deprived of the right to sell and to buy. See *Pravda,* December 14, 1929.

U.S.S.R. enacted into law the above-stated recommendations for a credit reform.[38]

The Act of January 30, 1930.—The reasons for, and the gist of, the Credit Reform are given in an introductory statement to the Act of January 30, 1930:

> The rapid development of socialistic beginnings in the national economy of the U.S.S.R. and the attained level of its planning necessitate a fundamental credit reform. The present system of selling goods on credit, as used in the socialized sector, hinders the flow of credit and makes difficult its planning. Its place must be taken by a system under which no other credit than that granted by a bank directly to the enterprise needing it is used.
>
> At the same time the successful results of the reorganization of the credit system in 1927 and 1928 serve as a basis for the taking of further steps towards concentrating short-term crediting in the State Bank.

Accordingly, all state and co-operative organizations as well as "mixed" joint-stock companies in which foreign capital was not invested, that is, all enterprises of the socialized sector, were forbidden to sell to one another goods or services on credit, or to make to one another advance payments or to give deposits without special permission from the State Bank.[39] Bank credit was declared to be the only credit permitted in the socialized sector. The act, as can be seen, followed very closely the proposed suggestions for a credit reform.

The following procedure was to be followed in connection with the granting of bank credit: the various combinations and trusts were to draw up, within the limits of the general credit plan agreed upon between the Supreme Council of National Economy (to which they were subordinated) and the State Bank, credit plans covering their own operations as well as those of their constituent enterprises. On the basis of these plans the State Bank,

[38] *Collected Decrees*, 1930, Decree 98.

[39] Writers outside of the Soviet Union sometimes speak of the "abolition of bills of exchange" in the latter country. Such statements must be qualified. The Act of 1930 did not abolish or prohibit the use of commercial paper in general. *Buyers'* paper alone was outlawed and then only in the socialized sector. Besides, the Russian word *veksel* denotes not only a bill of exchange but a promissory note as well. It was the promissory note, and not the bill of exchange proper that had circulated widely in Czarist and Soviet Russia. The bill of exchange was but little used.

through its branches, was to grant credit directly to the enterprises composing the combinations and trusts.

Another significant provision of the Credit Reform Act was that dealing with the liquidation of the branches of the two central co-operative banks, the Vsekobank and the Ukrainbank. Inasmuch as without the branches they could not continue their short-term credit business (covering the fields of consumers', housing, invalids', and, in part, producers' co-operatives, as well as the trade unions) the latter was taken over by the State Bank.[40]

The short-term agricultural credit business, it will be recalled, was transferred to the State Bank in 1928, with the understanding that the latter was to carry on that business through the medium of the lower links of the agricultural credit system. The Credit Reform Act of 1930 provided for a direct contact between the State Bank and the lower links of the agricultural credit system. By its terms the agricultural credit associations were directed to serve as correspondents for the State Bank.[41]

Together with the short-term credit business of the Prombank (and of the defunct Electrobank) which was transferred to it earlier, the State Bank may be said to have come, as a result of this legislation, into control of some nine-tenths of the total short-term credit of the country.[42] The Soviet Union thus made a big step towards one of its cherished aims, that of creating a *single* bank in which would be concentrated the monopoly of all credit functions and which would serve as the bookkeeping apparatus for the entire country. Such orientation called, of course, for the

[40] See Kaktyn, *Basic Problems of the Credit Reform*, pp. 7-8. The Vsekobank and the Ukrainbank continued as long-term credit banks, transacting their business through the branches of the State Bank.

[41] The act also provided for a reorganization of the Central Agricultural Bank as an All-Union Agricultural Co-operative-Collective Bank.

[42] The Vneshtorgbank (the Bank for Foreign Trade), as we have seen, had been deprived of the right to extend short-term credit in connection with the production of exports within the country, and of the marketing of imports. The Tzekombank (Central Municipal Bank), too, was deprived of the right to engage in short-term credit business. Thus, there remained only the municipal banks (of which there were some fifty or sixty, counting also the branches), which continued to serve as depositaries for the funds of the local budgets, local trade unions, certain types of co-operatives (housing, invalids', etc.) and in part, local industries, and which used these funds for the purpose of extending short-term credit to its depositors.—Kaktyn, *op. cit.*

transfer to the State Bank not only of all the short-term, but also of all the long-term, credit operations of the country. Attempts to transfer to the State Bank the latter type of credit operations were by no means lacking. On December 5, 1930, for instance, the Central Executive Committee and the Council of People's Commissars of the U.S.S.R. ordered that beginning with January 1, 1931, all long-term agricultural credit operations, theretofore performed by the agricultural credit system, become transferred to the State Bank, and that the newly organized All-Union Agricultural Co-operative-Collective Bank with all of its branches, together with the agricultural credit societies, terminate their existence.[43] There was also a recommendation made by the Supreme Council of National Economy that the Prombank be liquidated and that all long-term crediting of industry become concentrated in the State Bank. This latter project did not materialize, however. In part, this was due to the fact that the steadily increasing flow of capital investments into all branches of the national economy served to enhance the usefulness of the long-term credit institutions as supervisors and controllers of the expenditure of funds turned over to economic enterprises in the form of loans or as subventions (on behalf of the government); [44] largely, however, it was because the work of the State Bank during those years was anything but satisfactory and the management of the bank was under fire of merciless criticism. And as a result, by the Act of May 5, 1932, the long-term investment banks were reorganized. The long-term agricultural credit business of the State Bank was transferred to the newly created Bank for the Financing of Socialist Agriculture, and long-term investment banks were authorized to open branches of their own.[45] The reconstituting of the investment banks and the transfer to them of certain functions performed by the State Bank did not, however, in any way diminish the importance of the latter, even though it did postpone the day when it would become the only

[43] Provision was made for the reorganization of such of the agricultural credit societies as it was found advisable to convert into branches of the State Bank.

[44] Their usefulness as *banks*, nevertheless, kept on diminishing as they began to serve more and more as distributors of budgetary funds.

[45] See Chapter XV.

bank in the country. The State Bank continued as a monopolist of short-term credit, a bank of issue, a fiscal agent, a cashier for the investment banks (paying out to the clients of the latter and for their account the proceeds of long-term loans granted by them or of subventions granted by the state) and, in fact, for the entire national economy.

It has been stated above that in recent years the State Bank was being subjected to strong criticism. As will be presently shown, the dissatisfaction with its work grew out of the faulty application by it of the Credit Reform of 1930.

The Credit Reform in action.—Soon after the passage of the Credit Reform Act, the State Bank opened on its books for each of its clients a single current account (*conto corrento*) which it debited or credited from time to time, depending on the nature of the individual transaction. The actual procedure was somewhat as follows: when enterprise A sold goods to enterprise B, the former would present an invoice to that branch of the bank wherein it had an account, whereupon it would receive *payment* in the form of a credit entry to its *conto corrento*. Inasmuch as the above payment was made by the bank on behalf of B (a *buyer*), the next step, of course, would be to debit the latter's account. At the time this simple and automatic procedure charmed a good many people at home and abroad. Indeed, it looked like a harbinger of the higher phase of socialism, when the bank will serve as an accounting bureau of the nation's economy. Moreover, it was in line with attempts in practically all other branches of the country's economy (such as the rapid "mass collectivization" movement in the villages, suppression of private trade, elimination of mutual-credit societies, and, in general, of all vestiges of the New Economic Policy) to speed up, if necessary by legislative means, the transition to socialism.

The new procedure, however, proved extremely injurious to the entire economy.[46] To begin with, when the seller's account

[46] See Schwartzman, *op. cit.*, pp. 33-34; S. B. Rubinshtein, *Working Capital* (Moscow, State Finance Press, 1933), pp. 3-4; B. I. Levik, *Operating Technique and Accounting of Credit Institutions* (Moscow, State Finance Press, 1933), Pt. 1, pp. 10-15; N. A. Suponev, "Credit at a New Stage," in N. A. Suponev, R. A. Grutman, A. I. Mezhov and V. S. Voevodsky, *Financing and Credit at a New Stage:*

at the bank was being credited, the particular branch of the bank had no means of knowing the state of the buyer's account. The debit to the latter's account, it will be recalled, was made only after the seller's account had been credited. In consequence, the bank in a good many cases debited the accounts of enterprises (or, what is the same, *extended loans* to them) despite the fact that they had already borrowed to the limit of the *line of credit* set for them in the credit plan.[47] By violating an accepted accounting principle —namely, that the bookkeeping entry begin with a *debit item* (in this case, the borrower's account) rather than with a credit item —the bank helped to defeat the credit plan, upon the smooth performance of which so much depended.

Furthermore, by crediting the seller's account and then debiting the buyer's account without first obtaining from the latter a confirmation of its indebtedness, the bank denied the buyer an opportunity to pass on the quality of the goods delivered, the prices charged, and, in general, on whether or not the seller had complied with the terms of the sale. As a result there followed a slackening of interest on the part of the seller in the quality of the goods it sold, and in the cost of their production. Buyers began to complain against unreasonable charges, delivery of goods of a sub-standard quality, disregard of the delivery date, and a number of other abuses. Also, claims and counterclaims choked the mails. Errors multiplied. Red tape lengthened. The clients as well as the bank experienced great difficulty in determining the exact status of their accounts. Because of the automaticity of the book entries and the unpreparedness on the part of the bank to handle all that work, buyers continued to remain for a considerable length of time in the dark with respect to the real cost of the

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in Connection with the Law concerning Working Capital (Moscow, State Press for Economic Literature, 1932), p. 5; K. L., "The Struggle for the Credit Reform," *Financial Problems of a Planned Economy* (Moscow, People's Commissariat of Finance, 1930), No.7/8, pp. 19-29; "The Credit Reform in Action" (questionnaire), *Economic Life*, June 11 and 12, 1930.

[47] The credit "limits" were being exceeded because the enterprises were unable to attain the qualitative indices set for them. In other words, they failed to lower the cost of production or to raise their productivity to the point designated by the Plan. Besides, the *conto corrento* made it impossible to see at a glance whether or not a given enterprise had borrowed to the limit.

goods, materials, and supplies received by them. This, naturally, interfered with the calculations of costs and of selling prices.

Another unsound practice followed by the bank at this time consisted of the following: when a business enterprise sold goods it was allowed to retain out of the proceeds from the sale of these goods no more than an amount equivalent to the *planned* cost of their production. The difference between that and the selling price used to be transferred to the account of the combination of which the enterprise was a constituent part. The bank paid no attention whatsoever to the question of whether or not the business enterprises actually produced at the *planned* cost figures. Now, it so happened that the *actual* cost of production of many enterprises during this period exceeded the planned cost. Inasmuch, however, as they were allowed to retain no more than the *planned* cost, they were bound to operate at a deficit even though the selling price exceeded the actual cost of production. On the other hand, and paradoxically enough, the combinations composed of these business enterprises, because of the above-described "legerdemain" were being credited with "profits" which were never earned, but which were passed on by them to the state budget to be used by the latter to finance capital construction.[48] Naturally, this practice helped to swell the volume of paper money and of bank credit. But how could the business enterprises go on if they were being left with less than their actual cost of production? Who made up the loss? In order to understand this it is necessary to bear in mind the automaticity with which credit was being granted by the bank in those days. The bank did not attempt to ascertain whether or not the borrowers were complying with their production plans, and whether or not commodities were being produced at planned cost. In fact, the bank no longer asked embarrassing questions, demanded no security, and did not scrutinize *individual* transactions. It was not even interested to know whether its credit was being used by the borrower to meet short-term, or, as was not infrequently the case, long-term needs. So long as a particular borrower's indebtedness to the bank did

[48] See "Improving the Practice of the Credit Reform," *The State Bank of the U.S.S.R. Economic Survey* VI, No. 1, January, 1931; also, Schwartzman, *op. cit.*, p. 34.

not exceed the "credit limit" set for him, no inconvenience whatsoever was caused him: the bank automatically satisfied all claims, just and unjust, against him. Once the credit limit was reached the borrower would tell the bank that the fulfillment of its production plan was impossible without extra credit, whereupon the bank would acquiesce and grant additional credit.[49]

Under those circumstances if an enterprise operated at a loss there was nothing for it to worry about, bank credit was sure to cover all of its losses. Meanwhile the bank was sinking its resources into what in reality amounted to non-returnable advances.

The practice described above led, furthermore, to a serious weakening of the incentive to operate efficiently and to earn profits. Indeed, with the State Bank making good all of their current obligations and the Prombank supplying their needs for fixed capital, the business enterprises felt secure and did not exert themselves in the direction of greater effort. Why strive to earn profits when the profits were not retained in the businesss and when the net effect of such exertion would be a smaller "loan" from the State Bank? Here and there managers took an "idealistic" interest in the enterprises entrusted to them. Here and there the socialist incentive proved strong; managers tried their best for the good of the country. But on the whole the results were sadly discouraging.[50] Through all those years the Soviet Union struggled hard to implant business management, better planning, and control. It was confidently hoped that the Credit Reform, by abolishing indirect mercantile credit and concentrating short-term credit in the State Bank, would promote that aim. Instead, however, the results were diametrically opposite: disregard of the principles of business management, unreliable planning, and ineffective control.[51] By requiring that all transactions within the socialized sec-

[49] Since during those years the bank was behind in its work, some time would necessarily pass before it would discover that the borrower was exceeding the credit limit.

[50] See Barun, *The Credit Plan of Combinations and Enterprises* . . . pp. 4-5; also Rubinshtein, *op. cit.*, p. 3.

[51] " . . . Since the time of the introduction of the new method of crediting," states the Council of People's Commissars in its well-known Act of March 20, 1931, "not only was there not attained a strengthening of control by means of the ruble over the fulfillment of production plans and over the accumulation of surpluses by all organizations of the socialized sector, but on the contrary there resulted a violation

tor be settled by entries on the books of the bank, the Credit Reform sought to maintain the volume of notes in circulation at a minimum. Instead, those years turned out to be years of excessive note issue. One must be careful, of course, not to blame the bank for all of the woes which beset the Soviet Union during those years. A rather large portion of these woes was created by forces for which the bank was not responsible. The Five-Year Plan, for example, included "enthusiastic" estimates which probably could not be realized even if the bank's procedure had been scientific and the old incentives had remained in force. For example, once the enterprises were unable to reduce their costs and to raise their productivity to a point considered feasible by the Plan, the fulfillment of the production and credit plans set for them was impossible. In that case, however, operation at a loss and the creation of additional credit (in excess of what was planned) and of note issue could not be avoided, even had there been no Credit Reform. Naturally, if the bank had employed scientific methods, it would have been in a position to detect the weak spots at once and to signalize the danger in time.

"Leftist ideology" as a cause of the difficulties.—A rather interesting question may be posited at this point: how is it possible that the State Bank, which was directed by men familiar with banking practices and which functioned quite normally for a number of years before 1930, could now be guilty of such poor judgment and of such unpardonable errors, errors which even a novice in the banking business would probably avoid?

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of the principles of business management, a slackening of interest in financial work and in financial discipline on the part of the economic units." (*Collected Decrees,* 1931, Decree 166.) A few months later, on June 23, 1931, Stalin declared at a conference of business managers: "Due to the unbusinesslike way of doing things, the principles of business management were completely undermined in a number of our enterprises and economic organizations. It is a fact that in a number of enterprises and organizations they stopped long ago to figure, calculate, and draw up thorough financial statements. It is a fact that in a number of enterprises and organizations such concepts as 'regime of economy,' 'decrease of unproductive expenditures,' 'rationalization of production,' went out of style long ago. Apparently, they figure that the *Gosbank* will provide them with the necessary funds anyway." Quoted in V. Diachenko, *Theory of Money and Credit of the U.S.S.R.* (Moscow, State Finance Press, 1933), pp. 67-68.

Doubtless more than one cause was responsible for this. For one thing, too many tasks were imposed upon the bank over too short a period of time, rendering it somewhat unwieldy. Besides, kaleidoscopic changes are not conducive to the development of scientific methods of operation and control. This happened at a time, too, when the economic life of the country was being leavened with the Five-Year Plan. Furthermore, the bank was face to face not only with the complexities arising from the application of untried bank methods amidst a rapidly changing economic order, but also with those arising as a result of the imperfections of the Five-Year Plan. Finally, one may add to the already formidable list one of the causes named by the Council of People's Commissars, namely, the "wrecking" activities ("vreditelstvo") of class enemies within the employ of the government.[52]

Yet, the very nature of the bank's missteps in 1930–31, and the seemingly calculated connection between them unmistakably point in the direction of a very important cause not mentioned above: the "sharp swing to the left" on the part of the bank officials, a swing, incidentally, for which the bank must not be judged too severely. The orientation of the entire national economy during those years, it will be recalled, was towards a speedy attainment of the higher phase of socialism. The bank re-echoed the general spirit. But how could a "swing to the left" affect the realization of the Credit Reform? In order to understand that, one must apparently get acquainted with the "leftist ideology."

[52] For a detailed account of the wrecking activities, see F. Degtiarev, *About "Vreditelstvo" in the Financial System* (Moscow, State Finance Press, 1931), *passim*; also V. J. Bliakher, *Outline of Theory and Practice of State Credit* (Moscow, 1932), pp. 75-79. Sher, a ranking official of the State Bank, testified in a Soviet court that he and a group of other employees of the bank belonging to the *Menshevik* Party formed in the bank a "cell" having for its purpose "disorganizational activity," "derangement of the monetary circulation," and the like. This, he said, was being accomplished "by an allocation of credits to the various branches of the national economy in a way which was not for the best interests of those branches." A number of obstacles were created, Sher testified, to prevent the realization of the Credit Reform. For example, the instructions with respect to the Reform were sent to the co-operatives by telegraph. They were written out, however, in such a way that it was impossible to understand them. Hence, confusion and delay. Berlatsky, another defendant, testified that the statisticians supplied the State Bank with inaccurate data, and thus made it difficult for it to watch the various economic units, and the state of their indebtedness.

Now, the leftists, in common with all other communists, agreed that in a *communist* society there will be no banks, credit, or money. They showed a great interest, however, in the question of how the abolition of these institutions would be brought about.[53] At least two solutions were possible: (a) these institutions would be discarded as useless when the higher phase of socialism arrived, but not before; (b) the process of their disappearance would be a gradual one and would set in during the transitional period and advance in a measure as the country approached socialism. The "leftists" selected the second solution. They held, as a matter of fact, that the process of the disappearance of these institutions was already well under way. Since the practical abandonment of the New Economic Policy by the end of 1928 and the inauguration of the First Five-Year Plan constituted gigantic steps towards socialism, it therefore followed, according to them, that banks, credit, and money in the Soviet Union had already undergone a very important metamorphosis, that the State Bank was no longer a bank in the real sense of the word, that "credit" was an anomaly, and so forth. The discussion to which this gave rise centered about the problem as to what were the *nature* and the *rôle* of these institutions during the "transitional" period. One well-known Soviet economist, Trakhtenberg,[54] for instance, declared that the *exchange of commodities for money* (as against the socialist scheme of distribution) and the employment of *credit* in the Soviet Union were due to the coexistence there of socialized and non-socialized economies. He further declared that the presence of money, credit, and other capitalistic institutions in the socialized sector was due to the fact that the latter, when dealing with the non-socialized sector (to which all of these capitalistic characteristics were peculiar) did not act as a unified, isolated system. The Soviet bank, according to him, could be regarded as a *bank* only

[53] The program of the Communist Party states that "according as a planned social economy is being organized it will lead to the abolition of the bank and to its conversion into a central bookkeeping apparatus of the communist society."

[54] "Credit in the System of Soviet Economy," an appendix to his book *Contemporary Credit and Its Organization* (Moscow, 1929), pp. 285 ff. For a critical analysis of this and other points of view on the question of the nature and rôle of Soviet banks and credit, see V. Diachenko, *op. cit.*, pp. 92-107.

to the extent that it faced the non-socialized sector. In so far as it faced the socialized sector, it was an *institution for social accounting and control.* The existence of *credit* in the Soviet economy was merely a reflection of the existence of capitalistic elements in that economy. The spread of socialistic elements was to be attended by a corresponding spread of the *budgetary* method as a means for providing the economic units with needed funds. Plainly, the process of liquidation of banks, credit, and money sets in during the transitional period and progresses in a measure as the non-socialized sector is being liquidated.

Another writer, Shanin,[55] opposing Trakhtenberg's view that the presence of credit, money, and other capitalistic elements in the socialized sector during the transitional period was due to the capitalistic surroundings of the non-socialized sector, brought forth a different explanation. According to him, when the country found it necessary to adopt the New Economic Policy, the various capitalistic institutions, such as markets, banks, money, and the like, were needed to bind together the socialized and the non-socialized sectors. They were not needed, however, in the socialized sector. That they were introduced into it was to be regretted, for they caused it to become organizationally and technically weak. But as the socialized sector is being "strengthened" by the purging of the Nep elements still residing therein, banks and credit there will lose their capitalistic nature, *even though the capitalistic surroundings of the non-socialized sector survive.* There is, it will be noted, a rather significant difference between the implications that follow from Trakhtenberg's theory and those that follow from Shanin's. Trakhtenberg's theory seemed to lend encouragement to those who were eager to hasten the elimination of the non-socialized sector, while Shanin's seemed to give "aid and comfort" to those who were in no hurry to eliminate it. So while the former was said by critics to be tainted with "Trotzkyism," the latter was characterized as "right opportunism." [56]

[55] "Prolegomena to the Theory of the Soviet Bank," *Economic Problems* (*Problemy Ekonomiki*), 1929, No. 4/5.

[56] Rylsky, "About One Dangerous Theory," *Economic Problems,* 1930, No. 4/5; also Diachenko, *op. cit.,* pp. 97-99, 102-3.

A third writer, Kozlov, broached the subject of Soviet banks and credit in the following manner: [57] at the beginning of the transition period capitalistic categories are adopted. Gradually, however, those categories undergo a "regeneration," lose their original nature, and, finally, disappear. The process of "regeneration" of credit in the Soviet Union, according to this theory, is influenced by the steady expansion of the socialized sector at the expense of the non-socialized, by the consequent deepening and reinforcement of planning, and by the gradual, but direct, substitution of budgetary methods as means for reallocating the national income, in place of credit methods. Planning and the budget are, therefore, the two ways by means of which the "regeneration" and the complete abolition of credit (and with it of all categories characteristic of a society in which goods are produced for sale) is brought about. It will be recalled that elsewhere in this book it has been said that "planning" was one of the characteristics of Soviet credit. According to Kozlov, however, such a statement is quite incomplete and needs to be qualified as follows: "planning is a method for the *complete abolition of credit.*" [58] Fully planned credit, he says, stops being "credit" even in the transitional period, and is nothing more than a mere reallocation of resources according to a plan. He entirely overlooks the fact that credit, whether planned or not, is by definition an uncompleted transaction which is closed at a later period when the debtor meets his obligation. *Credit* (which, of course, is not to be confused with a reallocation of the national income by means of the budget in the form of *non-returnable grants*) as such never ceases to be credit. It can be *abolished,* of course. But as long as the transactions between the bank and its clients fit the above definition, *credit* is employed.

It is not difficult to see that if those directing the policies of the bank were to draw "inspiration" from the above theories, no matter from which one in particular, the national economy was bound to suffer. Unfortunately for the country, these theories did fall upon the ears of the heads of the bank. Especially, the theory

[57] "The Regeneration of Credit," *Economic Problems,* 1930, No. 2; also Diachenko, *op. cit.,* pp. 99-103.

[58] *Ibid.,* pp. 84-85.

promoted by Kozlov. It proved particularly comforting to those with a "leftist" turn of mind; it provided them with a "theoretical" foundation for their wishes and with a rational justification of their conduct. Indeed, inasmuch as planning by 1930 had covered almost the entire Soviet economy, it followed, according to Kozlov's theory, that the Soviet Union had already left the transitional phase behind and had entered the socialist phase. Therefore, the exchange of goods for money was no longer necessary. Nor was there room for credit or for "business" methods and relations in general. The bank, in the light of that theory, had *ceased* to be a credit institution and had evolved into a *pure* central bookkeeping apparatus as befits the higher phase of socialism. In fact, the "leftists" attempted to bestow upon this central bookkeeping apparatus additional functions theretofore performed by the State Planning Commission, namely, the planning of production and the distribution of the products.[59]

It is very likely that the "leftist" ideology was more responsible for the defeat of the aims of the Credit Reform in 1930–31 than all other causes combined.[60]

Amendatory legislation.—By the middle of 1930, barely a few months after it was put into actual operation (April 1), the country was already fully aware that all was not well with the Credit Reform.[61]

[59] V. Diachenko and A. Levin, "The Marxian-Leninist Teachings on Money, Credit, and Banks during the Transitional Stage," *The Works of the Moscow L. M. Kaganovich Finance-Economic Institute* (Moscow, State Finance Press, 1934), Pt. 1, p. 88.

[60] Compare Malcolm Campbell, "Money, Credit, and Banking," *Red Economics*, Gerhard Dobbert, ed. (New York, Houghton Mifflin Co., 1932), p. 172, who, speaking of the Credit Reform, says: "Slowly and surely, however, the belief is beginning to prevail, that, in this case, the fault lies with the lawmaker. The fact is, the reorganization of the credit system might very well have been carried through to success had it been backed up by expert guidance on the practical side."

It must be remembered, however, that the unsound practices developed by the bank were not mentioned in the Credit Reform Act of January 30, 1930. Nor were they mentioned in the discussions of the heads of the bank or in the "Theses" adopted by them before the passage of the act. On the contrary, the discussions and the "Theses" emphasized sound practices. It was to experts in banking that the government had entrusted the giving of "guidance on the practical side."

[61] See, for example, the letters of the heads of the various branches of industry to *Economic Life* (for June, 1930) in which they complained of the ruinous effect of the Reform.

Acting "on the strength of a report by the People's Commissariat of Workers' and Peasants' Inspection on the results of its investigation of the practical workings of the Reform, and of a report by the bank concerning the course of its realization," the Council of People's Commissars of the U.S.S.R. on August 16, 1930, published a regulation in which, after describing some of the defects, it outlined a number of measures for their correction.[62] Among the defects mentioned at this early stage were: lack of preparation for the Reform on the part of the bank and of its clients, as well as on the part of the regulating agencies; lack of skilled personnel; defective planning on the part of the bank and of its clients; the slowness with which the instructions to place the enterprises of the socialized sector on a commercial footing were being carried into effect; the extreme complexity of settlements between the enterprises; the hostile attitude on the part of industrial leaders towards the Reform, and so forth. As correctives, the Council of People's Commissars ordered strict adherence to credit plans and credit limits, the drawing up by the bank not only of quarterly credit plans but also of monthly cash plans; and steps by the Supreme Council of National Economy and other Commissariats as well as by the co-operative centers to place all enterprises on a commercial basis not later than October 1, 1930. The Council also ordered the bank to take steps to bring the accounts of its clients up to date, and to rationalize and expedite the movement of documents in connection with the loans granted by it. Although the enumerated defects did exist (even if their list was not exhaustive) and the ordered remedies were likely to prove extremely beneficial (even if they did require considerable time for realization), the Council failed at the time to come to grips with the real problem. It, therefore, soon became necessary to legislate anew. This did not come, however, until 1931, when the government passed a number of important acts, which helped to restore the national economy to an orderly functioning. Chief among them were those of January 14, 1931, of March 20, 1931, and of July 23, 1931.

By the Act of January 14, 1931, the Council of People's Com-

[62] *Collected Decrees*, 1930, Decree 504; also Schwartzman, *op. cit.*, pp. 7-11.

missars of the U.S.S.R. ordered that, beginning with April 1, 1931, the bank when transferring credit from the buyer's to the seller's account should begin with a *debit* entry (and not with a *credit entry,* as it was doing during 1930), that is, it should begin with the borrower's (buyer's) *conto corrento.* Furthermore, the borrower's (buyer's) *conto corrento* was to be debited only upon his approval of the seller's invoice or upon his authorization (letter of credit) to make payment for his account. It was not until then that the seller's account was to be credited.[63] This simple change of procedure enabled the buyers to protect themselves against the sharp practices of sellers, and the bank, against the practices of the buyers (borrowers) in drawing against it in excess of the credit limits set for them.[64]

Some two months later, on March 20, 1931, the Council of People's Commissars published a new act in which, after enumerating a number of defects surrounding the Reform as well as causes which led up to those defects, it prescribed additional corrective measures. Among the defects the Council at this time mentioned: [65] (a) the granting of credit by the bank "on the basis of the plan" rather than on the basis of the individual transaction

[63] *Collected Decrees,* 1931, Decree 52. Inasmuch as under the new procedure the seller had to wait some time before receiving payment, the bank was instructed to place at the disposal of enterprises and organizations additional credit covering "sums in transit." The additional credit was to be included in the general "line of credit" at the time when the credit plan was drawn up. It is not uninteresting that originally, when the plans for the Reform were being discussed by the directorate of the bank, strong emphasis was being placed on the *accepted invoice* and the *letter of credit* as instruments to be relied on when transferring credit from one account to another. See, for example, the report of V. V. Sher (who later was denounced as one of the "wreckers") at the Conference of the State Bank branch managers on June 19, 1929, in *The Credit Reform,* p. 17, as well as the "Theses" adopted by the bank.—*Ibid.,* p. 68.

[64] Noteworthy among other provisions of this act are: the formation of special reserves by the bank so as to enable it to handle the demand for credit in excess of the "limits." Another provision of the act affected the transfer of "profits" from business enterprises to their combinations. According to this provision the regular accounts of the combinations were to be credited with but 50 percent of the "profit" (the difference between the selling price and the *planned* cost of production), the other 50 percent was to be carried to a special reserve or "insurance" (*strakhovoi stchot*) account of theirs, and was to be drawn against only after the actual cost of production was established by the monthly reports of the enterprises. By order of the Council of People's Commissars of March 21, 1932, the "insurance" accounts were eliminated and the practice described above was entirely discontinued.

[65] *Collected Decrees,* 1931, Decree 166.

(which, in the opinion of the Council, led to credit automaticity and elimination of conscious control); (b) the failure to introduce the principle of contractual relations into the dealings of buyers and sellers (which, according to the Council, led to the weakening of control by the buyer over the seller in matters of quality, assortment, date of delivery, conditions of settlement, and so forth); (c) the disregard of business management on the part of enterprises and combinations, which, along with the effacement of their profits and of working capital, caused them to lose interest in the financial results of their activity (for example, in the lowering of costs, in the accumulation of profits); (d) the technical unpreparedness on the part of the bank and hence its inability to orientate itself towards the new system, and the extreme (unnecessarily so) complexity of the settlement technique, which prevented it from exercising real "ruble control" over production and distribution.

Among the causes of those defects the Council mentioned unsatisfactory guidance, inadequate preparation for the carrying of the Reform into effect, outright "wrecking" activities on the part of hostile elements, and, finally, the fact that the bank "incorrectly understood" what its real tasks were and attempted to usurp functions for which it was not qualified. Instead of striving to become a clearing (accounting) bureau for the socialized economy and a central state apparatus for the audit of production and distribution of commodities, instead of striving to insure control by "means of the ruble" over the fulfillment by the socialized sector of the various plans and to implant business management within it, the bank, according to the Council, attempted to usurp the functions of planning and of regulating economic processes. The Council, apparently, was explicitly referring here to the "leftist" ideology which caused the executives of the bank to believe that the "Plan" was all-sufficient and to regard such categories as purchase and sale, money, business management, contractual relations, and the like as having outlived their usefulness and as being, therefore, no longer necessary institutions.

With a view to overcoming these defects, the Council in its Act of March 20, 1931, decreed that the mutual relations of state,

economic, and co-operative agencies, in so far as the transfer of goods and the rendition of services were concerned, must be governed by contract. The contract is to indicate the form of settlement. The bank is to grant credit on the basis of these contracts (that is, on the basis of *individual* transactions) in conformity with the credit limits and, in a measure, as the contracts are being actually performed. The bank, according to this act, must under no circumstances absorb the losses of economic units, even though they are in great majority state enterprises.[66] Should any enterprise fail to honor its obligation before the State Bank, the latter, after a preliminary warning, must resort to the following measures: (a) limit or completely stop the withdrawals from the *conto corrento* of the defaulting enterprise; (b) execute a forced sale of the goods and other material values of the defaulter. It was also ordered that all economic organizations prepare and publish within prescribed dates statements of their condition.[67]

But no matter how important the principles enunciated in it and the changes ordered by it were, the Act of March 20, 1931, was powerless to remove all the difficulties created under the Credit Reform. Like the preceding pieces of amendatory legislation, it was incomplete, covering but one phase of the situation. The *conto corrento* and the resulting confusion as to what was owed and what was owned by an enterprise remained unredressed by it. It was soon realized, therefore, that further legislation was needed. Accordingly, a new act was published, this time by the Council of Labor and Defense, on July 23, 1931.[68]

[66] In its Act of June 16, 1931 (*Collected Decrees*, 1931, Decree 282), the Council of Labor and Defense lays down the following ruling: if, as a result of the unfulfillment of the quantitative and qualitative indices of the production and credit plan ("promfinplan"), an enterprise operates at a deficit, and that deficit cannot be met out of the total amount of credit placed at the disposal of the combination heading it, a special permission will have to be obtained from the Council of Labor and Defense before the enterprise in question is given the means wherewith to meet that deficit.

Upon the application of an enterprise for credit in excess of the line (limit) set for it, the agency of which the enterprise is part must immediately launch an investigation into the reasons for the financial "break" (Article 10).

[67] On June 16, 1931, the Council of Labor and Defense published an act in which it clarified and amplified the above provisions as well as those contained in the Act of January 14, 1931.

[68] *Collected Decrees*, 1931, Decree 316, or Schwartzman, *op. cit.*, where all of the legislation pertaining to the Credit Reform is given.

By its terms, the government ordered that all state combinations, trusts, and other economic organizations must become endowed, at the expense of the state budget, with a working capital in an amount sufficient to enable them to carry on, unassisted by bank credit, all their *normal* operations.[69] After they were so endowed with a basic working capital of their own, short-term credit was to be granted to them only for "seasonal" requirements, and in general for the purpose of enabling them to meet *temporary* and *occasional* needs, for which their own working capital did not suffice. The credits granted to them under these circumstances were to take the form of advances for a *specific purpose,* repayable at a *given, fixed* date.

As their normal operations expand, the various state combinations, trusts, and other economic organizations will, of course, require a larger basic working capital. Provision for this must be made annually at the time when the production and financial plans are submitted for approval. The increase either will come out of their own accumulation of profits or else it will be provided by the state or local budgets. When the former is the case, the combinations are required to leave at the disposal of the individual enterprises a part of their profits.

In prescribing the above procedure the government took one more step in the direction of sound banking. It subscribed to the widely accepted principle that a minimum, irreducible, or "fixed" working capital, which is needed by an enterprise to enable it to maintain the regular circulation of current assets, must be raised in the same way as is fixed capital, namely, through permanent investment, or *long-term* borrowing. Indeed, if this rule is not followed, if an enterprise attempts to provide "fixed" working capital, which is needed in its business *at all times,* through short-term loans, its path is bound to be beset with difficulties and sooner or later it is liable to find itself unable to meet its obligations.[70]

[69] Co-operatives were required to build up and replenish their own working capital by means of profit accumulation. See S. B. Rubinshtein, *op. cit.* (Moscow, State Finance Press, 1933), pp. 9-11.

[70] The bank's circular of September 15, 1931, bears testimony to this. It states among other things that "until now almost the entire requirement on the part of

The Act of July 23, 1931, in addition to the provisions pertaining to working capital and short-term borrowing at the State Bank, contained a provision with respect to the *conto corrento*. According to this provision, all funds of an enterprise, whether its own or borrowed, must be shown in a *separate* so-called "settlement" or "clearing" (*rastchotnyi*) account,[71] against which it may draw whenever it chooses. Similarly, all the indebtedness of an enterprise to the bank must be shown in a separate account ("specific purpose time loan account"). Thus, the troublesome *conto corrento* was separated into its two constituent parts, a loan account and a "clearing" (deposit) account. This promised to make the dealings of an enterprise with the bank, and the financial status of the former, more transparent. As a further incentive to business management the above act permitted an enterprise to retain in its possession and for its use all of the savings effected by it in excess of what was called for by its plan.

The reconstitution of the clearing departments.—Under the Credit Reform, it will be recalled, the bank's clients were required to effect all of their payments and disbursements through their *conto corrento*. The State Bank, therefore, proceeded to liquidate its clearing departments by means of which its clients cleared claims against one another.[72]

Since under the new procedure single items, and not net balances (as before), were being settled, the bank became swamped with work, fell behind in its postings and, in consequence, lacked up-to-date information concerning the real balances of its clients' accounts. To lighten the bank's burden, the Council of People's

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business enterprises for working funds was being satisfied by the State Bank, despite the fact that a portion of those funds, by the very nature of production, could not be set free by them, hence bank funds became tied up as non-returnable. In that manner, the bank was becoming an organ for financing rather than crediting [that is, a long-term rather than a short-term credit institution.—Author]."—Schwartzman, *op. cit.*, p. 54.

[71] The former deposit or current account. The State Bank, however, no longer opens deposit or current accounts for *business* enterprises. It does open current accounts for public organizations connected with the budget, trade unions, and so forth. The function of the deposit proper is vested in the savings banks.

[72] *The State Bank of the U.S.S.R. Economic Survey*, V, No. 18, October, 1930.

Commissars in its Act of January 14, 1931, decreed that only claims of 1,000 rubles or more were to be presented to the bank for settlement. A few months later the Council of Labor and Defense in its Act of June 16, 1931, decreed the opening of special departments by the branches of the bank to facilitate the mutual settlement of indebtedness by their clients. Organizations and enterprises, which regularly dealt with one another, were authorized, on the basis of that act, to settle balances at such intervals and according to such a procedure as might be agreed upon by them and the State Bank. Similarly, a combination could arrange for the internal settlement of balances among its constituent enterprises.[73] In accordance with the act, the State Bank on June 20, 1931, issued a circular in which it laid down the rules and regulations pertaining to the formation, operation, and liquidation of Departments of Mutual Clearing (Otdely Vzaimnykh Rastchotov).[74]

The effect of the policies of this period upon the credit work of the bank.—As we have seen, the nature of the amendatory legislation of 1931 was such that it was impossible to put all of it into effect at once. Needless to say, "sound business management" cannot spring up overnight in response to government decrees. Steps, however, were taken in the direction indicated by those decrees. The work of calculating the minima of working capital needed by the various enterprises consumed more time than was originally contemplated and it was not until November, 1931, that the provisions of the Act of July 23, 1931, with respect to this began to be put into effect.[75] In the months that followed, business enterprises became endowed with a working capital of their own. The means by which this was accomplished were those indicated in the regulation of the Council of Labor and Defense of October 29, 1931. First there was redistributed the excess of working capital

[73] To facilitate the work of clearing, certain branches of the economy (e.g., the leather, cotton, and woolen industries) had organized within the last few years special bureaus of mutual clearing.

[74] See the bank's circular, no. 307. Schwartzman, *op. cit.*, pp. 223-31.

[75] See the regulation of October 21, 1931, by the Council of People's Commissars, and by the Central Committee of the Party in *Izvestia* of the C.E.C., October 22, 1931; also the Joint Decision of the Collegium of the Commissariat of Finance and of the Directorate of the State Bank of October 18, 1931, in *Economic Life*, October 21, 1931.

possessed by some enterprises, while the balance, the lion's share, was raised through a *special loan*.[76] Altogether the latter involved the huge total of 5,500,000,000 rubles.[77] The effect that this operation had upon the accounts of the State Bank may be gleaned from the financial statements of the latter. These statements reflect, moreover, other important aspects of the bank's work during that period. Let us, therefore, turn to them (Table 58).

On October 1, 1928, when the First Five-Year Plan was inaugurated, the bank's loans and discounts were in excess of 3,000,000,000 rubles. A year later, on October 1, 1929, these increased to 3,800,000,000 rubles (or by 25.4 percent). The passing of another year, which witnessed the introduction of the Credit Reform as well as the further acceleration (intensification) of the country's industrial march, resulted in an increase of the total short-term indebtedness to 6,100,000,000 rubles. The short-term indebtedness on October 1, 1930, was, therefore, double that of October 1, 1928. The upward march continued. On October 1, 1931, the short-term indebtedness stood at 8,500,000,000 rubles, that is, 5,400,000,000 rubles, or almost 180 percent, above the 1928 level. Three months later, on January 1, 1932, when the regime of the *conto corrento* and much of the unsound banking practice that had been employed in connection with it was already a thing of the past, the short-term indebtedness jumped another 2,000,000,000 rubles, thus reaching the 10,500,000,000-ruble mark. As compared with the October 1, 1928, figure, this represented a 7,500,000,000-ruble (or 244 percent) increase.[78] It will be recalled that under the First Five-Year Plan the short-term indebtedness was supposed to increase during the five-year period of 1928–29 to 1932–33 by no more than 3,375,000,000 rubles, that is by less than half of what it actually did.

The bank's deposits and current accounts at first underwent an increase. Between October 1, 1928, and October 1, 1929, they

[76] S. B. Rubinshtein, *op. cit.*, p. 23.

[77] E. Z. Lande, "Credit and Monetary Circulation between the XVI and XVII Party Conferences," *Economic Life,* January 8, 1934.

[78] It may be that the actual increase was even larger. It will be noticed that the bank's statements for January 1, 1932, and May 1, 1932, contain an item "Other Assets" amounting to 1,147,700,000 and 2,253,100,000 rubles, respectively. Such an item may represent claims (current or past-due) against clients.

TABLE 58

BALANCE SHEETS OF THE STATE BANK OF THE U.S.S.R.

1929–32 [a]

(*In millions of rubles*)

	October 1 1929	*October 1 1930*	*October 1 1931*	*January 1 1932*	*May 1 1932*
Assets					
Cash	76.0	41.7	177.0	208.9	165.4
Gold bullion, coin, precious metals, foreign currency	348.5	560.1	690.5	711.4	729.6
Bonds of the Bank for Long-Term Credit	...	....	....	3,947.8	5,501.9
Government securities	348.7	313.8	....	....	....
Short-term debtors [b]	3,833.7	6,124.8	8,487.8	10,524.6	8,533.7
Special loans to industry and agriculture on account of Com. of Finance	113.9	90.9	56.3	206.4	208.7
Special loans to agriculture	244.6	....	....	1,835.2 [c]	2,094.5 [c]
Other assets	403.8	668.8	619.5	1,147.7	2,253.1
Total assets	5,405.2 [d]	7,800.1	10,031.1	18,582.0	19,486.9

Capital and liabilities					
Capital	250.0	400.0	400.0	400.0	400.0
Reserve fund	99.9	176.3	176.3	176.3	302.3
Special reserves	33.0	....	....	....	....
Undivided profits	50.9	....	589.1	768.1	572.7
Note issue	1,466.3	2,145.5	2,527.2	2,784.4	2,739.8
Currency note account of the Commissariat of Finance (from 1930)	....	1,848.7	2,338.6	2,577.4	2,641.6
Deposits and current accounts	2,028.7	2,079.2	1,921.2	7,077.3	8,135.8
Government funds for special loans	118.9	105.2	74.2	245.5	274.4
Government securities	....	....	95.9	....	....
Commission and interest	307.1	215.2	....	....	....
Treasury moneys for long-term agricultural loans	....	....	....	1,672.7	1,821.4
Offices, branches	25.0	....	756.2	975.0	975.5
Other liabilities	1,025.4	830.0	1,152.4	1,905.3	1,623.4
Total capital and liabilities	5,405.2	7,800.1	10,031.1	18,582.0	19,486.9

[a] *The State Bank of the U.S.S.R. Economic Survey*, IV, No. 35, October 15, 1929; V, No. 18, October, 1930; VI, Nos. 10-11, October–November, 1931; VII, No. 1, January, 1932; VII, Nos. 4-5, April–May, 1932.

[b] Before the Credit Reform of 1930 was introduced, this account was known as "Loans and discounts." It will be recalled that during 1930 and 1931 the "single current accounts" reflected both credit and settlement (clearing) transactions. It was only after the *conto corrento* had been done away with that the debit account "Short-term debtors" began to show pure credit (loan) transactions, and the credit account "Deposits," settlement transactions.

[c] Long-term agricultural loans.

[d] Apparently one of the items is understated by 36,000,000 rubles. As it is the total is 5,369,200,000 and not 5,405,200,000 rubles.

rose from 1,550,000,000 rubles to 2,000,000,000 rubles (30.6 percents). During the troublous years 1930 and 1931 their totals remained almost unchanged, but by January 1, 1932, they leaped to an unprecedented height, 7,100,000,000 rubles, and, a few months later, on May 1, to 8,100,000,000 rubles.

The "Bonds of the Bank for Long-Term Credit" on the assets side of the State Bank's balance sheets of January and May, 1932, served as the medium by which this remarkable metamorphosis was brought about. These bonds were discounted by the State Bank and the latter credited the deposit (settlement) accounts of the various enterprises with the proceeds. As a net result of this bookkeeping transaction, the bank's portfolio became enriched on May 1, 1932, by some 5,500,000,000 rubles of such bonds, and the ever widening gap between its clients' indebtedness and deposits was practically closed. Thus, the short-term indebtedness and the deposits, which on October 1, 1931, stood at 8,500,000,000 and 2,100,000,000 rubles, respectively, were on May 1, 1932 (after having advanced on January 1, 1932, to 10,500,000,000 and 7,100,000,000 rubles, respectively), 8,500,000,000 and 8,100,000,000 rubles, respectively.[79] The business enterprises became endowed with a working capital of their own. The ease and simplicity with which enterprises in deficit were placed financially in a strong position, and the credit machine was enabled to escape unscathed despite the huge losses that it was called upon to finance, were made possible by the highly centralized governmental apparatus.

According to official figures, the State Bank's "frozen" assets (amounts owed it by enterprises in deficit) in 1930–31 amounted to 1,200,000,000 rubles.[80]

[79] Throughout the above discussion reference was being made to "short-term indebtedness" and to "deposits." This needs to be qualified, inasmuch as during the regime of the *conto corrento* in 1930 and 1931, the debit and credit sides of that account, even though labeled in the above statements as "short-term indebtedness" and "deposits," were in reality mixed with claims (whether just or not) of clients for goods and services rendered to one another. The net figures, however, are not available.

[80] M. I. Kalmanovich, "Credit in the Service of Trade Turnover," from a report to the enlarged session of the Directorate of the State Bank, *Economic Life*, January 9, 1934; also E. Z. Lande, *op. cit.*

XIII

THE PRESENT CREDIT AND PLANNING APPARATUS OF THE STATE BANK

The net changes in the bank's credit procedure.—The amendments to the Credit Reform of 1930, although very comprehensive, did not, as was thought by some, destroy the salient features of the Reform itself. The institution of indirect commercial credit, as we have seen, was not revived by the amendatory legislation. And, of course, buyers were not permitted to resume the old practice of giving sellers promissory notes or accepting bills of exchange drawn by the latter against them.[1] Also, short-term credit and all settlement in connection therewith, as contemplated by the Reform, remained concentrated in the hands of the State Bank. It may be pointed out in addition that the rôle of the bank as a clearing center for the entire national economy was in no sense abridged by the amendatory legislation. The latter merely laid to rest any theory that the time had come when the State Bank could cease to be a credit institution and remain only a clearing center. The government made it known that during the transitional stage the bank must continue not only as a clearing center but also as a credit institution.

The bank, as we have seen, grants for its own account only short-term credit. Long-term credit is granted solely on behalf of others and for their account. Its loans fall into two groups: planned and extra-planned or non-planned. The former are loans for which provision is made in the plans of the various business enterprises; conversely, non-planned loans are loans for which provision is not made in the plans of the various business enterprises. The State Bank, however, makes an allowance in its credit plan for such non-planned loans and notifies its branches as to the

[1] In practice, however, a good many Soviet enterprises deviated and still deviate from the procedure outlined for them by the legislators. They manage to escape the surveillance of the State Bank and to become *indebted to one another.* The total of such indebtedness is said to have reached large proportions at the time. See Commissar Grinko's report to the First Session of the Central Executive Committee of the U.S.S.R. of the Seventh Assembly, *Economic Life,* February 9, 1935.

size of the working reserve that each of them should set up.[2] But no matter in which of these two groups the loan falls, it has a definite maturity and is given for a definite purpose. Generally speaking, the upper time limit for a short-term loan in the Soviet Union is six months, except in the case of certain branches of the economy (such as agriculture, forestry, and the like) and of remote localities, where the period may extend to nine months and even a year.

The planned loans can be classified as follows: (a) those granted against *values in transit,*[3] (b) those granted to enable the meeting of seasonal needs for raw materials, supplies, and the like, and, finally, (c) those granted to enable an enterprise to carry on the seasonal processes of production.

For a clearer understanding of the group of loans mentioned first, those against *values in transit,* it is necessary to review the methods employed in the settlement of interurban (or out-of-town) transactions between buyers and sellers.

Three methods of settling debts have been introduced: the *acceptance* method, the *accreditive* method, and the *special account* method. Under the *acceptance* method, which is widely used at present, the seller (or supplier) presents the invoices to his (seller's) bank and the latter forwards them for collection. The buyer, provided the invoice meets with his approval, is required to stamp the invoice "accepted" within the course of three days and to make payment (i.e., authorize his bank to debit his account) within ten days of the receipt of the invoice.[4] The consigned goods are made available to the buyer as soon as he "accepts" the invoice.

[2] See the circular of the State Bank for September 15, 1931, Schwartzman, *Legislation on the Credit Reform,* p. 57; also B. I. Levik, *Operating Technique and Accounting of Credit Institutions,* Pt. 1, p. 23. Past experience and the immediate outlook provide the basis for such estimates.

[3] These are not infrequently placed in a class by themselves, and there is a good reason for that: it is quite impossible to estimate them in advance with any degree of exactitude, for that presupposes a knowledge of the daily shipments of goods over the planned period. See O. J. Efimov, *The Technique of Credit and Cash Planning* (Moscow, State Finance Press, 1933), pp. 3, 11.

[4] See *Economic Life,* August 10, 1935, where the method introduced on August 1, 1935, is described; and *ibid.,* June 4, 1936, where the decree of June 4, 1936, entitled "Changes in the System of Crediting Trade Turnover," is presented.

The *accreditive* method is somewhat similar to the *acceptance* method. Under it the purchaser authorizes the bank to honor the seller's invoices and requests for payment (provided he complies with the terms of the agreement). This method is particularly well adapted to cases where enterprises are under contract to make and receive periodic deliveries of goods. Under the *special account* the procedure is the same as under the *accreditive* method. The buyer opens an account at the seller's bank and authorizes the latter to debit it as deliveries are made.

The above methods of settlement give rise to the first type of loans, those against *values in transit.* For example, when the *acceptance* method of settlement is used, the *seller* has to wait some time before the buyer accepts the invoice and authorizes the bank to make payment. The *seller* is, therefore, in need of credit. Hence, a loan against *values in transit.* The request for such a loan must be accompanied by documents evidencing the shipment of goods.

The seller's plan and his agreements with buyers serve as a basis for the rough estimation of the average amounts that will be tied up in transit, as well as of the average length of time that must elapse before the seller's invoices will be honored. Because enterprises cannot estimate in advance with any degree of exactitude the daily shipments, the Main Office of the State Bank sets merely general "limits" for such loans for each of its offices.

When the *accreditive* method is employed, the buyer's account is debited as soon as he instructs the bank to set aside and hold in readiness for the seller a sum sufficient to satisfy the latter's claim. Some time will elapse before the payment is made, but meanwhile a part of the buyer's working capital is, so to say, tied up in transit. Consequently, he needs bank credit. This type of loan, too, comes under the category of *values in transit.*

Inasmuch as the *special account* is but a variation of the *accreditive,* what has been said above about the latter applies equally to the former.[5] So much for loans against *values in transit.*

The second type of loans—loans that are granted for the purpose

[5] The maturity of the loan must not exceed 20 days when the *accreditive* is employed, and 25 days when the *special account* method is used.—Levik, *op. cit.,* p. 25.

of enabling the various economic units to meet the *seasonal* requirements for raw materials, supplies, and the like—are self-explanatory. The Soviet Union, as we have seen, at the present time pays strict adherence to the widely accepted principle that the portion of the working capital which is needed in business throughout the year must be owned by the enterprises themselves, while additional funds which are needed to satisfy peak, seasonal, and occasional production are to be procured by means of short-term bank loans.

The third type of loans essentially resembles the second in that it too is granted for the purpose of satisfying the *seasonal* needs of economic enterprises. It is, however, intended to meet the seasonal increase of productive expenditures of such branches of the economy as agriculture, forestry, fisheries, and so forth, even though these expenditures are often unconnected with the purchase of raw materials. Such loans are governed by the monthly plans (based on the approved quarterly plans) presented to the bank by the borrowers, and are granted either in advance of, or after the consummation of, the expenditures. The production plans of borrowers and their actual performance serve the bank as guides in its attempt to insure a proper utilization of the borrowed funds.[6]

Non-planned loans, as distinguished from the planned loans treated above, are generally granted in the following cases: when the shipment of goods by a producer or seller is hindered by transportation difficulties, embargoes, or failure of buyers to honor invoices; or when the orderly process of production is broken by a failure to receive in time raw materials, supplies, and the like. In each of the above cases the producer or seller is likely to find himself with a stock of goods or supplies (whether finished, semi-finished, or raw materials) in excess of that provided for by his plan. To help him to tide over the difficulties, the bank in such cases, after a thorough investigation, grants him short-term credit. Such loans are granted for a period of time not to exceed 30 days and in an amount not to exceed 90 percent of the planned cost

[6] *Loc. cit.*

of the surplus of finished goods,[7] and 90 percent of the actual cost of the surplus of raw materials, supplies, and the like.

Non-planned loans are also granted when it is desired to expand production beyond the limits set by the plans or to bring about the production of goods for which provision had not been made in the regular plans. It was by means of such loans that an attempt was made in 1932 to meet the shortage of necessities.

The bank considers the goods, materials, and supplies which are produced, purchased, or carried with the aid of the credit granted by it as security for the loans.[8] The borrowers, furthermore, must furnish the bank with details as to the contemplated utilization of the borrowed funds.

Inasmuch as non-planned loans are granted in emergencies, they cannot be estimated in advance with any degree of exactitude.

The paradox: credit expansion accompanied by a qualitative improvement of the credit machine.—Within the space of one year, 1933, the bank's outstanding short-term credit expanded by about 4,000,000,000 rubles, or 40 percent, reaching on November 1, 1933, 14,423,600,000 rubles.[9] The balance of its clients' clearing accounts (which shows principally the balance of the working capital owned by the latter as well as the unused bank credit) on the same day amounted to 3,899,900,000 rubles. The difference between the two foregoing figures, that is, between the figure indi-

[7] Only 75 percent when transportation difficulties are the cause.

[8] See the bank's circular of September 15, 1931, in Schwartzman, *Legislation on the Credit Reform,* pp. 54 ff.; also B. I. Levik, *op. cit.,* which presents a concise but adequate treatment of the subject. It must be pointed out, however, that at the present time the branches of the bank are discouraged from selling goods because of non-payment by buyer for them, or, in general, because loans are not met at maturity. If "absolutely essential" such sale can be made only by special permission in each case by the Chairman of the State Bank's Board (at the Main Office). Furthermore, the request for such permission must be routed by the branch through the regional or territorial office by which it is supervised. See *Economic Life,* July 4, 1934.

[9] Kalmanovich's report to the enlarged session of the Directorate of the State Bank, *op. cit.;* and E. Z. Lande, "Credit and Monetary Circulation, between the XVI and XVII Party Congresses," *Economic Life,* January 8, 1934. The bank's financial statement at the end of 1933 balanced at 25,500,000,000 rubles.—Commissar Grinko's report to the Seventeenth Party Congress (*Economic Life,* January 26, 1934).

cating the total credit outstanding and that indicating the balance in the clearing accounts, therefore, amounted on November 1, 1933, to almost 10,500,000,000 rubles.[10] The latter figure may be regarded as the *net* State Bank short-term credit outstanding on that day. A comparison of this figure with those showing the *net* credit outstanding on earlier dates is not uninteresting. On May 1, 1932, for instance, after billions of credit rubles were poured into the accounts of the bank's clients, lifting them out of "bankruptcy" and the bank out of an embarrassing situation, the net credit outstanding was a mere 397,900,000 rubles. It means that within a year and a half the bank's net credit outstanding increased by more than 10,000,000,000 rubles. The corresponding figure for October 1, 1929, one year after the First Five-Year Plan had been inaugurated, was 1,800,000,000 rubles; for October 1, 1930, 4,000,000,000 rubles, and for October 1, 1931, just before the "Augean stable" of State Bank credit was cleansed, almost 6,600,000,000 rubles. As a result of the cleansing, or, to change the figure of speech, as a result of the transaction (described in Chapter XII), by means of which the bank's clients became endowed with additional capital, the bank's outstanding *net* short-term credit was brought down to 3,400,000,000 rubles on January 1, 1932, and to as low as 397,900,000 rubles on May 1 of the same year. But, as we have already seen, the wave of credit expansion carried the 1933 volume of short-term credit to a new height.

The expansion of the volume of State Bank credit, however, continued. On January 1, 1935, it stood at 17,400,000,000 rubles,

[10] Of the above total net short-term indebtedness the enterprises of the People's Commissariat of Heavy Industry were responsible for 861,400,000 rubles; those of the Commissariat of Light Industry, for 674,200,000; those of the Commissariat of Forestry, for 584,700,000; and the agricultural economy, for 862,100,000. The balance, about 70 percent of the total, had been advanced to enterprises of the People's Commissariat of Supplies, to the Storing Committee of the Council of People's Commissars, and finally to enterprises engaged in trade and commerce. The bulk, as can be seen, had been used for the purpose of facilitating state trade turnover as well as to enable the government to procure the needed raw materials. That so small an amount went to the favored heavy industry need cause no surprise. To begin with, enterprises of that industry received much larger shares in 1931 when the distribution of working capital among the various enterprises of the nation's economy took place, and so needed less short-term credit. Secondly, short-term credit is granted principally in connection with seasonal demands, and a good many enterprises of the heavy industry have no such peaks.—E. Z. Lande, *op. cit.*

and on January 1, 1936, at 26,600,000,000 rubles (an increase of 53 percent).[11] Between January 1, 1933, when it amounted to 10,381,700,000 rubles, and January 1, 1936, the volume of outstanding State Bank credit increased by 156 percent. During the same time the trade turnover increased from 35,504,300,000 to 80,000,000,000 rubles, or by 125 percent.

Despite the rather unusual credit expansion, the quality of the bank's work has experienced a distinct improvement during recent years. It may be recalled that at the end of 1931 the bank's frozen assets amounted to 1,200,000,000 rubles. This amount, together with whatever additional frozen assets the State Bank had accumulated after 1931, were reduced by January 1, 1935, to 480,000,000 rubles. Now, it may be assumed that the simultaneous appreciable shrinkage in its clients' newly acquired working capital played an important part in that connection.[12] But, then, on January 1, 1936, the amount of overdue loans stood at only 280,000,000 rubles, or slightly more than 1 percent of the 26,600,000,000 rubles' credit outstanding on that day.[13]

Particularly noteworthy are the bank's efforts to lift the management and, in general, the efficiency of its clients to a higher plane. How does the bank do it? The following will serve as an illustration. An investigation in 1932 of the Nadejdinsky Works of the Eastern Steel Combination disclosed an accumulation of 12,000 tons of ingots in excess of the quantity specified in its production plan. The excess accumulation was found to have been caused by two factors: (a) production did not run smoothly, and (b) there was a disparity between the capacity of the furnaces and that of the rolling mills.[14] Soviet conditions make it advisable

[11] From the speech of L. E. Mariasin (Chairman of the State Bank's Board) before the Second Session of the Central Executive Committee of the U.S.S.R. of the Seventh Assembly. *Economic Life,* January 20, 1936. The trade turnover during 1935 increased by some 33 percent (from 61,000,000,000 to 80,000,000,000 rubles).

[12] Commissar Grinko, when speaking at the First Session of the C.E.C. of the U.S.S.R. of the Seventh Assembly about the safeguards thrown around the short-term credits of the bank, declared: "We had firmly adhered to this line throughout the year 1932, and not only did not allow the freezing of bank's credits, but compelled enterprises to repay the bank more than 1,000,000,000 rubles of old debts." *Economic Life,* February 9, 1935.

[13] L. E. Mariasin, *loc. cit.*

[14] See E. Mittelman, "Regularization of Business Management, Industry, and the State Bank," *Finance and Socialist Economy* (December, 1932), No. 35/36, pp. 31-32.

that production go on even though the management make mistakes, or even if, as a result of faulty planning of plant construction, there happen to be disparities between the capacities of furnaces, mills, and the like. The State Bank, therefore, not infrequently supplies credit to enterprises even though it is aware of their shortcomings. The bank, however, is charged with the duty of applying its financial control in such a way as to eliminate these shortcomings. In the case cited above, the bank as a result of the investigation ordered its branches to refuse to grant non-planned loans against accumulated inventories to borrowers who were unable to furnish concrete plans for the employment or disposal of such excess materials.[15] Meanwhile, the authorities having jurisdiction over the borrower began taking steps to rectify the faulty construction and so forth.

To take another example: the candy and preserves factories belonging to the "Plodoovosch" were notoriously inaccurate in meeting their obligations to the State Bank. The Tartar office of the latter, on whose territory they operated, in 1935 launched an investigation. It discovered that their inability to meet obligations when due was being caused by their inability to find or to hold buyers. The latter circumstance was found to have been caused by the poor quality of their product, its bad assortment, and high cost. The office undertook to make a special study of this and similar cases, with a view to recommending in each case to the proper authorities measures for the removal of those defects.[16]

These are not isolated cases. They portray a characteristic activity not only of the State Bank, but of the investment institutions as well. Such work on the part of the bank helps, of course, to improve its own position and that of the national economy as a whole.

[15] In the case of *trading* enterprises, the government by its decree of August 16, 1933, specifically provided that no short-term credit was to be given them in the ordinary course of business if they had "immobile" working capital, earned no profits, or failed to fulfill the planned trade turnover.

[16] *Economic Life,* June 6, 1935; also E. M. Greenberg, "How We Struggle With Delays," *ibid.,* July 2, 1934. According to him (he is acting manager of the Mid-Asiatic office of the bank) the bulk of overdue payments is the result of excessive inventories and of losses brought about by poor management.

As has already been intimated, the bank in recent years has not remained unmindful of the fact that the quality of its own work was badly in need of improvement. In fact under the Soviet system, the bank, or for that matter any other organization or enterprise, cannot hide its shortcomings very long. To begin with, there are investigating agencies such as the powerful Soviet Control Commission.[17] Besides, employees and workers in the Soviet Union are encouraged to expose the weaknesses of the organizations and enterprises employing them. Such exposure is accepted as proof of one's communistic zeal and not infrequently leads to reward and promotion. But even apart from this, one does not mind seeing his name in print. The employees and workers are joined in these efforts by the dissatisfied customers and clients of such organizations and enterprises. Hence, a steady flow of this kind of correspondence to the newspapers and periodicals. It brings results. For example, on June 2, 1934, there appeared in *Economic Life* an exposé of some of the methods used by the Semionovsky branch (Ivanovo-Industrial Region) of the State Bank. In that branch chairmen of various collective farms were daily using up time and patience trying to withdraw from their own accounts enough cash to purchase seeds. The bank neither honored their checks as soon as they were presented by them, nor paid out against them as much as they called for. The exposé attracted the attention of the regional office of the bank. It was found that the facts were as represented in the exposé. The branch

[17] The Commission is attached to the Council of People's Commissars of the U.S.S.R., and one of the alternate chairmen of the Council serves as Chairman of this body. It is the duty of this Commission to conduct systematic investigations and examinations to see whether the various Soviet organizations, institutions, and enterprises carry out the state's will. Its central apparatus is composed of a number of groups (such as the chemical group, the financial and accounting group, and so forth). The Commission's financial and accounting group is interested in the activities of the Commissariat of Finance, of the banks, and in those of the Central Management of Economic Accounting of the State Planning Commission. The Plenum of the Commission meets at least once every three months. Between sessions there functions a bureau composed of eleven members. The members of that bureau are approved by the Council of People's Commissars. The Commission may recommend the promotion and reward of those deserving it. On the other hand, it may discipline, demote, or remove the inefficient and the faithless, and, when the cases warrant, turn them over to the courts for prosecution. *Collected Decrees*, 1934, Decree 75.

manager was removed from his post.[18] The Semionovsky branch of the bank, unfortunately, was not the only one to resort to such shortsighted tactics. The collective farm peasants, therefore, preferred to hoard their cash. As a result of an intensive campaign the treatment of peasants by the banks underwent a remarkable change, and the balance of the current accounts of the collective farms at the State Bank rose between January 1, 1935, and January 1, 1936, from 275,000,000 rubles to almost 1,000,000,000 rubles.[19]

Whether as a result of public criticism or because of its own initiative, in one way or another, the bank in recent years has improved its apparatus. That such a thing could be accomplished during a period of rapid credit expansion is not at all surprising, if it is remembered that in the Soviet Union things are not permitted to take their "natural" course, but are steered along certain grooves.

The expansion of the bank's resources.—The bank's towering structure of credit demanded for support a wider base of credit resources. Accordingly, its authorized capital was, by virtue of the decree of the Council of People's Commissars of July 29, 1932, increased from 400,000,000 to 600,000,000 rubles. This increase, though, was brought about by a transfer of the required amount from the bank's own profit account. By the end of 1933 the bank's capital and reserves were in excess of 1,000,000,000 rubles.[20] Thereafter, however, the bank's resources were augmented by a total of 5,346,000,000 rubles. Of this amount 3,046,000,000 rubles came from the surplus budgetary revenue for the year 1933.[21]

[18] *Economic Life,* July 3, 1934.

[19] *Ibid.,* January 17 and 20, 1936.

[20] A. Levin, "The Largest Credit Institute in the World," *Economic Life,* November 7, 1933.

[21] The *estimated* 1933 All-Union budget provided for 35,010,920,000 rubles revenue and for an expenditure of 33,230,920,000 rubles. The *actual* revenue amounted to 40,153,086,822 rubles and the *actual* expenditure to 35,666,551,289 rubles. The First Session of the C.E.C. of the U.S.S.R. of the Seventh Assembly, therefore, resolved that the difference (or surplus), amounting to 4,486,535,533 rubles, be used for the following purposes: 1,440,535,533 rubles for the formation of a state reserve, and 3,046,000,000 rubles for the strengthening of the State Bank's credit resources. The decree to that effect was signed on February 8, 1935. *Collected Decrees,* 1935, Decree 70.

The remainder, 2,300,000,000 rubles, came from the 1935 budget.[22]

Another increase in the resources of the State Bank was made possible by the decree of the Council of People's Commissars of February 29, 1936, relative to the revaluation of the ruble. The bulk of the resulting "profit" apparently, however, went to the treasury.[23]

Interest rates: recent changes.—Towards the end of 1931 the interest rates charged by the State Bank for planned loans and loans against "values in transit" stood at 8 percent; those for extra-planned loans, at 10 percent; and, for overdue loans, 18 percent. In 1934 these rates were changed to 6 percent on planned loans; to 4 percent on loans against "values in transit"; and to 8 percent on extra-planned and overdue loans. At the same time the interest paid by the bank on its clients' balances in the settlement accounts was reduced from 5 to 3 percent, and on balances in their current accounts, from 6 to 3 percent. This, however, did not apply to the current and time deposits made by collective farms. On those the bank, in an attempt to stimulate their growth, paid 8 and 12 percent, respectively.

There followed also a reduction in charges made by the State Bank for various services. From May, 1933, to the end of that year, the bank charged its clients 58,000,000 rubles for services which it performed at a cost of 26,000,000 rubles. During 1934 the bank

[22] The *estimated* revenue of the 1935 All-Union budget was 65,900,551,000 rubles, the *estimated* expenditure, 65,400,551,000 rubles. The 2,300,000,000 ruble item for the strengthening of the bank's credit resources was listed not only among the expenditures but also among the revenue items. In the latter group it was shown as revenue "from a revaluation of the seasonal remainder of raw materials and commodities on January 1, 1935." (*Loc. cit.*) This requires an explanation. Concurrently with the partial abolition of the rationing card system beginning with January 1, 1935 (see Ch. XIV), the prices of such commodities as bread, grain, flour, groats, and macaroni were raised. A number of other commodities too went up in price on the same date, among them cotton, flax, hemp, and tobacco. And so the government on December 23, 1934, ordered the enterprises, organizations, and institutions of the socialized sector to write up the values of their inventories as of January 1, 1935, and retain for themselves as much as was needed to enable them to maintain the prescribed norms of raw materials and supplies on hand (at higher prices). The balance was to be transferred to the State Bank. The 2,300,000,000 rubles which the bank was to get in that manner were to strengthen its resources and enable it to grant credits *at a higher price level. Ibid.*, Decree 11.

[23] See Chapter XIV.

charged 91,000,000 rubles for its services, thus earning a profit of 25,000,000 rubles. In 1935, however, it charged for services no more than their cost (64,000,000 rubles).[24]

Since the government is eager to bring about a lowering of the price level, or, what is the same, a strengthening of the purchasing power of the ruble, it wages a vigorous campaign for the reduction of costs. Interest being one of the items in the cost of production, the government turned its attention upon it. On June 14, 1936, the Council of People's Commissars ordered all banks to lower their interest rates beginning with July 1, 1936. The State Bank's charge for short-term credit was fixed at 4 percent; for loans against "values in transit," at 2 percent; for overdue loans, at 6 percent. The interest to be paid by it on the deposit and settlement accounts of business enterprises, public organizations, state institutions, and local budget funds was fixed at 1.5 percent; on those of savings banks and of collective farms, at 3.5 percent; on balances of the Agricultural Bank, at 3.75 percent; and on those of the Tzekombank, local municipal banks, and of the Vsekobank, at 2 percent.[25] All this despite the increased demand for credit.

The Law of May 25, 1935. The new planning apparatus.—For many years the organizational structure of the bank remained the same despite the various changes in the set-up of the national economy. By order of the Council of People's Commissars of May 25, 1932, however, it underwent an important change.[26] To bring the bank closer to the various branches of the country's economy so that it may better understand and, therefore, better serve their needs, as well as to strengthen financial discipline and exercise greater control, the Council ordered the former to reorganize along departmental lines. Accordingly, at the Main Office of the bank (*pravlenie*), there were formed a number of *departments* (*upravlenia*), each of which exercises supervision with respect to the credit and planning work pertaining to a given branch of the national economy. There are departments for the crediting of

[24] G. Schwartz, "The Strengthening of the Ruble and the Cheapening of Credit," *Economic Life*, June 30, 1936.

[25] *Ibid.*, June 16, 1936.

[26] *Collected Decrees*, 1932, Decree 250; also *Economic Life*, May 28, 1932.

each of the following: heavy industry,[27] light industry, forest industry, consumers' co-operatives and state trade, rural economy, enterprises of the People's Commissariat of Supplies of the U.S.S.R. and of the Storing Committee of the Council of Labor and Defense, ways and means of communication, handicraft co-operatives. In addition to the above, the Main Office has a number of other departments, such as the Foreign Operations Department (a special sector or division of which is in charge of the credit and planning work in connection with foreign operations), the Rationalization and Accounting Department, and the Organizational and Auditing Department.[28]

To achieve greater specialization, the departments for the crediting of the various branches of the economy were subdivided into groups or "sectors," each of which supervises a separate industry. Along with the industrial sectors, there exist, however, within the various departments so-called *general-planning* or consolidating groups (*svodnoplanovye groopy*) that prepare general or consolidated credit plans for the particular branches of the economy (in their entirety) which their departments supervise.

These credit plans are turned over to a special department

[27] It will be noticed that by decree of the C.E.C. and of the Council of People's Commissars of the U.S.S.R. of January 5, 1932, the Supreme Council of National Economy was reorganized as a Commissariat of Heavy Industry. The "light" and "forest" industries were subordinated to two new commissariats, respectively: the Commissariat of Light Industry and the Commissariat of Forest Industry (*Collected Decrees,* 1932, Decree 4). Under the jurisdiction of the Commissariat of Heavy Industry came the following industries: fuel, mining, metallurgy, power stations, power supply, electric, chemicals, silicates, etc. Under that of the Commissariat of Light Industry: textiles, leather, matches, fats, perfumery, etc. Under the Commissariat of Forest Industry: timber, paper. The Commissariat of Supplies, which is mentioned in the above list, had jurisdiction over the following industries: flour-milling, bread, sugar, salt, oil-mills, fish, preserves, wines, alcohol and vodka, tobacco, confectionery, etc. In 1934 the Commissariat of Supplies was divided and reorganized as two separate commissariats: one, of Domestic Trade; another, of Food Industry.

[28] The Rationalization and Accounting Department is charged with the installation and rationalization of accounting and operating technique, the maintenance of proper accounting methods by the entire State Bank system, the control over interbranch accounts, and the preparation of annual financial and credit bank reports. The Organizational and Auditing Department is concerned with organizational problems and with the auditing of the branches. It also drafts the annual total estimates for the State Bank and its branches, and prepares reports showing the administrative and general expenses.—B. I. Levik, *op. cit.,* pp. 7-8.

known as the Economic-Planning Department (Planovo-Ekonomicheskoie Upravlenie), by which they are later presented to the directorate (pravlenie) for approval. It is by means of the Economic-Planning Department that the work of the various departments at the Main Office is co-ordinated. It prepares a consolidated credit plan for the bank as a whole. It issues instructions to the departments and to the offices of the bank with respect to the credit plans. It checks the work of the departments as well as of the entire network to insure adherence to the adopted plans, and, in general, the compliance with the credit and planning policies of the directorate. It also investigates credit, currency, and clearing problems, attempting to find solutions. The Economic-Planning Department is also entrusted with the fixing of the limits for the extra-planned loans by the bank's offices.

We have so far dealt with the planning apparatus at the Main Office. Now, it will be remembered that the Main Office does not engage (save for foreign credit operations) in actual banking operations. That work is done by the bank's branches. The branches, in addition to their regular banking business, carry on credit-planning, and, consequently, have planning apparatuses of their own. Let us, therefore, get a clearer understanding of the branches.

The branches.—The number of the bank's branches, in the years under review, underwent a sharp increase. From somewhat less than 600 on October 1, 1928, their number increased to 615 on October 1, 1930, to 648 on January 1, 1931, and to 2,570 on October 1, 1931. The mild increase before 1931 was due to the administrative reform as a result of which the *counties* (*okrugi*) were abolished and their functions were transferred to smaller and hence more numerous *sections* (*raiony*). The State Bank proceeded to open branches in the newly established *raiony* as well as to augment the number of these in the old localities. The sharp increase during 1931, on the other hand, was due to the transfer at the beginning of 1931 to the State Bank of the function of extending credit to agriculture and the consequent reorganization of the agricultural credit societies (of which there were 2,759 on

January 1, 1931) as branches of the State Bank.[29] Although later (by decree of May 5, 1932) the financing of agriculture was transferred by the State Bank to a newly organized Agricultural Bank, which proceeded to establish a network of its own, the number of the State Bank's branches did not shrink to their pre-1931 status. On January 1, 1934, they numbered 2,200, and on January 1, 1936, 2,800.[30]

The branches can be classified as follows: (1) regional, territorial offices (kraevye, oblastnye kontory), which are directly subordinated to the Main Office and which are located in the main cities of the Union republics, regions, and territories, and of autonomous republics that are not part of the regions and territories; (2) republican offices (respublikanskie kontory) in the main cities of autonomous national republics, and territorial offices (oblastnye kontory) in the main cities of autonomous territories and of territories forming a part of republics and regions (in the Ukraine, Kazakstan, and the Far East); these are subordinated to the regional offices mentioned above; (3) district branches (raionnye otdelenia), which constitute the basic operating links in the State Bank's network, performing all ordinary banking operations; they are subordinated to the offices; (4) agencies (rastchotnye kassy) in the *raiony* where there are no branches; these are directly subordinated either to offices or to branches, and engage in banking operations in a limited sphere; (5) sub-agencies (pripisnye kassy), which are located close to certain combinations and storing points for the purpose of providing them with banking facilities; they are subordinated to the higher units, perform only such functions as the latter delegate to them (generally of a more restricted nature than those of agencies), and carry on no elaborate bookkeeping of their own, inasmuch as their operations are recorded on the books of the units which direct them.[31]

[29] *The State Bank of the U.S.S.R., Economic Survey,* VI, No. 2, February, 1931; also *The National Economy of the U.S.S.R. Statistical Manual for 1932* (Moscow, State Social-Economic Press, 1932), p. 602.

[30] E. Z. Lande, "Credit and Monetary Circulation between the XVI and XVII Party Conferences," Pt. 1, *Economic Life,* January 5, 1934, and January 20, 1936.

[31] Levik, *op. cit.,* pp. 6-7.

The offices carry on a banking business in the cities where they happen to be located, and guide and co-ordinate the activities of the lower units in the bank's network, which are subordinated to them.[32] The operating functions of the office are organizationally separated from those pertaining to the supervising of the subordinated units. The operating apparatus of an office is built along departmental lines with separate *sectors* for the various types of operations.

In addition, the offices carry on planning work embracing their own clientele, and, as has been intimated above, supervise the planning work of the subordinated units.

The planning apparatus of an office is organized along the same lines as that of the Main Office. The various credit-planning units, which engage in the drawing up and the regulating of credit plans pertaining to the particular branches of the economy of which they have charge, are here known, however, as *credit-planning sectors* and not as credit-planning departments. The number of such sectors in an office depends, naturally, upon the economic development of the particular region in which the office is located. The leading branches of a region's economy are each assigned to separate credit-planning sectors, while the weak and little-developed branches are bunched in a common credit-planning sector.

The offices also have general or consolidating planning sectors. The general or consolidating sector of an office prepares a consolidated credit plan of the office as well as of the subordinated units, prepares a consolidated cash receipts and disbursements plan, oversees their fulfillment in the region covered by it, receives reports on the progress of that fulfillment, and studies the region's economy. This sector also maintains a statistical division.

The various sectors of an office are subordinated to its executive head, the manager. Under his supervision they carry out the instructions received from the *credit-planning departments* at the Main Office. Each credit-planning department of the Main Office issues instructions to the corresponding credit-planning sectors of the regional offices governing the drawing up of credit plans

[32] There are forty-two regional offices at present.

for the particular branch of economy over which it has charge.[33] In a like manner they issue regulations with respect to the procedure to be followed when granting credit as well as to the accounting procedure. The managers of the offices, as well as the respective sectors, are held responsible for the proper execution of those orders.

The apparatus of a district branch (raionnoe otdelenie) is of necessity considerably simpler, but here too the departmental principle dominates, and a small number of sectors are maintained. The typical district branch is organized into three sectors: (a) the credit sector, which deals with the "credit limits," with the preparation (on the basis of directions given by the offices) of cash and credit plans, as well as with the evaluation of the material submitted by clients; (b) the bookkeeping sector; and (c) the cash sector, in charge of valuables. Separate functions are entrusted to individual responsible officers, who are grouped into sectors. Some functions, however, such as general office work and administrative work, are performed outside of the sectors. The operating apparatuses of branches located in large industrial cities resemble those of the offices.

The operating apparatus of an agency or sub-agency is very simple indeed, consisting of a group of employees performing the various types of work under the general supervision of an officer in charge.[34]

Planning is carried on even by the small units, which have at least one planning inspector (*inspector planovik*). Units with a large clientele have several such planners even if they do not have a special planning sector.

The planning technique.—As has already been pointed out, all credit institutions in the Soviet Union operate according to plan. The *credit plans* of the State Bank (that is, short-term credit plans) are drawn up on a *quarterly* basis. Although yearly plans are prepared, they are nothing but very rough estimates of the anticipated changes in the volume of credit flowing into the various branches

[33] The Economic-Planning Department passes on those instructions before they are dispatched.

[34] Levik, *op. cit.*

of the economy (and not into separate economic units). Monthly short-term credit plans are not being drawn up.[35]

In addition to a credit plan, the State Bank also draws up *quarterly* and *monthly cash plans* (i.e., cash receipts and disbursements plans). In the case of the cash plan, however, it is the monthly plan that serves as the operating plan. These plans help to regulate the currency circulation and the turnover of cash resources in the tills of economic units, credit institutions, and various organizations. It is not difficult to see that without a cash receipts and disbursements plan the bank could not very well estimate the extent to which loans could be paid off during a given quarter, the demand for loans, and the changes in the balances of clients' clearing and current accounts, and so forth. In short, the two, the credit and cash plans, are closely related.

The plans of the bank are based upon the credit and the financial plans of the various producing, distributing, and service-rendering organizations. Each economic unit having a loan or a clearing account at the bank is required to submit, among other data, an estimate of its credit and cash requirements and of the movement of its clearing account within the next quarter of the year.[36] Similarly, organizations having current accounts at the bank are required to submit estimates as to the anticipated changes in these accounts during the next quarter. The dates upon which the required material must be submitted are fixed.

Whether the material will be submitted to the Main Office, to a regional office, to a branch, or to any other division of the bank depends upon the location of the agency submitting it. For example, enterprises of what is known as *local importance* submit their plans to the local bank unit. Enterprises of an *All-Union* or of a *republican importance* submit their data to a local bank unit only when the headquarters of the combination to which they belong are located outside of Moscow. But then a consolidated plan covering all of the constituent units is submitted by the com-

[35] O. J. Efimov, *The Technique of Credit and Cash Planning* (Moscow, State Finance Press of the U.S.S.R., 1933), *Soviet Credit*, Pt. II, p. 5.

[36] These estimates deal with the amount of credit that the given undertaking will need during the following quarter (and for which it now applies), the purpose for which the credit is wanted, and the dates upon which payments will be made.

bination. If the headquarters of the combination to which the enterprises of an All-Union or republican (R.S.F.S.R.) importance belong are located in Moscow, the plans are submitted directly to the Main Office of the bank. In consequence of this arrangement, the determination of the volume of credit that will have to be placed at the disposal of enterprises of an All-Union and of a republican importance originates in the regional offices and at the Main Office.

Not so with the volume of credit that will have to be placed at the disposal of enterprises of a local importance. Its determination originates with the lower bank units to which these enterprises submit their data. True, the regional offices and the Main Office pass upon and fix the final figures here too, but they do this on the basis of the plans prepared by the lower bank units. The latter, as may be seen, are entrusted with important planning work. Indeed, they pass on such questions as whether the client will be able to pay off the loan at maturity, or whether the client réally needs as much credit as he wants to get during the ensuing quarter, that is whether the client needs as much of the supplies, materials, or goods in order to carry out his *promfinplan* (industrial and financial plan) or, if the client is a trading concern, the *torgfinplan* (commercial and financial plan), as he seems to think he needs. They also have to take into consideration the client's past performance as well as his performance under the current industrial plan.[37]

To be sure, the State Bank system receives regularly from its clients operating and financial reports which enable it to ascertain the progress that is being made by them, and, in general, their financial position. The clients, however, are no longer oppressed by the unreasonableness of the demands on the part of bank officials.[38] The Main Office forbids its branches to demand or receive any material or data other than that prescribed by it. The clients furnish them with copies of the annual reports at the same time that these reports are submitted by them to the organizations of which they form a part, as well as with monthly reports. Special reports

[37] Efimov, *op. cit.*, p. 8.

[38] This used to be the case when the planning apparatus was new.

are rendered (by borrowers) with respect to inventories and to wages paid out.[39] Except in certain special cases, provision for which was made by the Main Office, no other reports are required.

After a study of their clients' estimates and a decision as to the size of credit really needed by them, as well as a study of the anticipated changes in the clearing and current accounts of those of their depositors who do not expect to borrow,[40] the bank units draw up credit plans covering their clientele.[41]

Having completed their work, the lower bank units dispatch the data pertaining to the credit plan to the regional offices to which they are subordinated. The offices check the findings of the lower bank units with respect to enterprises of local importance and append their own conclusions. Inasmuch as they have clients of their own, they must plan (on the basis of materials furnished them by their clients and by the agencies regulating those clients) the credit needs of the latter before a *consolidated* credit plan covering the entire region can be prepared by them.

When completed the consolidated credit plan of the regional office covers all enterprises of that region except, as has already been pointed out, those of an All-Union and of a republican (R.S.F.S.R.) importance with headquarters in *Moscow*. The regional offices send the data pertaining to the quarterly plans to the Main Office. The consolidated credit plan which was mentioned above, together with a plan covering the resources and an explanatory memorandum, go to the Economic-Planning Department, while the plans covering separate branches of the economy (as worked out by the respective planning *sectors*) go to

[39] Efimov, *op. cit.*, p. 66.

[40] The anticipated changes in the balances of clients' clearing accounts are being determined at the same time that their needs for credit are scrutinized, and are shown in the plan separately for each of the clients included in the list. The changes in the current accounts of the Union, republican, and local budgets, as well as of budgetary organizations and of social and professional organizations, are calculated separately on the basis of their cash and financial plans. Special attention is given to the current accounts of the collective peasants, inasmuch as they are the recipients of large amounts of cash. Banks are instructed to come to an understanding with each collective farm separately as to its requirements. *Ibid.*, pp. 17-18. But here again it will be noticed that a miscalculation on the part of the lower bank units as to the future balances of their depositors may result in a demand much heavier than the one planned upon the resources of the bank.

[41] See credit plan forms Nos. 1 and 2 which are used by the State Bank's network.

the corresponding departments (at the Main Office).[42] The plans as submitted by the offices, in addition to containing the estimates of the anticipated "planned" loans, contain also estimates of the needed *reserves* in the respective regions for extra-planned loans, as well as estimates of the anticipated size and movement of loans against *values in transit*. The accuracy of these latter figures naturally depends upon the ability of the offices to foresee the unforeseen. Still, past experience and conversance with the dynamics of the particular branches of the economy help them to arrive at scientific guesses.

The plans drawn up by the sectors of regional offices and covering separate branches of the economy are analyzed by the corresponding departments at the Main Office. The latter append their conclusions with respect to the economy of a local and republican importance, and, upon reaching an agreement with the respective head organizations, determine the volume of credit which will have to be placed during the next quarter of the year at the disposal of organizations of an All-Union importance.

[42] The offices, in fact, submit to the Main Office *separate* estimates and planned balances accompanied by explanatory memoranda for each combination, trust, or autonomous enterprise of an All-Union or R.S.F.S.R. type with headquarters outside Moscow. If the anticipated increase in the indebtedness of such a combination, trust, and enterprise does not exceed 500,000 rubles the offices need not furnish planned balances and explanatory material covering the *constituent* enterprises, and only the total amount for the entire combination need be given in such cases. In some instances the Main Office raises that limit to 1,000,000 rubles. In the case of enterprises of a republican (other than the R.S.F.S.R.), local, or regional importance, the credit estimates of the offices are presented in the form of a total sum and a *general* memorandum is appended justifying the size of the requested credit. In the case of consumers' co-operatives the estimates are given for each *system* separately. In the case of handicraft producers' co-operatives, the estimate presented to the Main Office is in the form of a total figure (covering all systems), although some offices, because of their location, are required to present separate figures on forest and peat co-operatives. The data requisite for the estimates with respect to these producers' co-operatives are obtained from the general economic and planning material of the Union, and the lower bank units present no estimates as to the quarterly credit requirements of the separate *arteli* (associations). Certain branches of the economy, whether on account of their structure, composition, or the necessity for centering upon them special attention, are accorded special treatment. In the case of light industry of local importance, credit estimates, together with planned balances and explanatory memoranda, are furnished for each organization of a limited number of the largest trusts, and so forth.

Prolixity and circumlocution are at present barred from the explanatory memoranda submitted by the offices by the rigid rule of the Main Office that they may not exceed 3 to 4 pages each. Efimov, *op. cit.*, p. 14.

Form No. 1

CREDIT PLAN FOR THE...QUARTER OF 19... [a]
(*In thousands of rubles*)

Clients and Branches of Economy	*Estimated Balance of Indebtedness at the Beginning of the Quarter*	*Change during the Quarter*	*Estimated Balance of Indebtedness at the End of the Quarter*	*Intra-quarterly Excess*	*Dates on Which Payments are Due*			
1	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*

[a] Forms No. 1 and No. 2 are filled out by the various bank units. Form No. 1 deals with the credit requirements of their clientele. It represents an estimate of the movement of their indebtedness to the bank unit, as well as of the dates on which payments fall due. The enterprises are listed in accordance with the prescribed nomenclature (the enterprises of the People's Commissariat of Heavy Industry, e.g., grouped under such subtitles as fuel, mining, metallurgical, electro-technical, and so on, come first; next come those of the Commissariat of Forest Industry, with such groupings as forestry and paper; these are followed by the textile, leather, match, and other enterprises of the Commissariat of Light Industry, and so forth).

As the plans drawn up by the offices begin to pour in, and not infrequently in advance of their receipt, the credit-planning departments of the Main Office busy themselves with the preparation of

Form No. 2

CREDIT PLAN FOR THE.. QUARTER OF 19... [a]
(*In thousands of rubles*)

	Actual Balance on May 1	*Planned Balances*	
		On July 1	*On October 1*
1	*2*	*3*	*4*
1. Clearing accounts (these are listed in accordance with the prescribed nomenclature).....			
2. Current accounts:			
State budget of the republic.....			
Local budget...			
Trade unions			
Budgetary organizations.....			
Collective farms.....			
Others.....			
3. Deposits of credit institutions..... (each listed separately)			

[a] Form No. 2 analyzes the resources of the particular bank unit. It shows the actual balances of the clearing and current accounts as well as of deposit accounts of credit institutions. It will be recalled that "business" enterprises have "clearing" rather than current accounts. In connection with these the same nomenclature is followed as that outlined in the footnote above. The nature of institutions having "current" accounts may be seen from section 2. Only those units which are located in the centers of the constituent republics supply figures pertaining to the republican budget. Form 2, like Form 1, includes data with respect only to those enterprises, organizations, and institutions with which the particular unit happens to deal.

preliminary credit plans covering the separate branches of economy. These they turn out on the basis of estimates furnished them by the separate head organizations and the largest combinations. With the help of these preliminary plans, and also with the aid of available information pertaining to the dynamics of the trade turnover, to the progress made by the national economy with re-

spect to the operating and financial plans (*promfinplans*), as well as with respect to the storing (*zagotovki*) operations, and so on, the consolidating-planning sector of the Economic-Planning Department draws up a preliminary quarterly credit plan for the bank as a whole. In a measure as the credit plans from the regional offices arrive and as the head organizations refine their original estimates, changes are made, and the final credit plan emerges. The final credit plan takes the form of a statement showing the anticipated resources of the bank for the coming quarter of the year and their apportionment among the various branches of the national economy.[43] The bank as a rule appends an enumeration of measures requisite for the successful realization of the plan.

After a preliminary consultation with the respective administrative heads,[44] during which the directorate of the bank (the Main

[43] See Credit Plan Form No. 3. In considering the resources for the next quarter, the bank naturally also determines its policy with respect to note issue during that period.

[44] The various enterprises, it will be recalled, are grouped into combinations and trusts, and these are subordinated to various commissariats or to agencies of the latter (chief administrations). As has been pointed out above, plans of the State Bank depend upon the plans of the national economy. Each combination, or trust, on the basis of the plans submitted to it by its constituent enterprises, draws up a single master plan covering the entire combination or trust. These are then submitted for approval to the respective People's Commissariats of the *U.S.S.R.* (of Heavy Industry; of Light Industry, and so on), if the combinations are of an All-Union importance. If they are of republican importance, their plans are submitted to the respective *Republican* People's Commissariats (or to their agents); and if they are of local importance, then to the agencies or representatives of the commissariats in the district where they are located. On the basis of the material received the district agencies or representatives draw up and send to their headquarters plans covering the local industry within their district. Similarly, the various Republican Commissariats are required to draw up plans of the industries of their republics and submit them to the corresponding *Union* Commissariats.

With the aid of the material received from the Republican Commissariats and that received *directly* from the All-Union combinations, the various *Union* Commissariats draw up operating, credit, and financial plans covering the particular industries headed by them. It is with these latter plans that the bank compares its own credit plan. The short-term credit plans of the combinations constitute a part of their general financial plans. The latter, whether annual or quarterly, are estimates of all the funds required for the acquisition of fixed and current assets, and the meeting of operating expenses to enable the fulfillment of their production plans. In fact, the financial plan of a combination is but a part of its *promfinplan*, i.e., of its *operating* and *financial* plan. The financial plan of a combination consists of two basic parts: (a) the receipts and disbursements statement, and (b) balance sheets, *provisional* and *directive*. Both of these, naturally, show

Form No. 3

THE MAIN OFFICE (PRAVLENIE) OF THE STATE BANK OF THE U.S.S.R.

THE ECONOMIC-PLANNING DEPARTMENT

CREDIT PLAN FOR THE ...QUARTER OF 19 ..
(In millions of rubles)

Resources	*Income*	*Channels into which the Resources Will Be Directed*	*Outgo*
1. Profit		1. Seasonal requirements:	
2. Current accounts:		(1) P C. of Heavy Industry	
(a) State budget		(2) P C of Light Industry	
(b) Local budget		(3) Forest industry	
(c) Central Board of Social Insurance		(4) P C. of Supplies	
(d) State insurance		(5) Com of Storing at the Council of People's Commissars	
(e) Trade unions		(6) Selling organizations (*Torgi*) of the P. C. of Supplies	
(f) Savings banks		(7) P. C. of Foreign Trade	
(g) Collective farms		(8) P. C of Agriculture	
(h) Other social and state organizations		(9) P C. of Transportation	
3. Clearing accounts		(10) P. C of Waterways	
4. Repayment of old indebtedness:		(11) P. C. of State Farms	
(1) P. C. [a] of Heavy Industry		(12) Central Board of Road Transport (*Tzudotrans*)	
(2) P C of Light Industry		(13) Consumers' co-operatives	
(3) Forest industry		(14) Handicraft producers' co-operatives	
(4) P. C of Supplies		(15) Hunters' co-operatives	
(5) Com. of Storing at the Council of People's Commissars		(16) Enterprises of other organizations	
(6) Selling organizations (*Torgi*) of the P C of Supplies		(17) Collective farms and centers	
(7) P. C. of Foreign Trade		(18) *Orsy* (Division for the Supply of Workers)	
(8) P C. of Agriculture			
(9) P C. of State Farms			
(10) Consumers' co-operatives			
(11) Handicraft producers' co-operatives			
(12) *Orsy* (Division for the Supply of Workers)		2. Values in transit	
5. Credit institutions:			
(a) Prombank			
(b) Tzekombank and municipal banks		3. Deductions·	
(c) Co-operative banks		(a) to the P. C. of Finance from profits	
(d) Other credit institutions		(b) to the *Fubr* (Fund for the Improvement of Workers' Conditions)	
(e) Agricultural Bank			
6. Other liabilities			
Total		Total	

[a] Abbreviation for People's Commissariat.

the size of the required funds and the sources for meeting them. The receipts and disbursements statements, however, present an itemized and detailed picture of all the operations (here one will find the anticipated outlay for raw materials, fuel, various supplies, wages, payments into the budget on account of profits

Office) establishes the difference between its estimates of the credit needs of the separate branches of economy and theirs, and a reconciliation of the credit plan with the general plan of the nation, the budget, the cash plan, and the plans for long-term investments, the State Bank submits the projected credit plan (together with directions for its successful execution) to the higher authorities for approval. The higher authorities consider the discrepancies between the bank's estimates and those of the administrative organizations, and arrive at a decision. As soon as that is communicated to it, the bank makes a final apportionment of the planned credit among the various administrative organizations. These, in turn, make then an apportionment of planned credit among the combinations, trusts, and enterprises which are subordinated to them. The combinations and trusts, in their turn, carry out the apportionment of credit among the constituent enterprises. Both, the administrative organizations and the combinations, are permitted to retain a part of the credits allotted them for apportionment as working reserves.[45]

After the combinations and trusts, on the basis of the credit at their disposal, set up upper credit *limits* for each of their enter-

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earned, and so forth, as well as the receipts from the sale of the product, from the budget, from banks, and the like), in short a dynamic picture. The balance sheets, on the other hand, present snapshots of the financial conditions as they will exist at a future time. Even though the changed balances of the various accounts contained in them indicate the nature of the projected plan, they do not show by means of what operations the changes will be wrought. The receipts and disbursements plans are made out in such a way as to show which of the items will be paid in cash, which by means of *moneyless* settlements, and which by means of open account. This classification of receipts and disbursements enables the State Bank to draw up its *cash plans*. The difference between the two types of balance sheets (provisional and directive) is that the former is a rough estimate, let us say, in May of what the financial condition of the combination will be in June or July. In the quarterly financial plan such a provisional balance sheet is given with respect to the *beginning* of the planned period. The *directive* balance is the one picturing the *end* of the planned period. It is so called because it directs the combination or enterprise to perform certain tasks which would produce the results indicated in it. See M. A. Barun, *The Credit Plan of Combinations and Enterprises under the New Credit Conditions* (Moscow, State Finance Press, 1932), pp. 20-23, 37-39.

[45] The credit-planning departments of the Main Office also are endowed with additional working reserves for the purpose of meeting the requirements of their clients for planned seasonal loans, provision for which was not made by them (the departments) in their quarterly plans.

prises and these were gone over by the bank, the latter would send out to its *offices* what was known as *limiting letters.* These letters contained information with respect to the purposes of those loans, the limits for each purpose separately, the documents which had to be presented by the borrower, when and how the loans were payable (these latter depended, of course, upon the client's nature of business). These letters were generally accompanied by helpful instructions and explanations.

Inasmuch, however, as the rigid limits tended to stifle the activities of efficient trading enterprises, the Council of People's Commissars in its decree of June 4, 1936, ordered that their fixing be discontinued. Under the new procedure, the Council of Labor and Defense determines the *total* amount of credit that the State Bank may grant to trading enterprises during any quarter of the year. The Main Office of the bank then sets limits for its republican, regional, and territorial offices, and the latter, in turn, for district branches. When district branches need additional credit for trading enterprises they apply to the offices to which they are subordinated. The Main Office passes on additional credits for republics, regions, and territories.

The Main Office supplies all of its offices with copies of the approved credit plan. The latter shows the *control figures* for the income and outgo, as well as the size of the reserves for extra-planned and *value-in-transit* loans. The offices then proceed to send instructions to the various branches and units subordinated to them.

So much for *planned* loans. As we have seen, however, there are also *extra-planned* loans and loans against *values in transit.* With respect to those the Main Office fixes general limits for its regional offices, and the latter distribute them in such a way as to promote the best interests of the economy of their regions. This, in brief, is the short-term credit planning procedure in the Soviet Union at the present time.

In so far as "cash" planning is concerned, attention has already been called to the fact that all enterprises, organizations, and institutions are required to draw up and present cash plans to the banks periodically. The procedure with respect to their presentation

to the banks differs from that employed in connection with the credit plans. All enterprises and organizations must present their plans directly to the local bank units. The directorates of the combinations, the co-operative and the socialized centers draw up cash plans covering merely the operations of the headquarters, but no consolidated cash plans embracing their constituent enterprises. Each enterprise, in other words, submits its own cash plan.[46]

The banks for long-term financing and the savings banks too present their cash plans. The plans of the former include the cash plans of all their clients who maintain with them clearing or current accounts. The cash plans of the savings banks include the operations (arranged by kind) of their clientele.

The State Bank system, as well as other credit institutions to which cash plans are submitted, scrutinize those plans carefully with the aid of the information contained in the financial plans of the respective organizations. Following that, the lower bank units fuse the cash plans of the various enterprises, banks for long-term financing, savings banks, and treasury offices into consolidated cash plans for the particular locality. Similarly, the regional, district, and republican bank offices draw up cash plans covering their own clientele, audit and consolidate the cash plans of the lower bank units, and, finally, turn out consolidated cash plans for entire regions. These are forwarded to the Main Office of the bank where they are consolidated into a cash plan for the entire U.S.S.R., or, to be more exact, for its socialized sector. The cash plans are of two types, quarterly and monthly.[47] As soon as the quarterly cash plans are approved, the various organizations are required to draw up monthly cash plans that are based upon and are in consonance with these quarterly plans. "Limits" are not applied to cash plans. This, however, does not mean that the various enterprises may dispose of their cash balances in the banks as they choose or in disregard of the plans. As soon as the consoli-

[46] An exception, however, can be pointed out in the case of organizations connected with the *local* budget. These do not present their cash plans to the banks. Instead, the respective treasury offices, along with submitting their own cash plans (pertaining to the anticipated flow of taxes, realized state loans, various fees, and so forth), submit also consolidated cash plans of the various organizations connected with the local budget.

[47] These are alike in form.

dated cash plan for a lower bank unit is approved, and quotas are established by it for its clients (on the basis of their cash plans), the latter must adhere to those quotas. The banks are careful to see that the cash withdrawals of an enterprise for the purpose of meeting the payroll and its administrative and other expenses are in close agreement with the specifications in its *cash* and *credit* plans.[48] The two plans it will be remembered are closely interwoven. In case of overdraft the banks notify at once the proper authorities, taking no other steps.[49]

As has already been pointed out in a previous chapter, present planning in the Soviet Union is on a far higher plane than was that during the earlier years. The evolution of an efficient labor supply, an improvement in management, and, so to say, normalized economic conditions will be a boon to planning.

[48] A special procedure with respect to the payment of wages was introduced on February 22, 1933. When presenting to the banks their cash plans, all enterprises and organizations, business or budgetary, had to submit on standard forms certified *information* with respect to the contemplated amount of wages to be paid out during a given period. This *information* used to be issued to the various enterprises by the higher agencies which regulated them. Thus, the various People's Commissariats approved once quarterly the amount of such expenditure for the subordinated combinations and trusts (for the quarter and by months), and the latter then notified the enterprises constituting them (also once quarterly) as to what they could pay out in wages (during the quarter of the year and during each month). When procuring cash at the banks to meet their payrolls, enterprises indicated on the checks, which they cashed for that purpose, the month for which wages were being paid. The banks verified the checks before making payment. This procedure was repealed on June 11, 1935.

[49] The author wishes to acknowledge his indebtedness to O. J. Efimov (*op. cit.*), upon whom he freely drew for material in this section. See also the various issues of the *Working Material for Credit Planning* (Moscow, Main Office of the State Bank, 1933); also *On the Crediting of Commercial Operations* (Moscow, Main Office of the State Bank, 1933); also O. J. Efimov, *Banking Statistics* (State Finance Press, 1933), Parts I, II, and III.

XIV

MONEY, PRICES, AND GOLD SINCE 1928

Currency circulation under the First Five-Year Plan.—It will be recalled that between October 1, 1928, and October 1, 1933, the loans and discounts of the short-term credit system were to increase, according to the approved variant of the first Five-Year Plan, from about 3,900,000,000 to 7,275,000,000 rubles, and the demand and current deposits, from less than 1,600,000,000 to about 3,250,000,000 rubles.

As has been shown in an earlier chapter, the bank's *actual* short-term credit outstanding on November 1, 1933, amounted to 14,423,600,000 rubles, while the balance of its clients' *clearing* accounts (former deposit accounts) remained at a 2,000,000,000-ruble level during 1929, 1930, and 1931, and, then, due to extraordinary measures (as a result of which its clients became endowed with a new, sizable working capital), it was lifted to 8,135,800,000 rubles on May 1, 1932, but sank to 3,899,900,000 rubles by November 1, 1933.

The note issue, over the five-year period (1928–33), was to rise by no more than 1,250,000,000 rubles. Since the total currency in circulation on October 1, 1928, was 1,971,400,000 rubles, it follows that on October 1, 1933, it was to be no higher than 3,221,400,000 rubles. The *actual* currency circulation followed, however, quite a different course. In less than two years its total volume swelled to what it was expected to become only at the end of the fifth year. Within the first year of the Plan (October 1, 1928, to October 1, 1929) the volume of the currency had expanded by one-third (34 percent). As shown by Table 62, on October 1, 1930, exactly two years after the Plan went into effect, the total currency circulation amounted to 4,263,900,000 rubles, that is, over 1,000,000,000 rubles, or 32 percent in excess of the amount planned for the end of the period. As may be gleaned from this same table, in the second year of the Plan (October 1, 1929, to October 1, 1930) the total circulation registered a rather phenomenal increase of 60

percent. Despite the efforts of the government to make the specially created quarter (October–December) in 1930, as well as the third year of the Plan (1931), free from note issues,[1] the total circulation continued to expand, increasing between January 1, 1931, and January 1, 1932, from 4,302,000,000 to 5,673,310,000 rubles, or by 32 percent. By July 1, 1933, the circulation, according to the official figures, mounted to 6,825,046,000 rubles, and by the end of that year, to 6,861,548,000 rubles. At the latter date the circulation was almost three and a half times as high as that on October 1, 1928, and 113 percent higher than the maximum set for October 1, 1933.[2]

With the causes of the serious discrepancy between the planned and the actual credit and currency figures we are already familiar. The Credit Reform of 1930 with its "automaticity," as has already been suggested, was one of the causes. The Plan itself was not free from imperfection. At its very foundation lay the assumption of a material increase over 1928–33 of the productivity of labor (from 60 percent in construction work, 75 percent in the transportation branch, to 110 percent in industry), and of a material decrease (in industry on the whole, by 35 percent) in the cost of production. It was figured that this would enable the carrying out of the various projects with a certain given rise in the number of those employed (in industry, by a 33 percent rise over the five years). Inasmuch, however, as those expectations did not materialize, and the various enterprises required more fuel, more raw materials, more workers, and so forth, than was anticipated by the Plan, additional credit and additional currency had to be issued.

As shown by Table 59, the difference between the expenditure and revenue of those years was covered almost entirely by the further expansion of the state debt.

Changes in the ratio between banknote and treasury currency circulation.—Although the treasury circulation in the Soviet Union is handled by the State Bank and is used by the latter for the same

[1] *Finances of the Three Years of the Five-Year Plan* (Moscow, State Finance Press, 1931), pp. 2, 28, 29, 31.

[2] But see the report of the People's Commissar of Finance of the U.S.S.R., G. F. Grinko, at the First Session of the Central Executive Committee of the U.S.S.R. of the Seventh Convocation. *Economic Life*, February 9, 1935.

TABLE 59

UNIFIED STATE BUDGET OF THE U.S.S.R.

1928/29–1932 [a]

(*In millions of rubles*)

	1928–29	*1929–30*	*October 1–December 31, 1930*	*1931*	*1932*
Revenue					
1. Tax revenue	4,004.1	6,083.7	2,563.3	12,115.5	20,050.9
(including trade turnover tax)	....	....	(2,172.0)	(10,601.0)	(17,693.4)
2. Non-tax revenue (industry, transport, and so on)	3,461.2	5,402.0	1,742.4	7,381.8	7,011.4
3 State loans	724.8	1,278.4	356.1	3,269.0	3,921.7
4. Other sources	32.2	35.6	8.9	388.6	46.9
(including: (a) Revenue from issue of metallic money	(32.2)	(19.8)	(8.9)	(25.3)	(46.9)
(b) From local budgets)	....	(15.8)	....	(363.3)	....
Total revenue	8,222.3	12,799.7	4,670.7	23,154.9	31,030.9
Carried over from previous years	205.4	186.8	651.5	706.2	598.6
Total	8,427.7	12,986.5	5,322.2	23,861.1	31,629.5
Total expenditure	8,240.9	12,335.0	4,616.0	23,145.8	30,740.4

[a] Central Administration of Economic Accounting of the Gosplan of the U.S.S.R., *Socialist Construction of the U.S.S.R., Statistical Yearbook* (Moscow, 1935), pp. 644 ff.

purpose as it uses its own notes, it is nevertheless noteworthy that the total circulation (6,861,548,000 rubles) on January 1, 1934, was made up of almost equal parts of banknotes and treasury currency. This, as we know, was not the case in the years following the Monetary Reform of 1924. Article 3 of the Law of February 5, 1924, pertaining to the issue of treasury notes, it will be recalled, provided that the aggregate treasury note issue on the first day of any month must not exceed *one-half* (50 percent) of the amount of banknotes in circulation on that day. Inasmuch, however, as an expansion of the volume of currency was unavoidable and the available and anticipated firm cover placed an automatic limitation upon the amount of banknotes in circulation, it became necessary to liberalize the Law of 1924. Indeed, as early as August 1, 1928, the Central Executive Committee and the Council of People's Commissars of the U.S.S.R. decreed the adding of the following supplementary clause to Article 3 described above: "At times when the requirements of trade for currency of a 5-ruble and lower denominations rise sharply, there is permitted a temporary increase of the norm governing the issue of treasury notes from one-half to three-quarters of the total amount of banknotes in circulation." [3] The revised Article 3 remained in effect until September 18, 1930, when the above-mentioned governmental bodies ordered its repeal and the substitution in its stead of a new (that is, once more revised) Article 3. Henceforth the volume of treasury notes was not to exceed the volume of banknotes in circulation (as indicated in the balance sheet of the Issue Department of the State Bank on the first day of each month).[4] In the preamble to the above decree the following reason was given for raising the legal ratio of treasury notes to chervontzy from 75 percent to 100 percent: "In connection with the wide development of settlements requiring no cash, especially in the socialized sector, the need for currency of high denominations (chervontzy) diminished considerably, and the need for currency of lower denominations (treasury notes) relatively increased."

Changes were also made in the provision for the regulation of

[3] *Collected Decrees,* 1928, Decree 424. [4] *Collected Decrees,* 1930, Decree 508.

TABLE 60

THE BALANCE SHEETS OF THE ISSUE DEPARTMENT OF THE STATE BANK OF THE U.S.S.R.

1928–36 [a]

(*In thousands of rubles*)

	Assets					*Total*	*Liabilities*	
	Gold Coin and Bullion	Other Precious Metals in Coin and Bullion	Foreign Currency	Foreign Bills and Drafts	Short-Term Credit		Banknotes Transferred to the Main Office	Balance to Which Notes May Be Issued
January 1, 1928...	188,585.00	20,726.00	73,500.00	2,665.00	774,524.00	1,060,000	1,044,037.00	15,963.00
October 1, 1928....	148,102.00	47,093.00	84,325.00	2,710.00	817,770.00	1,100,000	1,090,096.00	9,904.00
January 1, 1929....	178,558.90	44,362.60	78,455.60	2,758.10	825,864.80	1,130,000	1,122,561.50	7,438.50
October 1, 1929....	255,947.40	38,476.90	74,765.20	2,852.50	1,097,958.00	1,470,000	1,466,280.00	3,720.00
January 1, 1930...	285,696.20	34,609.10	67,851.10	2,917.40	1,148,926.20	1,540,000	1,536,266.00	3,034.00
October 1, 1930....	483,888.64	23,689.59	47,252.40	3,040.52	1,592,028.85	2,150,000	2,145,650.00	4,350.00
January 1, 1931....	483,643.14	22,258.48	52,071.54	3,023.60	1,559,003.24	2,120,000	2,100,409.42	19,590.58
October 1, 1931....	569,313.09	22,382.70	50,296.20	2,290.97	1,885,717.04	2,530,000	2,527,150.08	2,849.92
January 1, 1932....	637,942.85	22,800.80	44,925.42	1,544.40	2,087,786.53	2,795,000	2,784,413.09	10,586.91

June 1, 1932.....	650,817.06	20,744.50	31,048.55	1,419.43	2,110,970.46	2,815,000	2,766,839.62	48,160.38
July 1, 1933.....	779,464.52	13,990.49	25,072.41	3,231.80	2,813,240.78	3,635,000	3,356,253.24	278,746.76
October 1, 1933....	808,482.38	13,603.08	33,253.88	3,231.80	2,776,428.86	3,635,000	3,387,438.31	247,561.69
January 1, 1934...	807,708.34[b]	9,090.22	42,279.36[c]	2,864.38[d]	2,772,957.70[e]	3,635,000	3,432,502.46	202,497.54
January 1, 1935...	854,341.07[b]	8,414.42	29,503.76[f]	4,344.56[g]	2,948,396.19[g]	3,845,000	3,838,362.10	6,637.90
April 1, 1935.....	858,355.83[b]	7,399.92	34,727.32[h]	4,344.56[g]	3,080,172.37[g]	3,985,000	3,978,041.50	6,958.50
October 1, 1935. .	963,369.86	7,399.91	31,299.49[i]	3,389.76	3,994,540.98	5,000,000	4,998,554.42	1,445.58
April 1, 1936.. ...	1,403,963.34[j]	.....	113,765.21[k]	.....	4,432,271.45	5,950,000	5,934,994.53	15,005.47

[a] The figures for 1928–31 were taken from *Vestnik Finansov*, 1928, No. 12, p. 161, and from *The State Bank of the U.S.S.R. Economic Survey*, 1929, IV, No. 1, p. 3; No. 35, p. 7; 1930, V, No. 1, p. 7; No. 18, p. 19; 1931, VI, No. 1, p. 14; No. 10/11, p. 6.
The figures for later years were taken from *Economic Life*, January 2, June 1, 1932; July 21, October 16, 1933; January 18, 1934; February 6, April 14, October 28, 1935; April 14, 1936.

[b] Gold valued at 1.29 rubles per gram.
[c] £ valued at 6.34 rubles; $ valued at 1.24 rubles; German marks at 46 copecks.
[d] After an allowance of 10 percent was made for possible shrinkage.
[e] After an allowance of 10 percent was made for bad debts.
[f] £ = 5.68 rubles; $ = 1.15 rubles; mark = 46 copecks.
[g] After writing off 10 percent.
[h] £ = 5.54 rubles; $ = 1.15 rubles; mark = 46 copecks.
[i] £ = 5.67 rubles; $ = 1.15 rubles; mark = 46 copecks.
[j] Gold valued at 5.6807 rubles per gram ("free gold"), and not at 1.29 rubles per gram as before.
[k] £ = 25.04 rubles; $ = 5.06 rubles, French francs = 33.38 rubles per hundred.

TABLE 61

NOTES AND COIN PLACED IN CIRCULATION BY THE PEOPLE'S COMMISSARIAT OF FINANCE OF THE U.S.S.R.

(THAT IS, BY THE TREASURY) [a]

(In thousands of rubles)

Date	Treasury Notes	Silver Coin	Copper Coin	Bronze Coin	Total
January 1, 1928	479,800.0	171,900.0	9,000.0	4,200.0	664,900.0
October 1, 1928	711,000.0	181,800.0	9,400.0	5,500.0	907,700.0
January 1, 1929	730,400.0	190,600.0	9,700.0	6,400.0	937,100.0
October 1, 1929	983,400.0	212,000.0	9,400.0	9,200.0	1,214,000.0
January 1, 1930	1,028,200.0		243,800.0		1,272,000.0
October 1, 1930	1,859,100.0		274,500.0		2,133,600.0
January 1, 1931	1,946,300.0		275,300.0		2,221,600.0
January 1, 1932	2,577,454.1	267,552.2	8,105.1	35,785.3	2,888,896.7
June 1, 1932	2,687,866.4	286,086.9	7,757.9	32,928.9	3,019,640.1
July 1, 1933	3,102,573.2	316,486.8	7,451.6	42,281.7	3,468,793.3
January 1, 1934	3,060,586.0	317,141.8	7,373.7	43,944.7	3,429,046.2
January 1, 1935	3,499,024.7	341,142.6	7,254.3	47,949.1	3,895,370.7
April 1, 1935	3,500,925.5	344,569.3	7,234.6	48,637.2	3,901,366.6

[a] *The State Bank of the U.S.S.R. Economic Survey*, 1928, III, No. 45; 1929, IV, No. 36; 1931, VI, No. 5/6, *Economic Life*, January 16, June 29, 1932; August 1, 1933; February 3, 1934; February 20, and April 12, 1935. The figures for 1928–31 represent treasury currency in actual circulation. Those beginning with 1932, currency issued by the treasury. The 1936 figures are at present unavailable.

the size of separate issues. According to Article 4 of the Law of February 5, 1924: "The size of each separate issue of treasury notes, within the limits stated in Article 3, is to be fixed by special decision of the Council of Labor and Defense." On January 16, 1930, the Central Executive Committee and the Council of People's Commissars, however, decreed the repeal of this article, inasmuch as "the size of the issue of banknotes of the State Bank of the U.S.S.R. and of treasury notes is being fixed by the government

for each quarter" (subject, of course, to the general limitation established by Article 3).[5] In the decree of September 18, 1930, with which we have already dealt, the government further provided that the size of separate issues of treasury notes, within the limits established by Article 3, was to be fixed "by the People's Commissar of Finance of the U.S.S.R. in accordance with the directives of the Council of Labor and Defense."

Gold reserve and total firm cover.—The bank's total firm cover (i.e., its gold reserve together with its other precious metals, foreign currency, and foreign bills) had expanded from 282,230,000 rubles on October 1, 1928, to 861,942,300 rubles on January 1, 1934.[6] The slightly lower rate of increase of firm cover (205 percent) as against that of banknotes transferred to the Main Office between those two dates (214 percent) accounts for the fact that on October 1, 1928, the reserve ratio was 25.9 percent, while on January 1, 1934, it was 25.1 percent. During the intervening years the reserve ratio, on the whole, stood close to the statutory 25 percent. On July 1, 1933, though, it fell slightly, to 24.5 percent. The year 1935 witnessed a further decline, to 22.7 percent on April 1. The above percentages were computed, however, with respect to banknotes *transferred to the Main Office* rather than to those in actual circulation. There is a difference. To assure an adequate supply of currency throughout the Soviet Union, where the distances between the outlying regions and the center are immense, the bank issues more banknotes than are required for the immediate needs of its branches. Naturally, the ratio with respect to banknotes in actual circulation is higher.

As has already been suggested, however, such ratios are not very significant in a country like the Soviet Union, where the currency is inconvertible, where prices are not influenced by world prices, and where the gold supply is protected from an outflow. The purchasing power of a ruble there has very little, if anything, to do with the gold reserve, while outside of the country it is not legally quoted, being a purely internal currency.

The outside world is not so much interested in the State Bank's

[5] *Ibid.*, Decree 91.
[6] See Table 63.

TABLE 62

TOTAL CURRENCY IN CIRCULATION AND RETAIL TRADE

1928–36 [a]

(In thousands of rubles)

	Banknotes	*Treasury Notes and Coin*	*Total Currency in Circulation*	*Index of Circulation (Oct. 1, 1928 = 100)*	*Total Retail Trade Turnover*		*Index of Retail Trade Turnover (1927–28 = 100)*
January 1, 1928.....	1,002,900	664,900	1,667,800	....	....	....	....
October 1, 1928	1,063,700	907,700	1,971,400	100	1927–28	14,740,500	100
January 1, 1929.....	1,090,700	937,100	2,027,800	103	....	....	....
October 1, 1929. ...	1,428,200	1,214,000	2,642,200	134	1928–29	16,634,700	113
January 1, 1930.....	1,501,000	1,272,000	2,773,000	141	....	....	....
October 1, 1930.....	2,130,300	2,133,600	4,263,900	216	1929–30	17,564,000	119
January 1, 1931.....	2,080,400	2,221,600	4,302,000	218	....	....	....
January 1, 1932.....	2,784,413	2,888,897	5,673,310	288	1931	24,725,200	168
June 1, 1932.....	2,766,840	3,019,640	5,786,480	293	1932	35,504,300	241

July 1, 1933.....	3,356,253	3,468,793	6,825,046	346	....	....	....
January 1, 1934.....	3,432,502	3,429,046	6,861,548	348	1933	48,700,000	331
January 1, 1935.....	3,838,362	3,895,370	7,733,732	392	1934	61,000,000	414
April 1, 1935.....	3,978,041	3,901,366	7,879,407	400	....	....	....
October 1, 1935.....	4,998,554	Unavailable	....	....	....	....	....
April 1, 1936.....	5,934,994	Unavailable	....	....	1935	80,000,000	542

[a] The figures were taken from sources cited in the preceding tables. Also, Central Administration of Economic Accounting of the Gosplan of the U.S.S.R., *The Soviet in Figures* (Moscow, Soyuzorguchot, 1934), p. 165; *Socialist Construction of the U.S.S.R., Statistical Yearbook* (Moscow, 1934), pp. 362-63; and 1935, p. 552. *Stenographic Report of the Third Session of the Central Executive Committee of the U.S.S.R. of the Sixth Assembly*, January 23–30, 1933 (Moscow, Press of the C. E. C., 1933), Bulletin 11, p. 3; *Economic Life*, January 17, 1936. The figures for 1928–31 represent currency in *actual* circulation (that is, the balances after the currency in the vaults of the State Bank, or not as yet issued, had been deducted).

reserve *ratio* as it is in the *size* of that reserve. It wants to know, among other things, whether or not the Soviet Union will be able to meet its indebtedness at maturity. As may be seen from the official figures given in Table 63, the bank's gold stock and claims to gold experienced within recent years a rather substantial growth, from 282,230,000 rubles on October 1, 1928, to 1,005,459,020 rubles (of which 963,369,860 rubles were represented by gold coin and bullion) on October 1, 1935. By April 1, 1936, the State Bank's firm cover jumped to 1,517,728,550 rubles (of which gold coin and bullion amounted to 1,403,963,340). On the latter date, however, the bank, in conformity with the decree of the Council of People's Commissars of February 29, 1936, relative to the ruble's revaluation, valued its fine gold at 5.68 rubles per gram (and not at 1.29 rubles per gram as before), American dollars at 5.06 rubles per dollar (as against 1.15 rubles per dollar as on October 1, 1935), English pounds sterling at 25.04 rubles (as against 5.67 rubles on October 1, 1935), and French francs at 33.38 rubles per hundred (as against 7.50 rubles as before). The bulk of the "profit" from this transaction, as has already been suggested, was apparently transferred to the treasury. Unfortunately, the size of the total gold stock held by the latter for emergency purposes is unknown.

Although the Soviet Union had a favorable balance of 109,900,000 rubles in 1933 and 186,900,000 rubles in 1934, almost 300,000,000 rubles within those two years, it was not its foreign trade that accounted for the rapid increase of the bank's gold reserves. As will be recalled, the Soviet Union was unable to create over the years 1928–29 to 1932–33 (as planned) a favorable foreign trade balance of 820,000,000 rubles, partly because of adverse world conditions. In fact, between October 1, 1928, and the end of 1933, Soviet exports amounted to 4,009,800,000 rubles and the imports, to 4,294,500,000 rubles—the difference being a net unfavorable balance of 284,700,000 rubles.[7]

If taken over the last fifteen years (1920–34) the total of the unfavorable balance of the Soviet Union's foreign trade amounts,

[7] See Chapter XII, Table 57.

TABLE 63
BANKNOTE ISSUE AND FIRM COVER
(*In millions of rubles*)

	Banknotes Transferred to Main Office	*Total Firm Cover*	*Ratio (%)*
January 1, 1928	1,044.0	285.5	27.3
October 1, 1928	1,090.1	282.2	25.9
January 1, 1929	1,122.6	304.1	27.1
October 1, 1929	1,466.3	372.0	25.4
January 1, 1930	1,536.3	391.1	25.5
October 1, 1930	2,145.6	557.9	26.0
January 1, 1931	2,100.4	561.0	26.7
October 1, 1931	2,527.1	644.3	25.5
January 1, 1932	2,784.4	707.2	25.4
July 1, 1933	3,356.2	821.7	24.5
October 1, 1933	3,387.4	858.6	25.3
January 1, 1934	3,432.5	861.9	25.1
January 1, 1935	3,838.4	896.6	23.3
April 1, 1935	3,978.0	904.8	22.7
October 1, 1935	4,998.5	1,005.5	20.1
April 1, 1936	5,935.0	1,517.7	25.5

according to official figures, to 709,700,000 rubles.[8] In addition the Soviet Union paid foreign experts for services and maintained representatives abroad. Whence, then, came the substantial increase in the State Bank's gold reserves? To begin with, the combination known as *Torgsin,* which from 1930 operated within the Soviet Union a network of stores selling commodities in a greater variety and of higher quality than in other stores to anyone able to pay

[8] See Chapter IX, Table 30, for earlier figures.

in gold, silver, gems, or foreign currency, took in between that date and February 1, 1936 (when the Torgsin was liquidated and its network of stores was transferred to the Commissariat of Domestic Trade), some 250,000,000 rubles.[9] Some 70 percent of that amount came from hoards; the balance, from transfers from abroad (16 percent), and payments made in foreign currency within the country (14 percent). Other sources are confiscated hoards and the sale of precious objects. Finally, and most important, the Soviet Union is one of the world's largest producers of gold, and is steadily forging ahead with an avowed determination to wrest the supremacy from South Africa.[10] It will be remembered that, even before the present regime came into power, Russia was an important producer of gold. For example, the registered output of gold in that country in 1912, 1913, and 1914 was 3,569 puds, 3,715 puds, and 4,056 puds, respectively.[11] In 1915 as a result of war conditions the output fell to 3,006 puds, rallying, however, in 1916 to 3,764 puds.

In 1917, when the present regime came into power, the output was but 1,885 puds; in 1918, 1,612 puds. During 1919, 1920, and 1921 it was a mere 482, 169, and 151 puds, respectively.[12] Thereafter, it experienced a steady rise, amounting in 1922, 1923, 1924, and 1925 to 322, 700, 1,035, and 1,200 puds, respectively.[13] Beginning with 1926 the publication of detailed statements pertaining to the gold industry and output had ceased. In a recent report [14] the production of gold in the Soviet Union between the year 1929 and the end of 1933 was said to be as shown in Table 64:

[9] See *Collected Decrees,* 1935, Decree 476; also Harold Denny's article in the *New York Times* of February 1, 1936. The word "Torgsin" means "trade with foreigners," home export, so to speak.

[10] For interesting details pertaining to the Soviet gold industry (its mechanization and so forth), see the article by A. Serebrovsky (director of "Glavzoloto," or of the "Chief Department of the Gold Industry") in *Izvestia* for June 3, 1934.

[11] "Natural Resources of Siberia," *Asiatic Russia* (St. Petersburg, 1905), Vol. II. Quoted by A. V. Baikalov, "The Gold Industry and the Gold Reserves of the Soviet Union," in *Money, Prices and Gold in the Soviet Union* (School of Slavonic and East European Studies in the University of London, November, 1934), Monograph No. 3, p. 25. A pud = 526.6 oz. troy.

[12] A. I. Krylov's report in *The Gold Industry in the U.S.S.R.* (Moscow, 1927), quoted by A. V. Baikalov, *op. cit.,* pp. 25-26.

[13] *Vestnik Finansov,* 1925, No. 11.

[14] The London *Financial Times,* April 3, 1934, quoted by A. V. Baikalov, p. 27.

TABLE 64
PRODUCTION OF GOLD IN THE SOVIET UNION

1929	1,085,000 oz. (2,060 puds)
1930	1,434,000 oz. (2,720 puds)
1931	1,701,000 oz. (3,420 puds)
1932	1,990,000 oz. (3,780 puds)
1933	2,490,000 oz. (4,730 puds)

The 1934 output, according to the published figures of the American Bureau of Metal Statistics, jumped to 4,200,000 ounces (the value of which, at $35 per ounce, is $147,000,000).[15] Apparently it was this increasing gold stock that enabled the Soviet Union over the past years not only to meet promptly all of its foreign commercial obligations, despite the many trade barriers created against it abroad, but also to amass a respect-compelling gold reserve.

According to a recent statement issued by Mr. Sherover, president of the Soviet American Securities Corporation, the planned output of gold for 1935 was to have a value of $225,000,000; that of 1936, $335,000,000; and of 1937, $500,000,000. It may be, of course, that the actual output will fall behind the planned. After a campaign of self-criticism and denunciation, and an appeal

[15] The figures of the American Bureau of Metal Statistics are in line with those quoted above, except that the output for 1933 is placed at 2,820,000 ounces. On the other hand, Mr. A. V. Baikalov, in the Monograph already cited, disputes the figures for 1929–33 published by the *Financial Times*. His own figures are compiled "on the basis of evidence indirect and sometimes controversial in character." As he says, "The ground of controversy lies in the apparent fact that Soviet statisticians add to the amount of actually mined gold an amount representing old gold—tsarist coins and jewellery—which Soviet institutions partly recover from circulation and hoards, and partly extract from the population." His estimate (p. 28) of the *actual* production is as follows (in puds):

1926	about 1,250	1930	about 2,350
1927	" 1,350	1931	" 2,800
1928	" 1,550	1932	" 3,600
1929	" 1,800	1933	" 4,400

His estimates, however, are not accompanied by information which would permit the checking of sources and the verification of figures.

for more "udarniki" (shock workers), the goal (if past experience can be relied upon), however, will be reached.

The spread of non-cash settlements.—The proposition that a country in which non-cash settlements (such as those effected by means of the checking system) are highly developed needs relatively less cash than one in which such settlements are hardly developed is quite axiomatic. No one can deny that the United States, where upward of 90 percent of all monetary transactions are settled by means of checks, or England, another example of a country with a highly developed checking system, would require a much larger monetary stock if they chose to settle all monetary transactions in cash.[16]

The checking system, however, is but one of the forms which non-cash settlements take. Another form is that known as the *giro* system, a system which received its development in Germany and under which the participants form, so to say, a circle within which payments are effected by means of bookkeeping transfers from one account to another. The work of the system is explained in a prospectus issued by the Württemberg giro-union (*Giroverband*) of savings banks:

When, for example, the owner of a building opens an account in the giro cash office of the city savings bank, all tenants are enabled to deposit to his account, either in cash or by means of a transfer from their own accounts, if they have such, the rent due him. The owner of the account is notified about each payment, and he, in his turn, may make all payments due from him to other participants of the giro-system in the most convenient way, that is, by transfers from his to their accounts. Thus, he may request the bank to pay interest on his mortgage to the bank; taxes, and dues to the tax department; tuition for his children's education to the school board; purveyors' bills; as well as gas, water, electric, newspaper, and telephone bills; deductions to the local hospital cash-office; in a word, to make payments of all kinds.[17]

The transfer from one account to another is effected on the

[16] As pointed out by V. S. Korobkov in his *Settlement of Commercial Transactions without the Employment of Cash* (Moscow, the Press of the People's Commissariats of the U.S.S.R. and of the R.S.F.S.R., 1930), p. 9, pre-war Germany, where the checking system was not well developed, needed from 9 to 15 times more cash than England.

[17] V. S. Korobkov, *op. cit.*, pp. 39-40.

basis of a giro-order in which the depositor states the date, the amount to be transferred, the account from which the transfer is to be made, and the account to which it is to be transferred. The giro-order differs from the ordinary check in that it is not negotiable—being payable only to the person indicated in it—and, furthermore, in that it is usually a mere instrument for the transfer of sums from one account to another and is not to be cashed.

The depositor may order the bank to transfer from his account a certain amount to another account (a *single* order), or he may at one and the same time order the transfer from his account to a number of other accounts (a *multiple* order), or, finally, he may give the bank a *good-until-canceled* standing order to effect periodically recurring payments to various indicated accounts.[18] The last-mentioned form is particularly attractive, and, it must be added, particularly suited to the Soviet economy.

As pointed out in the Württemberg prospectus cited above, the giro system enables an individual to eliminate the need for cash in connection with all of his periodically recurring payments. It eliminates the danger of loss of cash by fire, theft, acceptance of counterfeits, and so forth. It saves labor, time, and expense that are connected with cash payments. Although its handling is costly, this method of non-cash settlements is socially desirable, inasmuch as it reaches large layers of society that do not make use of the checking system and encourages them to deposit their earnings with banks.

It was not unnatural that in its attempt to devise ways and means to stem the rising tide of currency the Soviet Union should intensify its campaign to widen the sphere of non-cash settlements.

In the resolutions of the stenographic report of the XVI Party Conference that was held in April, 1929, we find, for example, an admonition ". . . to spread more widely the experiment of organizing non-cash payments in the sphere of mass payments by the population to the state, municipal, and public organizations."[19]

[18] K. Lupandin, *Problems of Bank Credit in the U.S.S.R.* (Moscow, State Finance Press, 1930), pp. 86-87.

[19] Of course, it is not improbable that the swing to the left at the time was responsible in part for this movement. Such a spread of non-cash payments, it must be remembered, would be a big step toward converting the banks into mere bookkeeping centers and toward the abolition of money—ideas which some of those

By this resolution the Party Conference sanctioned the preliminary work of the People's Commissariats of Finance and of the Workers' and Peasants' Inspection, which was begun by these two bodies in 1929, with a view to organizing a giro system in the Soviet Union.[20] In April, 1929, the giro method was introduced in Moscow in connection with payments for the use of electricity and of the telephone. Next, the giro method of payments was extended to gas bills, water bills, and similar charges. Other cities followed Moscow's example. Attempts were, of course, made to include as many objects of payment (particularly wages) as possible. It cannot be said, however, that this method of payment met with instant success in the Soviet Union. Its rapid development was hindered by such obstacles as lack of proper technique and the fact that the population (even urban) was not acquainted with such methods.[21]

It was at the same time decided to reduce the employment of cash in the socialized sector to a minimum. As was explained by Stalin to the XVI Party Congress, the measures adopted by the party with a view to achieving a rational organization of the credit work and a proper maneuvering of money reserves ran along two lines: (a) the concentration of all short-term credit in the State Bank, and (b) the organization of non-cash settlements in the socialized sector. "As a result, in the first place the State Bank becomes an all-state apparatus for the accounting of the production and of the distribution of products, and, in the second place, the volume of currency in circulation is appreciably reduced." [22]

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present at the conference no doubt cherished and believed possible of almost immediate execution.

[20] K. Lupandin, *op. cit.*, p. 90. Also, by decree of January 26, 1930, the Council of People's Commissars resolved not only to approve the above measures, but also "to include the development of non-cash settlements among the problems to be taken care of by commissions for furthering state credit and the work of savings banks." *Collected Decrees*, 1930, Decree 109.

[21] For an analysis of the early difficulties, see V. S. Korobkov, *op. cit.*, pp. 56-59. It was, of course, far more difficult to convert the peasantry to the use of this method than the urban population. See G. I. Bronshtein, *Credit Work in the Village and in the District* (Moscow, State Finance Press, 1931), pp. 36-37.

[22] *Stenographic Report of the XVI Congress of the All-Union Communist Party*, Second stereotyped edition (Ogiz, Moscow Worker, 1931). This statement of Stalin

As we know, those measures became crystallized in the Credit Reform of 1930, and in the amendatory legislation that followed it.[23] It will be recalled that upon the introduction of that Reform all settlements between enterprises of the socialized sector themselves and between them and the State Bank began to be effected by means of the *conto corrento* to which all of their funds were being deposited and from which all payments were made. Although the *conto corrento* was abandoned and "clearing" accounts (and loan accounts) were opened in its stead, the enterprises continued to be required to deposit all resources, whether their own or borrowed, to the new account against which they were to draw for the purpose of meeting expenses and obligations. The methods of settling debts which they now use all partake of the nature of bookkeeping entries, that is, non-cash settlements. Only petty expenses and wages continue to be met in cash.

The progress made by the Soviet Union in widening the sphere of non-cash settlements over the space of a few years is remarkable. For example, whereas in 1926–27 only 48 percent of all payments were effected without resort to cash, in 1929–30 the percentage rose to 61. The bulk of this increase came, however, from the spread of non-cash settlements in the socialized sector.[24] The continued expansion of the latter served to pave the way for a further widening of the sphere of non-cash settlements.

Valuta-checks.—Another device that helped to diminish the need for currency and that was used in the Soviet Union, beginning with the summer of 1931, was the so-called *Valuta-Trade-Settlement-Checks* (*Valiutirovannye tovarorastchotnye checki* or "V.T.R. Ch."). These combined some of the features of currency and

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is occasionally misunderstood. It must be borne in mind that he also added: "There can be no doubt whatsoever that these measures will lead (they are already leading) to a regularization of all credit work and to a strengthening of our chervonetz." *Loc. cit.*

[23] But even before that, on November 18, 1929, the Council of People's Commissars in an unpublished decree directed that settlements among enterprises take place by means of the *conto corrento*. The Credit Reform proceeded along those lines.

[24] S. B. Shachnovskaia, "The Problem of Reconstructing the Financial System," *At the New Stage of Socialist Construction,* Collected Essays (Moscow, Plankhozgiz, 1930), II, 277-78.

checks. In Moscow, for example, they were issued by the State Bank in various denominations. The amounts were printed on the checks as was also the signature of the bank. In this respect, then, they resembled banknotes. Like banknotes, too, they could be transferred from hand to hand, but only after being indorsed by the transferrer.[25] Their use was limited to the socialized sector of the city wherein issued.[26] They could not be used for the payment of wages. When presented at the bank they were accepted for deposit only (never cashed). Also, the life of each such check was limited to twenty days from the date of its issue. The velocity of their circulation, we are told, was high, inasmuch as "many V.T.R. checks return to the bank with four indorsements on the third, fourth, and fifth day, and there are cases of checks passing by indorsement in one day through four organizations." [27]

The valuta-checks had a number of desirable features from the bank's point of view as well as from the point of view of its clientele. They enabled the bank to keep the issue of banknotes to a lower level than would otherwise have been possible. Besides, inasmuch as these checks circulated like currency and were passed on from hand to hand, they helped to relieve the bookkeeping congestion at the bank. Now, this was a very important factor from the bank's point of view, for as a result of the Credit Reform it was practically submerged under a tidal wave of "documents" presented to it by its clients. Among the features that appealed to the clientele were: certainty that the checks were good, and especially, that they enabled them to carry on at least a part of their business as they chose, without bank "interference." Need-

[25] Although the feature of indorsement, as a rule, is not associated with banknotes, it is not uninteresting to note that "the practice of indorsing banknotes was widely used in England a century ago and continued until recent years when the larger denominations of Bank of England notes were frequently indorsed." George W. Edwards, *Principles of Banking and Finance* (New York, the Ronald Press Company, 1932), p. 138.

[26] Their use was compulsory in the case of (intra-city) transactions involving less than one thousand rubles. In larger transactions they could be used only by mutual consent of the parties involved. G. Roginsky and J. Rubinshtein, *Credit and Settlements* (Moscow, State Finance Press, 1932), p. 56.

[27] A. Sharovarov, "V.T.R.Ch.—A New Form of Non-Cash Settlement," *Finance and Socialist Economy*, May, 1932, No. 12, p. 30. Four indorsements was the maximum allowed.

less to say, this last feature also made them highly undesirable from the Soviet point of view. Any device which makes possible the settlement of accounts without recording at the bank serves to weaken control. This is one of the reasons why they are very little used in the Soviet Union at the present time.

The rise of prices. Introduction of ration cards.—Obviously, the absolute and relative increase in the volume of non-cash payments could have no other effect than that of narrowing down the sphere wherein cash could be used. Cash, however, for reasons already stated, continued to be pumped in large volume into circulation. True, some of that cash found its way back into the treasury either as a result of increased deposits in savings banks, or—and this was a more important factor—as a result of selling government bonds to the population.[28] But even though the fund so received from the population was considerable it could not affect appreciably the demand for goods. It merely resulted in a shift of purchasing power from the laboring classes to the government, which immediately used it for the purpose of capital construction, employing more workers, and placing purchasing power in their hands.

Under a free competitive system this would send prices skyrocketing. The system of price regulation in the Soviet Union, as we have seen, tends to make this impossible. Prices, nevertheless, did rise appreciably there during those years. The available price indices fail, however, to reflect that. For example, the official wholesale price index (1913=100) on October 1, 1928, 1929, and 1930, stood at 176.1, 181.7, and 186.5, respectively.[29] The retail index stood on the same dates at 211, 215, and 204, respectively. On January 1, 1931, it dropped further to 192. Thereafter the publication of price indices terminated, and rightly so, for they were not very meaningful, particularly so beginning with 1929, when prices of the socialized sector alone were being included in the index. The "free" market, it should be understood, continued to play an important rôle. It is estimated, for instance,

[28] See Chapter XV.

[29] *State Bank of the U.S.S.R. Economic Survey,* III, No. 45; IV, No. 36; V, No. 18; VI, No. 1.

that the "free" market furnished in 1926–27, 48 to 50 percent; in 1927–28, 35 to 38 percent; in 1928–29, 33 to 36 percent; and in 1929–30, 25 to 27 percent of all consumers' goods.[30]

During 1928–30 the worker depended upon the "free" market for from one-fifth to one-third of his food provisions. In that market prices for bread rose in 1928 by 40 percent (as compared with 1925–27, a period during which market prices for bread became more or less stabilized) and in 1929, by 119 percent.[31] The rise of prices in the "private" sector of course was not confined to bread alone. All commodities of primary importance were affected. In fact, the price index of the "free" market rose in 1928–29 (as compared with 1927–28) by 26 percent, and in the first half of 1929–30, by another 32 percent. On the whole, retail prices in the "private" sector exceeded those in the "socialized" sector by about 25 percent in 1927–28, by 50 percent in 1928–29, and by more than 200 percent in 1929–30.[32] But already by 1930 the prices of a number of commodities in the private sector exceeded those in the socialized sector by from 12 to 15 times.[33]

As early as 1928–29 the government introduced ration cards, which entitled the holders (generally speaking, workers and employees) to buy at so-called *closed* shops limited quantities of goods at relatively low prices. Prices in the *closed* shops, however, did not remain stationary. They too kept on moving to higher levels. Particularly sharp was the rise of prices at the beginning of 1932.[34] Beginning with 1933 the state began to open so-called *commercial* shops or stores at which anybody could buy goods in any quantity but at considerably higher prices than at the *closed* shops.[35] And,

[30] L. M. Gatovsky, "On the Nature of Exchange Connections at the New Stage," *At the New Stage of Socialist Construction*, II, 25.

[31] G. Neiman, "Abolition of Cards, Unfolding of Trade, and Strengthening of the Ruble," *Economic Problems* (Problemy Ekonomiki), 1935, No. 1, p. 49.

[32] Gatovsky, *op. cit.*, p. 26.

[33] Neiman, *op. cit.*

[34] See Malcolm Campbell, "Money, Credit, and Banking," *Red Economics*, p. 181. According to him "foodstuffs had jumped from 25 to 75 percent; cotton goods, 209 percent; footwear, 40 to 45 percent; articles of clothing, 30 to 35 percent." See also Pietro Sessa, "Social Problems and Social Conditions," *ibid.*, p. 265.

[35] In 1933 the following prices per kilogram (2.2 pounds) were paid at the *closed* shops: black bread, 27 copecks; white bread, 52 copecks; meat, 2 to 4 rubles; herrings, 3 to 10 rubles; sugar, 2 rubles; butter, 6 to 8 rubles. On April 1, 1934, the

to appease the now collectivized peasantry as well as to solve the food-shortage problem, the government permitted and encouraged them to sell their surplus foodstuffs at competitive prices at authorized collective markets (*kolkhoznye bazary*).[36]

The small-change famine of 1930.—An interesting phenomenon occurred in 1930. In that year silver coins disappeared from circulation. N. P. Bruikhanov, then Commissar of Finance, gave the following explanation: [37]

> . . . Counter-revolutionary agitation exerted a certain influence upon the not very discerning elements of the city and village, which, ignoring paper money, demand silver coin exclusively in payment for their products, hiding it for speculative purposes. It is possible to cite numerous facts, uncovered by investigating officials, when silver coin hidden by private individuals was and is the subject of turbulent speculation. . . . *The causer of our present difficulties with small change is our class enemy.*

Explanations similar to the above are found in the works of a number of Soviet writers.[38]

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bread prices were increased 100 percent, to 54 and 104 copecks, respectively. In that year the prices per kilogram at the *closed* and *commercial* shops compared as follows (in rubles):

	Commercial Shop	Closed Shop
Black bread	2.00	0.54
White bread	3.00	1.04
Meat	10.00–12.00	2.00–4.00
Butter	30.00	6.00–8.00

Erich Wollenberg, "The Abolition of the Bread Cards in the Soviet Union." *The New International,*" a Monthly Organ of Revolutionary Marxism (New York), March, 1935, II, No. 2, 73-74.

[36] In 1934 one paid at these markets from 2 to 4 rubles for (approximately) a quart of milk, and one ruble per egg.—*Ibid.* Naturally prices fluctuated from time to time and varied from place to place.

[37] "Lack of Change is the Work of Counter-Revolutionary Elements," *Finance and the National Economy,* July 30, 1930, No. 20/21, p. 3.

[38] See, for example, F. Degtiarev, *About the Damaging Activities in the Financial System* (Moscow, State Finance Press, 1931), p. 25, who says: ". . . we all remember last summer's attempt on the part of kulaks, nepmen, speculators, and all other counter-revolutionary elements to create within our country a change crisis by means of purchasing and hiding small-change coins, circulating false rumors about the collapse of the Soviet monetary system, about the 'abolition' of money, and so forth. Not limiting themselves to this alone, counter-revolutionary elements inflated prices, aiming in that way to depreciate our ruble . . ." Or, B. Lebedev and V. Bliakher, *Is Money Needed in the Soviet Union?* (Moscow, State Finance Press,

It is not unnatural, of course, for a government to blame its enemies for whatever difficulties beset it. This, however, is not to say that the counter-revolutionary elements within the country and the enemies of the Soviet Union abroad did not spread (and for that matter continue to spread even today when the position of that country from every point of view is incomparably stronger than it was in 1930) false rumors. Nevertheless, it must be understood that there were more important factors at work. In 1929–30, it will be recalled, the already inflated paper currency underwent an extremely rapid further expansion, increasing within the course of one year from 2,642,000,000 to 4,263,000,000 rubles, or by 62 percent. Inasmuch as the physical volume of goods underwent no appreciable increase in the meantime, it was but to be expected that such an increase in the supply of rubles would result in a catastrophic decline of their purchasing power in the free market. That, as we have seen, was the case. But then it is not unusual that the people, already steeped in the vagaries of inflation, should, when in fear of a continued decline of the ruble's purchasing power, refuse to accept such money or prefer to retain the better money, in this case the silver coins possessing a certain intrinsic value. Metallic coins will, as a rule, disappear from circulation whenever inflation becomes discernible. This phenomenon need not surprise Russians; it took place in Russia on a number of occasions, in recent times under the Czarist government in 1914–15.[39] But it is by no means confined to that country alone; it happened on numerous occasions (under similar circumstances) in a good many other countries.

To combat the hoarding of silver coins the Soviet government first of all resorted to administrative measures. The following dis-

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1931), pp. 27-32, give the above causes and cite a number of other examples of attempts to ruin Soviet currency, such as those by *foreign* enemies to flood the Soviet Union with counterfeit chervontzy, the damaging activities by the Vladivostock branch of the Japanese Chosen-Bank (which was closed on December 13, 1930, by order of the Collegium of the People's Commissariat of Finance of the U.S.S.R.), which, it is alleged, carried on unlawfully exchange operations, speculative purchase and sale of chervontzy, and even issued its own banknotes on Soviet territory . . .

[39] See Chapter III.

patch to the *New York Times* of August 19, 1930, is particularly illuminating:

> Moscow, Aug. 18.—The four men put to death the other day by an OGPU firing squad in Moscow for hoarding gold and silver money and small change were accused of counter-revolutionary speculation . . . Some of them amassed as much as 5,000 rubles (about $2,500) in coins. In Kiev a woman peddler earning perhaps 2 or 3 rubles a day was arrested for having 800 rubles in small change, and a search throughout that town uncovered hoards of small change amounting to 30,000 rubles. In Moscow the directors of restaurants and stores were searched for possible hoarding . . . The money the government seizes in searches is immediately put back into circulation.

As the reader probably surmises, these measures failed to keep the metallic coins in circulation. Attempts were also made to replenish the withdrawn coins by newly minted ones. To relieve the shortage of small change, the government, however, found it necessary to resort to the issue of paper tokens ("bons").

Later on, by the decree of February 27, 1932, the government authorized the Commissariat of Finance to issue 10, 15, and 20 copeck coins made of *nickel*. These were to circulate on par with silver coins. Their low intrinsic value was certain to discourage hoarding.

The Soviet government, however, did not confine itself to those measures exclusively. As we have seen, it took steps to revise the Credit Reform of 1930, to improve planning, to improve relations with the collectivized peasantry, and to widen the supply of consumers' goods. All of which, it must be conceded, was well conceived and executed, and bore desirable results. In fact the policies pursued by the government during those years show unmistakably that it was not unaware of the real difficulties.

The question of whether there was inflation in the Soviet Union during 1928–34.—It has thus far been shown in this chapter that the years during which the First Five-Year Plan was in operation were marked by a serious expansion of credit and currency coincident with the employment of valuta-checks by the bank, and, in general, of measures to spread non-cash payments, by the raising of the legal ratio of treasury notes to banknotes from 50 to 100

percent, by the rise of prices, introduction of ration cards, and by the disappearance of metallic coins from circulation. It is not uninteresting to note the rather wide disparity between the official index of circulation during these years and the index based on retail sales (as measured in rubles).[40] Between October 1, 1928, and October 1, 1929, the total volume of currency in circulation expanded by 34 percent, the retail sales between 1927–28 and 1928–29 by only 13 percent. By October 1, 1930, the volume of the currency showed a 116 percent increase over that on October 1, 1928, whereas the retail sales in 1929–30 exceeded those in 1927–28 by a mere 19 percent.[41] These figures help to show why the situation became so critical in 1930. To continue the comparison: between October 1, 1928, and January 1, 1932, the currency expanded by 188 percent, while the retail sales of 1931 exceeded those of 1927–28 by 66 percent. The figure showing the volume of the currency on January 1, 1933, as we have seen, has not been published. It may be presumed, however, that between October 1, 1928, and January 1, 1933, the increase in currency amounted to from 193 to 246 percent; on the other hand, the increase in retail sales between 1927–28 and 1932 amounted to 141 percent.[42] Do these facts, derived from the officially published figures, point to inflation? According to Soviet opinion, NO. The following extract from an authoritative Soviet source is indicative of that trend of thought: [43] "Bourgeois newspapers are filled with calumnies relative to 'inflation' in the Soviet Union,

[40] See Table 62.

[41] From October 1, 1929, to October 1, 1930, the already expanded currency underwent a further increase by 62 percent, while retail sales in 1929–30 were only 5 percent larger than those in 1928–29.

[42] The two continued to come closer. Between October 1, 1928, and January, 1934, the currency expanded by 248 percent, while the retail sales in 1933 exceeded those in 1927–28 by 231 percent. By January 1, 1935, the volume of currency was 292 percent in excess of that on October 1, 1928, while the retail sales in 1934 exceeded those in 1927–28 by 314 percent. Assuming that the volume of treasury notes in circulation on April 1, 1936, equaled that of the banknotes, and that the total currency in circulation on that date, therefore, was 11,869,989,060 rubles, this would constitute a 500 percent increase over the October 1, 1928, figure, as against a 442 percent increase in retail sales between the years 1927–28 and 1935.

[43] *The Finances of the Three Years of the Five-Year Plan* (Moscow, State Finance Press, 1931), pp. 27-28; also Karl Elster, "Is There Inflation in the U.S.S.R.," *Financial Problems of a Planned Economy*, 1931, Nos. 1-2, pp. 81 ff.; also *The State Bank of the U.S.S.R. Economic Survey*, December, 1930, V, No. 20.

'flood' of paper money, and imaginary catastrophic 'fall' of the purchasing power of our ruble."

On what ground did Soviet economists and writers deny that there was inflation in the Soviet Union in those years? On the whole, on the ground that in a planned economy, where prices are fixed or controlled by the state and where the distribution of available commodities is arranged by the latter, according to plan, in such a way as to satisfy the needs of the toilers, there can be no inflation. The Soviet economists and writers in question did not define inflation, but, judging by the fact that they pointed to the almost stable official price index to prove their point, they apparently meant by it "a condition in which prices are, for non-commodity reasons, raised to an abnormal or excessive level." Naturally, when a state undertakes the distribution of goods and the rendering of services, and also fixes prices, the price level need not rise even though the increase in the volume of means of payment should outstrip that in the volume of goods and services. But, as we have already seen, under such a regime an excessive supply of means of payment leads to an unsatisfied effective demand for goods and services. Inflation there, in other words, takes a different form; there are "shortages" of all kinds, or "commodity famines." And this is why the present writer defined inflation as a *condition that is caused by an increase in the volume of purchasing power that is not accompanied by a corresponding increase in the volume of goods and services available for distribution.*[44] But no matter which of these two, or for that matter of any known, definitions of inflation are employed, the conclusion that inflation existed in the Soviet Union in 1928–33 cannot be avoided. After all, even if all other phenomena are ignored, it cannot be denied that the currency (and credit) did expand to an extraordinary degree, that the rate of its increase did outstrip the rate at which retail sales increased, that the demand for commodities by far exceeded their supply, and that prices did experience a pronounced rise, particularly of course, in the private sector.

It may be that in years to come Soviet writers and economists

[44] Chapter IX.

will admit that inflation did exist in the Soviet Union during 1928–33 and that the sacrifices made by the population were great, but will claim that such course was justifiable in view of the ends that it helped to achieve. However that may be, it is important to understand that inflation in the Soviet Union is fraught with less injustice and inequity than in capitalist countries. The rationing cards and the state and co-operative supply systems assure workers and employees at least a minimum of subsistence. Creditor-debtor gains and losses, which as a rule accompany our inflationary periods, have no significance under the Soviet system. Railroads and traction, gas, electric, and telephone companies are granted increases in rates as soon as their costs begin to mount. Should the ruble's purchasing power be threatened with extreme depreciation the government would no doubt, as it did during its early years of existence, insure savings against loss, and so forth. Still, inflation is not rendered harmless by the Soviet system. It may, if it occurs again (and if the rural economy is still *collectivized* rather than *factorized*), threaten the relations between the city and the village. It would certainly disrupt economic accounting, planning, and budget-making, and in that way interfere with the vital activities of the national economy.

The extent of the ruble's depreciation.—From time to time writers outside of the Soviet Union make attempts to estimate the extent of the ruble's purchasing power. Their estimates, however, vary widely. "While the average monthly wage of the Russian factory hand," Mr. Chamberlin says, "has increased between 1929 and 1933 from about seventy-five rubles to about one hundred and twenty-five rubles, his cost of living has doubled or trebled, even when one makes the most generous allowance for the fact that prices in his coöperative shop were controlled and therefore rose much less than prices on the free market." [45]

"Whether the Bolsheviki like it or not," writes Mr. Duranty, "this sum [i.e., the average wage of 125 rubles.—Author] will buy here in the open market no more than $3 will buy in America." [46] He adds, however, that ". . . it is true that the Soviet worker

[45] William Henry Chamberlin, *Russia's Iron Age* (Boston, Little, Brown and Co., 1934), p. 278. [46] The *New York Times*, February 4, 1934, p. 3 E.

receives rent, medical treatment, social insurance, and annual holiday and all forms of amusement, from theatres to ice hockey at a cost so low as to be negligible." It may be added, too, that the worker bought in the open market only those things which were not obtainable in the low-priced shops specially maintained for his benefit.[47]

Another interesting attempt to evaluate the ruble's purchasing power was made by Miss Alice Hughes in the *New York World-Telegram* of August 10, 1933. Carrying out all of her calculations in terms of American money, Miss Hughes proceeded to show that the value of the ruble fluctuated from 75 cents to zero. Thus, the legal rate of exchange of the ruble at that time, as fixed by the Soviet government, was 75 cents. In Constantinople, however, according to her, one could buy rubles at a little over a cent each (90 to the dollar). In Moscow rubles sold on the "black" exchange at 2 cents each; in Odessa the illegal rate was 70 to the dollar; in Kharkov, 45; in Kiev, 60. The internal purchasing power of the ruble (presumably in the open market) was equivalent to 4 cents. Finally, one could not get any American money whatsoever for the ruble upon presenting it at the State Bank.[48] But no matter how interesting this information may be, it fails to tell us what the real purchasing power of the ruble is.

Before the World War, when the principal countries were on the gold standard and governments did not unduly influence rates of exchange, these were reliable indicators of a currency's purchasing power. Even today, with certain exceptions, the rates as quoted on the foreign exchanges enable us to get an idea of a currency's buying power. But, as we have seen, the ruble is not quoted on the legitimate exchanges. That the official or legal rates of exchange which are set by the Soviet government have no bearing upon the ruble's purchasing power is obvious. But how about

[47] Mr. Duranty, however, did not engage, in this particular article, in a study of the ruble's purchasing power. See his articles in the *New York Times* of January 8, 1933, and of March 31, 1935, where he takes up that question.

[48] See also Mr. Peter Fleming's article in the *New York Times Magazine* of January 27, 1935, where he states that, although the legal rate is less than 6 rubles to the pound sterling, "the pound is worth anything from 200 rubles in Moscow to 300 in Vladivostok."

the "black" exchanges in the Soviet Union and abroad? Their rates were not at the time and are not now representative of the ruble's purchasing power. The speculator who bought dollars or other foreign currency in the Soviet Union during those years did so with a view to using them in illegitimate trade, such as contraband or the resale of commodities bought by him at the Torgsin stores (where goods used to be sold for precious metals, foreign currencies, or claims against them). Those who bought commodities from him did so either because they were not granted rationing cards (which were then in use) altogether, or because, having been granted such cards, they found it impossible to get the commodities they wanted, the quality they wanted, or the quantity they wanted in the low-priced state and co-operative "closed" shops.[49] In either case they expected to pay prices at least as high as those which prevailed in the open market. These prices enabled the speculator to make high profits, and that in turn influenced his valuation of foreign currencies. It may be said, of course, that his valuation of foreign currencies depended upon the prices which prevailed in the open market. Even so, those prices were not representative, inasmuch as the "closed" shops which satisfied so large a demand charged much less. It is for the same reason that direct conversions of Soviet prices into dollars, sterling, and other foreign currencies conveyed a distorted view of the ruble's purchasing power.

Apparently there is only one device left for measuring that purchasing power, a representative price index. But here we come upon insuperable obstacles. As has been seen, whatever usefulness as an indicator of the ruble's purchasing power the official price index possessed was lost by it when, beginning with October 1, 1929, it began to be based upon prices prevailing in the socialized sector exclusively. Besides, its publication terminated in 1931.

But why can we not construct a representative price index for those years ourselves? Because the extreme complexity of the Soviet exchange system during those years makes that quite impossible. Indeed, prices in the open market (i.e., in the "com-

[49] The "closed" shops and the ration cards had already passed out of existence. See the section following this.

mercial" stores and the peasant markets) were several times as high as those in the "closed" stores and distributing centers.[50] Besides, the "commercial" stores sold goods of a higher quality and had a larger and better assortment of goods. Nor are these the only difficulties. Although theoretically the fixed prices in all the "closed" stores and restaurants were held at any one time at about the same level (except for transportation and distribution costs), the purchasing power of one's ruble, paradoxically enough, depended upon the particular factory or office in which one worked, and to which the "closed" co-operative store or restaurant in question was attached. In some co-operative stores and restaurants, particularly in those well managed and attached to "important" factories or offices, one found a larger variety of commodities and of food and a much better quality than in others. The purchasing power of one's ruble, therefore, depended upon the particular "closed" store or restaurant with which one had to deal. Moreover, the better the "closed" store and restaurant the less one had to buy in the open market, where the purchasing power of the ruble was extremely low. As Mr. Duranty says: [51]

Suppose the recipient [of an average wage.—Author] is a worker in one of the large factories like the Amo Motor Plant. In this case he will be getting for his 125 rubles not much less material satisfaction than an American worker would get for $100. The Amo man will be able to rent two clean rooms for 10 rubles a month; receive good food at his factory kitchen, free medical and dental treatment and free education if he wishes it; buy clothing and household goods of fair quality and at extremely low price from his factory store, and have the use of the factory swimming pool, gymnasium and stadium.

Another man in a smaller factory may find that his 125 rubles have a buying power equivalent to only $10 or $15 in America. Perhaps

[50] See *Banking and Credit in the Soviet Union* (School of Slavonic and East European Studies in the University of London), February, 1935. Monographs Nos. 4-5, pp. 12-14. When the "commercial" shops were first opened, their prices are said to have been as much as 30 times higher than those in the "closed" shops. The prices in the "commercial" shops, however, kept on declining, while those in the "closed" shops kept on rising, so that by the end of 1934 the former were probably only 5 to 10 times as high as the latter. Supply and demand, which constituted an important factor in the open market, it will be noticed, played an insignificant part in the fixing of prices for goods sold in the "closed" shops. The latter prices were composed of the following elements: cost of production, transportation and distribution costs, fixed profit, and the government turnover tax.

[51] The *New York Times Magazine*, March 31, 1935.

the food in his factory kitchen is poor and needs to be supplemented by purchases on the open market where butter, for instance, costs 20 to 30 rubles a pound. He may be unable to get clothing and household goods from his factory store, and so again be forced to supplement them by purchase at excessive "free market" rates. In short, one frequently finds the paradox here that a man who earns 500 rubles a month is worse off than some one at another factory who earns one-fifth of that salary.

Present position of the ruble.—The important gains on the agrarian front (due to the progress made by the national economy as a whole, to the improved technique and organization in agriculture, as well as to the legalization of "collective farmers' markets") paved the way for the abolition of rationing cards. Steps in that direction were taken on November 26, 1934, by the Plenum of the Central Committee of the All-Union Communist Party when it resolved to deration, beginning with January 1, 1935, bread, flour, and grits. Henceforth, these products were to be sold by the various state and co-operative stores to all at uniform retail prices (varying, however, in the different sections of the country).[52] The price paid at the time by those having rationing cards was 48 copecks for a kilogram (2.2 pounds) of black bread, and one ruble for a kilogram of white bread.[53] In the open market the prices for black and white bread were 2 and 3.5 rubles, respectively. To stimulate the peasant to greater efforts it was decided to raise the prices theretofore paid him by the state supply agencies for grain and other products. This necessitated the fixing of the new selling prices of bread and other products at a considerably higher level than that prevailing in the "closed" stores. To compensate the consumers for this rise in the cost of living it was decided to raise the wages paid to workers and employees, the stipends granted to students, the pensions, and so forth. This resolution was translated into law by the decree of the Council

[52] *Economic Life,* November 29, 1934.

[53] Those having cards could buy in these stores a maximum of 800 grams (slightly in excess of one and three-quarters pounds) a day, if they were classed as workers, and 400 grams (seven-eighths of a pound) if classed as employees. The rations were considerably smaller during lean years (1932–33). Some 55,000,000 depended on these rations.

of People's Commissars of December 7, 1934.[54] The new prices were fixed, depending upon the particular region of the country, at from 80 copecks to 1.5 rubles for a kilo of black (rye) bread; 90 copecks to 1.6 rubles for the cheaper variety of white (wheat) bread, and from 1.2 rubles to 2.8 rubles for a kilo of the better quality white bread.[55]

On September 25, 1935, the Council of People's Commissars decreed the derationing, beginning with October 1, 1935, of meat and its products, butter, vegetable oils, fish and its products, sugar, and potatoes. By January 1, 1936, the rationing system and the "closed" shops became largely a thing of the past. On February 1, 1936, too, the Torgsin system of stores, where goods were being sold for precious metals and foreign currency, terminated their existence. Henceforward all living in a given region, whether they were high officials, workers, or priests, were to pay the same prices for commodities with no restriction (provided, of course, one was not a speculator) as to the quantity purchased. As in the case of the products derationed earlier, the prices of commodities derationed since October 1, 1935, were fixed at a level considerably higher than the former ration prices. On the whole, they were fixed at a point approximately midway between the ration prices, or prices charged by "closed" shops, and those which were charged by "commercial" shops. In the meantime, however, the volume of consumers' goods kept on rising. This, together with the deflationary policy adopted by the Soviet government in recent years, served to protect and strengthen the purchasing power of the ruble.[56]

[54] *Collected Decrees*, 1934, Decree 445.

[55] The lowest prices (80 copecks for black bread and 90 copecks for white) were fixed for Central Asia. The highest, for the Far East. In Moscow the prices were fixed at one ruble per kilogram for black bread and one ruble and ten copecks for white.

[56] See, for instance, G. Neiman, "The Abolition of Cards, the Unfolding of Trade, and the Strengthening of the Ruble," *Economic Problems* (*Problemy Ekonomiki*), 1935, No. 1, p. 55, where he shows that the doubling of trade turnover by "commercial" stores in 1934 (from 6,300,000,000 rubles in 1933 to 13,000,000,000 rubles in 1934) was accompanied by a lowering of prices of a number of commodities: sugar by 50.2 percent; confectionery products, 10.9 percent; soap, 23.7 percent; cotton thread, 30 percent; butter, 14 percent, and so forth. The widening of "commercial"

The discontinuance of the "closed" shops and of the Torgsin stores makes possible the construction and publication of a reliable price index. Only such an index can give a correct view of the ruble's purchasing power.

The nature of Soviet money and the present monetary policy.— In the preceding pages we have dealt with a puzzling currency. What is its real nature and function? Many attempts have been made to answer that question, both outside the Soviet Union and within it.

Writers outside the Soviet Union from time to time refer to the paper ruble as an "internal currency" meaning by the term that it is not employed in international settlements. Although constituting a correct observation this description deals merely with one characteristic of the ruble. It does not tell us whether the Soviet monetary unit differs in any other respect from "capitalistic" monetary units.

Here and there the paper ruble is referred to as a currency "without value." If by this is meant that the paper ruble is inconvertible and that it has no *intrinsic* value, it is at best a careless expression. Of course, the paper ruble has no intrinsic value; no paper money possesses such value. It cannot be denied, however, that the paper ruble has exchange value. It was to such

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trade and the lowering of prices there served to exert pressure on prices in the peasant market. The price of bread there declined in 1933 by 60 percent, and from January to October, 1934, by an additional 18 percent. The 1934 average of prices of eleven most important food products in that market declined by 31.5 percent as compared with the 1933 average. Prices continued their decline in 1935. See, for example, *Economic Life* for April 10, 18, and 24, for May 28, for June 12, and for July 5, 1935. As reported by the correspondent of the *New York Times* (in its issue of July 28, 1935), open-market prices in the Soviet Union underwent the following decline in 1935 (in rubles):

	FEBRUARY, 1935	JULY, 1935
Pork (kilo)	12 to 20	9 to 18
Beef "	11 to 14	9 to 14
Butter "	26 to 29	24 to 27
Women's coats	271 to 470	230 to 400
Woolen dresses	244 to 484	200 to 350
Men's suits	425	220

And as the correspondent adds, "Reductions on textiles, household utensils, and in fact on consumer goods in general are on the same scale."

observers that Stalin addressed himself at the Joint Plenum of the Central Committee and of the Central Control Commission of the Communist Party on January 7, 1933: "How can it be maintained," asked Stalin, "that our Soviet currency does not represent any value? Is it not a fact that with this currency we built Magnitostroy, Dneprostroy, Kuznetzkstroy, and the Stalingrad and Kharkov tractor plants, hundreds of thousands of collective farms, and thousands of state farms? Were these enterprises all built with straw or clay, and not with real materials of definite value?"

In a continuation of this speech Stalin answers those who assert that the value of the paper ruble is determined by the ratio between the total volume of paper money in circulation and the gold reserve. "How is the stability of Soviet currency secured," asks Stalin, "if one has in mind, of course, the organized market, which is of decisive importance in the trade turnover of the country, and not the unorganized market, which has but a subordinate part? Certainly not by means of the gold reserve alone. The stability of Soviet currency is secured, first of all, by the tremendous volume of commodities in the hands of the state and placed in circulation at stable prices. What economist can deny that such security, which exists only in the Soviet Union, is a more real security for the stability of currency than any gold reserve? . . ."

Indeed, the gold reserve of the Soviet Union, in view of the peculiarities of its system with which we are already familiar, has practically no direct influence upon the purchasing power of the ruble. Of course, it can influence it indirectly, if a part of it is used to buy consumers' goods abroad; or, in an even vastly more important way, through the effect which it may have upon foreign lenders of long-term credit. Such credit would no doubt enable that country to pursue a more conservative monetary policy and that, of course, would enhance the buying power of the ruble.

Another characteristic that is frequently bestowed upon Soviet currency by writers and lecturers outside of the Soviet Union is that it is a managed currency. In a sense, this is true. All phases

of the national economy are "managed" or planned in the Soviet Union, and Soviet currency is no exception. It will be remembered, though, that this term has a special meaning. In recent years it has been applied to a monetary standard proposed in 1923 by John Maynard Keynes.[57] Under the proposed plan a nation's monetary system would take the form of an inconvertible paper standard. Unlike, however, the "old" ill-reputed paper standard, which, generally, comes about unwanted as a result of some major upheaval or catastrophe, the new paper standard would be "controlled" or "managed" with a view to maintaining internal prices at a specified level.[58] To accomplish this the central bank would so regulate its rediscount rate and open-market operations, and the treasury, the note issue and the volume of its short-term obligations (which can be regarded as "cash at one remove") as to bring into creation a volume of means of payment that is no smaller and no greater than that needed to produce the desired results.[59] The price index would serve as a guiding beacon. Managed currency, in fact, is defined as "an irredeemable currency in which prices are kept at a specified level or near it by manipulation of the conditions of creation, and quantity allowed to be

[57] *Monetary Reform* (Harcourt, Brace and Co., 1924), Chapters IV, V.

[58] Although gold coin, under this plan, is not be to employed in circulation and a gold reserve against notes is not needed, gold would continue to play a rather important rôle. It would be used for the purpose of settling international balances of payments, to prevent inordinate fluctuations of exchange rates, as well as to serve as an "ultimate safeguard and a reserve for sudden requirements." The bank's buying and selling price of gold would take the place of the par of exchange and the limits set by the "gold points."

[59] Mr. Keynes's plan for a "managed currency" is related to Professor Fisher's "compensated dollar." The latter, it will be recalled, is a plan "to substitute a gold dollar of varying weight and fixed purchasing power for a gold dollar of fixed weight and varying purchasing power." This, Professor Fisher believes, can be done by increasing or decreasing the weight of the dollar (or by raising or lowering the price of gold bullion) in "exact proportion to the deviations above or below par of the index number of prices." It is essentially a "managed currency" that Professor Fisher proposes. But whereas under his plan the management is to be largely automatic (i.e., the exact extent of the increases and decreases of the weight of the monetary unit is to be governed by the position of the price index and not by the judgment of any official), that under Mr. Keynes's plan calls for the exercise of judgment on the part of appointed or elected officials. See Irving Fisher, *Stabilizing the Dollar* (New York, The Macmillan Co., 1920), *passim;* also his *The Purchasing Power of Money, Its Determination and Relation to Credit and Interest* (New York, The Macmillan Co., 1926), pp. 494-502.

issued, of bank credit." [60] But how can this concept be applied to an economy where prices are *regulated,* where index numbers of prices are the results of such regulation rather than the result of a manipulation of credit and currency, where the discount policy of the bank is not meant to serve as a regulator of credit, where "open-market" operations (sale of government bonds to the people) have an entirely different purpose, where credit and currency are influenced by plans of production, and therefore play a subordinate rôle? In fact, a system of regulated prices can be said to be diametrically opposed to a system of "managed currency." The lowering of prices would create a phenomenon similar to that of an increase in the means of payment, and the raising of prices would, conversely, create a phenomenon similar to that of a decrease in the means of payment. It appears, therefore, that the term "managed currency," which was meant to apply to a controlled currency of a country whose economy otherwise is not covered by plan, is ill-suited to describe the Soviet system of currency. That currency can be best described by the term "planned currency."

Of far greater interest to us, however, is the *Soviet* philosophy of the nature of the ruble, of its rôle and functions. Upon that philosophy, upon that attitude, more than upon anything else, depends the future of the ruble. The Soviet philosophy with respect to the nature of the ruble, as we have seen, did not remain stationary. As the national economy would enter a new "phase," economists and statesmen, depending on whether they thought they stood closer to socialism or to capitalism, would formulate "appropriate" theories. It will be recalled, for example, that during the period of War Communism, when the communists believed that they were ushering in communism pure and simple, money was looked upon as a dying institution. It was during this period that the very word "money" became officially replaced by the more pleasing term "settlement or reckoning tokens," [61] which

[60] H. P. Willis, J. M. Chapman, and R. W. Robey, *Contemporary Banking* (New York, Harper and Brothers, 1933), p. 771.

[61] The populace, which was less sophisticated but more realistic, preferred to call the "millions" which they were handling "lemons" (in Russian millions is "milliony" and lemons is "limony").

was to emphasize the conviction that money as such has no place in a communist society. Whether the Commissar of Finance at the time, Gukovsky, was serious or not, there was no less meaning in his statement before the First Congress of the Soviets of National Economy that "Finances are not supposed to exist in a socialist society, and I, therefore, beg to be forgiven for their existence as well as for my appearance here," than in that of Larin and other economists to the effect that the closer the ruble's purchasing power was to zero, the better. The same philosophy underlay those ideas. It may also be recalled that an influential group of economists and financiers was at the same time busily engaged in discussing and perfecting a plan to replace money with *treds* (*labor units,* or a labor standard of value).

To save the country from ruin it became necessary to resort to a new economic policy and to reintroduce private trade. Hence Strumilin's project of the *tred* had to be scrapped. Private trade meant, of course, the circulation of commodities (as against a direct exchange or distribution of products). The change to a "commodity form" of economy compelled a revision and change of the attitude, for the time being, towards the institution of money. As expressed by A. Leontiev: "Currency circulation is directly bound up with the commodity form. More than that, the monetary form is in reality nothing but the obverse side of the commodity form. Therefore, so long as the commodity form continues to exist, the monetary system must be retained." [62] It was a philosophy such as this that was instrumental in the re-establishment of banks and currency. The term *settlement tokens* was thrown away, its place being taken by *money tokens.* "Stabilization of currency," and not "abolition of money" began to agitate Soviet minds.

Soviet experts, too, perceiving the new phase of economy to have a "capitalistic" form, and that Soviet currency resembled very closely capitalistic currency, decided to tie the chervonetz to gold. Commissar Sokolnikov, for example, who was so instru-

[62] "On the Characteristics of a Monetary System in a Transitional Economy," *Socialist Economy* (Sozialisticheskoye Khoziaistvo), 1927, II, 55; also *The Works of the Moscow Comrade Kaganovich Finance-Economic Institute* (State Finance Press, 1934), II, 73.

mental in effecting the Monetary Reform, in a polemic with Strumilin over the adoption of a gold base for currency, declared: "Would it not be better, though, to recall the ABC of the Marxian theory of money and admit that we, Soviet Russia . . . cannot reject the laws that are peculiar to a commodity economy of currency circulation, inasmuch as we have entered upon a *commodity economy.*" [63] And, again, ". . . in a developed commodity economy it is *gold* that is *money;* all other currencies perform their functions of money only to the extent to which they *represent* (or *substitute*) *gold.*" [64] Impressed by the "capitalistic" or rather "state capitalistic" forms of development of the Soviet economy in general and currency in particular, Sokolnikov was not averse to permitting a close relationship between Soviet Russia's and world prices. It was doubtless with a view to this that he counseled a change in the system of foreign trade "in the direction of greater elasticity, in the direction of abolishing the absolute character of the monopoly of foreign trade." [65]

At the XIV Congress of the All-Union Communist Party in December, 1925, Sokolnikov proceeded to center attention upon the capitalistic nature of Soviet institutions:

> Our foreign trade is conducted like a state-capitalistic enterprise . . . Our domestic trading companies are also state-capitalistic enterprises. And I must also say, comrades, that the State Bank is just as much a state-capitalistic enterprise . . . Our monetary system . . . under conditions of the developing socialism . . . is permeated with principles of capitalistic economies . . . And the problem in all of those branches is to organize the economy—under conditions of a dictatorship of the proletariat—in such a way that there should take place an increase of socialistic elements, that there should take place a building of socialism.[66]

But before the XIV Congress came to a close, Sokolnikov's

[63] "The Stable Ruble and the Unstable Strumilin," *Pravda,* June 9, 1922.

[64] "A Commodity Index or a Commodity Ruble?" *Economic Life,* December 8, 1922. The emphasis, throughout, is his.

[65] Report to the Second All-Russian Congress of Finance Representatives in October, 1922. Reprinted in his *Financial Policy of the Revolution,* I, 246 ff., particularly 262-63.

[66] *Stenographic Report of the XIV Congress of the All-Union Communist Party* (State Press, 1926), p. 235. These views were made public by Sokolnikov, in fact, as early as December, 1921. See for instance his article "Proletarian Power and Banks" (*Financial Policy of the Revolution,* I, 281).

views were denounced there by Stalin. Why does Sokolnikov make such mistakes, asked Stalin, and answered:

> Because Comrade Sokolnikov does not understand the dual nature of the Nep, the dual nature of trade under the present conditions of the struggle between socialistic elements and capitalistic elements, he does not understand the dialectics of development in the setting of a dictatorship of the proletariat, in the setting of a transitional period, where the methods and weapons of the bourgeoisie are used by the socialistic elements with a view to overcoming and liquidating the capitalistic elements . . .[67]

Stalin's philosophy that the Nep, which brought with it familiar capitalistic institutions, constituted in reality an attack upon capitalism was apparently ill understood or, if understood, was not shared by certain economists. Such well-known economists, for example, as Yurovsky and Bronsky, not to mention a number of others, apparently continued to assume that the development of capitalistic institutions in the Soviet Union was an end in itself. It was probably due to this idea that they proceeded to advise adherence not only to a gold standard "such as is used by the most developed modern capitalistic countries," [68] but also to the "capitalist" laws of value.[69] Bronsky, despite the qualifications that he makes and his frequent and sympathetic references to socialism and planning, appears to have sought for the Soviet monetary system conditions which would enable it "to fulfill the functions of the law of value, and to serve as a regulator of the national economy with a fixed purpose of establishing an 'equilibrium' in the national economy." [70] Among the conditions necessary for that he enumerated the gold standard as a link to world prices and "freedom of price formation," that is a state of affairs under which

[67] *Loc. cit.*, p. 496.

[68] Bronsky in *Socialist Economy*, 1928, III, 18.

[69] Although he spoke of such economists as Yurovsky as "economists who sincerely and honestly study given problems with a view to helping the state, but who cannot rid themselves of the traditional ideology on which they were brought up and nurtured and adopt the ideology of the revolutionary class . . ." (*Ibid.*, p. 7), Bronsky himself was apparently afflicted with the same malady. See V. P. Diachenko, "The Right-Opportunistic Theories of Soviet Money," in the *Works of the Moscow Comrade Kaganovich Finance-Economic Institute*, II, 54-95.

[70] *Socialist Economy*, 1928, III, 14.

prices are formed as a result of the interaction of supply and demand. To readers in capitalist countries such philosophy may appear thoroughly sound. The communists, as we have seen, consider it dangerous, inasmuch as it contains a veiled attempt to destroy or weaken the institution of planning and threatens to retard (by tying up unproductively large reserves of gold) socialist construction. From a purely theoretical point of view the communists regard this, if one may paraphrase Engels, as even worse than an attempt to apply the same economic laws to Tierra del Fuego and to England.

The inauguration of the First Five-Year Plan and the attendant intensification of planning, the rationing system, the "closed" shops, the rapid collectivization of the peasantry, and the drive against private trade made it clear that the economy of the Soviet Union entered a new phase. The "closed" distributing centers, the varying price levels compelled one to notice the difference between Soviet trade and capitalistic trade. And, as if to emphasize this, when the People's Commissariat of Trade was reorganized towards the end of 1930, the two resulting Commissariats were named: the People's Commissariat of Foreign Trade and the People's Commissariat of Supplies.[71] The word "trade" was preserved only in the case of the Commissariat dealing with the *outside* world. The changes above-mentioned also compelled a reappraisal of the nature of Soviet banks, credit, and money under the new conditions. With the results of that attempt in the field of banking and credit we are already familiar. Inasmuch as the philosophy developed by the well-known economist, Preobrazhensky, in his article dealing with the economic nature of Soviet money and the perspectives of the chervonetz became the backbone of the "leftist" ideology, let us get acquainted with it.[72]

The evolution of Soviet money under the Nep, Preobrazhensky believes, can be divided into two periods:

[71] In 1934, when the attitude and policy towards trade was already quite different, the latter was divided up into two separate commissariats: (a) the People's Commissariat of Domestic Trade of the U.S.S.R., and (b) the People's Commissariat of Food Industry. *Collected Decrees*, 1934, Decree 313.

[72] *Under the Banner of Marxism* (Pod Znamenem Marxisma), Moscow, 1930, No. 4.

First, the period of a temporary approach of our money, mainly in form, but partly also in substance, towards paper money and inconvertible banknotes of capitalistic countries.

Second, the period of development in our economy of elements, which were to turn this process in a different direction, namely, in the direction of a certain original transformation of our money into something new, which simultaneously is money in the ordinary sense and is not.

According to Preobrazhensky, therefore, the development of socialistic elements in the Soviet Union caused Soviet money to cease being money. This naïve idea was no doubt the product of such peculiar phenomena of that day as the "closed" shops and the *varying* price levels.[73] Another economist, A. Maimin, for example, was led by the same phenomena to the conclusion that the principal characteristic of Soviet money is its varying (at the same time) purchasing power, an explanation which his critics dubbed "the theory of the multifaced ruble." But as has been said before, it was Preobrazhensky's theory that became the foundation stone of the "leftist" ideology. As seen by the "leftists," money is money when it circulates in the "private sector," but when it circulates in the socialized sector it stops being money and becomes "settlement tokens" or "orders." Since the socialized sector, under the guidance of the First Five-Year Plan was rapidly expanding, the fate of money, according to them, was sealed. It was but a step from this philosophy to another, namely, that if money is to disappear, why not issue more of it at once so as to endow the state with larger resources . . .[74] And, of course, nothing was to be done to stimulate or to develop trade, for the economy of the country, as they believed, was entering a phase of socialism where the direct distribution of products would prevail.

The leaders became alarmed at the spread of such dangerous views. The December, 1930, Plenum of the Central Committee

[73] That is, the ruble's purchasing power in those days depended upon its holder's status, and whether or not he had access to *desirable closed* shops.

[74] See B. Lebedev and V. Bliakher, *Is Money Needed in the Soviet Union?* (Moscow, State Finance Press, 1931), pp. 15, 18-25; also A. Maimin, *For a Marxist-Leninist Theory of Soviet Economics and Finances* (Moscow, State Finance Press, 1932), pp. 21 ff.; also P. Perlstein and N. Nikitin, "On the Problem of the Nature of Soviet Money," *Economic Problems (Problemy Ekonomiki)*, 1933, No. 3, pp. 125-56.

and of the Central Control Commission of the Party resolved "to strengthen the chervonetz and to wage a decisive fight against the underestimation of the rôle and significance of the financial system at the present stage of socialist construction." A little over a year later, in February, 1932, the XVII Party Conference laid particular stress in its resolutions upon the anti-bolshevist character of the "leftist" phrases concerning the transition "to a system of direct exchange of products" and the "fading out" ("otmiranie") of money "already at the present stage of socialist development." It also stressed, among other things, the importance of developing trade, especially retail trade, and the importance of adhering to business principles.[75] The XVII Party Conference did not, of course, relinquish hopes of achieving socialism. As the Commissar of Finance, Grinko, expressed it, "The dialectic of our progress lies in the fact that the sooner we organize our present monetary system on a sound basis, and the more we do to stabilize our chervonetz, the sooner will the work of building up the socialistic society be accomplished and the sooner will it be possible to throw our inheritance into the scrapbag of history." [76]

As we already know, in order to improve the living conditions of the masses the Soviet government legalized and encouraged trading by peasants in the so-called *collective* (*kolkhoznye*) markets, proceeded to develop "commercial" stores, and so forth. Apparently, regarding this as a retreat towards capitalism, as a Neo-Nep, so to say, a good many communists, even non-leftists, disdained it. In this connection Stalin's report to the XVII Party Congress, which was held from January 26 to February 10, 1934, is most illuminating and significant: [77]

As you see, development of Soviet trade is an urgent problem without the solution of which further progress is impossible.

Nevertheless, although this truth is perfectly obvious, the Party

[75] See G. F. Grinko, *Soviet Finances on the Borderline between Two Five-Year Plans* (Moscow, State Finance Press, 1932), pp. 7-19.

[76] This translation of an excerpt from Grinko's speech was adapted from Malcolm Campbell's chapter on "Money, Credit, and Banking" in *Red Economics*, Gerhard Dobbert, ed. (Boston, Houghton Mifflin Co., 1932), p. 157.

[77] *Stenographic Report of the XVII Congress of the All-Union Communist Party* (Moscow, Party Press, 1934), p. 26. The present translation was adapted from the *Moscow News* of February 3, 1934.

had to break down, during the period under review, many obstacles in the way of developing Soviet trade which could be briefly formulated as a result of distorted thinking by some Communists on questions pertaining to the necessity and importance of Soviet trade.

To begin with, among some Communists an extremely supercilious attitude towards trade in general, towards Soviet trade in particular, still prevails. These Communists (excuse the expression) regard Soviet trade as something of secondary importance, something which is hardly worth while, and the people engaged in trade as people done for. These people obviously do not understand that by their snobbish attitude towards trade they do not express Bolshevik views but the views of sickly aristocrats with big ambitions but deprived of ammunition. (Applause.) These people do not realize that Soviet trade is our own Bolshevik business and that those engaged in trade, including people working in stores, if they only work honestly, are performing our revolutionary Bolshevik work. (Applause.) It is clear that the Party had to give these (excuse the expression) Communists somewhat of a hiding and to throw their aristocratic prejudices into the rubbish heap. (Prolonged applause.)

It was further necessary to break down prejudices of another nature. I have in mind the leftist prattle current among some of our people to the effect that Soviet trade is a stage which we have already passed and that it is now necessary to proceed with the organization of direct exchange of products, that money will soon be abolished as it has allegedly already become a mere means of accounting, that there is no sense in developing trade once direct exchange is knocking at our doors. It should be observed that this leftist, petty-bourgeois prattling, which plays into the hands of the capitalist elements seeking to obstruct the development of Soviet trade, is current not only among certain Red Professors, but also among people working in the trading system. It is of course ridiculous and funny that these people who are incapable of organizing the simplest business of Soviet trade should prattle about being ready to organize the more complicated and more difficult business of direct exchange. But Don Quixotes are Don Quixotes because they have not the most elementary inkling of life. These people who are as far from Marxism as heaven from earth apparently do not understand that we shall continue to have money for a long time until we achieve the first stage of communism, the socialist stage of development. They do not understand that money is an instrument of bourgeois economy which the Soviet Government has taken into its hands and adapted to the interests of socialism in order to give full vent to the development of Soviet trade and thereby prepare the conditions for direct exchange of products. They do not

understand that direct exchange can come only to supplant, and as a result of an ideally organized system of Soviet trade, something which we are far from having and which we shall not have so very soon. Naturally, the Party, aiming to organize extensive Soviet trade, has deemed it necessary to give the "Left" cripples a drubbing and blow their petty-bourgeois prattle to the winds.

It means that the Communist Party and the Soviet government are determined to follow a sound monetary policy and to crush those who would hinder it. The recent marked improvements are the outcome of that determination.

Revaluation of the ruble.—It will be recalled that in 1924 the Soviet Union stabilized the ruble at its pre-war mint parity, and that it was criticized at the time for this on the ground that the internal price level was too high to justify such step. Foreign trade being a state monopoly, the government had no difficulty in maintaining the officially fixed rates of foreign exchange. Also, these rates had no influence upon the internal purchasing power of the ruble, inasmuch as prices in the Soviet Union, even though influenced by the interaction between the supply of and the demand for goods and services, are planned and regulated by the state.

Since foreigners living or sojourning there were required to exchange their currency for paper rubles at the high exchange rates fixed by the government, and since the price level kept on rising, the government, to stimulate tourist travel, introduced, beginning with 1931, a different system. Under the new system foreigners paid in their own currencies at the official rate of exchange in the Torgsin shops, where goods—though quoted in rubles —were sold exclusively for precious metals and foreign currency, and in the hotels specially provided for them. Inasmuch as paper-ruble prices in "commercial" stores were considerably higher (at times tenfold) than those in the Torgsin stores, there developed a lively trade on the "black" exchanges where paper rubles were being sold and bought at rates far below those fixed by the government.

But, as we have seen, improving conditions enabled the government in 1935 to deration commodities and to do away with

the "closed" shops. To make prices more uniform and to eliminate speculation, the government by its decree of November 14, 1935, ordered the liquidation of Torgsin stores, beginning with February 1, 1936. Inasmuch as the paper-ruble price level was several times higher than that of the Torgsin stores, it again became necessary to make some provision for foreigners. Hence, the same decree which provided for the liquidation of the Torgsin stores also declared that "in order to develop tourist traffic in the U.S.S.R. and to attract foreign exchange," the State Bank was permitted to exchange in 1936 foreign currency (transfers or cash) for chervontzy at a rate of 1 French franc = 33⅓ copecks, or 3 francs = 1 ruble, with a corresponding adjustment for other currencies. France at the time being practically the only gold-standard country, the franc was chosen as the yardstick for conversions.

The decree of November 14, 1935, applied, however, only to foreigners within the Soviet Union, it did not apply to foreign trade. It was only on February 29, 1936, that the Council of People's Commissars instructed the Commissariat of Foreign Trade, the Commissariat of Finance, and the State Bank to apply, beginning with April 1, 1936, the rate 1 ruble = 3 francs to all transactions involving export and import organizations, and, in general, all transactions involving foreign exchange. Furthermore, the State Bank was instructed to revalue as of April 1, 1936, all its gold holdings and foreign exchange on the above basis.[78] Accordingly in its balance sheet of April 1, 1936, fine gold was valued at 5.6807 rubles per gram (as against 1.29 rubles per gram before); dollars, at 5.06 rubles (as against 1.15 rubles before); and sterling, at 25.04 rubles (as against 5.67 rubles before).[79] This amounted to a devaluation of 77.5 percent. In view of the fact that on October 1, 1936, the gold content of the franc was lowered from 65.5 milligrams to from 43 to 49 milligrams (9/10 fine), the Soviet government changed the rate to 1 ruble = 4.25 francs.

Considering the overvaluation of the ruble and the world-wide devaluation policy of recent years, as well as the fact that on October 1, 1935, the State Bank's firm cover constituted but 20.1

[78] *Collected Decrees*, 1936, Decree 86.
[79] See Table 60.

percent of the note issue (as against the statutory 25 percent), and that between October 1, 1935, and April 1, 1936, the issue jumped from 4,998,500,000 to 5,935,000,000 rubles,[80] this was no doubt a wise step. The ruble, however, is still overvalued. But then it must be borne in mind that the Soviet government is bending its efforts towards the lowering of the price level, and so towards the raising of the ruble's purchasing power.

[80] See Table 63. By July 1, 1936, there followed a further increase to 6,535,991,510 rubles. Assuming that the volume of treasury notes outstanding equaled the above amount (as in the past), then the total currency in circulation on July 1, 1936, stood at about 13,000,000,000 rubles.

XV

THE PRESENT SYSTEM OF LONG-TERM INVESTMENT INSTITUTIONS

The reorganization of the special banks.—We have seen that during the early part of the Nep the Soviet Union tried to find ways and means to finance industrial rehabilitation and expansion. Since foreign long-term credit was unavailable and attempts at home to raise such credit by borrowing directly from savers or through the specially created long-term credit banks failed, different methods had to be employed. Through its policy of price regulation or control of the spread between the cost of produced or sold goods and their selling prices, the Soviet government helped industry and trade to create surpluses ("involuntary savings," so to say) which the latter were required to set aside for capital construction, or which were taken away from them in the form of taxes and then redistributed by the budget. For example, during the six years beginning with 1922–23 and ending with 1927–28 the capital investments (including capital repairs) in industry and electrification were slightly in excess of 4,500,000,000 rubles. The net profit of industry during this period amounted to 2,865,000,000 rubles and the budgetary grants to industry, to 1,859,000,000 rubles.[1] The expansion of working capital was carried out by means of credit borrowed from the banks.

The very limited resources of the special banks, which were then in the process of development, were formed mainly at the expense of the budget. For example, on October 1, 1927, before the Bank for Long-Term Crediting of Industry (B.D.K.) was formed, the combined capital and special funds of the Electrobank, Central Agricultural Bank, and Central Municipal Bank (Tzekombank) together amounted to 820,000,000 rubles, of which 365,000,000 rubles, their statutory and reserve capital almost in

[1] See articles on the financing of Soviet industry by A. Segal in the *Vestnik Finansov*, 1928, No. 4, and in *Finance and National Economy*, 1927, No. 42 (50); also G. Tochilnikov, *Finances and Industrialization* (Moscow, State Finance Press, 1929), pp. 64-70. The reserve for depreciation set aside by industry during those years amounted to 1,625,000,000 rubles.

its entirety, was contributed by the budget, and another 352,000,000 rubles, their special funds, were borrowed from the budget and the State Bank. On that date they had altogether some 3,500,000 rubles of time and an equal amount of demand deposits.[2] In other words, even in those days the special banks served as appendages to the budget.

The policy of industrializing the Soviet Union rapidly enough so that within the shortest possible space of time it would catch up with and overtake the level of industrialization attained by the most advanced countries of the world called for an outlay of billions of rubles for the capital expansion of the various branches of the national economy, principally, however, of the "heavy" industries. It will be recalled, that under the First Five-Year Plan the country raised a total of 120,100,000,000 rubles of which 80,200,000,000 rubles was used for financing the development of the national economy. Of the latter amount 52,400,000,000 rubles was used for capital investments, and the rest, to provide working capital and to meet the "operating" expenses, as well as the expense of "acclimatization," of new enterprises.

The importance of the budget in connection with raising and redistributing funds under the First Five-Year Plan becomes patent when it is recalled that of the 120,100,000,000 rubles directed into the national economy during that period, the state budget redistributed a total of 72,800,000,000 rubles (60 percent), and that together the state and local budgets redistributed about 82,000,000,000 rubles (or 69 percent of the total).

The importance of the budget as a source for the financing of capital construction became especially accentuated beginning with 1931. Between that year and the beginning of 1935 the capital investments in Union industry amounted to 57,500,000,000 rubles of which 46,700,000,000 rubles (or about 80 percent) was advanced by the budget.[3]

[2] S. Rubinshtein and I. Tzypkin, *Financing and Crediting of Capital Investments*, Soviet Credit, Pt. III (Moscow, State Finance Press, 1933), p. 13.

[3] See G. F. Grinko's report to the First Session of the C.E.C. of the U.S.S.R. of the VII Assembly, *Economic Life*, February 9, 1935; also his report to the Third Session of the C.E.C. of the U.S.S.R. of the VI Assembly, *Stenographic Report* (Moscow, Tzik Press, 1933), Bulletin 11, pp. 22-23. The budgetary financing of the capital investments of the Commissariat of Heavy Industry amounted to 87 percent; of Light Industry, 60 percent; of Forestry, 84 percent; of Food Industry of the

With the part that the long-term credit banks were expected to play under the First Five-Year Plan we acquainted ourselves in Chapter XII. In view of the fact, however, that the actual investment of funds differed substantially from the planned figures, the part assigned to them too had to be considerably changed.

Of the *actual* capital investments (under the First Five-Year Plan) amounting to 52,400,000,000 rubles, the long-term investment banks distributed only 27,900,000,000 rubles. A large portion of the funds distributed by them, 22,400,000,000 rubles (80 percent), constituted, however, either budgetary funds or else funds belonging to the various enterprises themselves. The total investment of strictly *banking* funds by the Prombank, Tzekombank, Vsekobank, and Selkhozbank amounted to but 5,400,000,000 rubles.

The Prombank alone financed capital construction of industry over that period to the amount of about 21,000,000,000 rubles. But of all the billions which it distributed, less than one was distributed by purely bank methods, the rest it distributed either on behalf of the treasury (budget), or as custodian of industry's surplus funds.[4] Here too the budget was paramount.

The duties of the long-term banks, however, were not confined to a mere distribution of funds. One of the most important problems that the Soviet Union must solve is the development of a degree of efficiency that will bring down the high cost of construction and of operation of state enterprises and organizations. It was with this in view that the long-term credit banks were charged with the exercise of *financial control* (the so-called "con-

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Narkomsnab, 50 percent. The budgetary financing of capital investment in agriculture amounted to 64 percent; of which those of the Commissariat of Agriculture amounted to 55 percent, and those of the Commissariat of State Farms, to 88 percent. Of all the capital investment in transportation and in other means of communication, 95 percent was carried out by means of the budget. For municipal and housing construction the respective percentage was 80.

[4] S. Rubinshtein and I. Tzypkin, *op. cit.*, p. 18. Capital investment in the transportation system (10,000,000,000 rubles) was carried out by the budget without the aid of those banks. The same can be said about a large portion of capital investment in agriculture (about 7,000,000,000 to 8,000,000,000 rubles) and in the "nonproducing" sphere.

trol with the ruble") over the application of funds transferred by them to their clients for capital construction. However, according to the Central Board of Economic Accounting, the index of the cost of construction rose from 77 (with 1925–26 as a base) in 1929–30 to 89 in 1930–31, and in 1932 showed a further rise of from 25 to 30 percent over that of the preceding year. It was this circumstance, no doubt, that led Commissar Grinko, when discussing the importance of lowering the cost of construction, to declare: "It must be admitted that all our finance and credit organs have thus far occupied themselves but very little with it, and that their accomplishment with respect to it was very unsatisfactory. Even the bank for long-term investments,[5] which especially was entrusted with the organizing of the financing of capital construction in industry and with the controlling of its cost, has accomplished insufferably little in connection therewith."[6] In fact, on June 9, 1931, less than a year prior to this declaration by Commissar Grinko, the Council of Labor and Defense made it known that the work of the Prombank was highly unsatisfactory.[7] The enumerated defects resembled closely those which surrounded the work of the State Bank during the same period, and not without a reason. The "swing to the left" and the disorganizing influence of the Credit Reform of 1930 also affected other banks. It will be recalled that they were shorn of their branches.[8] Although ostensibly motivated by a desire to concentrate all short-term bank credit in the hands of the State Bank it may be that the authors of that scheme had in mind the elimination of the long-term credit banks altogether and the transfer of their remaining functions to the former bank in realization of Lenin's ideal, a single bank for the Soviet Union.[9] But however that may

[5] The *Prombank* or *B.D.K.*

[6] *Soviet Finances on the Borderline of Two Five-Year Plans* (Moscow, State Finance Press, 1932), pp. 24-25.

[7] *Collected Decrees*, 1931, Decree 275.

[8] The Prombank was deprived of its branches in 1928.

[9] For a discussion of a plan to eliminate the special banks and to transfer their activities to the State Bank, see G-an, "Organizational Problems of Long-Term Credit," *Finance and National Economy*, 1930, No. 32 (196), pp. 25-26; also A. Kaktyn, *Basic Problems of the Credit Reform* (Moscow, State Finance Press,

be, the arrangement which deprived these banks of their branches proved highly unsatisfactory. The State Bank, through the medium of whose branch system the long-term credit banks had to carry on their operations, was employing at that time unscientific methods of banking. It used to release funds, as we have seen, automatically and with an idea of enabling its clients to realize "the plan." This had a double effect: first, the State Bank was granting credit on behalf of the long-term credit banks even though the debit side of their accounts used to put to shame the credit side, thus to all intents and purposes being itself the lender of long-term credit and using its right of note issue for that purpose; and, secondly, those applying for funds for capital construction were receiving them without regard to the actual progress of construction and irrespective of whether or not they were complying with their financial plans. The Prombank, therefore, even though it had its own representatives at some branches of the State Bank, could not during that period be very useful in the matter of exercising financial control over capital construction in industry. To end such practices and to bring the practice of financing capital construction into compliance with its regulations of January 14, and March 20, 1931, the Council of Labor and Defense promulgated the regulation of June 9, 1931.[10] On the basis of that regulation the Prombank was permitted not only to have its own representatives at those branches of the State Bank which continued to carry out transactions on its behalf, but to open its own branches in places where capital construction was being concentrated, and to have its representatives at large construction works. In furtherance of this legislation, as soon as the Prombank opened a branch of its own the branch of the State Bank located in the same city would transfer to it all business pertaining to the financing of capital construction in that city.

1930), pp. 10 ff. Following the Credit Reform, the Supreme Council of National Economy proposed that the Prombank be liquidated and its functions transferred to the State Bank. The business of granting long-term credit to agriculture was transferred to the State Bank on December 5, 1930 (*Collected Decrees*, 1930, Decree 626).

[10] *Collected Decrees*, 1931, Decree 275.

But, as we have already seen, its work in 1931 and 1932 was unsatisfactory.

It was quite natural that under a system of budgetary financing the Commissariat of Finance, which has charge of the budget, should want to exercise greater direct control over the expenditure of moneys allocated by it to the national economy. The special or long-term credit banks, however, were not directly subordinated to it. The Prombank, for instance, through which capital investment in industry was being effected, was at first under the jurisdiction of the Supreme Council of National Economy and later under the Commissariat of Heavy Industry; the Vsekobank was under the jurisdiction of the Centrosoyuz; and so forth. It was believed that their activities could be far better co-ordinated and the quality of their work improved, if they were directly subordinated to one and the same agency, namely, the Commissariat of Finance.

As a result of this conviction, the Central Executive Committee and the Council of People's Commissars of the U.S.S.R. by a decree signed May 5, 1932, resolved to reorganize the existing long-term credit banks into a new system under the Commissariat of Finance.[11] The system was to consist of four All-Union banks, as follows:

(a) The Bank for Financing the Capital Construction of Industry and Electrification [12] (Bank Finansirovania Kapitalnogo Stroitelstva Promyshlennosti i Elektrokhoziaistva) or "Prombank," which was to be reorganized from the old Prombank or B.D.K.

(b) The Bank for Financing Socialist Agriculture (Bank Finansirovania Sotzialisticheskogo Zemledelia) or "Selkhozbank."

(c) The Bank for Financing Co-operative Capital Construction (Bank Finansirovania Kapitalnogo Stroitelstva Kooperatzii)

[11] *Collected Decrees*, 1932, Decree 191.

[12] Its sphere of operations kept on widening. At present it finances capital construction and other capital needs of all state enterprises and construction companies belonging to the Commissariats of Heavy, Light, Timber, Food, and Local Industries, Means of Transportation, Waterways, Communications, Foreign Trade, and also to the Chief Departments of Civil Aviation and of Roads, and to the Cinema-Photographic Committee.

or "Vsekobank," which was to be reorganized from the old Vsekobank (or All-Russian Co-operative Bank).

(d) The Bank for Financing Municipal (Communal) and Housing Construction (Bank Finansirovania Kommunalnogo i Zhilistchnogo Stroitelstva) or "Tzekombank."

With the exception of the Tzekombank, which carried on its work through a system of local municipal banks, the above banks were directed to carry on their work through a network of branches of their own. As before, in places where these banks had no branches their work was to be performed for them by branches of the State Bank. In such cases they were allowed to have their representatives at the latter branches. Relations between any one of the investment banks and the State Bank were to be governed by an agreement entered into by the respective parties.

The network of branches and the maintenance of representatives at the State Bank branches were to be determined by the Commissariat of Finance, under whose jurisdiction they were placed, by agreement with the corresponding commissariats, departments, or co-operative centers.

Through the new long-term investment system, which represents all the basic branches of the country's economy, flow all the funds, whether budgetary or of whatever other source, intended for financing of capital construction during a given period. So that the nation's financial plan for capital investments in the various industries, electrification, transportation, communications, foreign trade, roads, and cinema becomes also the Prombank's plan. In a similar manner the financial plan for capital investments by trading enterprises and by co-operatives is also the Vsekobank's plan, and so forth. But although all the funds intended for financing capital construction are accounted for by these banks, the custody over the funds is vested in the State Bank, against which the former draw checks or issue orders (transfers). The long-term investment system, it may be added, was also authorized to grant short-term credit to the construction companies which they finance so as to enable them to meet the seasonal requirements for materials and supplies.

The management of these banks, with the exception of the Vsekobank, was entrusted to managers appointed by the Council of People's Commissars, on the recommendation of the Commissariat of Finance of the U.S.S.R.[13]

The management of the Vsekobank was placed in the hands of authorized bank shareholders assembled in a meeting and of the manager elected by them.[14] The former was also to elect an auditing commission.

Their chief task was to establish control over the use of funds released by them for capital construction. They were to advance funds only in so far as construction proceeded according to the approved plan and in a measure as its progress justified. The ultimate aim was, of course, to lower the cost of construction. The Act of May 5, 1932, did not, however, delimit the scope of their control. This led to complications.

The banks were desirous of performing properly the tasks imposed upon them, but they faced many obstacles. For example, the state of the records with respect to the progress and the cost of the work done was such that it was difficult for the banks to comply with the principle that funds be advanced only in so far as construction advances.

Again, they were anxious to show results in the matter of lowering the cost of construction. But here too they were faced with a dilemma. Costs, as we have seen, were progressively rising, and were particularly high in 1932. The per ton cost of metal construction in 1932 (1,500 rubles) was three times as high as that in 1929 (450 rubles); the cost of the main materials per cubic meter of dwelling construction in Leningrad in 1932 (12.73

[13] The provision that the management of each of these banks, except that of the Vsekobank, should be entrusted to a manager, and the order of his appointment were fixed by a decree of May 17, 1934 (*Collected Decrees*, 1934, Decree 282). Originally, that is, by the decree of May 5, 1932, the management of these banks, with the exception of the Vsekobank, was entrusted to boards. The chairmen of these boards and their alternates were to be appointed by the Council of People's Commissars, while the members of the boards, and the entire personnel of the auditing committees of these banks, by the Commissariat of Finance by agreement with the respective commissariats and co-operative centers.

[14] Under the Act of May 5, 1932, instead of a manager the shareholders elected a board.

rubles) was 2.3 times as high as that in 1929 (5.38 rubles); the cost of cartage (including loading and unloading) per cubic meter over a distance of five kilometers in 1932 (4 rubles) was 2.4 times as high as that in 1929 (1.65 rubles). The average daily wage of the Central Construction Union (Soyuzstroy) rose within 1932 by 60 percent (from 4.12 rubles in the first quarter of the year to 6.60 rubles in the last), notwithstanding the fact that the productivity of labor during the same year decreased by 8 percent. Overhead costs, which were expected to equal one-third of the direct costs, actually constituted one-half of the latter costs. The administrative costs (principally salaries to employees) were inordinately high, equaling 50 percent of the total wage payroll.[15] Inflation played, of course, its part here, but inefficiency and waste were conspicuous.

Conducive to the increasing cost of building was the unsatisfactory procedure adopted by the contracting parties, the organizations for which construction work was to be done and the building organizations which did that work. The former would often fail to enumerate in the contract all of the objects of construction. For the work that had to be done in addition to that mentioned in the contract the latter would charge on the basis of cost of construction plus a certain profit. In that way the contractors managed to shift rising costs to their "customers." There was little incentive to eliminate waste and inefficiency.[16]

In their attempt to institute a degree of control, which, in their opinion, would eliminate the undesirable features surrounding capital construction, the banks began to meddle unduly with the

[15] Rubinshtein and Tzypkin, *op. cit.*, pp. 36-37. The authors point out that in the United States all administrative expenses in connection with construction work amount to but 10–15 percent of the labor cost.

[16] This procedure was forbidden by the decree of the Council of People's Commissars of January 27, 1933. By that decree the contracting parties were required among other things to include in their contracts only such objects of construction as were included in the "customers'" approved plan. Furthermore, the agreement was to contain the contractual (and unchanging) price of all the work that was to be done. To eliminate another evil—interference with the progress of construction—the Council on July 20, 1933, decided to supply the building organizations (contractors) with working capital of their own. It specified which outlays on the construction job were to be financed by means of their own working capital, and which by means of advances made by the "customers."

business of their clients and to regulate those of their activities which fell under the jurisdiction of other agencies. The Prombank, for instance, refused to pay for lumber bought by its clients on the ground that it could have been bought in a different district where prices were lower. Interference of this kind reached a particularly high point in the case of the municipal credit system. The banks of that system not infrequently interfered with the proper execution of their clients' annual and quarterly plans, which were already approved by higher authorities.[17] Because an appreciable portion of the funds invested by them used to take the form of *loans* rather than of budgetary grants they felt that this demanded the exercise of greater control over their clients. Accordingly, they took upon themselves to determine the character of construction, the selection of building materials, and, if in their judgment expansion was desirable, they financed construction in excess of what was called for by the approved plans.

In an attempt to clarify the character of control which the investment banks were to exercise, the Council of People's Commissars promulgated the decree of April 27, 1933. According to that decree their duties were declared to be as follows: [18]

(a) To finance only such construction work as is covered by duly approved estimates, technical projects, and titular lists enumerating the objects of construction.

[17] The procedure employed in connection with planning of capital construction is somewhat as follows: The higher authorities set an upper limit for each of the commissariats or administrative units. The administrative unit is then able to allot funds for this purpose among combinations, and the latter are able on the basis of that to draw up construction projects and to furnish estimates of their cost. On the basis of the construction-financial plans, as well as of the technical plans submitted by the various enterprises and builders, the combinations prepare what are known as *titular* lists (*titulnye spiski*) in which are listed separately each object of construction. The titular lists contain only what is known as construction in *excess of the limit,* i.e., construction the cost of which exceeds a certain amount. The titular lists are sent by the combinations to their superior administrative units. Accompanying these lists are consolidated plans of capital construction in which are shown the total amounts for construction and reconstruction "in excess of the limit," the total amounts which are expected to be used for capital repairs, and other works "below the limit." The administrative units ultimately route these documents to the Gosplan and the latter, after a close scrutiny, forwards them to the legislative bodies for approval. When approved, the titular lists and the plans are returned to the combinations and enterprises, and, thereafter, must be adhered to.

[18] *Collected Decrees,* 1933, Decree 169.

(b) To pay the bills for building material and cartage on no other basis than the established prices.
(c) To pay the bills for equipment on no other basis than the prices indicated in the contracts or mentioned in the catalogues.
(d) To release money for the payment of wages only within the fixed payroll limits.[19]
(e) To pay out funds for the meeting of the initial outlay required to set the business going (after the construction work is completed and the equipment installed), for the training of personnel, for administrative expenses, research, and so forth, only on the basis of the approved estimates.
(f) To pay the bills on behalf of their clients (after the latter had approved them) for construction work completed, or equipment installed by contractors on the basis of the prices mentioned in the agreements of the contracting parties.
(g) And, finally, to cease financing construction works for which expenditures had already reached the estimated cost or the quarterly allotment fixed by the respective commissariats, combinations, or trusts.

In other words, the Law of April 27, 1933, directed the investment banks to exercise strictly *financial* (and not technical) control. They were to grant no funds whatsoever over and above that which was mentioned in the approved plans of their clients. They could give *advice* to their clients in the matter of drawing up workable plans, but they were not held responsible for the quality of those plans. Nor were they held responsible for the soundness of the agreements entered into by their clients. They were equally free from blame for the poor quality of the construction work which they financed. To be sure, these matters were to be strictly supervised, but by agencies other than the banks.

[19] To eliminate the widespread practice by enterprises and organizations of unauthorized increase of the number of workers employed by them and to check excessive payrolls, the Council of People's Commissars introduced on February 22, 1933, a new procedure for the payment of wages. Each organization was to be allotted by its superior administrative unit a certain fund for the payment of wages during the year, quarter of the year, and during any month. The bank's were to refuse anything in excess of the amount *certified* by the higher officials. This procedure was discontinued (by order of the Council) on June 11, 1935. The clients were still required, however, to fill out certain blanks to show how much they were allowed to pay out during a certain period.

It must not, of course, be supposed that the decree of April 27, 1933, or the other decrees pertaining to the same subject,[20] however useful and beneficial, resolved the difficulties surrounding capital construction in the Soviet Union. It must not be forgotten that the problem of turning peasant labor into an efficient, well-disciplined, high-class working force, and creating a trained up-to-date technical and administrative personnel, which would make possible the elimination of all waste in construction (or production, in general) is not such an easy task and cannot be accomplished overnight. Still, on September 3, 1934, the Council of People's Commissars was able to announce that great victories were achieved on the building front. It announced, however, at the same time, that the investment banks did not perform their control work sufficiently well. It ordered, therefore, that, beginning with October 1, 1934, they discontinue financing all objects of construction which were not covered by approved projects and estimates. It also ordered them to refuse financing of individual units, even though they were covered by such projects and estimates, if an approved project and estimate covering the entire construction needs of the enterprise was lacking.[21]

The shift to grants as a method for financing capital construction of state enterprises. The Law of March 9, 1934.—When the new system of investment banks was organized on May 5, 1932, the Prombank, the Agricultural Bank, and the Tzekombank (with its system of municipal banks) were charged with the extension of both long-term loans and grants. The Vsekobank was to finance capital construction of the co-operative system by means of long-term loans. It is not difficult to see that if the various state enterprises were burdened with the repayment of funds which were used extravagantly at a time when the country was only "learning" the use of intricate machinery and the art of modern construction, they would have to be permitted to make an upward

[20] On December 22, 1932, the government forbade all construction that was not covered by approved plans. On February 5, 1933, it ordered a "normalization" of prices for building materials and cartage. The decrees of January 27 and of March 23, 1933, sought to set up orderly and businesslike contract relations between the customers and builders.—Rubinshtein and Tzypkin, *op. cit.*, p. 36.

[21] *Collected Decrees*, 1934, Decree 354.

revision of the prices and rates that they charged for their products and services.

This in turn would call for a substantial increase in the nominal wage level, for a much larger note issue, and consequently for a further depreciation of the ruble. Such a method, naturally, did not appeal to the government. A different solution was needed. We have seen how the difficulties with respect to the short-term indebtedness of the various enterprises were overcome. The latter were in no position to meet their obligations at the State Bank, and so the government promulgated the decree of July 23, 1931, which made provision for their being endowed with sufficient working capital. It will be recalled that the Prombank issued for that purpose a sufficient amount of bonds, and that the State Bank discounted those bonds and credited the accounts of the borrowers with the proceeds. The decree of the Central Executive Committee and of the Council of People's Commissars of the U.S.S.R. of March 9, 1934, provided a solution with respect to the long-term indebtedness of state enterprises.[22] It ordered:

1. That all means (whether budgetary or non-budgetary) directed through the Prombank, Tzekombank, local municipal banks, and the Vsekobank for the purpose of financing capital construction (including housing, municipal and social-welfare construction and construction of the department of workers' supplies) of state enterprises in industry, transport and means of communications (of Union, republican and local importance) were to be advanced to those enterprises in the form of non-returnable funds.

2. That all indebtedness of the enterprises mentioned in Article 1 to the Prombank, Tzekombank, local municipal banks, and Vsekobank, due the latter as a result of long-term loans to finance capital construction (irrespective for whose account those loans had been granted) was to be annulled.

3. That all indebtedness of these banks to the enterprises mentioned in Article 1 in connection with the deposits and the "earmarked" (specific purpose) installments for the financing of capital construction made by the latter was to be annulled.

4. That the indebtedness of state enterprises to state enterprises in connection with loans granted as a result of participation in the financing of capital construction, in cases where the construction of the financed objects had been completed, was to be annulled.

[22] *Ibid.*, Decree 105.

This procedure was also to be followed in the future in the case of participation by some enterprises in the financing of capital construction of other enterprises.

As may be seen, the Agricultural Bank was left out of the above act. The collective farms not being *state* enterprises, their members were not entitled to any benefits under this act. Before the year was over, however, the government freed them from all long-term indebtedness contracted by them before January 1, 1933, and owed by them to the above-mentioned bank.

Needless to say, it was the fact of state ownership and control of the lending and borrowing agencies that rendered the problem easily solvable. The state suffered no loss on account of that act of magnanimity. Under Soviet conditions it makes very little difference whether the funds that are ultimately reinvestd in the national economy are contributed by the various enterprises in one form or another. All surplus funds are reached by the state in one way or another. Nor did the removal of the encumbrance diminish in any way the zeal of the managers of those enterprises.

The annulment of the indebtedness of state enterprises to the Prombank, Tzekombank, local municipal banks, and Vsekobank constituted, however, but one aspect of the decree of March 9, 1934. As shown above, Article 1 of that decree directed these investment institutions to finance the capital construction work of state enterprises by means of *grants*. But, as we have already seen, the method of financing construction by means of budgetary grants rather than by loans was widely used in the Soviet Union even before the publication of the above decree, particularly since 1931.

Inasmuch as some funds are advanced by these institutions in the form of loans they charge interest on those portions. By the decree of June 14, 1936, they were directed to charge, beginning with July 1, 1936, 4 percent on short-term loans (which, as a rule, are granted to the contracting construction enterprises),[23] and 6 percent on overdue loans. On long-term loans the institutions granting them were directed to make the following charges: the

[23] On loans granted against "values in transit" the Tzekombank and the local municipal banks charge 2 percent interest.

Agricultural Bank, 3 percent; the Tzekombank, local municipal banks, and the Vsekobank, 1 percent. It may also be added that all long-term institutions were required to pay 1.5 percent interest on the balances of their clients' accounts, except that on funds left by collective farms with the Agricultural Bank, 3.5 percent was to be paid.

Let us, however, pass from the consideration of the investment institutions as a whole to that of the separate systems.

The Prombank.—In Chapter XI and in the preceding pages of this chapter was described the tortuous career of the bank which on May 5, 1932, became the *Bank for Financing the Capital Construction of Industry and Electrification (Prombank)*. The Prombank is the only medium through which capital investment funds are directed into all state enterprises and construction companies (of Union, republican, and local importance) of the Commissariats of Heavy, Light, Timber, Food, and Local Industries, Foreign Trade, Transportation, Waterways, Communications, as well as of such departments as the Civil Aviation, Roads, and the Cinema.[24] It must be understood, however, that the Prombank is concerned only with the financing of strictly industrial capital construction. It does not, for example, finance housing construction or municipal construction, or the construction of clubs, hospitals, schools, and the like. These latter types of construction are financed by the Tzekombank.

The important rôle played by this bank was stressed in the preceding section, where it was shown that out of 27,900,000,000 rubles placed by the long-term investment institutions under the First Five-Year Plan, the Prombank was responsible for about 21,000,000,000 rubles. In 1929–30 it placed 2,645,300,000 rubles; in 1931, 6,544,000,000 rubles; in 1932, 8,961,700,000 rubles; in

[24] The financing of capital construction of the rail, water, and air transport was transferred to the Prombank beginning with June 1, 1933. The bank set up a special department (with a separate balance) for financing the transport. *Collected Decrees*, 1933, Decree 163. In four years, 1931–34, the Soviet Union appropriated 18,500,000,000 rubles for the reconstruction of the systems of transportation and communications, of which the railroads—one of the weakest links in the Soviet economy—received 12,200,000,000 rubles. During the single year 1934 the railroads received almost 4,000,000,000 rubles. From Grinko's report to the First Session of the C.E.C. of the U.S.S.R. of the Seventh Assembly, *Economic Life*, February 9, 1935.

1933, 9,179,300,000 rubles; and in 1935, around 15,000,000,000 rubles.[25]

It carries on its work by means of offices and branches, and through the medium of the State Bank. Offices are maintained by it in the centers of the different republics and regions. Towards the end of 1933 it had 28 republican and regional offices and 75 branches. In places where it has no branches it carries out its operations through the medium of the branches of the State Bank, on the basis of an agreement with the latter. In the latter case it maintains at the State Bank branches at more important points (of which in 1933 there were 57) its own representatives. Naturally, the amount and the nature of work performed by a given branch of the State Bank on behalf of the Prombank depend on whether the latter has its own representative at the branch. If it does, then the representative takes charge of the receipt and release of funds pertaining to financing by the Prombank, and assumes control over the expenditure of those funds by the clients of his bank. The State Bank branch in such cases attends merely to the accounting end and to the handling of cash. If, however, the Prombank has neither a branch of its own nor a representative at a point where the State Bank has a branch, then the latter receives and releases funds on behalf of the Prombank, and performs a certain modicum of control in connection therewith. The State Bank is responsible to the Prombank for any sums wrongfully paid out for its account. The financing of construction by the Prombank through the medium of the State Bank's network in 1935 amounted to 3,500,000,000 rubles, or to 23 percent of the total financing by the Prombank during that year.[26]

Into the Prombank flow funds from the budget and from the state enterprises (portions of their profits and reserves for depreciation). As we have seen, by virtue of the decree of March 9, 1934, all of the funds advanced by the bank to state enterprises must take the form of grants. In practice, however, the granting of

[25] Central Administration of Economic Accounting of the Gosplan of the U.S.S.R., *Socialist Construction of the U.S.S.R., Statistical Yearbook for 1935*, p. 690. Also *Economic Life*, June 8, 1936.

[26] *Economic Life*, June 8, 1936.

loans had been discontinued by it several years before the promulgation of that decree. But even during those years of the First Five-Year Plan when the bank used to advance loans their relative importance in the total invested in industry was very small indeed. For example, in 1930 Soviet industry[27] received for capital construction a total of 3,456,400,000 rubles, and in 1931, 6,609,400,000 rubles. During those two years the Prombank's loans to industry on its own account amounted to 376,300,000 rubles and 608,200,000 rubles, respectively.[28] Of the total amount of some 21,000,000,000 rubles advanced by the Prombank to state enterprises under the First Five-Year Plan, less than 1,000,000,000 rubles were represented by loans for its own account; the bulk consisted of funds transferred by the budget and of surpluses belonging to the state enterprises themselves.

The size of the grant received by a state enterprise from the Prombank depends neither upon the discretion of the latter nor upon the accumulations of surplus by the former. It is governed by plan. The plans for financing capital construction are worked out by the Commissariats which head the different branches of the national economy, by the Commissariat of Finance of the U.S.S.R., and by the State Planning Commission, and are then approved by the government. If the Prombank plays any part in the preparation of the plan for the financing of the country's capital construction, it is merely in a consultative capacity.

As soon as their annual and quarterly plans are approved by the government, the Commissariats send to the Prombank a number of documents, such as: (a) annual and quarterly titular lists, or lists in which are enumerated the various construction projects of the combinations and of the largest construction works; (b) annual and quarterly receipts and disbursements plans of the various combinations, showing on the one hand a detailed list of expenditures (in connection with construction work, expanding needs for raw materials, equipment, supplies, as well as on account of an

[27] Heavy, light, lumber, foreign trade, electrification, food, drink, and tobacco.

[28] N. G. Tumanov, "The Long-Term Bank for Industry and Electrification of the U.S.S.R. (Prombank) and Its Functions in the Matter of Financing Capital Construction Work," *The State Bank of the U.S.S.R. Economic Survey*, February–March, 1932, VII, Nos. 2-3.

anticipated increase in its debtors' accounts and the like), and on the other, the sources of income (the budget, reserves for depreciation, that part of the profits which is set aside to enable capital construction, and the increase in the accounts of creditors), and so forth; (c) annual and quarterly ultimate or *directive* balances, that is, the various accounts as they are expected to appear at the end of a planned period; and, (d) annual, quarterly, and monthly financial plans of combinations and trusts, showing the capital investments and the sources of funds for each separately.[29]

These last are drawn up in the following form:

THE PLAN FOR FINANCING CAPITAL CONSTRUCTION OF COMBINATIONS AND TRUSTS OF THE PEOPLE'S COMMISSARIAT OF HEAVY INDUSTRY OF THE U. S. S. R. FOR THE.....QUARTER OF 19....

Name of the Combination, Trust, or Structure	*Limit for Financing*	*Source of Funds*			
		Reserve for Depreciation	Profit	Budget	Other

The data shown in the financial plans of the different combinations and trusts are consolidated by the Main Office of the Prombank into a single financial plan, which becomes the bank's own financial plan. The Prombank, as can be seen, does not do any independent planning.

[29] See Rubinshtein and Tzypkin, *op. cit.*, pp. 40 ff.

The operations of the bank are governed by the financial plans, described above, and its own plan, into which they are consolidated. Upon them are based the quarterly and monthly "limits" for capital financing of the different combinations and trusts which are communicated by the Main Office of the Prombank to its respective offices and by the latter to the branches. The "limits" are communicated in special "letters of limitations." Of particular value in connection with actual operations are the *monthly* limits; the quarterly and annual appropriations are being constantly revised.

The receipts and disbursements plans as well as the *directive* balances are used by the bank merely as auxiliary material. They serve as a guide for appraising the state of, and the progress made by, the construction works which it is financing. These plans and directive balances are retained at the Main Office. The offices and branches of the bank are supposed to obtain the information contained in them directly from the construction works, and to guide themselves by it when reporting to the Main Office on the construction and financial aspects of the units under their care.

The titular lists are sent by the Main Office to its respective offices and branches. The offices receive similar lists from the combinations and trusts directly, compare the two sets, and then dispatch the various lists to the branches which do the actual financing of the structures enumerated in them.

It has been pointed out earlier that the work of the Prombank is not confined to a mere distribution of grants. It must exercise control—as laid down by the Acts of April 27, 1933, and of September 3, 1934—over the expenditure of the distributed funds. Although there are indications of an improvement in the quality of its control work, there is still much to be done in that direction.[30]

The Vsekobank (Torgbank).—With the history of the All-Russian Co-operative Bank, or Vsekobank, from its early begin-

[30] See, for example, *Economic Life* for April 26, and for June 6, 1935. According to L. M. Kaganovich, 63.2 percent of all railroad construction on January 1, 1934, lacked *estimates*. In 1935 the corresponding percentage was 11.2 percent. In a good many instances the Act of September 3, 1934, which forbids "projectless" and "estimateless" construction, is evaded by furnishing projects and estimates which cover not the entire construction but only those units which are built first.

nings under the Soviet regime to the introduction of the First Five-Year Plan in 1928–29, we are already acquainted.

It will be recalled that in the Credit Reform Act of January 30, 1930, the government made provision for the liquidation of the branch systems of the Vsekobank and the Ukrainbank (Ukrainian Co-operative Bank) and for the transfer of their short-term credit business to the State Bank. The remaining "shells," the Main Offices of those two banks, continued to grant long-term credits to co-operatives for the purpose of financing capital construction and to provide working and special capital. The Vsekobank also granted loans to the co-operatives in connection with foreign trade. The movement of the principal accounts of the Vsekobank before the promulgation of that decree is shown in Table 65:

TABLE 65

PRINCIPAL ACCOUNTS OF THE VSEKOBANK IN 1929–30 [a]

(*In millions of rubles*)

	October 1, 1929	*January 1, 1930*
Loans and discounts (short-term)	210.1	223.1
Special long-term loans	98.2	107.8
Capital and special funds [b]	197.3	211.9
Deposits	107.6	121.6

[a] The figures were taken from the *Balance Sheets* issued by the Vsekobank during those years.

[b] The paid-up share capital was 35,400,000 rubles on October 1, 1929, and 36,800,000 rubles on January 1, 1930.

The loss of its branches compelled the Vsekobank—following the policy laid down by the government in the above-mentioned act of "bringing the work of the co-operative banks and of the State Bank closer together"—to transfer to the latter bank a number of its important functions, such as, for example, the fulfillment of the plan and control over the funds granted for capital construc-

tion.[31] In fact, from May 1, 1931, the branches of the State Bank began to include the accounts of the Vsekobank in their own balance sheets.[32] With the sad results of this arrangement in the case of the Prombank we are already familiar. The Vsekobank fared no better. The funds over which it had nominal control were being released by the branches of the State Bank to clients, so to speak, automatically. Accepted banking formalities were waived. Approved projects and estimates of the cost of the contemplated capital construction were not required. No effort was made to ascertain whether the funds were used for the purposes requested.[33] This extravagance and waste was accompanied by a failure to "mobilize" co-operative funds to the extent specified in the quarterly plans. In 1931, for example, the funds so attracted by the Vsekobank amounted to but 63 percent of the planned figure (or 200,000,000 rubles less). Clearly, the Act of May 5, 1932, by which the old Vsekobank was reorganized as the Bank for Financing Co-operative Capital Construction (Vsekobank),[34] was very timely.

By that act the Vsekobank was enabled to open branches of its own in places where there was need for them. In places where the opening of a branch was not justified the Vsekobank was to transact its business through the medium of the State Bank branches, where it could maintain its own representatives. The question of where to open branches and where to maintain representatives was decided by the Commissariat of Finance, under whose jurisdiction the Vsekobank was placed, by agreement with the co-operative centers whose operations it was called upon to finance. In 1933 it had 19 offices, 6 branches, and 18 representatives.

The Vsekobank was authorized by the Act of May 5, 1932, to finance by means of long-term loans all types of capital construction of all co-operative systems except that of housing. The bank also retained the right to perform all other operations (such as extending to co-operatives short-term credit in connection with

[31] See S. Gendel and N. Lebedev, *The Gosbank and the Long-Term Banks* (Moscow, State Finance Press, 1932), pp. 39 ff.

[32] *Ibid.*

[33] See B. Ikonnikov, "The Problems and the Perspectives of the Vsekobank," *Finance and Socialist Economy*, 1932, No. 21, p. 8.

[34] The Vsekobank was also referred to as the All-Union Co-operative Bank.

foreign trade) [35] which it theretofore performed. In addition, by special regulation of the Commissariat of Finance, the Vsekobank was also entrusted with the financing of suburban capital construction (vegetable gardens and the like) and of the Departments of Workers' Supplies (O.R.S.), as well as with the financing of capital construction by the Storing Committee (Komitet Zagotovok) of the Council of People's Commissars.[36] The share capital of the bank was fixed at 40,000,000 rubles and was made up from the payments by shareholders. Although the latter represent all types of co-operative organizations, with a predominantly co-operative capital, it is the consumers' co-operatives which contribute the lion's share.[37]

The bank was required to set aside annually not less than 10 percent of its profits to form a reserve capital. In addition, it was to form special capital funds either as a result of setting aside a portion of its profits or as a result of an understanding with the various state, co-operative, and socialized organizations, which were to make special contributions for that purpose.

As may be seen from Table 66, the bulk of the funds extended by the Vsekobank to co-operatives for the purpose of financing capital construction came, in the main, from accumulations by the co-operatives themselves.

Only 3.4 percent (45,700,000 rubles) of its total resources (1,277,300,000 rubles) were derived from the budget.[38] The balance, save for the 127,700,000 rubles deposited with it by non-co-opera-

[35] Such loans were granted for periods not to exceed 12–18 months.

[36] The Storing Committee is charged with the collection of agricultural produce other than grain. The financing of capital construction of the above-mentioned suburban economy, of the O.R.S. (in part) and of the Storing Committee was carried out by means of budgetary appropriations.

[37] The number of shareholders in Soviet consumers' co-operatives increased between January 1, 1929, and January 1, 1933, from 24,700,000 to 73,100,000. The average shareholding increased between those dates from 8.72 rubles to 27.70 rubles. The total share capital, which on October 1, 1928, amounted to 183,300,000 rubles, rose by January 1, 1933, to 2,006,500,000 rubles. *Itogi*, p. 194.

[38] In the Vsekobank's plan for 1933, budgetary funds played a more important rôle, constituting 29 percent of the planned resources. The change, however, was due to the transfer to this bank of such clients as the O.R.S. and the Storing Committee of the Council of People's Commissars, which were financed by means of budgetary appropriations (see footnote 36). Rubinshtein and Tzypkin, *op. cit.*, p. 73.

tives, represented accumulations by the co-operative systems. The extent to which the different types of clients participate in the distribution of funds by the bank is shown by the financial-credit plan of the latter for 1933. According to that plan, the bank was to advance during 1933 about 1,000,000,000 rubles, of which 30 percent was to go to consumers' co-operatives, 24 percent to producers' co-operatives, 28 percent to the Department of Workers' Supplies (O.R.S.), and 11 percent to the Storing Committee. Of the total amount, 844,000,000 rubles, or 84 percent, was to be used for the

TABLE 66

THE VSEKOBANK

BALANCE SHEET ITEMS AS OF JANUARY 1, 1933 [a]

(*In millions of rubles*)

Short-term loans	117.0
Long-term loans to co-operatives	1,105.5
Long-term loans to non-co-operatives	16.2
Total capital	68.7
Special funds for long-term loans:	
Budgetary fund	45.7
Funds of co-operative societies	393.6
Long-term deposits by co-operatives	551.2
Long-term deposits by non-co-operatives	127.7
Reserve funds of co-operative societies	90.4

[a] From the *Balance Sheet* issued by the bank in 1933.

financing of capital construction; 115,000,000 rubles, or 11.5 percent, for expanding the working capital (principally, to the extent of 100,000,000 rubles, of producers' co-operatives).

The above-mentioned long-term funds and special deposits were formed as a result of allocations from profits, reserves for depreciation, and so forth. The consumers' co-operatives, for example, are required to contribute annually a portion of their profits towards

the formation of a fund for financing capital construction and for augmenting working capital. The size of the contribution and the dates upon which the payments are made are determined by the *Centrosoyuz* (that is, the central organization of consumers' co-operatives) in agreement with the bank. The consumers' co-operatives are also required to deposit with the bank the funds representing increases in the share capital, special contributions by the membership, and the reserve for depreciation. The producers' co-operatives, too, contribute a portion of their profits to the fund for long-term credit, as well as make special deposits (of so-called "mechanization" and "reconstruction" funds) in the bank. Special deposits are also left with the Vsekobank by non-co-operative organizations, such as trade unions, state industry, and state trade or are formed as a result of budgetary (state and local) appropriations.

The special deposits were returnable to their owners to be used by them for certain specified purposes. The fund for long-term credit, on the other hand, consisted of (non-returnable) *contributions* from the various co-operative systems. It formed a common pool from which advances were made irrespective of the source of the funds. This method was changed in 1934.[39] According to the new method, each co-operative enterprise is required to maintain with the Vsekobank in a special long-term credit fund account all of the sums which are designed by it for financing capital construction, and, in general, for long-term investment. The fund of long-term credit for each separate co-operative enterprise is to be formed from the following sources: (a) out of its respective share in the old long-term credit fund (the "common pool"), which was to be liquidated; (b) from allocations from profits as determined by the respective co-operative centers; (c) from reserves for depreciation; (d) from budgetary appropriations; (e) from earmarked deposits by state industry, trade, and so forth.

Like the other special banks, the Vsekobank is required to exercise strict financial control—along the lines indicated in the Act of April 27, 1933—over the expenditure of funds turned over by it to its clients. Inasmuch as capital construction by *co-operative*

[39] *Collected Decrees*, 1934, Decree 155.

THE FINANCIAL AND CREDIT PLAN OF THE VSEKOBANK

System / *Source*	*The Plan for Capital Investment and Sources of Financing*									
	Consumers' Co-operatives	Multi-Producers' Co-operatives	Metal Workers' Co-operatives	Invalids' Co-operatives	Fishermen's Co-operatives	Hunters' Co-operatives	O. R. S.	Storing Committee	Others	Total
1. State budget										
2. Allocations to the fund for long-term credit										
3. Special deposits by co-operatives:										
(a) To finance capital construction										
(b) To augment working capital										
(c) Non-returnable financing										
4. Special deposits by others										
5. Repayment of loans:										
(a) On account of loans for capital construction										
(b) On account of loans for the expansion of working capital										

6. Interest payments:										
(a) On account of loans for capital construction										
(b) On account of loans for the expansion of working capital										
7. Others										
Distribution of Funds										
1. Long-term loans for capital construction										
2. Loans for the expansion of working capital										
3. Others										
4. Reserve	(the difference between the planned receipts and disbursements)									

enterprises (as distinct from *state* enterprises) continues to be financed by means of long-term credits rather than grants,[40] and the extent of such financing is circumscribed by their own accumulations, it is quite evident that upon the vigilance of the Vsekobank depends the very expansion of the co-operative system. It is authorized to cut off the financing of a project not only when the sums advanced by it have already reached the figures called for by the estimate, or the limit set by the quarterly credit plan, but also upon detecting that the loan was being put to some other use than the one for which it was advanced. In such instances, the bank would not only serve notice upon the client, whose financing was stopped, but would also communicate the shortcomings of the client to the agency supervising the latter so that steps might be taken to remove those shortcomings.

The scope of the bank's work is guided by the annual and quarterly financial plans prepared by the various co-operative centers and commissariats and approved by the government. Its participation in the preparation of these plans is confined to the giving of information and counsel to the above-mentioned bodies. When the Vsekobank receives these plans, it weaves into them its own anticipated receipts and expenditures (if necessary, credit arrangements are made with the State Bank) and obtains in this way a financial-credit plan of the bank as such. In fact, it makes up a consolidated plan for the co-operative banking system as a whole and for each branch separately. When its plan is approved, it sends out copies of it, together with copies of titular lists and sources by means of which the financing is to be carried out.

The continuous expansion of state trading enterprises, which in 1934 were already responsible for about 60 percent of the retail trade turnover, serves to diminish more and more the importance of the co-operative system. In fact, on September 29, 1935, it was ordered (Decree 428) that the *Centrosoyuz* (the central organization of the consumers' co-operatives) transfer, between October 1

[40] The Act of March 9, 1934, relative to the financing of capital construction by *state* enterprises of industry, transport and means of communications by non-returnable grants, applies to the Vsekobank in so far as it deals with *state* enterprises. The same is true with respect to the annulment of indebtedness to it and by it.

and 20, 1935, all urban consumers' co-operative enterprises to the Commissariat of Internal Trade, that is, to the state. The transferred enterprises comprised not only stores, but also restaurants, bakeries, breweries, plants for the manufacturing of non-alcoholic drinks, and so forth. The Centrosoyuz was ordered to transfer all of its activity into the villages, where the distribution of consumers' goods is anything but adequate. The future will presumably witness the complete displacement in the Soviet Union of co-operatives by state trading enterprises. In the meantime the government, on August 17, 1936, ordered that the Vsekobank (All-Union Bank for Financing Co-operative Capital Construction) and the Ukrainbank (Ukrainian Co-operative Bank) as such be liquidated and their branches and business be taken over, as of July 1, 1936, by a new institution named *Torgbank* (that is, Trade Bank). The Torgbank, or the All-Union Bank for Financing Capital Construction of Trade and Co-operatives, will finance by means of grants the capital construction and other capital needs of trading enterprises under the jurisdiction of the Commissariats (Union and republican) of Domestic Trade as well as of those under the jurisdiction of the Storing Committee (for agricultural produce) of the Council of People's Commissars of the U.S.S.R., and of the Departments of Workers' Supplies. The financing of the capital needs of consumers', producers', and invalids' co-operatives, as well as the needs of the two last mentioned for working capital, will take the form of long-term loans and in special instances of grants. Following the practice of all other long-term financial institutions, the Torgbank will grant short-term credit to the construction companies to enable them to meet the seasonal requirements for materials and supplies.

The Agricultural Bank and the agricultural credit system.—In Chapter XI were traced the early evolution and the difficulties of the Soviet agricultural credit system. It was shown there that, as a result of an investigation by the Commissariat of Workers' and Peasants' Inspection, the government early in 1929 ordered certain changes in the agricultural credit system. Meanwhile, however, the movement for the mass collectivization of the peasantry began to spread. This became particularly rapid in the autumn of 1929, and

assumed wild-fire proportions at the beginning of 1930. In one way or another, millions of individual peasants were forced into collective farms (*kolkhozy*).

The reorganization of this most important branch of the national economy from an individualistic basis to a collective or co-operative basis necessitated appropriate changes in the agricultural credit system. Since the collective farms partook of the nature of co-operatives, it appeared that a *co-operative* agricultural bank could best tap their resources and best suit their needs. Furthermore, concentration in agriculture called for concentration in the banking system which served it. Accordingly, the government, by the Act of January 30, 1930 (the Credit Reform Act), ordered a reorganization of the agricultural credit system, as a result of which the Central Agricultural Bank was replaced by an All-Union Agricultural Co-operative-Kolkhoz Bank (Vsesoyuznyi Selsko-Khoziaistvennyi Kooperativno-Kolkhoznyi Bank, or "V.S.-Kh.K.K. Bank"). The seven former Federated (Republic) Agricultural Banks and other *intermediate* credit links became converted into offices of the new V.S.-Kh.K.K. Bank. Important changes were also introduced with respect to the lower links of the system—the agricultural credit-co-operative associations. Their number, through amalgamations and liquidations, was reduced from 10,358 prior to the mass collectivization movement to less than 3,000 in 1930.[41] Their functions, which, as we have seen, were not only of a banking but also of a trading and industrial nature, began to be restricted to those of a purely banking nature. They became, in fact, district agricultural banks. But although independent units, they served as agencies in their respective districts for the V.S.-Kh.K.K. Bank, in so far as long-term agricultural credit was concerned, and for the State Bank in so far as short-term credit was concerned.

The reorganized agricultural credit system was, however, short-lived, for by their decree of December 5, 1930, the Central Executive Committee and the Council of People's Commissars of the

[41] "The Agricultural Banking System of the U.S.S.R.," *The State Bank of the U.S.S.R. Economic Survey*, November, 1930, V, No. 19, pp. 7-8. As a rule, one such association was set up in each of the 2,291 districts (*rayony*) into which the country was divided. On January 1, 1931, the number of such associations amounted to 2,759.

U.S.S.R. ordered that, beginning with January 1, 1931, the All-Union Agricultural Co-operative-Kolkhoz Bank and all of its offices should terminate their existence as such, and their assets, liabilities, and the entire functioning apparatus should be transferred to the State Bank.[42] The same decree put an end to the remaining vestiges of the agricultural co-operative credit system, the agricultural credit-co-operative associations. Their assets and liabilities were ordered transferred to the State Bank. Those of the associations which were located in places where the State Bank had branches were merged in the latter. Others were reorganized as State Bank branches. The business of long-term agricultural credit was transferred, beginning with January 1, 1931, to the State Bank. The various assets that were transferred to the State Bank were turned by it into a separate, single, special fund for long-term production credit to agriculture. This fund was to be augmented periodically by transfers from the state and local budgets, and by means of monthly obligatory payments (dues) by the collective farms and other organizations which were served by the fund.

The Act of June 12, 1931, which sought to implant principles of business accounting within the collective farms, and to purge agricultural credit of the defects that permeated all branches of credit in 1930–31, laid down a number of rules which were to govern the extension and employment of long-term agricultural credit.[43] The State Bank was directed to grant long-term agricul-

[42] *Collected Decrees*, 1930, Decree 626. On August 1, 1930, the outstanding loans of the then 2,950 associations amounted to 1,129,300,000 rubles; their capital and various funds, to 175,300,000 rubles; their deposits, to 282,900,000 rubles; borrowed funds, to 980,000,000 rubles. On the same date, the outstanding loans of the V.S.-Kh.K.K. Bank amounted to 1,367,000,000 rubles; its basic capital, to 323,300,000 rubles; other capital funds, to 111,000,000 rubles; borrowed funds and funds to be loaned on behalf of other agencies, to 736,000,000 rubles; deposits, to 102,300,000 rubles. Inasmuch as 930,000,000 rubles of the total (1,367,000,000 rubles) loaned by the bank went to the associations, the combined outstanding loans of the entire agricultural credit system on that day amounted to about 1,500,000,000 rubles. *The State Bank of the U.S.S.R. Economic Survey*, November, 1930, V, No. 19, pp. 8-9.

[43] *Collected Decrees*, 1931, Decree 272. See also S. T. Boguslavsky, *Long-Term Production Crediting of Agriculture* (Moscow, State Finance Press, 1932), *passim*. Also S. I. Nedelin, *Credit to the Kolkhozy* (Moscow, State Finance Press, 1932), *passim;* and G. I. Bronshtein, *Credit Work in the Village and in the District* (Moscow, State Finance Press, 1931), *passim*.

tural credit on the basis of the annual and quarterly credit plans that were to be prepared by the *Kolkhozcenter* of the U.S.S.R. (the central organization of collective farms), and submitted through the Commissar of Agriculture to the Council of People's Commissars for approval. It was to be extended to the collective farms through the various specializing Kolkhozcenters (such as milk, hog-raising, chickens, and so forth) heading them, or directly, if they were not included in a Kolkhozcenter, to machine-tractor stations, harvesting stations, and the like. The collective farms were to be permitted to draw against the credits opened for them (in each case for a specific purpose) only in so far as they were fulfilling the contracts entered into with the respective Kolkhozcenters, as well as those with the supply procurement agencies to which they agreed to turn over given quantities of their products at set dates, and were meeting certain other conditions.[44] Collective farms and machine-tractor stations were to pay 4 percent per annum, and others 6 percent on the borrowed long-term funds.

The transfer of long-term agricultural financing to the State Bank raises an interesting question: why was it done? We know already that as a result of the swing to the left there was talk of liquidating all special banks and concentrating their functions in the hands of the State Bank. This orientation was no doubt a contributing cause. But was it the only cause? The agricultural banking system, it must be remembered, was the only one of all the special bank systems that was actually ordered to be liquidated. Apparently there were certain circumstances which made the retention of the co-operative agricultural banking system especially undesirable. The explanation lies, perhaps, in the fact that the government, seeing that many collectives were such only on paper and were using that form of organization merely as a façade to enable them to escape the wrath of the administration, decided that for political and economic reasons it was inadvisable to grant financial independence to the agricultural co-operative and collective systems. It was far safer to do away with the co-operative-credit associations and with the Co-operative-Kolkhoz Bank, and

[44] Such as investing a certain amount of their own funds, and showing that the progress of work justifies the release of funds by the bank.

entrust the control over the funds of collective farms to the State Bank.

The State Bank, burdened with numerous new duties, found it difficult to discharge properly the duties pertaining to the administration of long-term agricultural credit. This, together with the fact that a crusade against the "leftist" psychology had set in, compelled a revision of the step taken on December 5, 1930. It will be recalled that the government by its Act of May 5, 1932, ordered the establishment of the Bank for Financing Socialist Agriculture (Selkhozbank). To the new agricultural bank was turned over the "special fund for long-term production credit to agriculture," which theretofore had been administered by the State Bank. The new bank was renamed on August 27, 1933, Agricultural Bank (Selsko-Khoziaistvennyi Bank).[45] The abbreviated name "Selkhozbank" was retained.

The bank was entrusted with the financing, by means of grants and returnable long-term loans, of all types of capital expenditures by enterprises and organizations of the state sector of the rural economy, as well as of those by the collective system. Its work was to be carried on with the aid of its own branch system, and, as in the case of the other special banks, with the aid of the State Bank branches in places where it had no branches of its own. On July 1, 1933, the bank had 50 offices (26 of which were directly subordinate to the Main Office), 207 interdistrict and 242 district branches, and 386 inspectorial groups. The field of activities of the interdistrict, unlike those of the district, branches cover several districts (*rayony*). The inspectorial groups, each headed by a chief inspector, are attached to branches of the State Bank in places where the Agricultural Bank has no branches of its own. They are entrusted with the financing of agriculture, and the control over the expended funds in connection therewith, in the districts where they are stationed.

The Agricultural Bank finances the capital needs of the *state* sector of the rural economy, that is the state farms (*sovkhozy*), and their combinations and trusts, machine-tractor stations, and the regional administrations of the various tractor centers under the

[45] *Collected Decrees*, 1933, Decree 332.

Commissariat of Agriculture, by means of grants. The capital needs of the collective farms (*kolkhozy*), communes, and "arteli," as well as of individual members of the collective farms and of individual peasants (the latter by decision of the government and of the Main Office of the bank), on the other hand, are financed by it by means of long-term loans.

The funds advanced by the bank in the form of *grants* to the state sector are derived from appropriations by the state and republican budgets, as well as from accumulations by the enterprises of that sector (their reserves for depreciation, allocations from profits, and, in general, from their own resources).

The funds needed for the extension of long-term *loans* come from the bank's basic capital (the fund for long-term production credit), its reserve capital (to which 50 percent of its profits is periodically being transferred), and other capital funds. On January 1, 1933, for example, its capital and capital funds amounted to 1,025,000,000 rubles.[46] In addition to its own capital and capital funds, the bank operates with the free balances left with it by building organizations, with the balances left in the so-called "indivisible funds" accounts of the collective farms, and with the balances of other funds left on deposit with it.

The indivisible funds of the collective farms constitute a very important item in the bank's resources. They are composed of the following: entrance fees paid in by members of collective farms,[47] allocations of from 10 to 15 percent from the gross revenue of the collective farms, funds realized from the sale of surplus property, from insurance indemnities, and from voluntary contributions by their members. The directors of the collectives draw against the funds so deposited by them whenever their production plans and receipts and disbursements estimates require it. The funds are used to finance capital construction and repairs, to purchase livestock, fertilizers, to purchase and to repair machinery and equipment, and so forth. Under special circumstances the bank may permit them to borrow from the indivisible funds for purposes other than

[46] Rubinshtein and Tzypkin, *op. cit.*, p. 82. Its financial statement balanced on that day at 3,687,000,000 rubles.

[47] Peasant-workers (*batraks*) were assessed 3 rubles; poor and middle-class peasants, from 5 to 25 rubles.

capital investment. The collective farms were paid an interest rate of 8 percent per annum on the balances in their indivisible funds accounts. They paid 4 percent interest on the funds borrowed from the bank.[48] But, as we have already seen, on June 14, 1936, the interest paid on balances in the indivisible or any other capital funds of the collective farms was reduced to 3.5 percent, on balances in settlement accounts, to 1.5 percent. At the same time the bank was directed to charge 3 percent for long-term loans, 4 percent for short-term loans to contracting construction companies, and 6 percent for overdue loans.

During the period covered by the First Five-Year Plan the agricultural credit system redistributed for capital investment 273,300,000 rubles of budgetary funds, and 2,858,700,000 rubles of what may be regarded as the resources of that system.[49] These figures, however, do not show the real correlation between the investment of budgetary and strictly banking funds, inasmuch as about 8,000,000,000 rubles of budgetary funds invested in agriculture during those years passed through the hands of the State Bank, which at the time was the distributor of such funds.[50]

In 1933 the budgetary funds directed into agriculture amounted to 3,500,000,000 rubles.[51] According to the plan for that year budgetary funds were to constitute 65 percent, and banking resources 25 percent of the total investment in agriculture.

The ever increasing importance of the budget as a means for financing capital investments in agriculture may be best seen from the fact that, of a total of 20,800,000,000 rubles invested in the state farms, machine-tractor stations,[52] and collective farms in the years 1931 to 1934 (inclusive), the budget (state and local) was responsible for 17,500,000,000 rubles. It must be remembered,

[48] *Collected Decrees,* 1934. Decree 235.

[49] Of the latter amount, 2,011,300,000 rubles was derived from the repayment of loans.

[50] Beginning with 1933, budgetary funds for the state sector of the rural economy began to pass through the Agricultural Bank. A special account was opened for the latter for that purpose on the books of the State Bank.

[51] Commissar Grinko's report to the Fourth Session of the C.E.C. of the U.S.S.R. of the Sixth Assembly on December 31, 1933. *Stenographic Report* (Moscow, 1934), pp. 34-35.

[52] Altogether up to January 1, 1935, a total of 5,500,000,000 rubles was invested in the machine-tractor stations. *Economic Life,* May 10, 1935.

however, that the flow of budgetary funds was particularly strong in the direction of the *state sector* of the rural economy (that is, state farms and machine-tractor stations). The long-term loans extended by the Agricultural Bank to the collective farms over the same period amounted to 1,168,000,000 rubles.[53] As may be gleaned from Table 67, the Agricultural Bank granted the collec-

TABLE 67

THE INVESTMENTS AND DEPOSITS OF THE AGRICULTURAL BANK IN 1934 AND 1935 [a]

(*In millions of rubles*)

	1934	*1935*
Financing the state sector of rural economy	2,614.3	2,515.8
Long-term loans to the collective farms	297.0	448.4
Balances in the accounts of state farms and of machine-tractor stations (state sector)	334.2	654.7
Indivisible funds of collective farms	218.0	653.8
Balance of indivisible funds at the end of the year	119.4	215.1

[a] M. Vynosov, "Tasks for the Agricultural Bank," *Economic Life*, April 26, 1936.

tive farms in 1934, 297,000,000 rubles in long-term loans, and in 1935, 448,400,000 rubles. In 1936 the volume of loans was expected to rise to about 800,000,000 rubles. The state farms and the machine-tractor stations, on the other hand, received 2,614,300,000 rubles in 1934, and 2,515,800,000 rubles in 1935. Some will no doubt interpret this as indicative of the fact that the ultimate aim of the communists is to displace collectives by state farms (i.e. state-grain factories), thus obliterating the difference between the village and town economy and ideology.

It has already been stated that by virtue of the decree of De-

[53] *Economic Life*, February 9, 1935.

cember 23, 1934, the government resolved to extend financial aid to the collective farms by way of freeing them from all indebtedness to the Agricultural Bank contracted by them prior to January 1, 1933. Accordingly, the bank wrote off 437,529,000 rubles of their indebtedness to it. Inasmuch as on the day when the decree was published they owed the bank a total of 818,000,000 rubles, they were forgiven 54 percent of their total long-term indebtedness to it.[54]

As in the case of the other special banks, the work of the Agricultural Bank is not confined to a mere distribution of funds. It must exercise a type of financial control which will insure the proper utilization of every copeck that is advanced to agriculture, and the return flow—to the bank and to the budget—of as large a fund as possible. To accomplish this the bank must contribute its share towards implanting in the collective and state farms better business methods, and towards instilling in them a sense of financial responsibility. So far as control goes, the bank is of course guided by the Law of April 27, 1933, which has already been mentioned on several occasions. Still, both banks—the Agricultural Bank which handles the long-term financing of agriculture and the State Bank which serves its short-term needs—have Herculean tasks before them. The state farms and the collective farms are young institutions. Their business sense and financial responsibility leave much to be desired. It was, for example, reported that the agricultural construction program for 1934 fell woefully behind the plan; the percentage of unfinished construction works was inordinately high; too much was expended on extra-planned works; the cost of capital construction, and the cost of repairs of tractors and of other agricultural machinery mounted. It was brought out that the planned cost of construction had been exceeded by about 20 percent. As a result much of the working capital of the agricultural enterprises "disappeared." M. Vynosov

[54] From 1929 to 1934 (inclusive) the collective farms obtained over 1,700,000,000 rubles in long-term loans. Of that amount, 584,000,000 rubles was granted them for the development of farms for livestock breeding; 440,000,000 rubles for the purchase of draught animals, equipment, and the like; and about 700,000,000 rubles for other needs. *Economic Life*, May 10, 1935.

(manager of the Agricultural Bank),[55] who reported these conditions, attributed the financial difficulties of many state farms and machine-tractor stations to the fact that they have used up in that manner some 3,000,000,000 rubles of their working capital. In his opinion the quality of the control work of the bank in 1934 was extremely poor. The main fault was that the branches did not make full use of the materials and reports at their disposal, did not analyze the balance sheets, did not derive the necessary conclusions, and did not signalize the shortcomings. This, naturally, is a reflection, at least in part, upon the skill and executive ability of the bank's personnel.

It has been said above that the business sense of both state farms and collective farms, during those early years of formation, had not reached a high point of development. Thus far, however, mention was made only of the state farms. The situation with respect to the collective farms and the bank's share of the responsibility was described in the decree of the Council of People's Commissars of March 27, 1935, in the following words: [56]

The Council of People's Commissars of the U.S.S.R. establishes that, despite the tremendous importance which the proper keeping of pecuniary accounts and a strict financial discipline have in the matter of strengthening the economy of the kolkhozy, this work in many kolkhozy is in an entirely unsatisfactory state. The directors of the kolkhozy do not devote enough attention to the improvement of financial accounting, permit the investment of kolkhoz funds in unnecessary property, do not bother to collect from other organizations what is due them, and allow excessive administrative-managerial costs, thus undermining the economic strength of the kolkhozy and diminishing the income of the members of the kolkhozy themselves.

[55] "To a Higher Level," *Economic Life,* June 2, 1935. It may be of interest to note that in connection with the recent campaign of the government to strengthen the position of the ruble extraordinary steps began to be taken to stamp out the use of money substitutes such as coupons, specially printed receipts, and so forth, which were accepted in lieu of legalized money. It was said in this connection that the state farms were especially guilty of that. As one writer put it: "Some directors of the state farms had entangled their finances, squandered the funds given to them by the government, and, in order to extricate themselves, entered upon a path of serious crime." *Economic Life,* May 30, 1935. Translated into unemotional language it means that the financial difficulties and shortage of liquid funds, which were brought about by their inability to live up to the plan, caused the state farms to employ various substitutes for money.

[56] *Collected Decrees,* 1935, Decree 125.

Along with this there are numerous absolutely intolerable cases of unlawful disposition of kolkhoz funds on the part of local, state, and economic agencies. Extremely poor is the audit of and the control over the income of a kolkhoz, thus facilitating theft and plunder of kolkhoz property . . .

The Council, therefore, ordered:

1. To compel state, co-operative, and social organizations to settle with the kolkhozy in full by July 1, 1935, for whatever produce was bought from them.

2. To forbid the branches of the State Bank, of the Agricultural Bank, and the savings banks to make any deductions whatsoever from the current accounts of the kolkhozy, no matter by whom requested, save upon the order of the kolkhoz managements . . . the only compulsory deductions being in case of taxes and court orders.

3. All kinds of payments into various voluntary organizations (such as that for Soviet Aviation, Autoroad, "Children's Friend," and so on), dues to co-operative organizations, payments for lottery tickets, payments in connection with the subscription for government bonds, as well as payments of taxes and payments due from the personal economy of the members, may be made only by the members themselves from their personal income.

The last two clauses, it will be noticed, referred to the common practice at the time of making various deductions from the funds deposited by the collective farmers without their permission. This, coupled with the bad treatment accorded them and the difficulty experienced by them when withdrawing funds, caused them to hoard their funds. In *Economic Life* of April 26, 1935, for example, it is pointed out that during the first quarter of 1935, when the capital investments of the collective farms amounted to no less than 400,000,000 rubles, their withdrawals from the bank were but 75,200,000 rubles. In other words, over 80 percent of the total capital investments had been effected without the bank's mediation.

On September 22, 1935, the government in a new decree pointed out that, although the work of the Agricultural Bank showed improvement, there were still many shortcomings.[57] For example, a large part of the indivisible funds of the collective farms were still being withheld from the bank; the bank had

[57] *Ibid.*, Decree 434.

failed to prevent non-planned construction, its mounting cost, and the unlawful application of working capital towards capital construction. Also, the bank paid insufficient attention to the failure of borrowers to meet their obligations on time.

To help the bank overcome these shortcomings, the government prescribed the following procedure of planning with respect to the collective farms and collective farmers: the Agricultural Bank draws up annual production-credit plans for the entire Soviet Union, showing a distribution of funds among the federated republics as well as according to their uses. These plans are based upon the production plans of the People's Commissariat of Agriculture of the U.S.S.R. and, together with the recommendations of the latter, and of the People's Commissariat of Finance of the U.S.S.R., are submitted to the government (Council of People's Commissars of the U.S.S.R.) for approval.

The republican offices of the bank draw up annual production-credit plans for the individual federated republics showing a distribution of funds among the various autonomous republics, regions, and territories (and in republics with no territorial division—by districts) by their uses and sources. The plans are based upon the instructions from the manager of the Agricultural Bank,[58] and upon the production plans of the people's commissariats of agriculture of the federated republics, and, together with the recommendations of the latter, are submitted to the councils of people's commissars of the federated republics for approval.

The annual plans for the individual autonomous republics and regions (territories) showing a distribution of funds by districts, uses, and sources are drawn up by the republican and regional (territorial) offices of the bank along the lines outlined above, except that these plans are based upon the production plans of the commissariats of agriculture of the autonomous republics or upon those of the regional (territorial) agricultural administrations, and are submitted for approval to the councils of people's

[58] Except in the case of the R.S.F.S.R. the production credit plan for which is drawn up by the manager himself.

commissars, or to the executive committees of the respective autonomous republics, regions, and territories.

The production credit plans for the individual collective farms in the various districts are drawn up by the branches of the bank. They are based upon instructions from the republican and regional (territorial) offices of the bank, production plans of the district agricultural departments, and upon the applications of the collective farms. They are submitted, together with the recommendations of the district agricultural department, to the district executive committee for approval.

The quarterly plans are based upon the annual plans, and are drawn up and approved by the Agricultural Bank, its offices and branches upon consulting the respective agricultural agencies.

The task of implanting business responsibility in the collectives is not an easy one. It will take considerable time to accomplish it. Nevertheless, the determined efforts of the government have already brought a measure of success. The improved banking methods helped to recreate in the collective farmers confidence in the banks. On January 1, 1936, for example, the balances in the accounts of the collective farms at the State Bank and the Agricultural Bank amounted to 1,220,000,000 rubles, or 3.5 times as much as in 1934.[59]

The Tzekombank and the municipal bank system.—In Chapter XI was presented an account of the early development in the Soviet Union of local municipal banks and of the Central Municipal and Housing Bank (Tzekombank).

The work of the municipal banking system during the turbulent years of the First Five-Year Plan resembled in many respects that of the other banking systems already reviewed. Like them they failed to stress the principle of contractual relations, like them they failed to invoke financial control over their clients, and, hence, like them they failed to inculcate business principles in the latter.[60]

[59] M. Vynosov, "Cheap Credit to the Collective Farms," *Economic Life,* June 24, 1936. The cash income of the collective farms during 1935 increased from 5,400,000,000 to 10,000,000,000 rubles.

[60] See S. Gendel and N. Lebedev, *op. cit.,* p. 26.

The policy laid down by the Credit Reform Act of 1930 to shift all short-term credit business to the State Bank helped to convert the municipal banking system into a predominantly long-term banking system. For example, on October 1, 1929, the short-term credit business of the municipal banks amounted to 31 percent of all their loans and discounts, but towards the end of 1930 to only 12.7 percent.[61] Still, these banks, with the exception of the Tzekombank itself, which was entirely deprived of short-term business,[62] continued to extend such credit to the local budgetary authorities, to local industry, to the municipal economy, to housing, invalid, and other types of co-operatives (including to some extent consumers' co-operatives).

The retention by the local banks of some of that business was due to the pressure exerted by the local executive committees (*ispolkomy*) which, chiefly because they wielded influence over these local banks and the latter consequently overlooked a good many of their sins, found it to their interests to continue in the old ways.

But even so the central government, approaching the matter from a different angle, proceeded to enact legislation such as that of July 11, 1930, and of January 14, 1931,[63] which had for its purpose the increase of the long-term resources of these banks and the widening of their activities along the lines of long-term financing in order to convert them into long-term banks.

[61] "The Municipal Banks in 1929–30," *The State Bank of the U.S.S.R. Economic Survey,* February, 1931, VI, Nos. 2 and 5. In October, 1926, their short-term credits amounted to 66 percent of the total credits granted by them.

[62] It must be borne in mind that the municipal banks are independent local banking institutions (not mere branches), even though headed by the Tzekombank.

[63] The Law of July 11, 1930 (*Collected Decrees,* 1930, Decree 570), directed that the financing of housing and municipal construction—which is carried out by means of funds supplied by the state budget, or which is carried out by departments and institutions of the U.S.S.R. and by state enterprises of Union importance even by means other than those of the state budget—must be effected through the medium of the Tzekombank. In the latter had to be lodged all the funds which were to be used for such purposes. In a similar fashion the Law of January 14, 1931 (*Collected Decrees,* 1931, Decree 53), provided that the financing of medical and of prophylactic institutions (rest homes, resorts, sanatoria, and the like), irrespective of means (budgetary, medical aid funds, funds set aside for that purpose by industry, transport, co-operatives, or funds set aside for the improvement of workers' living conditions), must be effected through the medium of the Tzekombank and of the various local municipal banks.

As we already know, the joint-stock [64] Central Municipal and Housing Bank was reorganized, in pursuance of the Act of May 5, 1932, as the All-Union Bank for Financing Municipal and Housing Construction (still known as "Tzekombank"). The People's Commissariat of Finance of the U.S.S.R. exercises general supervision over it, approves the principal rules governing its operations, as well as its estimates, annual reports and disposition of profits, and conducts examinations—directly or through the bank's auditing commission. As has been stated in the general section of this chapter, the immediate and general administration of the bank's affairs is placed in the hands of a directorate, whose chairman and acting chairmen (alternates) are appointed by the Council of People's Commissars, and whose members are appointed by the Commissariat of Finance. The latter also appoints the entire personnel of the auditing commission.

Unlike the other special banks, the reorganized Tzekombank operates not through branches but through the various local municipal banks. Through the medium of these banks it carries out all its financing, except that pertaining to the building of cities and to certain types of construction work which it finances directly. But although the local municipal banks are still independent, the Tzekombank exercises general and operative supervision and control over them, examines them, issues instructions relative to preparation of financial plans, as well as to problems affecting the financing of construction, and regulates such matters as the banking procedure and methods employed by them, and their bookkeeping and statistical methods. In short, the Tzekombank together with the municipal banks form an *organized banking system.* In 1934 this system, besides the Tzekombank, con-

[64] The local municipal banks operating on the territory of the R.S.F.S.R. were ordered by the act of the C.E.C. and of the Council of People's Commissars of the R.S.F.S.R. of November 30, 1931, to reorganize as state credit institutions of a local nature with a capital *undivided* into shares. Their shares were annulled and their entire old joint-stock capital and surplus became the basic capital of the reorganized banks. On January 9, 1932, the Commissariat of Finance of the R.S.F.S.R. issued a special circular (No. 7) giving instructions for the procedure to be observed when reorganizing, and published a typical statute (with the consent of the Tzekombank) for the guidance of these banks. See *The Regulations and Orders of the People's Commissariat of Finance of the R.S.F.S.R.,* No. 5 (404), January 27, 1932.

sisted of 41 republican and local banks with 183 offices, branches, and agencies. In places where it has no outlets of its own, the Tzekombank system conducts its business through the State Bank branch system.

The Tzekombank system finances—by means of grants and loans—all *housing* construction, which is undertaken by industry, transport, state institutions, executive committees (ispolkomy), and cooperatives, except such projects as are undertaken by the state and collective farms and which are, therefore, financed by the Agricultural Bank, or except dwelling construction which is taking place in areas where simultaneously industrial plants are being erected. It also finances all municipal construction, such as waterworks, sewerage, roads, bridges, and so forth, except that which is exclusively to serve the needs of industrial or transport undertakings and which is, therefore, financed by the Prombank.[65]

In a similar way and with analogous exceptions it finances the construction of educational institutions, hospitals, sanatoria, public buildings for the housing of state and municipal institutions, and so forth. Besides financing the long-term needs of its clients by means of loans of from 20 to 60 years and grants, the Tzekombank system grants intermediate-specific-purpose loans for from one to five years for the repair and the renovation of dwellings,

[65] Of the 1,060 cities in Russia in 1910 only 219 of the largest had waterworks. In the World War, revolution, and civil war many of these deteriorated. The Soviet Union repaired and extended the area served by the old plants and constructed new ones. In 1928 their total numbered 280, in 1932, 338 (besides those which were under construction in 21 other cities). Sewerage was provided in pre-war Russia for 19 cities. In 1932 the number increased to 48 with 16 additional systems under construction. Electric lights were to be found before 1917 in about 70 cities. In 1932, 600 cities had them. In 1912 Russia had 115 power stations, in 1932, 510. The area served by the street-car lines increased from 1,581 to 2,647 kilometers, and service opened in 11 additional cities. Pre-war Russia had electric railways in 36 cities. The Soviet Union inherited 29 such systems. In 1929, 41 cities—out of 721—had street cars. The census of December 17, 1926, showed that the Soviet cities had a total housing area of 145,000,000 sq. meters, which was quite inadequate for its needs. Between 1929 and 1932 (inclusive) there were added 25,000,000 additional square meters, and another 3,500,000 were about to be completed. On the basis of 5.7 sq. m. per individual, as calculated by Soviet experts, this additional space was to provide housing for 1,200,000 families. See Y. L. Perelman, *Finances and Credit in the Service of Socialist Reconstruction of Cities* (Moscow, State Finance Press, 1933), *passim*. See also Y. I. Seglin, "Perspectives for Municipal Concessions in the U.S.S.R.," *Perspectives for Development of Local Finances of the U.S.S.R. in the Five-Year Plan* (Moscow, Gosplan, "Planned Economy" Press, 1929), pp. 53-63.

municipal buildings and works. Short-term credit, too, is granted by the system to a certain extent. In the case of the Tzekombank itself such credits are generally given in connection with expenditures preliminary to new construction and are later funded into long-term loans or grants. The local banks, however, make also other exceptions, as, for instance, in the case of credit granted to local authorities against anticipated revenue.

As has been seen, the Tzekombank system was authorized to finance its clients by means of loans and grants. Whether it advanced one or the other depended upon the source of the funds at its disposal and the instructions received from the agencies whose funds it was handling. For example, resources derived from its own capital—basic and special—were employed for the purpose of advancing loans and not grants. All advances to housing co-operatives (except in the case of their own share capital) took the form of loans. Similarly, advances to local soviets for local construction out of funds belonging to the state budget took the form of loans.

Grants—paradoxical as it may sound—came from the funds which the clients were required to set aside and deposit with the Tzekombank system. Chief among these were funds for the improvement of workers' living conditions, reserves for depreciation, and allocations from profits. In the case of other sources, including budgetary, the Commissariat of Finance decided which were to take the form of loans, and which, the form of grants.

It will be recalled, however, that according to the Law of March 9, 1934, all advances made by the Tzekombank system to state enterprises belonging to industry, transport, and communication —no matter what the source of those advances may be—must take the form of *grants*. Furthermore, that all of their previous indebtedness to the system and the latter's indebtedness to them was to be annulled.

The financing operations of the Tzekombank system, like that of the other banking systems, has expanded tremendously since 1928–29. During the period covered by the First Five-Year Plan it financed capital construction to the extent of 3,500,000,000 rubles. Of this sum 1,810,000,000 rubles was derived from banking sources and 1,690,300,000 rubles from sources other than bank-

ing. Chief among the banking sources were social insurance funds.

According to the plan for 1933, the financing operations of the Tzekombank were to measure 2,274,000,000 rubles and together with those of the local banks, 3,298,000,000 rubles. Housing, which occupies the chief place in the system's financing plan, was to receive 1,439,400,000 rubles (43.6 percent); municipal construction, 807,200,000 rubles (24.5 percent); and construction pertaining to the "social-welfare" needs of the people (including educational institutions), 978,800,000 rubles (29.7 percent).[66] In 1934 the total amount invested in the enumerated objects of construction reached 5,000,000,000 rubles.[67] The sources which feed the Tzekombank system with funds are manifold. In addition to the basic or statutory capital of the Tzekombank proper (50,000,000 rubles) and of the local municipal banks (in excess of 250,000,000 rubles), the system draws upon special capital funds, clients' own resources, and, finally, budgetary funds. Of the special capital funds those for workers' housing, and those for financing the municipal economy are the most important. The special capital funds for workers' housing are composed of a number of funds, such as the Union special capital fund for workers' housing, republican and regional special capital funds for workers' housing, and special capital funds of cities, resorts, and so forth.

The Union special capital fund for workers' housing is in its turn composed of budgetary (Union) appropriations, allocations from the fund for the improvement of living conditions of workers and employees (known as *Fubr*) of trade and credit institutions and organizations, allocations from the net profit of the State Insurance Fund, increased (for specific purposes) social insurance payments, allocations by the agencies in charge of the social insurance funds and direct appropriations by the Central Insurance Administrations, repayment of loans, and interest earned. Beginning with 1933 there were added new sources: allocation by electric power supply organizations of 25 percent, and by street cars,

[66] Rubinshtein and Tzypkin, *op. cit.*, pp. 18, 58. See also Central Board of Economic Accounting of the Gosplan of the U.S.S.R. *The U.S.S.R. in Figures* (Moscow, Soyuzorgutchet, 1934), p. 181; also *Economic Life*, June 11, 1934. The so-called "social-welfare" group includes education, health, and social insurance.

[67] *Economic Life*, June 16, 1935.

waterworks, and sewerage administrations of 35 percent of their gross revenue.

The Union special capital fund of the Tzekombank for workers' housing constitutes the most important source for financing workers' housing construction. On January 1, 1933, this fund amounted to 1,976,300,000 rubles. In the Tzekombank's 1933 plan for financing housing construction the advances from the above fund equaled 72.3 percent of the total planned figure. The relative importance of the sources feeding the Union special capital fund for workers' housing construction may be gleaned from the fact that of the total increase of that fund by 900,500,000 rubles in 1933 (according to plan), 64 percent was to come from social insurance and 33 percent from allocations by municipal economy.

The republican special capital fund for workers' housing construction is derived from (republican) budgetary appropriations and from allocations from the *Fubr* of trade and credit organizations of republican importance. The regional capital fund for workers' housing construction is derived from allocations from the municipal funds for workers' housing and from the *Fubr* of local trade and credit organizations, and so on. On January 1, 1933, the republican, regional, and cities' special funds for workers' housing with the Tzekombank system (mostly in the local banks) amounted to 373,100,000 rubles.

The special capital fund of the Tzekombank for financing municipal economy is composed of annual appropriations by the state budget, allocations (since 1933) from the gross revenue of municipal undertakings, appropriations by the Central Insurance Administration, repayment of loans and interest by municipal economy, and allocations from the profits of the Tzekombank. On January 1, 1933, the balance sheet of the Tzekombank carried this fund at 170,500,000 rubles. In its 1933 plan, municipal economy advances from this fund amounted to but 37.4 percent.

It will be noticed that the organizations which build up the above-mentioned funds have no claims upon the funds so formed. Nor is interest paid by the system on those funds.

As has been stated above, the Tzekombank system also draws

upon "the clients' own resources." This group is composed of allocations (of 75 percent) from the *Fubr* of *industrial* enterprises,[68] allocations from profits, payments into a reserve for depreciation by the various enterprises, appropriations by the Central Insurance Administration (principally along the lines of health insurance), and the share capital of housing co-operatives.

In addition to participating in the formation of special capital funds by the Tzekombank system, the state budget makes direct appropriations for housing construction. These funds, too, are administered by the Tzekombank. In its 1933 financial plan they were estimated at 857,400,000 rubles or 37.2 percent of the total.[69] The local budget was to appropriate in 1933, 509,500,000 rubles for municipal construction.[70]

The Tzekombank plays a more important part in the preparation of the annual and quarterly construction and financial plans than do the other long-term financial institutions. This is so because there is no Union commissariat of housing and municipal construction.

Its planning work begins with the assembling—with the aid of local municipal banks—of materials pertaining to the financing of housing, municipal, and "social-welfare" construction. This material supplies the Tzekombank with information relative to the actual fulfillment in the various districts of the physical and financial tasks that had been incorporated in the preceding plan, the present stage of construction, and the outlook for the future. It enables the bank to give useful advice to the governmental planning and administrative agencies when annual and quarterly plans are being prepared. As soon as their plans are approved, the Tzekombank draws up, with them as a basis, a consolidated financial and credit plan of its own in which are indicated the channels into which the funds intended for investment during the ensuing period will flow (together, of course, with their size) and

[68] In the Tzekombank's 1933 plan for financing housing construction the *Fubr* was estimated at 194,700,000 rubles or 15.4 percent of the total. The *Fubr* was used by the Tzekombank system for financing housing construction of those combinations and trusts which accumulated it.

[69] Of the 857,400,000 rubles so appropriated, 608,000,000 rubles was set aside for housing construction in connection with industrial undertakings.

[70] Rubinshtein and Tzypkin, *op. cit.*, pp. 59-61.

the sources from which those funds are expected to be derived. This plan is submitted by the Tzekombank to the People's Commissariat of Finance of the U.S.S.R. for approval. The local banks, on the other hand, submit their plans for approval to the local executive committees (*ispolkomy*). The Union commissariats and administrative bodies—on the basis of the sums allotted them in the plan approved by the government—make a distribution of these sums (set limits) among the combinations and trusts under them,[71] indicating at the same time the sources from which these sums are to be derived. They dispatch these figures to the Tzekombank. The latter also receives from the councils of people's commissariats of the R.S.F.S.R. and of the Ukrainian S.S.R., as well as from the republican people's commissariats a statement of the distribution of the sums (limits) allotted them under the plan among the regional (territorial) executive committees (*krayispolkomy*), the city soviets (*gorsovety*), and among the republican and local trusts, with an indication of the sources from which these sums are to be derived. The combinations and trusts present to the Tzekombank (in Moscow and Kharkov), and to the local municipal banks at other points, statements showing the distribution of funds (limits) among the enterprises composing them. They also furnish lists in which are enumerated individual construction projects, together with pertinent information.

The distribution of funds (limits) among the city soviets, regional organizations, district executive committees (*rayispolkomy*), housing co-operatives, separate trusts and enterprises of republican and local importance is carried out on the basis of statements sent by the councils of people's commissariats of the federated and autonomous republics, and by the regional (territorial) executive committees to the local municipal banks. These statements are accompanied by an enumeration of the sources from which the funds are to be derived, and by *titular lists.*

The limits for capital investment, as distributed by the *central* authorities among the combinations and trusts are communicated by the Tzekombank to the local banks in the respective districts.

[71] In the case of republican and local enterprises the distribution is among republics.

As has already been explained, it is through them that the former carries out the bulk of its operations.[72]

In its "control" work the Tzekombank system is, as we already know, governed by the Laws of April 27, 1933, and of September 3, 1934. Although in common with the other banks they have contributed considerably towards eradicating waste, extravagance, and unbusinesslike methods in general, there is still much room for improvement. A number of construction works financed by them was said to lack estimates. It was also asserted that many of the local banks were unable to contribute to the qualitative improvement of their clients' estimates.[73] The cost of construction showed a 13 percent increase in 1934. Then, too, of the planned repayment of loans in 1934 only 74.4 percent was collected—chiefly, because the local banks, which stand very close to the local authorities, extended to them loans for such purposes as meeting budgetary deficits. This particular fault is likely to prevail until such time as the local banks are converted into *branches* of the Tzekombank, and so entirely removed from the influence of the local government (*ispolkomy*). A warning to this effect was sounded in January, 1933, by Commissar Grinko when he said that "unfortunately there is an increase in the number of cases where the local budget reaches out into the municipal banks and uses their funds to finance that part of the local budget which has nothing in common with housing and municipal construction." If this continues, he added, "special measures will have to be taken to strengthen the subordination of local banks to the Tzekombank so as to afford the funds for housing and municipal construction greater protection against the desires of the local budget." [74]

Towards the end of 1935 the Council of People's Commissars, after listening to the report on the Tzekombank for 1934, noted the serious shortcomings in the work of the municipal banks and the inadequate control over them by the Tzekombank. Therefore,

[72] Adapted from Rubinshtein and Tzypkin, *op. cit.*

[73] See *Economic Life,* June 16, 1935.

[74] Report of Commissar Grinko to the Third Session of the C.E.C. of the U.S.S.R. of the Sixth Assembly, January 23–30, 1933. *Stenographic Report* (Moscow, Tzik, 1933), Bulletin 11, pp. 22-23.

it decreed on November 29, 1935, as follows: [75] The local municipal banks are governed in their work by the rules and instructions promulgated by the People's Commissariat of Finance of the U.S.S.R. The accounting procedure and forms employed by them are worked out by the Tzekombank in consultation with the Gosplan of the U.S.S.R. The local banks are accountable, in so far as their work is concerned, not only to the respective executive committees and city soviets but also to the Tzekombank. Their credit-financial plans are examined by the respective executive committees and city soviets and are then submitted for affirmation to the Tzekombank. The latter also approves their annual and quarterly reports, examines them at least once a year, issues instructions concerning all financing carried out at the expense of the state budget, and passes upon the appointment and discharge of managers of local banks by the local executive committees and city soviets. The local banks are forbidden to extend loans for the purpose of covering budgetary deficits. Those of the banks that act as fiscal agents for local budgetary authorities may extend loans to them but only for specific purposes, for a period no longer than a month, never to extend beyond the limit of a fiscal year, and not to exceed 10 percent of the bank's statutory capital. They are forbidden to extend short-term credit to local enterprises engaged in either trade or industry. Short-term credit to enterprises and organizations belonging to the housing and municipal economy may be granted by them only out of their own capital or short-term deposits.

The savings banks.—Because of their participation in the work of directing the flow of capital from savers to users, the savings banks may properly be included among the long-term investment institutions. Their organization and course of operations under the Soviet regime, from 1923 to 1929, has already been traced in Chapter XI.

The savings banks, it will be recalled, are under the jurisdiction of the People's Commissariat of Finance of the U.S.S.R. Their immediate administration is placed in the hands of a body subordinated to the latter, and known as the Chief Administration

[75] *Collected Decrees,* 1935, Decree 486.

(Board) of State Labor Savings Banks and of State Credit. The Chief Board has under it Republican Boards (Upravlenia) of State Labor Savings Banks and of State Credit. These are located at central points in the various federated republics and supervise the work of the savings banks within each of the republics through the medium of Regional or Territorial Boards of State Labor Savings Banks and of State Credit. The latter are located in the main cities of regions and territories and supervise the work of the savings banks located there.

The operating chain of the system consists of: (a) district savings banks, which in addition to the savings bank and state credit business are also charged with the guiding and supervising of savings banks within their districts; (b) city savings banks; (c) savings banks which are attached to railroad administrations and which, in a manner similar to that of the district savings banks, supervise the work of the savings banks functioning along given railroad lines; (d) branches of the district and railroad savings banks; (e) savings agencies attached to post-offices, and various enterprises; and finally, (f) sub-agencies with a limited scope of operations attached to various institutions and enterprises.

The basic problem of the state labor savings banks and state credit system, as shown by its name, is to attract savings deposits as such, and to sell government bonds to the population. The attracted savings deposits, less what is needed to carry on their business, are turned over by the banks to the Chief Board, which invests them, in accordance with the requirement stated in the statute of the savings banks system, in government securities. The funds realized from the sale of government securities are turned over by the banks to the local branches of the State Bank to be credited to the budget account of the Commissariat of Finance.

The interest to be paid by them was fixed, beginning with October 1, 1934, at 8 percent per annum for individual ("natural" persons) current accounts and 9 percent for individual fixed-term accounts. The collective farms were to be paid 6 percent per annum, and other legal entities, 3 percent.[76] Beginning with July 1, 1936, however, their interest rates were lowered (by order of

[76] *Collected Decrees*, 1934, Decree 381.

the decree of June 14, 1936) to 3 percent on deposits by individuals and collective farms, and to 1 percent on deposits by state enterprises and institutions, and by social organizations.

Whence came the revenue with which were paid the high interest rates before 1936 and which enabled the savings banks to meet all operating expenses? The interest which the Chief Board collected on the special block of government securities bought with the savings collected from the population certainly did not suffice for that. As has been stated above, the banks retained for that purpose a portion of the funds collected by them. The amount to which each of the banks was entitled depended on the volume and nature of each type of operation performed by it. It was allowed, for instance, some 9 percent on all of the deposited funds turned over by it to the higher agency before January 1, 1933, and about 12 percent on funds turned over during 1933. The rates, however, varied—depending upon location and the difficulty of obtaining business. Furthermore, to discourage the banks from concentrating on deposits of legal entities (on which they paid a relatively low rate of interest) rather than to seek the expansion of deposits belonging to "natural" persons, the rates paid them were contingent upon the maintenance of a 1 to 2 ratio between those two types of deposits. Failure to observe the specified ratio was penalized by a lowering of the compensating rate.

The banks were also entitled to a certain percentage of the total sales of government securities effected by them. In 1932 they were allowed 1.25 percent of their total sales to workers, and 2.40 percent of their total sales to village folk in general and to collective farms in particular. Besides, they received, as compensation for servicing the public debt, 2 percent of the total debt serviced. The banks were also paid so much for each transfer of funds made by them, and a certain percentage of the total insurance collected by them. In addition, they collected commissions from the State Bank and from various municipal organizations for operations performed on behalf of the latter.

Of their net profits they were required to transfer 50 percent to reserve capital, 30 percent to the treasury; 15 percent was to be retained by the Commissariat of Finance and was to be used

for equipment, repairs, and other needs of the savings banks as well as for bonus payments; 5 percent was to be turned over to the Chief Board for the improvement of the welfare of savings-banks employees (*Fubr*).[77]

The activity of the savings and state credit system during the period of the First Five-Year Plan may be seen from Table 68.

In its campaign to reach and enlist as depositors the entire population, the government, as shown by Table 68, increased the number of savings banks from less than 17,000 in 1928 to 57,684 banks—with staffs in excess of 100,000 people—by the end of 1932. Since the bulk of the population lived in the rural districts, 40,176 of these banks were placed in the villages. As a result of the government's intensive and unrelenting campaign the number of savings banks depositors ("natural" persons) swelled between October 1, 1928, and January 1, 1933, from around 3,500,000 to more than 24,000,000, with an increase in the amount of deposits from 213,200,000 rubles to almost 1,000,000,000 rubles.

On the basis of the above figures, the average savings deposit on October 1, 1928, for the country as a whole was 60 rubles. The average deposit for the urban population, however, was somewhat higher, 71 rubles, but that for the rural population was considerably lower, 30 rubles. By the end of the First Five-Year Plan the average deposit for the country as a whole shrank to 40 rubles. The average deposit for the urban population dropped to 54, and that for the rural population, to 23 rubles.[78]

The drop in the average deposits was probably due to the enrollment as depositors, during the campaign, of many people who could ill afford to save. It may be that this is why the number of depositors by April 1, 1935, was brought down to about 18,500,000 (a decrease of 23 percent as compared with January 1, 1933).[79] Reflecting the steady expansion of the volume of currency in circulation and the cash income of the population, as well as confidence in the ruble's future, the deposits reached

[77] Beginning with 1934. See *Collected Decrees*, 1934, Decree 391.

[78] But see *Economic Life* for April 22, and June 18, 1936, where it is stated that the average deposit amounted to 60 rubles *during* 1933; to 104 rubles on January 1, 1935; to 159 rubles during 1935; and to about 204 rubles on January 1, 1936.

[79] *Economic Life*, April 18, 1935.

TABLE 68

THE SAVINGS AND STATE CREDIT SYSTEM, 1928–33 [a]

	October 1, 1928			*January 1, 1933*		
	In Cities	In Villages	Total	In Cities	In Villages	Total
Number of banks	6,919	9,519	16,438	17,508	40,176	57,684
Number of "natural" depositors (in thousands)	2,562.6	960.6	3,523.2	13,578.7	10,467.8	24,046.5
Deposits by "natural" persons (million rubles)	183.5	29.7	213.2	736.0	241.8	977.8
Deposits by legal entities (million rubles)[b]	62.0	60.6	122.6	211.1	221.5	432.6
Total deposits (million rubles)	(245.5)	(90.3)	(335.8)	(947.1)	(463.3)	(1,410.4)
Number of operations performed during the year (in thousands)[c]	28,848.2	7,960.7	36,808.9	274,424.9	19,498.9	293,923.8
Number of state loan subscribers (in thousands)[d]	8,000.0	....	8,000.0	23,000.0	17,000.0	40,000.0
Total bonds distributed among population (million rubles)[e]	302.6	108.4	411.0	4,172.0	1,270.0	5,442.0

[a] Prepared on the basis of data given in G. I. Bronshtein, *Analysis of the Financial Economy and Profitability of Savings Banks*, second revised and enlarged edition (Moscow, State Finance Press, 1933), p. 39. It will be noticed that the figures for 1933 as given here are at variance with those given in Chapter XI. As has already been explained such discrepancies in Soviet statistics are the result of the practice of publishing "estimated" figures, "preliminary" figures, "final" figures, and "revised" figures.

[b] Deposits by "legal entities" include deposits by local budgetary authorities, by co-operatives, collective farms, trade unions, and so forth.

[c] A comparison between the years 1927–28 and 1932.

[d] In round figures.

[e] Classified on the basis of social classes rather than territorial division.

1,636,000,000 rubles on January 1, 1935; 2,460,000,000 rubles on January 1, 1936; and exceeded 3,000,000,000 rubles on June 10, 1936.[80]

Despite, however, the placement of more than 40,000 banks in the villages and the payment of high interest rates, the government found it difficult to attract peasant funds. According to the figures cited by Commissar Grinko in his report to the Fourth Session of the Central Executive Committee of the U.S.S.R. of the Sixth Assembly, the peasantry at the end of 1933 constituted but 27 percent of the total savings banks depositors (26,000,000). and their deposits amounted to no more than a mere 10 percent of the total deposits (1,050,000,000 rubles).[81]

The intensive activity of the labor savings and state credit banks with respect to the distribution of state loans among the population is attested by the fact that by the end of the First Five-Year Plan period these banks transferred to the treasury a total of 5,442,000,000 rubles, and during 1931–34 (inclusive), 10,500,000,000 rubles on that account.[82]

The savings banks system not only sold securities, paid interest, and prizes (on the lottery issues of the state loan) to bondholders, but also extended loans against the premiums paid. It likewise paid out pensions and grants on behalf of certain institutions. These, however, were by no means the only activities in which it engaged. It was also charged with spreading among the broad masses the method of settling pecuniary transactions without the employment of cash.[83] In consequence, the banks of that system began to perform such operations as the payment of their clients'

[80] *Economic Life,* April 18, 1935, April 22, 1936, and June 18, 1936.

[81] *Stenographic Report* (Moscow, Tzik, 1934), Bulletin No. 13, p. 19. The Fourth Session was held between December 28, 1933, and January 4, 1934.

[82] G. I. Bronshtein, *op. cit.,* pp. 3-5; *Economic Life,* April 22, 1935. Up to January 1, 1936, the Soviet government borrowed from its citizens about 17,000,000,000 rubles. On September 1, 1936, a new loan of 4,000,000,000 rubles was issued. At the same time the seven outstanding old internal loans of the average maturity of ten years, with interest rates from 8 to 10 percent (10 percent on loans issued before 1935, and 8 percent on loans issued in 1935) were ordered converted into a single "Internal Loan of the Second Five-Year Plan" with a maturity of twenty years and with interest rates (on the portion which is not a non-interest *lottery* issue) at 4 percent. *Economic Life,* July 2, 1936.

[83] See Chapter XIV.

electric bills, telephone bills, rent, trade union dues, co-operative dues, and so forth. It meant, of course, an additional burden and added costs. But then such settlements are socially desirable, particularly in a country like the Soviet Union. Besides, the treasury, as we have seen, was eager to keep the volume of currency circulation at a low figure.

To bring the banks close to the population and make the people see that the banks are intended to serve their interests, the savings system was permitted in 1930 to make long-term deposits in local municipal banks, and in agricultural banks, in each case with the permission of the respective Republican Board of State Labor Savings Banks and of State Credit and with the approval of the commissariat of finance of the given federated republic.[84] These deposits, however, were not to be in excess of 5 percent of the total increase in the deposits of that particular section of the country over the preceding year.

In 1932 and 1933 the banks were permitted to use a portion of the year's increase in deposits for the purpose of granting long-term loans to village and city soviets, district executive committees, and collective farms.[85] Furthermore, in an attempt to attract depositors and to develop their non-cash settlement transactions, particularly those concerning a very important item—wages, the savings banks began to serve as paymasters and fiscal agents for various organizations. They also agreed to receive, on behalf of municipal enterprises, *cash* payments for services rendered by the latter, undertook to sell street-car tickets, and so forth. The mushroom growth of the system's network, the rapidly increasing volume and variety of its operations, and the large additions to its staff of new, inexperienced employees hindered, of course, the development of proper organizational technique and efficient methods, as well as served to make the cost of obtaining savings inordinately high. The clients were not only poorly served, in general, but were not infrequently denied the right to withdraw their deposits in whole or in part. One can easily imagine the effect of this on depositors, particularly the peasantry whom the state was

[84] *Collected Decrees*, 1930, Decree 569.
[85] *Ibid.*, 1932, Decree 100; *ibid.*, 1933, Decree 338.

so eager to attract. Steps, however, were taken to stamp out the undesirable features. The Council of People's Commissars of the U.S.S.R., in the summer of 1933, after declaring that "the work of rendering service to depositors and holders of government bonds was insufficiently organized, that the number of savings banks and the cost of their upkeep was too high, and that not enough attention was being paid to the composition of the staff and the selection of new employees," requested the Commissar of Finance "to prevent the savings banks from hindering in any way whatsoever the withdrawal of deposits . . . and to prosecute those who are guilty of it." The Council also ordered a curtailment of the system's network.[86] Pursuant to the Council's decision, the number of savings banks had been reduced by the end of 1933 to 48,000. In 1934 the Commissariat of Finance ordered the savings banks system to discontinue the performance of such commissions as paying out wages to workers and employees of various city enterprises and institutions, the sale of street-car tickets, and the like. The savings banks were also required to curtail and discontinue the acceptance of *cash* payments due municipal organizations for services rendered. In the spring of 1935 they were further ordered to cease serving as fiscal agents for various organizations and bodies.[87] The present policy is to make these banks concentrate on the two main branches of their work—deposits and government securities. The improvement of the quality of the services rendered will, among other things, depend upon the betterment of the training imparted to the personnel of that system. It will also be necessary to make the compensation for that work more attractive. As it is, the turnover of the savings system's personnel is entirely too high.[88]

[86] *Ibid.*, Decree 230.
[87] See *Economic Life*, April 14, 1935.
[88] *Ibid.*, April 22, 1935.

XVI

SUMMARY AND CONCLUSION

THE history of banking and money in Russia is, in a number of respects, more instructive than that of any other country. It traces the evolution of these institutions through all stages of economic development, from a backward agricultural stage to a modern capitalistic stage, and then, by way of a most devastating war, revolution, and civil war, to a stage known as "War Communism," followed by a temporary retreat and reintroduction of certain capitalistic institutions—still, however, under a dictatorship of the proletariat and with the avowed aim of building socialism, and, finally, to a stage of an extremely rapid building of industry and agriculture along socialistic lines, according to plans covering the entire economy, and under central direction.

A brief summation of the most outstanding topics with which the preceding pages have dealt will help to refresh the history of these institutions in our minds.

Before the abolition of serfdom (1861) Russia lived largely under an independent, self-sufficient economy. Domestic trade and production for the market were relatively small. The state-owned banks, which began to be established in the second half of the eighteenth century, of necessity catered to agriculture, that is, to the landed aristocracy. Favoritism and lax methods in general characterized the early banks. Attempts to develop commercial banks were not very successful. After a number of reorganizations and in consequence of a serious financial panic in the late fifties of the preceding century, these banks were liquidated and their place was taken in 1860 by a new bank—the Imperial State Bank.

The unsound banking practices of those days were paralleled by an unsound monetary policy. The introduction of paper currency—the assignat—in 1769 was instrumental in substituting overissue of paper money for overissue of debased currency as a cause for the frequently recurring cycles of inflation. It was not until 1897 that the currency was finally stabilized, the gold stand-

ard introduced, and the right to issue "credit notes" granted to the State Bank.

The rapid economic progress which set in soon after the liberation of the serfs and which continued almost uninterruptedly until the beginning of the World War was made possible by, among other things, the evolution over the same period of a modern banking structure. On January 1, 1914, the latter, in addition to the State Bank—which evolved into a central bank with numerous branches—included 47 joint-stock commercial banks with 743 branches, engaged in both commercial and investment banking business; 1,108 mutual-credit societies; 319 municipal banks; 2 state banks for agriculture—the Nobles' Land Bank and the Peasants' Land Bank; a number of joint-stock land banks, and cooperative land banks; and over 8,000 savings banks.

Pre-war Russia depended to a large degree upon foreign capital and money markets as well as upon foreign goods. She was also one of the world's principal exporters of grain. The closing of her frontiers in 1914, therefore, seriously affected her economic and financial systems. The Law of July 27, 1914, put an end to the redemption of paper money in gold. It also authorized the State Bank to expand its fiduciary issue and to discount short-term treasury obligations. The State Bank, whose notes before the war were to all intents and purposes gold certificates, began to issue paper money against treasury bills, running into billions of rubles, as security. The currency in circulation rose from 1,630,400,000 rubles at the beginning of the war to 9,439,800,000 rubles on March 1, 1917 (at about the time when the Provisional government succeeded the Czarist government), and to 18,917,000,000 rubles on November 1, 1917 (at about the time when the communists came into power). On the latter date the ruble had a purchasing power of less than ten pre-war copecks. Owing to the shortage of commodities and the consequent privileged position of sellers, as well as to the steady depreciation of the currency, the volume of credit transactions declined considerably. Also, the government itself granted advances to makers of munitions. The joint-stock commercial banks, in an attempt to make the best of the changed conditions, speculated in commodities and securities,

and granted credit for such purposes to others. The State Bank was becoming less and less a bankers' bank and more and more an auxiliary of the treasury.

The seizure of power by the communists in November, 1917, ushered in extraordinary changes in the political, social, and economic life of the country. There followed, among other things, the abolition of private property in land, the nationalization of industry, and the banning of the open market. Old stores, the output of state and co-operative enterprises, and the requisitioned or confiscated agricultural products were directed into state warehouses and rationed out to the people. Pecuniary taxes, rents, payments for the use of gas, electricity, and other municipal services were discontinued. But although the orientation during the period 1918 to 1921, known as the War Communism period, was towards the abolition of such institutions as purchase and sale of commodities, and, consequently, of the use of money as a medium of exchange, commodities continued to be sold throughout this period on illegal markets, and wages were paid partly in kind and partly in money.

Banking was declared a state monopoly. The private joint-stock commercial banks were merged in the State Bank, which in 1918 was renamed the People's Bank. Their funds were confiscated and their shares annulled. The Nobles' Land Bank, the Peasants' Land Bank and all private mortgage banking institutions were liquidated as now useless institutions, inasmuch as land was no longer private property. A similar fate was shared by all other banking institutions. Nor was the People's (State) Bank itself spared. As early as March, 1919, the Eighth Congress of the Russian Communist Party proclaimed that "as a planned, social economy becomes organized this will lead to the extinction of the bank and to its transformation into a central bookkeeping apparatus of the communist society." In conformity with that philosophy a decree was published on January 19, 1920, directing the "abolition" of that bank and the transfer of its assets and liabilities to a Central Budgeting and Accounting Administration. The new body was concerned principally with the issue of paper money. Now the budgetary deficits of the Soviet govern-

ment for 1918, 1919, and 1920 were 31,126,000,000 rubles, 166,447,000,000 rubles, and 1,055,555,000,000 rubles, respectively. Since it could not borrow and could not raise pecuniary taxes (having destroyed the objects of taxation), it had to lean heavily on the printing presses. The notes in circulation rose from 19,577,400,000 rubles on November 1, 1917, to 1,168,596,900,000 rubles on January 1, 1921. Prices on the latter day, according to the official index, were 16,800 times as high as those in 1913.

The policy of War Communism, though serviceable on the military fronts of 1918–20, proved a complete failure on the economic "front." Accordingly, in 1921, following the closing of the war with Poland and the defeat of the White armies, the old policy was scrapped and a New Economic Policy (Nep) was adopted. Requisitions and confiscations were declared at an end. Instead, the peasants were required to pay a tax in kind. The open market became legalized and private trading was permitted. State enterprises were ordered to adhere to "commercial principles" and to strive to make profit. "Free" services no longer existed. A beginning was made in the introduction of pecuniary taxes. The new order could not, however, operate without banks and currency. And so in the fall of 1921 there was set up a State Bank "for the purpose of aiding by means of credit and other banking operations the development of industry, agriculture, and trade, as well as to concentrate monetary transactions and to carry out other measures for securing a sound monetary circulation." The bank was permitted to grant both short-term and long-term credits. In fact, it was at first intended that the State Bank (with branches) remain the only credit institution in Soviet Russia. Beginning, however, with 1922 other credit institutions began to spring up. Among them were the Industrial Bank (Prombank), the Co-operative Bank (Vsekobank), municipal banks (later headed by the Central Municipal Bank or Tzekombank), the Bank for Foreign Trade, private mutual-credit societies (no longer in existence), agricultural credit societies (later headed by the Central Agricultural Bank), and savings banks. These so-called special banks, each intended to minister to the needs of a par-

ticular branch of the nation's economy, were permitted to engage in both short- and long-term credit business.

The Soviet ruble (*sovznak*) continued, however, to depreciate rapidly. By the end of 1922 the total circulation reached 2,000,000,000,000,000 rubles. At that time the price level, according to Soviet indices, was 21,242,000 times as high as that in 1913. During the single year of 1922 prices rose by 7,270 percent. The rapidly depreciating currency operated as a brake upon the development of the newly created credit institutions and upon the development of the national economy in general. It was essential to stabilize the purchasing power of the ruble. That, however, was as yet impossible, inasmuch as the budget could not be balanced without the help of the printing presses. Attempts, therefore, were made to find a substitute for gold as a measure of value. Among the substitutes used were index numbers. Since they were imperfect and could not be employed as media of exchange, their usefulness was limited. The government, therefore, decided to permit the State Bank to issue banknotes (*chervontzy*). The latter were to be secured by a 25 percent precious metals and foreign exchange reserve. They were issued in high denominations, and were intended to serve wholesale trade and industry. Their issue began towards the end of 1922. Their purchasing power at first underwent a sharp decline but beginning with the second half of 1923 became more or less stabilized. The rapidly depreciating sovznaks, however, were still in circulation. An interesting phenomenon was, consequently, produced—the existence in a country side by side of a stable and a most unstable paper currency. The ratio of their exchange was constantly changing. Official quotations were, therefore, being published. They differed quite often from the rates of exchange prevailing in the free market. Such paper standard can be characterized as *bipaper* standard. It led to a great many difficulties. The use of *legal-tender* sovznaks could not be avoided. Trade, industry, and workers could not, despite the various protective devices, escape heavy losses on their exchange. Cost calculation, and even mere bookkeeping, became exceedingly difficult. Planning and estimating were quite im-

possible. The budget, to which state enterprises were shifting their losses in general and those sustained on the exchange of the sovznaks in particular, was also losing directly on the revenue collected by it. The desired "smytchka" (*rapprochement*) between the village and the town was being jeopardized. The peasantry began to restrict the sales of their produce, raised their prices, and, finally, began to refuse to accept the sovznaks altogether. The government decided to expedite the projected Monetary Reform. This was accomplished by a series of decrees in February and March, 1924. A new currency, treasury notes, of denominations of one, three, and five rubles, was issued; silver and copper coins were introduced, and the sovznaks were redeemed at the rate of one treasury ruble for 50,000 rubles of the 1923 pattern. Inasmuch as a ruble of the 1923 pattern equaled 1,000,000 pre-1921 rubles, 50,000,000,000 pre-1921 rubles exchanged for one treasury ruble. In a word, the holder of 500,000,000 old rubles received one copeck in coin.

The stabilization of the currency sent trade and industry upgrade. By 1927–28 a number of industries attained to the 1913 level. In this they were helped by the rapidly growing banks. During the formative period the special banks, eager to attract deposits, competed with one another and with the State Bank for clients. They tried, in fact, to convert the State Bank into a bankers' bank. As it was, the State Bank dealt directly with borrowers. However, by a governmental decree in 1927 the State Bank was given leadership over the other banks, clients were apportioned among them, and a foundation was laid for the transfer of all short-term credit to the State Bank. The special banks were to concentrate on long-term credit.

The Soviet banking system underwent very important changes after 1928. In that year, it will be recalled, there was inaugurated the First Five-Year Plan. Its purpose was to speed up the industrialization of the country, to effect a socialistic reconstruction of the economy in general and of agriculture in particular. It aimed to develop the country to a point which would enable it successfully to withstand attacks by enemies. In fact, the Soviet Union undertook to catch up with and to surpass the most advanced

countries. Some 120,000,000,000 rubles were expended with that in view between October 1, 1928, and January 1, 1933, when the First Five-Year Plan was declared completed. The Second Five-Year Plan (1933–37) calls for an outlay of 333,800,000,000 rubles. Although it proved impossible to attain the ambitious goal outlined in the First Five-Year Plan, the Soviet Union succeeded in laying a foundation for a vast industrial structure and in reconstructing its agricultural economy along *collective* lines.

As has been stated above, the adoption of the Five-Year Plan was responsible for the further shaping of the course of the country's banking system. Let us first briefly trace the changes which the State Bank underwent as a result of the adoption of a program of rapid industrialization. That program meant a deepening of planning. The credit which was being granted by one enterprise to another interfered, however, with proper planning. The Credit Reform of 1930, therefore, prohibited the employment of this kind of credit in the socialized sector. No longer was bank credit to be granted to "X," the seller, to enable him to extend credit to "Y," the purchaser. Instead, each enterprise was to be supplied with an amount of *bank* credit sufficient to enable it to meet all of its needs. As translated into practice by the State Bank, the Credit Reform gave rise to the following procedure: all accounts between enterprises of the socialized sector were cleared through the bank. For each enterprise there was opened a mixed account which was credited with all of its claims against other enterprises, and debited with all claims by other enterprises against it. The claims did not have to be proved, and, furthermore, the bank honored them irrespective of the state of the buyer's account. This unscientific procedure led to an uprooting of whatever sound business principles the various enterprises had theretofore employed and to an overexpansion of credit and currency. The unscientific methods which the State Bank pursued during 1930 and 1931 had their origin in the "leftist" ideology, or in the "swing to the left" that marked those years. The development of socialistic beginnings turned the heads of a good many influential communists. They believed that the country was nearing a higher phase of socialism and that such institutions as banks and money

were doomed. They counseled, therefore, the elimination of the special banks, and the transfer of their functions to the State Bank. Furthermore, the State Bank itself was to evolve into a clearing bureau with planning functions. Purchase and sale, credit and money, according to them, were about to disappear. Apparently State Bank officials took such talk seriously and tried to adjust themselves to the new order. Hence the peculiarity of the methods employed by them. The sad state of affairs demanded, however, a remedy. By a series of decrees (published on January 14, March 20, and July 23, 1931) the government ordered the bank to discontinue the "automaticity" surrounding the payment of claims and the release of credit by the latter, to restore contractual relations and business principles in general, and to wield financial control over the borrowers in such a manner as to induce them to take a greater interest in the fulfillment of their plans, in the reduction of their costs of production, and in the accumulation of profit. The bank was also ordered to cease granting credit for the purpose of enabling enterprises to cover up losses. Steps were at the same time taken to endow the various enterprises with a new sizable working capital of their own. This helped them to meet their heavy indebtedness to the banks.

In 1932 the structural apparatus of the State Bank was reorganized along departmental lines. As a result there were formed at the Main Office a number of departments each of which was entrusted with the supervision of the credit and planning work pertaining to a given branch or department of the national economy (such as heavy industry, light industry, and so forth). There are also a number of other departments (such, for example, as organizational and auditing, and foreign operations) at the Main Office. The activities of the various departments are co-ordinated by the Economic-Planning Department of the bank, which, among other things, is charged with the preparation of the consolidated cash and credit plans of the State Bank system. The various departments supervise the activities of the bank's branches (of which there are 2,800) through regional and territorial offices. The latter not only supervise the work of the branches in their regions but also engage in banking business as such. Their appa-

ratuses resemble that of the Main Office but are, of course, somewhat simpler. In the few years that have elapsed since that time the quality of the bank's work has shown considerable improvement. Its "frozen" assets, which in 1931 amounted to 1,200,000,000 rubles, decreased by January 1, 1936 (on which day its outstanding credit amounted to 26,600,000,000 rubles), to 280,000,000 rubles. Little by little the bank's planning work and financial control keep on improving.

Inasmuch as the bank is backed by the budget (which recently added more than 5,000,000,000 rubles to the former's resources), its financial strength did not suffer by the mistakes of 1930–31. By freeing the bank in 1932 from the long-term agricultural credit business (which was transferred to it in 1931), and by permitting the reorganized special banks to transact their business through the agency of their own branches (rather than through that of State Bank branches as they had been compelled to do since they were deprived of their branches), the government enabled it to concentrate on the work for which it is really adapted. At the present time it conducts short-term credit business, of which it has a monopoly, serves as a bank of issue, as a fiscal agent of the treasury, as a cashier for the special banks, and, in fact, for the entire country.

The lot of the special or long-term banks has not been on the whole a particularly happy one. Despite their efforts, it proved impossible for them to attract "free" funds. They depended, therefore, to a large extent upon the budget. In 1932 they were reorganized as four all-Union banks: Bank for Financing the Capital Construction of Industry and Electrification, or "Prombank"; Agricultural Bank, or "Selkhozbank"; Bank for Financing Co-operative Capital Construction, or "Vsekobank" (which in 1936 was reorganized as an All-Union Bank for Financing Capital Construction of Trade and Co-operatives, or "Torgbank"), and Bank for Financing Municipal and Housing Construction, or "Tzekombank"; these were placed under the direct jurisdiction of the Commissariat of Finance. With the exception of the Tzekombank, which carries on its work through a system of local municipal banks, the reorganized banks have a network of

branches. They finance the enterprises and organizations within the fields assigned to them by means of grants or repayable loans. The amounts granted or loaned depend, of course, upon the approved plans of the clientele. Although the long-term institutions are required to draw up plans of their own and follow them closely once they are approved, their plans constitute in the main a reproduction of the financial plans of the particular branches of the economy which they serve. Under the First Five-Year Plan, the long-term institutions were instrumental in investing a total of 27,900,000,000 rubles, of which 22,400,000,000 rubles (or 80 percent) were either budgetary funds or else funds which the various enterprises were required to set aside (allocations from profits, reserves for depreciation, and so forth) and turn over to the banks. The relative importance during that period of strictly "banking" funds in the case of the Prombank (which was responsible for placing more than 75 percent of the total investments by the four long-term institutions) becomes clear when it is recalled that of the 21,322,000,000 rubles invested by it under the First Five-Year Plan 95 percent were furnished by the budget, or were set aside by the enterprises themselves.

By the Law of March 9, 1934, the Prombank, the Tzekombank, together with the local municipal banks, and the Vsekobank were ordered to finance capital construction (including housing, municipal and social-welfare construction) of *state* enterprises in industry, transport, and means of communications by means of *grants* exclusively. They were further ordered to annul all indebtedness of such enterprises to them, as well as their own indebtedness to those enterprises. Furthermore, all indebtedness of state enterprises to one another contracted in connection with the financing of capital construction was to be forgiven in cases where the construction of the financed objects had been completed. This procedure was to be followed also in the future. It should be remembered, however, that during the few years preceding the passage of the Law of March 9, 1934, financing by means of grants assumed considerable proportions. As the First Five-Year Plan gained momentum, the Prombank, for example, began to finance state enterprises exclusively by means of grants. Financing

by means of budgetary redistribution of the national income, as shown by Soviet experience, facilitates planning. Inasmuch as there are other indices by which the efficiency of Soviet enterprises can be measured, and other incentives to cause them to carry out the state's plans for accumulation of funds, the shift to non-returnable financing will not in any way injure the economy. Such a method of financing very well suits Soviet conditions. Presumably, as co-operative enterprises give way to state enterprises (and collective farms to state farms), financing of capital construction by means of returnable loans will entirely disappear. The shift to non-returnable financing changes, however, the nature of the investment institutions. Despite their designation as banks, it is, in fact, difficult to think of them as such. Inasmuch as their chief function at the present time is the *exercise of control* over the expenditure of funds by their "clientele," they are in reality control departments of the Commissariat of Finance. It must not be supposed, however, that their present rôle is one of minor importance. One of the most difficult problems that the Soviet Union must solve is how to increase the productivity of labor and decrease costs. Financial control, when properly wielded, ought to prove helpful in this connection.

The nature of Soviet banks, as explained in Chapter X, differs markedly from that of capitalist banks. They are not free entities to do as they please. Their activities are at all times shaped in such a way as to synchronize with the economic and the socio-political life of the country. Their plans, like those of other enterprises and institutions, must be in line with the general policy. If their resources are not adequate to permit such compliance, the government will either provide them with additional means or, if that is impossible, tone down the projected expansion. Although they are permitted and even required to earn profit, this is not at all their leitmotif. It is a side issue with them. They have no choice whatsoever in selecting clients. If a client's approved credit or financial plan calls for a given amount of bank credit or budgetary financing, the bank in question must grant it, even though it may later invoke certain well-defined sanctions against him for non-compliance with the provisions governing the re-

payment or the use of such funds. Nor is the Soviet discount rate intended as a regulator of the volume of credit and currency, and of the flow of foreign funds to and from the country. Its sole purpose is to enable banking institutions to be self-supporting and to accumulate reserves.

Although Soviet credit and investment institutions are fighting hard to improve their usefulness to the country and have made substantial progress in that direction, they have not as yet purged themselves completely of bureaucracy, red tape, and inefficiency. One, however, must not judge them too severely; rapid expansion and too many changes are not conducive to improvement. Nor must they be held responsible for the shortcomings of the still young and green national economy which they serve.

The improvement of the ruble's position will no doubt facilitate the work of these institutions. It will be recalled that when dealing with the Credit Reform of 1930 it has been stated that the unscientific methods surrounding its introduction into practice were responsible for an overexpansion of credit and an overissue of money. This, however, was but one of the factors which contributed to the currency inflation of that period. The figures of the Five-Year Plan, it will be recalled, were based upon the assumption that the productivity of the country's labor would rise by a given percentage and that the cost of production, in consequence of this and other factors, would decline to a certain assumed point. Inasmuch as these assumptions did not materialize, and the credit to which the financial plans of the various enterprises entitled them proved, in practice, utterly inadequate, the State Bank had to expand the volume of its credit and of its note issue beyond what was planned. In fact, this is why the total actual outlay under the First Five-Year Plan considerably exceeded the planned outlay. According to the plan, the total short-term credit of the country was to increase between October 1, 1928, and October 1, 1933, from 3,900,000,000 to 7,275,000,000 rubles. On November 1, 1933, however, the short-term credit granted by the State Bank stood at 14,423,600,000 rubles. Similarly, the total currency in circulation, which was to increase between the two above-mentioned dates from 1,971,400,000 to 3,221,400,000 rubles,

stood at the end of 1933 at 6,861,548,000 rubles. The employment of money substitutes and the expansion of "moneyless" settlements, as described in Chapter XIV, helped in getting along with a smaller volume of printed money in circulation than otherwise would have been necessary. Furthermore, the raising of the legal ratio between treasury notes (which are issued by the State Bank on behalf of the treasury, and used by it for the same purposes as banknotes) and banknotes from 50 percent at first, to 75 percent (in 1928), and then, to 100 percent (in 1930) helped to preserve the statutory gold-reserve requirement behind the latter. Prices in the open market, upon which the workers in 1928–30 depended for a considerable part of their supplies, began to soar. The government, therefore, introduced ration cards. The cards enabled the holders (workers and employees) to buy in special so-called "closed" shops limited quantities of bread and other commodities at low prices.

On July 1, 1936, the volume of banknotes transferred to the Main Office of the State Bank amounted to 6,535,991,510 rubles. If the volume of treasury notes in circulation, the figure for which is not yet available, equaled that of the banknotes (as in the past), then the total volume of notes in circulation on that day stood at about 13,000,000,000 rubles. The volume of State Bank short-term credit outstanding on January 1, 1937, rose to 34,000,000,000 rubles. But because of an appreciable increase in the volume of consumers' goods in the meantime the ruble's position not only did not become more difficult, but even eased.

Between 1927–28 and the end of 1932 the retail trade turnover increased from 14,740,500,000 to 35,504,300,000 rubles. In 1935 it amounted to 80,000,000,000 rubles. The output of producers' goods keeps on mounting and makes possible the further expansion of consumers' goods. This is in line with the avowed aim of the Second Five-Year Plan (1933–37) to raise the workers' level of consumption by from 2.5 to 3 times.

The success attending the campaign for the mass collectivization of the peasantry, which originally was fraught with great danger, and the consequent increased supply of foodstuffs, raw materials, and commodities in general made possible the abolition of the

rationing system. On January 1, 1935, the sale of bread, flour, and cereals was derationed. On October 1, 1935, the sale of meat and its products, butter and vegetable oil, fish, sugar, and potatoes was derationed. By January 1, 1936, it became possible to abolish the rationing of manufactured goods.

Now it may be recalled that as the First Five-Year Plan was progressing there evolved a rather unique system of retail distribution. Rising prices and a commodity famine were responsible for the introduction of the "closed" shops wherein limited quantities of goods were sold to holders of ration cards at relatively low prices. Towards the end of the First Five-Year Plan, the government decreed the establishment of so-called "commercial" shops wherein unlimited (that is, so long as the supply lasted) quantities of goods were sold to all who were able to pay prices several times those prevailing in the "closed" shops. The government also authorized the establishment of open markets wherein peasants were permitted to sell foodstuffs at competitive prices. Another unique organization, the "Torgsin" system, was launched in 1930. In the Torgsin stores unlimited quantities of goods of wide variety and best quality were sold to holders of precious metals (czarist gold coins, jewelry, and so forth) and foreign exchange—a domestic export trade so to speak.

The purchasing power of the ruble under these circumstances depended, among other things, upon whether or not one was a holder of a ration card (and that in turn depended on one's status), and upon the type of shop to which one had access. The quantity, variety, and quality of goods sold differed materially from shop to shop. If one was assigned to a poorly equipped "closed" shop, and therefore, depended upon the open market for a larger portion of his total purchases, his ruble would naturally buy less. If one had access to a Torgsin store, he could buy goods at reasonable prices without standing in long lines. Price indices under these conditions could not be very significant. The publication of official price indices was discontinued in 1931.

As we have seen, the "closed" shops were discontinued during 1935. The Torgsin shops were discontinued beginning with February 1, 1936. At present all living in a given zone, no matter

what their status, pay the same prices for goods with no restriction (except in the case of speculators) as to the quantity purchased. The new prices, however, were fixed at a point approximately midway between the ration prices and those which were charged by the "commercial" shops. The higher price level was needed not only for the purpose of bringing the demand for goods into equilibrium with their supply, but also to make possible the upward revision of prices paid to the peasantry for their produce, so as to stimulate them to greater production. To enable the worker to meet the higher cost of living an upward revision of wage scales followed. At the same time the government unrelentingly pursued its policy to increase the purchasing power of the ruble through an expanded output of goods, and a lowered cost of production. As a result, prices in 1935 and the early part of 1936 considerably declined.

The elimination of the "closed" and Torgsin shops makes possible the construction of a representative index of prices. It is only with the aid of such an index that the true purchasing power of the ruble can be determined. The elimination of the Torgsin shops, it may be added, made possible the elimination of illegal traffic in rubles on the "black" exchanges in so far as such traffic was made profitable by the divergence of prices charged by the "commercial" and Torgsin shops.

The ruble, as we have seen, is an *internal* currency and is not quoted on the foreign exchanges. The Soviet Union pays abroad in gold, and the official exchange rates established by it at home are based on the assumption that the chervontzy are *gold* rubles. These rates are generally held close to parity. The expansion and modernization of the gold industry help the Soviet Union not only to meet all foreign commercial obligations promptly but to amass a sizable gold reserve. The total firm cover of the State Bank, which on October 1, 1928, amounted to 282,230,000 rubles, jumped by October 1, 1935, to 1,005,459,020 rubles (of which 963,369,860 rubles consisted of gold coin and bullion). The 1934 output of gold in the Soviet Union amounted to 4,200,000 ounces (or, priced at $35 per ounce, $147,000,000). Determined, however, to outdistance South Africa, the Soviet Union set before itself the

goal of bringing up the production of gold in 1937 (the completion of the Second Five-Year Plan) to $500,000,000. Whether South Africa is outdistanced or not and whether the particular goal set for 1937 will be reached in that year or not, the gold industry and the output of gold in the Soviet Union are likely to expand.

Under the Monetary Reform of 1924 the ruble was stabilized at its pre-war mint parity even though the Soviet price level at the time was higher than that of Russia in 1913 or of gold-standard countries in 1924. Had it not been for such organizations as the Torgsin shops, where foreigners could buy goods at reasonable prices—even though the price level kept on rising—tourist traffic would have been discouraged. Hence the same decree (of November 14, 1935) which ordered the discontinuance of the Torgsin shops also directed the State Bank to exchange in 1936 foreign currency (transfers or cash) for rubles at a new rate of 3 francs = 1 ruble (or 33.3 rubles per 100 francs, as against 7.6 rubles per 100 francs before) with a corresponding adjustment for other currencies.[1] France being the principal gold-standard country, the franc was chosen as the yardstick for conversions. The new rate, however, applied only to exchanges carried out within the Soviet Union; it did not apply to foreign trade. By a further decree of February 29, 1936, the government ordered its application beginning with April 1, 1936, to all transactions involving foreign exchange. In its balance sheet of April 1, 1936, the State Bank, following the instructions laid down in the above decree, valued fine gold at 5.6807 rubles per gram (as against 1.29 rubles before); dollars, at 5.06 rubles (as against 1.15 rubles before); sterling, at 25.04 rubles (as against 5.67 rubles before). This amounted to a devaluation of 77.5 percent. The ruble, however, is still overvalued. But as has been pointed out above, the Soviet government is bending its efforts to raise the purchasing power of the ruble.

A question which is not infrequently raised by students whenever the subject of Soviet banking is brought up is: is the Soviet banking system superior to that of a capitalist country and could such system or any of its features, particularly those pertaining to planning, be successfully used in a capitalist country?

The naïveté of this question is, of course, apparent. A banking

[1] But see p. 448, *supra*.

system is good or bad depending on how well it serves the needs of the particular economy for which it is designed. Even though yielding excellent results in one country, it may prove utterly unsuitable under a different economic or political set-up. The Soviet banking system, in particular, can thrive only under such economic, social, and political conditions as are found in the Soviet Union. That means extreme centralization of authority, and nationalization not only of the banks but of all branches of the national economy. This is not to say that the planning feature as such, albeit in a somewhat restricted fashion, could not be used by banking systems in capitalist countries. To be *effective,* however, planning must embrace the entire national economy. Its successful employment in such countries, therefore, demands the cartelization of trade, industry, mining, transportation, and so forth; concentration in agriculture—either along the same lines as in industry or else along co-operative lines; concentration, perforce, in banking, and the apportionment of clients among the separate banking units; the setting-up of a central planning authority to which plans drawn up by the various business organizations are submitted for the purpose of being co-ordinated and welded into a national plan, the creation of price and profit regulating agencies, and the readiness and ability of the treasury to extend loans and to grant subsidies (presumably out of funds raised for that purpose by taxation) to enterprises which are socially desirable but commercially unprofitable. Extreme centralization of authority such as exists under fascism can hardly be avoided under such order. Of course some advocates of planning for capitalist countries seem to create the impression that this can be accomplished without resorting to radical changes. If they are sincere, such people betray a very superficial knowledge of planning. At any rate, it must be remembered that half-measures sometimes result in more harm than good.

Another question that may be raised is: what of the future trend of Soviet banking and monetary development? In the absence of extraordinary happenings that development in the immediate future will presumably proceed along the present lines. It may be expected that financial institutions will still be required

to exercise rigid control of all expenditure of funds advanced by them, as well as to enforce business principles in general. Stress will continue to be laid upon the necessity of exercising greater judgment in selecting future "financiers" and of imparting more thorough and better training to them than in the past. The State Bank will presumably continue to widen the field of non-cash settlements. The long-term financial institutions will presumably continue to evolve into departments of the Commissariat of Finance for the enforcement of control over the funds that are being invested in the national economy.

As to the future of the ruble, one may recall the declaration of Stalin: ". . . We shall continue to have money," he said early in 1934 at the XVII Party Congress, "for a long time, until we achieve the first stage of communism. . . ." But first of all it is necessary to develop "an ideally organized system of Soviet trade, something which we are far from having and which we shall not have so very soon." The present policy of the Soviet Union, as we have seen, is to strengthen the position of the ruble.

But what of the more distant future? In this connection it may be useful to recall that projections into the future are usually predicated upon the assumption that the road which is being traversed in the present will continue to be traversed in the future. Despite the progress made by science, our mind's eye cannot as yet, however, see conditions which do not exist in the present, but which may arise years later. This, of course, is one of the reasons why so many projections into the future, which looked plausible when originally made, proved false later on. Even short-time projections are not free from such fate. No student of finance, for example, could know in 1913, or even immediately before the Revolution, what was going to happen to Russian banks and money, say, in 1918–21. The more distant the future in which projections are made, the wider the margins of error, and the smaller the survival value of such projections. It is best, therefore, not to attempt the impossible.

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INDEX

Abolition of money, whether intended in 1917–21, 99–110
"Abstract" gold standard, use of, 139 ff.
Acceptance method of settling debts, 365 *n*, 376–77
Accreditive method of settling debts, 365 *n*, 376–77
Adams, T. S., 139 *n*
Agricultural Bank (Central)
1924–28, organization of, 283, 302; statutes of, 302–3; capital of, 302, 304; interest rates of, 302 *n*; rôle of, 303; deposits in, 303, 304; loans and discounts of, 304; amendment of statute, 306–7
since 1928, reorganization of, 352 *n*, 455 ff., 478–79, 481; management of, 455, 456, 457; financial control by, 452–53, 457–61, 485 ff.; financing by, 461 ff., 481–82, 483–85; interest rates of, 463–64; debts forgiven by, 463, 485; functions of, 481; branches of, 481, 488–89; capital of, 482; sources of grants and loans, 482; "indivisible funds" and, 482–83, 484; budget and, 482, 483; deposits in, 484, 489; shortcomings of, 485 ff.; planning procedure of, 488–89
Agricultural banks
before the World War, 5–8, 23–25
after Revolution, liquidation of, 63–64
1922–28, organization and evolution of, 283, 284, 300 ff.; network of, 284, 303, 303 *n*; statutes of, 301; shortcomings of, 305–6; amendment of statutes, 306
since 1928, 334, 477–89; interest rates, 480; budget and, 482, 483–84; state sector and, 483–84; collectives and, 483–85, 485 *n*
Agricultural credit associations: organization and operations of, 283 *n*, 300, 303 *n*; reorganization of, 478–79; financial statement of, 479
Agricultural credit societies: organization and operations of, 283, 301, 302, 303 *n*, 306, 388–89; effect of inflation on, 286
Agricultural credit unions, 303 *n*
All-Russian Co-operative Bank, *see* Vsekobank
All-Ukrainian Co-operative Bank, *see* Ukrainbank
All-Union Agricultural Co-operative-Collective Bank, 352 *n*, 353, 478–79
All-Union Co-operative Bank, *see* Vsekobank
Annulment of debts, by and to investment banks, 461 ff.
Arbitrage transactions, rôle of, 84–86
Assignat banks, established in 1769, 4, 4 *n*
Assignats, French, 180
Assignats, Russian, 4–5, 179–80, 507
Austro-Hungarian Bank, inconvertible banknotes of, 148 *n*
Automatic equilibrium, in the U.S.S.R., 150–51, 158–60
Averbakh, I., 345 *n*

Bachi, R., 222 *n*
Baikalov, A. V., 416 *n*, 417 *n*
Bakunin, M., 103 *n*
Bank for Financing Municipal and Housing Construction, *see* Tzekombank
Bank for Financing Socialist Agriculture, 353, 455, 481
Bank for Foreign Trade, *see* Vneshtorgbank
Banknotes, *see* Chervonetz
Banknotes, why issued in larger denominations, 155
Bank of Long-Term Credits for Industry and Electrification, *see* Prombank
Banks: agitation for commercial and investment, 281–82; in early times, 5–9, 507; 1860–1914, 10–26; 1914–17, 27–52; 1917–21, nationalization and liquidation, 53–71; 1921, re-establishment of, 111–145; 1921–28, short-

Banks (*Continued*)
term, 111–74, 244–80; 1922–28, evolution of specialized long-term investment, 281–331; Russian abroad, 299 *n*; since 1928, short-term, 332–403; since 1928, specialized long-term investment, 450–506; socialist philosophy on the rôle of, 54 ff., 100 ff., 360 ff., 360 *n*, 375; distinguishing characteristics of Soviet, 273–75; effect of inflation on development of, 283–86; lesson furnished by Soviet, 522–23; future of Soviet, 523–24
Banovich, M., 331 *n*
Barou, N., 297 *n*, 302 *n*, 304
Barun, M. A., 357 *n*, 400 *n*
Beckhart, Benjamin H., 148 *n*
Beckmann, Fritz, 150 *n*
Beer, M., 100 *n*
Bellers, John, on money, 100
Bernatzky, M. W., 14 *n*, 19 *n*, 27 *n*, 29 *n*, 42
Bilimovich, A. D., 25 *n*
Bimetallic standard: rated, 176, 177; unrated, 177, 179
Bipaper standard, 175–80, 197
Bliakher, V. J., 359 *n*, 425 *n*
Bliakhov, J. R., 260 *n*, 264 *n*
Bogolepov, M., 34 *n*, 334 *n*
Boguslavsky, S. T., 479 *n*
Brailowsky, A. M., 99 *n*
Branches, *see* under respective banks
Bray, John Francis, on money, 101
Bronshtein, G. I., 328 *n*, 420 *n*, 479 *n*, 503 *n*, 504 *n*
Bronsky, M., 107 *n*, 442 *n*
Bruikhanov, N. P., 425
Budget: effect of inflation upon, 198–99; balancing of, and stable currency, 236–37, 237 *n*
1914–17, 33–35
1918–21, 72 ff., 94–97, 104, 111
1921–28, 116–18, 130, 136–37, 188, 190 ff., 207–11, 242–43
since 1928, 333, 334, 336, 384, 385 *n*, 406
Budgetary grants, financing by means of, 288 ff., 450 ff., 461 ff.
Bukharin, N., 55 *n*, 56 *n*, 70 *n*, 103, 104, 105, 106
Butaev, K., 323 *n*

Campbell, M., 363 *n*, 424 *n*, 445 *n*
Capital investment
1922–28, 450
since 1928, 332 ff., 450 ff., 483–84
Capital market, before the World War, 20–22, 23–26, 27
Carli, G. R., 138 *n*
Cash planning, by State Bank, 276–79, 364, 392, 398–400 *n*, 401–3
Cassel, G., 141
Central Agricultural Bank, *see* Agricultural Bank, Central
Central Budgeting and Accounting Administration, as successor to People's Bank in 1920, 71
Central Municipal and Housing Bank, *see* Tzekombank
Centrosoyuz, 67 *n*, 118, 473, 476, 477
Chalkushian, S., 134 *n*
Chamberlin, W. H., 430 *n*
"Change stamps," 31, 80–81
"Change tokens," 31, 81
Chapman, J. M., 439 *n*
Charitable boards, banking functions of, 7
Chernekhovsky, E. D., 307 *n*, 310 *n*
Chervonetz: meaning and origin of, 145, 148 *n*
1922–24, 146–74; purposes for which issued, 147; metallic reserve behind, 148–52, 158, 159; how placed in circulation, 155–58, 178–79; purchasing power of, 158–71, how influenced, 160–61, 165 ff.; depreciation of, 170–71; relation between sovznak and, 175–80; ratio between treasury currency and, 206, 212, 241
1924–28, volume of and security behind, 255–56; quoted on foreign exchanges, 262 ff.
since 1928, planned volume, 334; actual issue, 373, 404–5, 407, 408–9, 412–15, 448–49; ratio between treasury currency and, 405–11, 427–28
Chervonetz—standard accounts, 195
City banks, *see* Municipal banks
Civil War, 53 ff., 73, 105, 107
Clearing accounts, *see* Settlement accounts
Clearing departments, 369–70
"Closed" shops, 424–25, 432 ff., 444, 448
Cole, G. D. H., 150 *n*
Combinations: types of, 350 *n*; working capital of, 368, 369, 370–71, 374, 380

Commercial-Industrial Bank, *see* Prombank
Commercial paper, use of, 37, 44, 345, 345 *n*, 347 *n*, 348, 349, 351 *n*, 375
Commercial shops, 424–25, 432 ff., 445
Commissariat of Finance, functions of, 341 *n*
Committee of Banks (1924), 266–67
Commodity ruble, 137, 139 ff., 218–19
Consumers' Co-operative Bank (Pokobank), 282, 296–97
Conto corrento, 348, 349, 354, 365, 367, 369, 371, 373 *n*, 374, 421, 421 *n*
Contraband import trade, 224–25
"Controlled" inflation, whether possible, 115 ff.
Convertibility of notes: in the U.S.S.R., 148–52, 154; principle of, 154
Conveyor method of credit, 348
Co-operative Capital Construction, Bank for Financing, *see* Vsekobank, Torgbank
Co-operative credit, *see* Vsekobank
Co-operative credit, old central bank of: merged in the People's Bank, 65–67
Co-operatives: during War Communism, 65–67, 67 *n*; during Nep, 113–14, 296, 297, 300; diminishing importance of, 476–77
Co-operative Transit Bank (Riga), 299
Cost of construction, 453, 457–58, 485, 488, 498
Credit, *see* Banks, and under names of respective banks
Credit, "earmarked," 135
"Credit Bureau," 316 *n*
Credit notes, introduction of (1841), 5
  before 1917, 240 *n*
  of 1918, 78, 79
Credit planning, *see* Planning, Five-Year Plan
Credit Reform of 1930: short-term credit and, 270 *n*, 352; reasons for, 345–49, 351; history of, 346 ff.; gist of, 351; faulty application of, 354–58, 363 ff.; "leftist" ideology and, 358 ff.; and amendatory legislation, 363 ff.; after amendatory legislation, 375; reorganization of agricultural credit system and, 478–79
Crimean War, and inflation, 5, 8–9, 11
Currency, *see* Money

Dalbank, *see* Far Eastern Bank
Debasement of coins, in early Russian history, 3–4
Debts, Soviet methods of settling, 346–49, 351, 354–56, 376–77
Degtiarev, F., 359 *n*, 425 *n*
Delimitation of banking activities, 267 ff.
Dementiev, G., 34
Demostenov's index of food prices (1914–16), 49
Denis, Ch., 98 *n*
Denny, Harold, 416 *n*
"Denznaks," 81
Depreciation (*see also* Index numbers of prices, Inflation), insurance against, 133, 134, 249
Derchenkov, G., 331 *n*
Devaluation of currency: compared with repudiation, 223 *n*; "benefit" from, through expanded exports, 238; before twentieth century, 3, 5, 13; in 1921–22, 79 *n*, 126–27; in 1935–36, 264 *n*, 409 *n*, 414, 447–49, 522
Dezen, A. A., 134 *n*, 135 *n*, 245 *n*, 254 *n*
Diachenko, V., 240 *n*, 358 *n*, 360 *n*, 361 *n*, 362 *n*, 363 *n*, 442 *n*
Discount policy, difference between Soviet and capitalist, 248–49
Discount rates, *see* Interest, and under respective banks
Dmitriev-Krymski, G. N., 118 *n*
Dobb, Maurice, 174 *n*, 203 *n*
Doroshenko, A., 297 *n*
Drisin, I. B., 147 *n*, 153 *n*, 265 *n*, 266 *n*, 303 *n*, 323 *n*
Dulles, E. L., 223 *n*
"Duma" notes, 43, 78, 80
Duranty, Walter, 430, 431 *n*, 433
Dzenis, O., 323 *n*

"Earmarked" loans, meaning of, 135
Economic trends
  before 1860, 3–9, 507–8
  1860–1914, 8, 9, 17, 21–22, 23, 24, 25, 208, 210, 508
  1914–17, 27–30, 32 ff., 42, 43, 44, 46, 47 ff.
  1917–21, 53 ff., 63 ff., 72 ff., 87 ff., 105, 107, 111, 112, 114, 117, 509–10
  1921–28, 111–14, 116, 117, 126, 130–32, 143–44, 160, 170, 171–74, 175, 184–90, 193–99, 200 ff., 239, 241–42, 244–

Economic trends (*Continued*)
45, 256–57, 270–76, 281 ff., 297, 300 ff., 307, 318 ff., 333
since 1928, 322–23, 332–39, 345 ff., 381–84, 385 ff.; 398 *n*–99 *n*, 403, 404 ff., 412–13, 415–18, 423 ff., 450 ff., 512 ff.
Edie, Lionel D., 141 *n*, 222 *n*, 237 *n*
Edwards, George W., 422 *n*
Efimov, O. J., 278 *n*, 376 *n*, 392 *n*, 393 *n*, 394 *n*, 395 *n*, 403 *n*
Eisler, Robert, 238 *n*
Electrobank: organization and early history of, 283, 293 *n*; liquidation of, 293; balance-sheet items of, 294
Eliacheff, B., 34 *n*, 40 *n*
Elkin, W. A., 149 *n*, 153 *n*
Elster, K., 428 *n*
"Ened," meaning of, 110
Engeev, T., 178 *n*
Engels, Friedrich, 54, 55, 56, 106, 443
England, restoration of gold standard in 1925, 220–22
Epstein, E., 20 *n*, 43 *n*, 44 *n*
Equilibrium between Soviet and world price levels, why not practicable, 238
Exchange, "black," 84, 86, 161–63, 166, 180–84, 225, 232, 432, 447, 448, 521
Exchange Fund, 234 *n*
"Exchange" losses by holders of sovznaks, 194 ff.
Exchange rates, *see* Foreign exchange rates
Exploitation of "colonies" within a country, theory of, 203
Exporters, direct dealings between foreign firms and Soviet, 260
Export-import plans, 261
Exports, expansion of, and devaluation of a currency, 238
Extra-planned loans, 375 ff.

Falkner, S. A., 170 *n*
Far Eastern Bank, 258, 282, 285, 329–30
Feiler, Arthur, 141 *n*
Feitelberg, M., 82 *n*, 84 *n*, 85 *n*
Fiduciary issue: of State Bank expanded, 30, 42, 77–78, 106; why formal declaration of its expansion needed, 77
Finance capital, 54, 55 *n*, 56 *n*
Financial control by investment institutions, 452, 453, 457–61, 468, 473–76, 485–88, 489, 498, 517, 524
Firm-cover plan, 261
Fiscal and economic year, changed, 336 *n*
Fisher, Irving, 139 *n*, 438 *n*
Fisher, W. C., 139 *n*
Fisher's compensated dollar, 438 *n*
Fisk, H. E., 40 *n*
Five-Year Plan, First: rapid transition to socialism under, 323, 332, 333, 337, 345, 346, 351, 352–53, 354, 358; estimates and actual performance, 332–38, 404–5, 518; expansion of deposits under, 334, 371–74, 404; expansion of short-term credit under, 334, 371, 372, 379–81, 404; imperfections of, 358, 359, 405, 518; Credit Reform of 1930 and, 346 ff.; State Bank and, 332–449; money, prices, and gold under, 404–49; long-term investment institutions under, 450–506
Five-Year Plan, Second, 338
Fixed prices, confiscatory under inflation, 53, 73
Fleming, P., 431 *n*
Foreign banks, liquidation of, 64–65
Foreigners, and the problem of exchange, 447–48
"Foreign exchange inflation," after Monetary Reform, 233
Foreign exchange plans, 261–62
Foreign exchange policy, 260–64
Foreign exchange rates: 1878, 12; as a measure of purchasing power, 47–52, 92; 1914–17, 47–51; 1917–21, 83–86; 1922–28, 160–66, 232–33, 264; since 1928, 409, 414, 448, 522; paper standard and, 260–61; under a monopoly of trade, 263–64; fixing of, 263, 264; and Soviet prices, 447
Foreign exchanges, methods to protect a currency on, 262–63; chervontzy and, 262–64
Foreign exchange transactions, regulations, 164–66, 260
Foreign investments in Russia, 21, 21 *n*, 22, 26, 27
Foreign loans, annulled in 1918, 53, 72
Foreign markets, dependence upon, before the World War, 27–28
Foreign trade
1909–13, 27, 210
1914–17, 28
1918–28, a state monopoly, 53; balance of, 117, 210; policy, 257–60

since 1928, 334–35, 414–15
Foreign trade, Bank for, *see* Vneshtorgbank
Foreign trading agencies, 258–60
Free market, rôle in 1926–30, 423–25, 432 ff.
Friedman, S. L., 45 *n*, 312 *n*, 321 *n*

Gaido, G., 328 *n*
Gatovsky, L. M., 424 *n*
Gendel, S., 470 *n*, 489 *n*
Germany, post-war stabilization of mark, 223–24
Gide, Charles, 100 *n*, 101 *n*
Gindin, I., 20 *n*
Giro system, 418–20
Gold: confiscation of, 61, 86; as equilibrator of world prices, 150; price of, 409, 448; production of, 1912–37, 416–18
Gold coin, valued higher than bullion in 1922–24, 161–63
Gold reserves: importance when off gold standard, 40–41; purchasing power of ruble and, 437
1862, 12
1897–1914, 16
1914–17, 37, 39–41
1921–28, 136, 148–52, 158, 159, 255–56
1928–36, 408–9, 411–14
Gold ruble: rates, 12, 13, 86–87, 160–66, 232–33; old, content of, 14 *n*, 148; as a measure of value during inflation, 139 ff.
Gold standard: old Russia, 13–14; Soviet Union, 137, 139, 142–43, 148–52; restoration of—in England in 1925, 220–22, 223; in Italy, in 1927, 222, 223; in France, 1928, 222–23
Golovanov, S. A., 74 *n*
Gosbank, *see* State Bank
Government loans, 254, 503, 504, 504 *n*
Gray, John, on money, 100–101
Greenberg, E. M., 382 *n*
Gregory, T. E., 222 *n*
Gresham's law, and paper money, 82, 197
Grinko, G. F., 379 *n*, 381 *n*, 405 *n*, 445, 451 *n*, 453, 464 *n*, 483 *n*, 498 *n*
Groman, V. G., 172 *n*
Guriev, D. A., 5, 6–7

Hensel, P. P., 73 *n*, 209 *n*
Hawtrey, R. G., 219 *n*
Hoover, Calvin B., 174 *n*
Hughes, Alice, 431
Hungarian communists, handicapped by money of own design, 82–83
Hyper-inflation, 1923–24, 180 ff.

Ikonnikov, B., 470 *n*
Imperial Assignat Bank, 4 *n*, 5 *n*
Inconvertible banknotes, *ab initio*, 148, 154
Index numbers of prices: use of, in early times, 137 ff.; as a measure of value during inflationary period, 137 ff.
1914–17, 47–52
1918–22, 90–93, 126–32
1923–24, 166–71, 173, 186–87
1924–28, 230, 257
1928–31, 423; discontinuance of, in 1931, 423 ff.; estimates of price level in the absence of, 430 ff.
Industrial Bank, *see* Prombank
Industrial Fund, project for, 291–92
Industry (*see also* Economic Trends): production of—in 1913, 208; in 1918–20, 88; in 1921–24, 208; in 1927–28, 333; in 1932, 336–37; in 1937 (planned), 338; reorganization in 1929, 349–50
Inflation: defined, 231–32, 429; steps to return to normalcy after, 11–12; lack of confidence a factor, 47–52, 89, 115–16; effect upon government loans, 73; effect upon taxation, 73; whether possible to control, 115 ff.; impeding economic progress, 131–32, 197–99; evils of, under bipaper standard, 193 ff.; protection of various classes against, 194–97; France said to exemplify advantages of, 223 *n*; under a regime of regulated prices, 231–32; development of banks checked by, 283–86; rendered less dangerous, 430; in early times, 3–5, 11, 12
1914–17, indices of prices, exchange, and currency compared, 47–52, 90 *n*; under the Provisional government, 42–43
1917–21, prices, exchange, and gold rates, 83–96; currency shortage, 96–97
1921–22, 126–32
1922–24, 180 ff.

Inflation (*Continued*)
1924–25, 228 ff.
1928–34, question of, 412–13, 427–36
Insurance against depreciation, 133, 134, 249
Interest, why central banks do not pay, 254
Interest rates
of State Bank: 1914–17, 19, 38; 1921–22, 133; 1923–28, 245–46, 254; since 1928, 245, 254, 385–86
of investment and savings banks: 1922–28; 302 *n*, 321, 325, 331; recent, 463–64, 500–1
private: 1922–23, 134; 1925, 319, 321
International balances, settlement of: before 1930, 258–59; after 1930, 259–60
Investment banks (*see also* Long-term investment institutions) 281–331, 450–506

James, F. Cyril, 221 *n*
Jevons, W. S., 138 *n*
Joint-stock commercial banks, Czarist: before the World War, 19–22; balance sheets, 1875–1914, 21; 1914–17, 29, 43–47; balance sheets, 1914–17, 45; merged in State Bank, 60–63
Joint-stock land banks, Czarist: 23–24, 25; nationalization and liquidation of, 60, 64
Joint-stock specialized banks, Soviet, 281–331

Kaganovich, L. M., 468 *n*
Kaktyn, A., 172 *n*, 270 *n*, 321 *n*, 352 *n*, 453 *n*
Kalmanovich, M. I., 374 *n*, 379 *n*
Kankrin, E. F., 5, 7
Katzenellenbaum, Z. S., 77 *n*, 82 *n*, 117 *n*, 133 *n*, 176 *n*, 197 *n*, 244 *n*, 285 *n*
Kaufman, I. I., 4 *n*, 148 *n*
Kemmerer, E. W., 115–16
"Kerenky" notes, 42, 43, 78, 80, 82
Keynes, J. M., 155 *n*, 220 *n*, 438
Kirillov, I. A., 287 *n*
Kisch, Sir Cecil H., 149 *n*, 153 *n*
Kiselev, S., 171 *n*
Klepikov, and the "ened," 110 *n*
Kondratiev, N. D., 169 *n*, 171 *n*
Korobkov, V. S., 345 *n*, 418 *n*, 420 *n*
Kovalevsky, V. M., 3 *n*
Krylov, A. I., 416 *n*
Kuperman, J., 171 *n*, 267 *n*
Kuzovkov, D., 126 *n*, 170 *n*, 199 *n*, 231 *n*, 240 *n*

"Labor unit" as money, 107 ff.
Lags and premiums, under hyper-inflation, 180–81
Land, abolition of private ownership, 53
Lande, E. Z., 371 *n*, 379 *n*, 380 *n*, 389 *n*
Lebedev, B., 425 *n*
Lebedev, N., 470 *n*, 489 *n*
"Leftist" ideology, difficulties caused by, 358 ff., 444
Legal tender, 211, 213, 214, 215
Lemaire, G., 58 *n*
Lenin, N.: followed Marx, 56; on the Paris Commune lesson, 56; on nationalization of banks, 56–60; list of immediate measures (1917), 57; on money, 103, 104 *n*, 105; on the errors of War Communism, 111–12 *n*; on the future of gold, 113; on the stabilization of the ruble, 145 *n*; giant monopolistic bank favored by, 270, 281, 453
Leontiev, A., 440
Levik, B. I., 329 *n*, 354 *n*, 376 *n*, 377 *n*, 379 *n*, 387 *n*, 389 *n*
Levin, A. A., 260 *n*, 264 *n*, 384 *n*
"Limits," credit and investment, 356–57, 364, 365 *n*, 367 *n*, 377, 391, 400–1, 468, 497
Liquidating technical collegiums, 62
Liquidity, importance under Soviet conditions, 275
Livshitz, F. D., 297 *n*, 307 *n*, 309 n, 317 *n*
Livshitz, M., 323 *n*
Loan for economic reconstruction (1925), 290–91
Loans, *see* Government loans
Loans and discounts, *see* under respective banks
Loans during inflation, 131–32, 133–34
Local note issues (1918–21), 97–98
Loevetzky, D. A., 83 *n*, 164 *n*, 165 *n*, 225 *n*, 237 *n*, 264 *n*
Long-Term Credit, Department of, 289, 292
Long-term investment institutions
before 1860, 5 ff.
1860–1914, 20–26, 27
1914–17, 43–47
1918–21, 59–64

1922–28, 281–331
since 1928, 334, 450–506; financial control by, 452, 453, 457–61; branches of, 453–54, 456; reorganization of, 455 ff.; management of, 455, 456, 457; functions of, 455 ff.; short-term credit of, 456; 470–71, 472, 477, 478, 490, 493, 498; financing by means of grants, 461 ff.
Lowe, J., 138 *n*
Lupandin, K., 251 *n*, 264 *n*, 278 *n*, 279 *n*, 280 *n*, 289 *n*, 312 *n*, 348 *n*, 349 *n*, 419 *n*, 420 *n*

MacCrosty, H. A., 222 *n*
Managed currency: explained, 437–38; related to ruble, 438–39; related to compensated dollar, 438 *n*
Mariasin, L. E., 381 *n*
Marx, Karl: on the rôle of banks, 54 ff.; on the transitional stage, 70; on the influence of money, 99 *n*; differed with utopians on rôle of money, 101 *n*, 102–3; on money, 151, 152 *n*; on the rôle of gold in a monetary system, 152 *n*
Measure of value, inflation and, 136–45
Mekler, S. S., 290 *n*
Menger, Anton, 101 *n*, 102 *n*
Metallic coins, disappearance of, 31, 426
Metallic reserve: inclusion of silver in, 149, 149 *n*; against banknotes, in the U.S.S.R., 149–52, 407, 411 ff.; recommended by World Economic Conference in 1933, 149 *n*
Michelson, A. M., 33 *n*, 34 *n*
Mid-Asiatic Bank, 258, 283, 285, 330
Mitchell, Wesley C., 138 *n*
Mittelman, E., 381 *n*
Molotov, V., 337 *n*
Monetary Reform
1897, 4–5, 11–15
of 1924, 200–243 immediate causes for adoption, 200; opposition to, 205–6; Sokolnikov's draft of, 206–7, 440–41; foundation for, 207 ff., 241; postponement impossible, 211; how executed, 211 ff.; and shortage of commodities, 224, 229 *n*, 230–33; and shortage of small change and notes, 233 ff.; appraisal of, 236 ff.; and development of banks, 286
Money: origin and evolution, 3–4; early history, 3 ff., 507; volume in circulation, before 1860, 4–5, 11 *n*; 1860–97, 11–12, 14 *n*; 1897–1914, 16; 1914–17, volume and purchasing power of, 35, 37, 41–42, 48–51, 508; 1917–21, 76–77; kinds issued, 78–83; varying purchasing power, 79, 82–83; preference for old designs, 79–83; depreciation—in terms of foreign exchange, 83–86; in terms of price level, 87–96; in terms of gold, 86–87; causes for decreased demand, 88–89; total purchasing power, 93–94; shortage, 96–97; by whom issued, 97–98; whether its abolition was intended, 99–110; volume in circulation, in 1921–22, 128–29; depreciation in 1921–22, 126–32; devaluation in 1922, 79 *n*, 126–27; uniformity introduced, 127 *n*; volume in circulation, 1922–24, interesting phenomenon, 175–80; how reduced to stable currency, 191; and Monetary Reform of 1924 (which see), 200–243; composition at time of Monetary Reform, 212 *n*; regulations pertaining to metallic, 213 ff.; reintroduction in 1924 of metallic, 213 ff.; volume, 1924–28, 227–28, 255–57; since 1928, 334, 373, 404–5, 407, 408–9, 410, 412–13, 426–27, 428, 519; Soviet, nature of, 436–47; Soviet attitude toward, 439 ff.; Soviet, future of, 524
Moneyless economy, 54
Moneyless settlements, 106–7, 418–21
Moratorium of 1914, 29
More, Sir Thomas, on money, 99
Morin, A. I., 346, 347 *n*
Morgunov, P., 264 *n*
Moscow City Bank, *see* Mosgorbank
Moscow Narodny Bank, Ltd., 299
Moscow Narodnyi Bank, circumstances surrounding its nationalization, 65–67
Mosgorbank (1923–28), organization of, 282–83; branches of, 285, 310; capital of, 308, 309; operations of, 308–10; interest rates of, 309; principal accounts of, 309
Mukoseyev, V. A., 19 *n*, 22 *n*, 23 *n*

Municipal and Housing Bank, Central, *see* Tzekombank
Municipal and Housing Construction, Bank for Financing, *see* Tzekombank
Municipal banks (*see also* Mosgorbank, Tzekombank)
before 1914, 19, 22–23
1922–28, early history of, 282–83; branches of, 285, 310; model statutes for, 308; operations of, 308, 310; interest rates of, 309; capital of, 310, 314; relations with Tzekombank, 310–12; deposits in, 310, 314; resources of, 312–15; planning by, 312 *n*; detailed analysis of loans, 314–15; short-term credit and, 352 *n*
since 1928, financial control by, 452, 453, 457–61, 489; interest rates of, 463–64; shift to long-term investments, 490; relations with Tzekombank, 490 *n*, 491–92, 499; share capital eliminated by, 491 *n*; operations of, 492–93; resources of, 493–96; short-term credit and, 498–99; shortcomings of, 498
Municipal construction, progress of, 492 *n*
Mutual-credit societies: before 1914, 19, 23; liquidation of, 64
1922–28, re-establishment of, 318–19; number of, 285, 320; purpose of, 318–19; 321–22; capital of, 319, 320, 321, 324; interest rates of, 319, 321; operations of, 319 ff.; decline and disappearance of, 320 ff.

Nagler, G., 290 *n*
Nationalization of banks, 53–71
Nationalization of industry and trade, 53 ff.
Natural economy, 54, 74, 88–89, 94–95, 107
Nedelin, S. I., 479 *n*
Neiman, G., 424 *n*, 435 *n*
New Economic Policy: and attitude toward money, 111 ff.; capitalistic forms under, 316, 316 *n*; Stalin on, 442
Nickel coins, reason for issue in 1932, 427
"Nikolaevskie" notes, 78, 79, 80, 82
Nobles' State Land Bank, 23–25, 63
Non-cash settlements, *see* Moneyless settlements
Non-planned loans, 375 ff., 378–79
Non-socialized sector, 322–24, 360 ff.
North-Caucasian bank, 285
"Northern rubles," and the Bank of England, 98 *n*
Note issue (*see also* Chervonetz, Money): revenue from, obtained by Czarist government, 193 *n*, by Provisional government, 193; 1918–21; 94–95; 1922–24, 190 ff.

Obligations of the R.S.F.S.R., 81
Obligations of the Tzentrokassa, 1922–25, 192 *n*
O.D.K., 289, 292
Ol, P. V., 27 *n*
Orbelov, A., 318 *n*, 321 *n*
Orlov, A. G., 309 *n*
Ottolenghi, C., 222 *n*
Owen, Robert, on money, 100, 101
Ozerov, I., 3 *n*

Palaschenko, I., 301 *n*
Paper money (*see also* Money): eulogized, 95–96; "parallel," 176; foreign exchange rates and, 260–61
Pawnshops, 283, 330–31
Pearson, Frank A., 139 *n*
Peasants' Land Bank, 23–25, 63
Pecqueur, Charles, 55 *n*
"Penzenki" notes, 78
People's Bank of the R.S.F.S.R.: State Bank's name in 1918 changed to, 60, 62–63, 88; various organizations merged in, 67–68; shortcomings of, 68–69; abolition of, 70–71
Perelman, Y. L., 492 *n*
Permanent revolution, theory of, 203
Pevzner, S. L., 147 *n*, 153 *n*, 265 *n*, 266 *n*, 303 *n*, 323 *n*
Piatakov, G. L., 347 *n*, 348 *n*
"Piatakovki" notes, 78 *n*
Planned loans, 375 ff.
Planning (*see also* Five-Year Plan): by State Bank, 276–79, 350–52, 355, 357, 364, 367, 386–88, 390–403; by investment banks, 306, 456, 466–70, 472, 474–76, 496–98; by industry, 398–400 *n*, 400–401, 456, 466–68, 474; of

capital construction, 459 *n*; in agriculture, 480, 488–89; by capitalist countries, 522–23
Pogrebetsky, A. I., 99 *n*
Pokobank, 282, 296–97
Popov, A. T., 324 *n*
Popov, P. I., 47 *n*
Porter, G. R., 138 *n*
Potiaev, A., 66 *n*, 67 *n*, 68 *n*
Precious metals, early Soviet policy, 61, 86
Premiums and lags, under hyper-inflation, 180–81
Preobrazhensky, E., 55 *n*, 56 *n*, 70 *n*, 96 *n*, 203, 443, 444
Pre-war gold ruble, 137, 139 ff.
Price level (*see also* Index numbers of prices): methods of comparing world prices with a given country's, 140 ff.; atttempts to lower, 224 ff., 386, 427, 449; since 1928, 404–49
Price regulation, 229–32
Private trade, 53–54, 68, 73, 88, 89, 111–12, 134 *n*, 322–24, 360 ff.
Prombank
1922–28, why established, 202; early history of, 282; branch system of, 284; organization and administration of, 287–88, 293 ff.; capitalization of, 287, 289, 293–94; operations of, 288 ff., 293 ff.; loans and discounts of, 288 ff., 293, 295; deposits of, 288–90, 294–95; balance-sheet items of, 289; Department of Long-Term Credit within, 289, 292; inadequate resources of, 290–93; reorganization in 1928, 292–93; statutes of reorganized, 293–96; short-term business transferred to State Bank, 270, 293; annual credit plans of, 295; control functions of, 295–96
since 1928, and First Five-Year Plan, 334; and the Credit Reform of 1930, 453–54; reorganization of, 455 ff., 464.; management of, 455, 456, 457; rôle and functions of, 452, 453–55, 464–65, 492; financial control by, 452, 453, 457–61, 468; financing by, 452, 461 ff., 465–66; interest rates of, 463–64; branches of, 454, 465; planning by, 466–68
Protecting a currency on foreign exchanges, methods of, 262–63
Proudhon, P.-J., 55 *n*, 101, 103
Public debt: annulled, 53, 63; conversion of, 504 *n*
Purchasing power of ruble, *see* Index numbers of prices
Purchasing power parity, 140–41

Railroads, financing of, 464 *n*
Ramsay, David, 217 *n*
Rationing cards, 424, 430, 432 ff., 447
"Reckoning" tokens, *see* Settlement tokens
Redemption of notes, *see* Convertibility of notes
Reingold, I., 290 *n*
Repudiation of currency, compared with devaluation, 223 *n*
Requisition of agricultural products, 53, 88, 111
Reserve ratio, *see* Gold reserves
Revaluation of ruble (1935–36), 264 *n*, 409 *n*, 414, 447–49
Revolution, November, 1917, effect of, 53 ff.
Ricardo, David, on labor as a measure of value, 109 *n*; premium on gold a measure of depreciation, 140 *n*
Robertson, D. H., 221 *n*
Robey, R. W., 439 *n*
Rodbertus, Karl, on money, 101, 102
Rogers, J. H., 223 *n*
Roginski, G., 245 *n*, 254 *n*, 422 *n*
"Romanov" notes, 43, 78, 79, 80, 82
Ronin, S., 21 *n*
Rosenberg, Otto, 148 *n*
Roskombank, history of, 282, 313–16
Rubinshtein, J., 59 *n*, 245 *n*, 254 *n*, 422 *n*
Rubinshtein, S. B., 291 *n*, 354 *n*, 357 *n*, 368 *n*, 371 *n*, 451 *n*, 452 *n*, 458 *n*, 461 *n*, 467 *n*, 471 *n*, 482 *n*, 494 *n*, 496 *n*, 498 *n*
Ruble (*see also* Chervonetz, Inflation, Money): silver, 3–5, 14, 31, 213–14, 235–36; gold content of old, 14 *n*, 148; of the 1923 pattern, meaning of, 184 *n*; control, *see* Financial control; depreciation of, before 1931, *see* Inflation; depreciation of, after 1931, 424–25, 427 ff.; revaluation of in 1935–36, 264 *n*, 414, 447–49, 522; Soviet attitude toward, 439 ff.
Russian Commercial Bank, *see* Roskombank

Safe deposit boxes, confiscation of contents in 1917, 61
St. Petersburg Private Commercial Bank, 20
Saint-Simonians, and centralization of credit, 55–56 *n*
Savings banks: before the World War, 7, 25, 327, 328; distribution of costs in 1913 and 1924–25, 327
1918–21, 325 *n*
1922–28, organization and administration of, 283, 324–25; number of, 325–28; growth of, 325–29; deposits in, 325, 326, 328; interest rates of, 325, 329 *n*; protection against inflation, 325–27; and principle of business accounting, 327–28; and "moneyless" payments, 329
since 1928, administration of, 499–500; system of, 500; functions of, 500, 503, 504–6; interest rates of, 500–1; expenses of, how met, 501; allocation of profits by, 501; expansion of, 502–4; number of depositors, 502–3, 506; average deposit in, 502; deposits classified, 503–4; sale of bonds by, 503–4
Savings certificates (1928–30), as money substitutes, 329
Schachnovskaia, S. B., 421 *n*
Schick, Alexander, 197 *n*
Schumpeter, J., 150 *n*
Schwartz, G., 134 *n*, 245 *n*, 304 *n*, 322 *n*, 386 *n*
Schwartzman, A. O., 349 *n*, 354 *n*, 356 *n*, 364 *n*, 367 *n*, 369 *n*, 370 *n*, 376 *n*, 379 *n*
"Scissors" crisis, 171–74, 175, 193 ff., 200 ff.
Scrope, G. P., 138 *n*
Seasonal requirements, loans to meet, 368, 376, 378
Securities exchanges, 29, 61–62, 163 *n*, 164
Segal, A., 450 *n*
Segal, L., 323 *n*
Seglin, Y. I., 492 *n*
Selkhozbank, *see* Agricultural Bank
Seller-to-buyer credit, planning and, 345 ff.
Seraphim, H. J., 241 *n*
Serebrovsky, A., 416 *n*
Sessa, P., 424 *n*
Settlement accounts, 369, 379, 380, 404
"Settlement tokens," 79, 80, 81, 106, 126 *n*, 439–40
Sevruk, P., 286 *n*, 302 *n*
Shanin, L., 304 *n*, 361
Sharovarov, A., 422 *n*
Sher, V. V., 359 *n*, 365 *n*
Shmelev, and "labor unit of account," 108 ff.
Shortcomings of Soviet economy: banks help to overcome, 381–82; spotlight turned on, 383–84
Short-term treasury bills: rôle of in financing World War, 32, 34, 35, 37, 38–39; as a vehicle for inflation, 35, 38–39
Shtern, A. B., 69 *n*, 136 *n*
Silin, N. D., 245 *n*
Silver (*see also* Ruble): monometallic standard, 5, 14; abrogation of free coinage in 1893, 13; inclusion in metallic reserve, 149, 149 *n*
"Small change famine," 31, 181, 425–27
Smith, Adam, on labor as a measure of value, 109 *n*
Socialist philosophy, of banks, credit, and money, 54 ff., 99 ff., 359–63, 375, 419–20, 439 ff.
Socialized sector, 322–23, 333, 337, 337 *n*, 351, 360 ff., 444
Sokal, Max, 148 *n*
Sokolnikov, G. Y., 58 *n*, 60 *n*, 69 *n*, 74 *n*, 75 *n*, 103, 112 *n*, 131 *n*, 145 *n*, 147 *n*, 166 *n*, 179 *n*, 192 *n*, 194 *n*, 204 *n*, 218 *n*, 240 *n*, 290 *n*, 440
Sokolov, A. A., 290 *n*
Soliterman, M., 324 *n*
Solovei, G. G., 74 *n*
South Eastern Commercial Bank, 282 *n*, 330
Soviet attitude towards ruble, 439 ff.
Soviet Control Commission, 383 *n*
Sovznaks: meaning of, 79, 137, 144, 175; denominations of, 78, 80–81, 189, 190, 190 *n*, 213 *n*
1918–21, 78 ff.
1921–22, 126 ff.
1922–24, volume in circulation, 128–29, 186–87; relation between chervontzy and, 155, 175–85; devalorization of, 126–27; premium on, 180–81; depreciation of—in terms of banknotes, 180–84; in terms of gold, 181 ff.; in terms of price level, 128–

32, 184–90; index of circulation, 186–87; stabilization impossible, 188, 239–40; and Monetary Reform of 1924, 200–243; cessation of printing and issuing, 213; redemption of, 215–18; rate of redemption, 217
Spahr, Walter E., 232 *n*
"Special account" method of settling debt, 376, 377
Specialized banks, 281–331, 450–506
Specie payment, 12, 13, 30, 148
Speransky, M. M., 5
Stabilization of a currency, procedure for, 204–5, 215
Stabilization of price level: difficulties surrounding, 215, 219 ff.; method used in 1924, 229 ff.
Stable currency: proposals for, 147 *n*; methods of change from depreciated to, 220 ff.; interdependence between balanced budget and, 236–37, 237 *n*
Stable unit of money, 136 ff.
Stalin, J., on stable currency, 242, 420–21 *n*, 445–47; on misapplication of Credit Reform of 1930, 357 *n*; on the nature of Soviet institutions, 431, 441–42; on the Nep, 442
State Bank
Imperial, 1860–1914, product of a reorganization, 9; organization and administration of, 10; original statutes of, 10–11; statutes of 1894, 10–11; capital of, 10; note issue of, 13–16; a central bank, 15, 17–19; loans and discounts of, 17–20; treasury deposits in, 17–18; deposits, 18; discount rate of, 19, 38
1914–17, loans and discounts, 29–30, 36–38; expansion of fiduciary issue, 30, 42; altered rôle, 36–43; notes in circulation, 37, 41–43; gold reserves, 37, 39–41; deposits, 37, 41; discount rate of, 38
State Bank, 1917–20: seizure by communists, 56 ff.; "single bank" idea, 57, 60, 270, 281, 352–54; arrangement with private banks a failure, 59–60; renamed "People's Bank" in 1918, 60, 62–63; abolition of, 70–71
State Bank of the U.S.S.R.
1921–28, re-establishment in 1921 as State Bank of the R.S.F.S.R., 118 ff.; renamed State Bank of the U.S.S.R., 119 *n*; statutes of 1921, 119–26; capitalization of, 119–20, 246, 249, 249 *n*; problem of protecting resources from inflation, 132–35; loans and discounts of, 133–36, 244–46; 252–53; interest and discount rates and policy of, 133, 245–49, 254; deposits in, 133, 246–47, 249–54; branches of, 136, 265–66; right to issue notes, 147 ff.; metallic reserve of, 148–52, 158, 159, 246–47, 255–56; note issue of (*see also* Chervonetz), 157 ff., 246–47, 254–57; foreign exchange monopoly of, 165 ff.; balance sheets of, 246–47, 270 ff.; foreign trade and, 258–59, 318; fiscal agent, 265; relations with other banks, 266–70; planning by, 266 ff.; concentration of short-term credit in, 267–70, 270 *n*, 272, 352, 453; leading rôle of, 267 ff.; comparison between Czarist bank and, 270–73; characteristic features of, 270 ff.; co-operative credit and, 296, 299; agricultural credit and, 301 ff.; private credit and, 319 *n*
since 1928, and Five-Year Plan, 334; credit expansion, 334, 371, 404, 519; statutes of 1929, 339–45; and Credit Reform of 1930 (*see* "Credit Reform of 1930"), 346 ff., 479–81; expansion of short-term credit business, 352; co-operative credit and, 352; agricultural credit and, 352, 353, 388–89, 479–81; loans and discounts of, 371, 372, 373 *n*, 374, 379–81, 404, 462, 519; deposits in, 371–74, 380; balance sheets of, 372–73, 408–9; recovers losses, 374, 381, 462; credit procedure since 1931, 375 ff.; social-mindedness of, 381–82; improvement of credit machine by, 383–84; relations with collectives, 383–84; expanded resources of, 384–85; charges for services by, 385–86; interest rates of, 385–86; new planning apparatus of, 386–88; planning by, 386–88, 390–403; branches of, 388–89; planning by branches of, 390–91; note issue of, 404–5, 408–9; balance sheets of issue department of, 408–9; reserves of, 408–9, 411–14, 415; issue of valuta-checks, 421–23

State Commercial Bank: of 1754, 6; of 1817, 7–10
State Loan Bank, of 1786, 6–9
State Loan Bank for the Nobility (1754), 6
Steiner, William H., 155 *n*
Stock Exchange, why closed upon declaration of War, 29
Stocks and bonds, dealings in forbidden, 62, 63
Strumilin, S. G., 108 ff, 212 *n*, 280 *n*
"Sums in transit," 365 *n*
Suponev, N. A., 354 *n*
Syndicates, credit functions of, 348

Taxation, *see* Budget
Titular lists, 459, 497
Tochilnikov, G., 294 *n*
Torgbank (*see also* Vsekobank), rôle of, 477
Torgsin shops, 415–16, 432, 447, 448, 520–21
Trade (*see also* Economic trends)
  1924–28, 227–28, 256–57, 322–23
  since 1928, 322–23, 381, 412–13, 423, 428
Trading agencies abroad, 258–60
Trakhtenberg, I. A., 360, 361
Transportation certificates (1923–24), circulated as money, 178 *n*, 193
"Treasury change tokens," *see* "Change tokens"
Treasury circulation (*see also* Inflation, Money, Sovznak), ratio between banknotes ("chervontzy"), and, 206, 212, 241, 405–11, 427–28
Treasury deposits, 17–18, 251, 252, 271, 273
Treasury loans, by central banks, restrictions, 153–54
Treasury notes of 1924, 211 ff., 235
Treasury offices, 265, 285 *n*
"Tred," 107 ff., 440
Trotsky, Leon, on "scissors" crisis, 201 ff.; and theory of "permanent revolution," 203
Tufesko, K., 327 *n*
Tumanov, N. G., 119 *n*, 258 *n*, 466 *n*
Tzekombank
  1925–28, organization of, 283, 310; branches of, 284, 311; statute of, 310–11, 312; as head of the municipal credit system, 310–12; capital of, 310, 311; principal accounts of, 311; operations of, 311–12
  since 1928, reorganization of, 456 ff., 491; management and supervision of, 455, 456, 457, 491; and municipal banks, 456, 490 *n*, 491–92, 499; financial control by, 452, 453, 457–61, 489, 498; financing by, 452, 461 ff.; 492, 493 ff.; interest rates of, 463–64; functions of, 464, 492–93; deprived of short-term business, 490; sources of funds of, 490, 494–96; planning procedure of, 496–98
Tzypkin, I., 451 *n*, 452 *n*, 458 *n*, 461 *n*, 467 *n*, 471 *n*, 482 *n*, 494 *n*, 496 *n*, 498 *n*
Tzypkin, M., 291 *n*

Ukrainbank: 1922–28, foundation of, 282 *n*, 298; operations of, 270 *n*, 298; loss of branches in 1930 by, 352, 469; liquidated in 1936, 477
Unification of the currency (1921–24), 241–42
"Unrated" bimetallic standard, 177, 179
"Unrated" inconvertible paper money, 176 ff.

"Values in transit," loans against, 376, 377, 386, 399, 401
Valuta-checks, 421–23, 427
Valutin, M., 298 *n*
Varga, E., 83 *n*
Veselovsky, B. B., 310 *n*, 313 *n*
Vinokur, S., 237 *n*
Vneshtorgbank: rôle of, 258, 259, 318; organization and administration of, 282, 313, 316; operations of, 317–18; principal accounts of, 317; present status of, 318; short-term credit and, 352 *n*
Vsekobank
  1923–28: establishment of, 282, 296–97; branch system of, 284, 298; management of, 297; early difficulties of, 297–98; capitalization of, 297, 298; operations and rôle of, 298-99; principal accounts of, 298–99; correspondents of, 299–300
  since 1928: loss of branches in 1930 by, 270 *n*, 352, 469; reorganization of in 1932, 455 ff., 470; management of, 455, 456, 457, 470; financial control

by, 452, 453, 457–61, 473–76; financing by means of grants, 452, 461 ff., 471 *n*, 476, 477; interest rates of, 463–64; capital of, 469, 471, 472; source of funds of, 469, 471–73; branches of, 469–70; operations of, in 1929–30, 469, 470 ff.; planning by, 469–70, 472, 474–76; reorganized in 1936 as Torgbank, 477
Vynosov, M., 484 *n*, 485, 489 *n*

"Wages Fund," 460 *n*
War (*see also* World War): computation of cost of, 33; how to finance, 31–32
War Communism, 53–110
Warren, George F., 139 *n*
White, Horace, 196 *n*
Whitney, Caroline, 139 *n*
Whittlesey, Charles R., 151 *n*
Widows' banks, 7
Willis, H. Parker, 4 *n*, 13 *n*, 148 *n*, 155 *n*, 439 *n*
Witte, S. Y., 12–13
Wolfe, Bertram D., 203 *n*
Wollenberg, E., 425 *n*
Workers' control, 53, 60, 68
Working capital, how to finance, 368, 368–69 *n*
World War: and the national economy, 27–30, 50, 50 *n*; how financed—by Russia, 31–35; by Great Britain, 35; by France, 35; by Germany, 35
"Wrecking" activities, 359, 359 *n*, 364, 366

Young, J. P., 51 *n*
Yugoff, A., 237 *n*
Yurovsky, L. N., 49 *n*, 74 *n*, 77 *n*, 94 *n*, 105 *n*, 130 *n*, 136 *n*, 143 *n*, 176 *n*, 194 *n*, 197 *n*, 219 *n*, 304 *n*, 442

Zagorsky, S. O., 27 *n*, 47 *n*
Zemstvo banks, 25
Zheleznov, V. J., 130 *n*, 212 *n*