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Soviet Inflation: Causes and Consequences*

I. Introduction
There has been some disagreement in Western literature in recent years on the extent of both open and repressed inflation in the Soviet Union. This disagreement is not surprising since the quality and quantity of Soviet data necessary to analyze macroeconomic phenomena of this nature are very inadequate. The purpose of this paper is to present a theoretical framework in macroeconomic behavior in the Soviet context, and to use this framework to try and sort out the bits and pieces of the puzzle of Soviet inflation provided by the available data. I will begin with a brief description of Soviet financial assets and institutions and their relationship to the inflationary process.

II. Soviet Financial Institutions and Practices
There are three types of financial assets in the Soviet Union which can be classified as money-enterprise deposits, currency and savings deposits. Enterprise deposits are used in all interenterprise transactions and in all transactions involving the enterprise and the state agencies. Currency is used in all transactions between the enterprise and the household sectors, in interhousehold transactions, and in transaction between the household and the state. Households may deposit their currency holdings in state savings banks, which pay 2 to 3 percent interest depending upon their accessibility. Certain routine bills, such as utilities, may be paid directly from one's savings account, but savings deposits are not subject to check.

The total quantity of money is determined by the volume of credit extended by Gosbank, the state bank, to enterprises for working capital. Since all credit takes the form of enterprise deposit creation, and since there is no bank reserve requirement there theoretically is no limit on the amount of money created by Gosbank. Gosbank should be viewed as a central bank with an unlimited ability to create money, rather than as a commercial bank.

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ed in its lending ability by the excess reserves.

The division of the total money supply into its three components is determined by the volume of wage disbursements. Wage payments result in an exchange of enterprise deposits for currency. Households determine the mix of currency and savings deposits they hold based upon the relative liquidity and opportunity costs of the two assets. In fact, except for a limited quantity of fixed interest government bonds, currency and savings deposits are the only financial assets which are available to Soviet households.

Although the ability of Gosbank to increase the money supply through credit creation is theoretically unlimited, its ability in fact is severely constrained by narrowly worded official credit guidelines. Each enterprise maintains one current and a variety of loan accounts at its branch of Gosbank. A separate loan account is required for each category of loans, and all loans must fall into an approved category. Since all enterprises operate on the principle of khozraschet, the basic function of credit has been to provide the enterprise with working capital to bridge the gap between expenditures and receipts. Since the 1965 reforms, credit has also been extended for longer term investments. The basic principle of short term credit is that it be used for specific purposes consistent with the fulfillment of the output plan. Thus, the major function of credit in the Soviet Union has been a microeconomic one. The concern is that the enterprise be provided with funds that are just sufficient to allow it to carry out all planned transactions. This credit function complements the other major function of Gosbank—control by ruble.\(^3\) The net effect, however, of credit creation is to determine the rate of growth of the total money supply as defined above. Additions to the stock of currency occur when new credit results in wage disbursements, since enterprises exchange bank deposits for currency in order to pay their workers.

In an attempt to monitor the total volume of credit and currency in circulation, Gosbank prepares a credit and a cash plan for each year. The Credit Plan, disaggregated to the total volume of short-term credit to be extended to the enterprise and the specific purposes and intervals for which it is to be used. A major objective of the plan is to keep enterprise cash balances at a minimum to prevent possible unplanned expenditures. The bulk of short-term credit is to finance inventories and goods in transit, and norms are set by the state to limit the amount of credit extended for these purposes.

The Cash Plan, an itemized list of all deposits and withdrawals of currency, is derived from the Balance of Money Incomes and Expenditures, a projection of household receipts and expenditures. The total quantity of currency in circulation, including any net credit creation, is designed to be just sufficient

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\(^3\) This term refers to the role of Gosbank as a supervisor of all enterprise transactions. See Garvy, *Money, Banking*, pp. 31-36.