

Why Was There a Soviet Investment Cycle in 1933–7? Preliminary Notes and Worries

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This is a discussion paper, not intended for publication. You are welcome to cite it, and especially welcome to send me comments on it.

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Aspects of this paper are developed in a forthcoming article by R. W. Davies and Oleg Khlevnyuk on 'Stakhanovism and the Soviet economy', to be published in *Europe-Asia Studies*. It was prepared as part of our ESRC project on the role of the Politburo in economic decision-making in the 1930s. This topic will also be discussed in my book on the second five-year plan.

Studies of the Soviet economy (e.g. Zaleski; Harrison) have drawn attention to the 'investment cycle'. In both the Stalin and the post-Stalin periods, a phase of relatively high growth in investment, which put particular strain on the economy, would be followed by a 'retreat' into a phase in which investment grew more slowly, or even declined.

In the years 1928-37 two successive cycles can be clearly observed. In the first cycle, 1928-33, very rapid increase in investment in 1928-32 was followed by a slow-down in 1933. In this year investment was actually lower (in terms of current prices as well as fixed prices) than in the previous year (a rare event in Soviet peacetime economic history). A cautious investment policy continued to be pursued in 1934, and at the beginning of 1935.

In the second cycle, 1935-7, a rapid increase in investment in 1935 and 1936 was followed by a marked shift to a slower increase in investment, both in the 1937 plan and still more in its actual outcome.

The following table illustrates these developments:

Table 1¹

Capital investment (million rubles at current prices)	
1928	7276
1929	8451
1930	9250
1931	14914
1932	19000
1933	18053
1934	23540
1935	27157
1936	35311
1937 (prelim)	33852

NB: This series excludes investment by collective farms from own resources, and labour of population on roads. It includes extra-limit (vnelimitnyye) investment under decree of September 19, 1935.

These figures are higher than those in the annual state plans in Tables 2 and 3, because the state investment plans do not include growth of livestock, extra-limit expenditure, and various other minor items. The Actual figures for Agriculture which form part of the totals above include gross additions to livestock, and so are wider than the Plan figures, which includes only net additions to livestock.

Note also that, as these figures and those in later tables are in current prices, they cannot be used to estimate changes over time in real investment.

Let us look at the 1934-7 period in more detail.

1934

Investment increased rapidly in 1934 after the drastic cutback in 1933 (by 30 per cent, measured in current prices). Nevertheless, it may be correct to characterise 1934 as a 'moderate' year in terms of investment policy. The 1934 plan, after much argument behind the scenes, incorporated an investment target of 25100 million rubles. But in April 1934 this figure was reduced to 23000 million rubles on the grounds that industrial production would be insufficient to meet the plan; and in the outcome approximately this amount was spent.²

¹ This is a preliminary table; the data are roughly comparable but need some adjustments. For 1928-32, see R. W. Davies, J. M. Cooper and M. Ilic, Soviet Official Statistics on Industrial Production, Capital Stock and Capital Investment, 1928-1941 (CREES, University of Birmingham, 1991), 52-3 and 56 (General note).

For 1933-37, see RGAE, 4372/92/101, 77.

² See R. W. Davies and O. Khlevnyuk in E. A. Rees, ed. Decision-Making in the Stalinist Command Economy (1997), 53.

1935

The 1935 plan for investment was even more cautious. In the summer of 1934 Gosplan aggregated the claims of its various sectors. Each Gosplan sector covered a branch of the economy, a group of industries, or an aspect of the economy. The claims of the sectors were based partly on the requests of the commissariats, and partly on the sectors' own estimates of the investment which would be required in the sector in order to carry out the projects included in the second five-year plan (1933-7). The second five-year plan was adopted in its final form more or less simultaneously with the preparation of the 1935 plan. The total claims for investment in 1935 amounted to 33786 million rubles, an increase of 50 per cent on the expected outcome in 1934. These claims were of course unrealistic, and Gosplan apparently imposed two successive ceilings (see Table 2). The lower of these was 23500 million rubles, which was only a small increase on the expected outcome in 1934.

But the Politburo was extremely cautious, and on July 28 adopted a plan of only 18000 million rubles. This figure was increased when the plan was adopted at the beginning of 1935, but the total was still no higher than that achieved in 1934 (see Table 2).

Table 2³
 The capital investment plan for 1935:
 rival estimates
 (million rubles at current prices)

1934 (expected fulfilment, summer 1934)	22285
1935P (as in second five-year plan)	25704
1935P (claims of Gosplan sectors)	33768
1935P (Gosplan first ceiling)	26537
1935P (Gosplan second ceiling)	23500
1935P (Politburo July 28 1934)	18000
1935P (as at end of 1934)	21190

The 1935 plan did not involve simply leaving all the main branches of the economy with the same level of investment as in 1934. The Politburo decided to increase investment in the railways from 3000 to nearly 4000 million rubles, and also to increase investment in civil aviation and in the Northern Sea Route project. In consequence, investment in other sectors had to be reduced, notably in heavy industry (Narkomtyazhprom).

When Gosplan discussed the draft investment plan in the summer of 1934, it was already clear that the restriction on investment in Narkomtyazhprom would make it impossible to carry out major projects which formed part of the second five-year plan. In July 1934, a Gosplan document on the iron and steel industry pointed out that if investment in the industry in 1935 was at the same level as in 1934, the plans to construct the second phase of the Kuznetsk iron and steel works and the new works in Bakal would have to be abandoned.⁴ The investment for iron and steel remained at this level, and these major projects were duly moth-balled. The proposal to reduce investment in the oil and coal industries was very strongly resisted by the fuel sector of Gosplan, and the investment plan approved at the end of 1934 provided for a slight increase in investment in this sector.⁵ The main cut in Narkomtyazhprom fell on the machine-building industry.⁶

³ The first five rows are taken from tables in RGAE, 4372/33/122, 161-160; these are not dated, but were evidently prepared before the Politburo decision of July.

For the Politburo decision, see RGASPI, 17/3/949, 6.

For the plan as at the end of 1934, see Narodno-khozyaistvennyi plan na 1935 god (1935), 260-1; this figure excludes the 'bread addition' to wages and to fodder costs consequent on the abolition of rationing (494 million rubles).

⁴ RGAE, 4372/33/122, 259-244.

⁵ For the oil industry, see RGAE, 4372/33/63, 9-14 (not dated), and 4372/33/63, 117-121 (dated November 13, 1934); for the coal industry, see 4372/33/63, 66-88 (dated November 12, 1934).

⁶ Discussion of this has not yet been traced.

Following the adoption of the 1935 plan at the end of 1934, investment policy followed a quite different course during 1935 than in the previous year. Instead of reducing the investment plan, the Politburo and Sovnarkom accepted piecemeal a series of proposals from the commissariats to increase their allocation. Most branches of the economy were affected. The main increases were (1) in Narkomtyazhprom, where total investment was eventually planned at 7 per cent above the 1934 level;⁷ and (2) in capital construction by the People's Commissariat of Defence, which was raised from 628 to 1108 million rubles.⁸ In 1935 actual investment (in current prices) approximately equalled the revised plan.

We should not jump to the conclusion that the revised investment plan for 1935 was already a 'high' plan in the sense that it was placing an exceptional strain on the economy. In 1935, as in 1934, industrial production increased very rapidly; and in 1935 the harvest was well above normal. Investment in 1935 increased by 'only' 15 per cent, less than the rate of growth of industrial production. On the other hand, 1935 was a difficult year for the state budget.⁹ The degree of strain on the economy in 1935 requires further investigation. But undoubtedly the reaction of the Politburo to the investment proposals it received in the course of 1935 reflected a shift to a more optimistic mood.

1936

The Politburo decisions on the investment plan for 1936 were a major shift towards more ambitious planning. Unlike the Politburo, Gosplan was astonishingly cautious. On July 19 Mezhlauk, head of Gosplan, proposed that investment in 1936 should amount to only 17700 million rubles, a reduction of nearly 30 per cent as compared with 1935 (see Table 3). The economy was continuing to expand rapidly, so this extreme caution is difficult to understand. In his memorandum of July 26 to Stalin and Chubar', Mezhlauk stated that an investment plan of this size would make it possible to achieve a budget surplus of 2000 million rubles, and to set aside a reserve of about 10,000 million rubles for price reduction. 'The policy of further increasing real wages and gradually reducing unified [retail] prices, which has been firmly established by the central committee...requires a reserve of approximately 8000 million rubles for price reduction'.¹⁰ But a drastic cut in investment was a high price to pay for price reduction. Gosplan's caution at this time requires further study.

⁷ The main change in Narkomtyazhprom was to restore the cut in machine-building; the details of this have not yet been examined.

⁸ See M. Harrison and R. W. Davies, 'The Soviet Military-economic Effort in the Second Five-Year Plan (1933-1937)', *Europe-Asia Studies*, vol. 49 (1997).

⁹ See Khlevnyuk and Davies, 'The End of Rationing in the Soviet Union, 1934-1935', *Europe-Asia Studies*, vol. 51 (1999).

¹⁰ GARF, 5446/26/66, 266.

Table 3¹¹
 The Capital Investment Plan for 1936:
 the rival estimates
 (million rubles at current prices)

	1935 Plan (July 1935)	19.vii.35	21.vii.35	26.vii.35	28.vii.35	9.xii.35	29.v.36
NKTP	8420	5500	6000	6600	8000	8500	10005
NKLegP	666	900		1050	1250	1250	1372
NKPP	644			800	900	1130	1178
NKs	495			345	700	930	1078
Mestprom							
NKLes	517	400		450	650	900	899
Narkomzem	1502	1100		1200	1400	2202	2192
NKPS	4068	3000	3000	3650	4100	4809	5487
NKO	1105			2245	2400	2400	
Education	361			1000	1100	1100	
Other	5675			4660	6841	8394	
Total	23453	17700	19000	22000	27341	31615	35053

The 1936 capital investment plan was discussed at a series of conferences in the party central committee between July 21 and 28, 1935. Molotov, chair of the Council of People's Commissars (Sovnarkom), was away, and Stalin was the central figure in the discussion. On July 21 he wrote to Molotov that Mezhlauk had that day presented a memorandum proposing that investment should amount to 19 milliard (19,000 million) rubles, but instead 'I proposed a figure of 22 milliard'.¹² Four days later Molotov, who was on the side of caution, replied that 'it is possible and necessary' to keep to the figure of 22 milliard:

I consider it extremely undesirable to increase the construction programme above 22 milliard rubles. I am guided in this by the desire to strengthen the ruble and also to reduce the cost of construction.¹³

But Stalin did not agree. A few days later he reported to Molotov that after a further meeting the plan had been increased to 27 milliard rubles (which would be reduced to 25 milliard if construction costs were reduced as planned):

¹¹ Sources

1935 plan: as given in GARF, 5446/26/66, 263 (July 26, 1935).

19.vii.35: GARF, 5446/26-4/9,254-255, 247.

21.vii.35: Pis'ma I. V. Stalina V. M. Molotovu, 1925-1936gg.: sbornik dokumentov (1995), 249-50.

26.vii.35: GARF, 5446/26/66, 263.

28.vii.35: RGASPI, 17/3/969, 1, 31-6.

9.xii.35: RGASPI, 17/3/973, 43-6, 60-3; GARF, 5446/57/38, 171-2.

29.v.36: RGAE, 4372/34/130, 145-6 (memorandum from Kviring, deputy head of Gosplan, to Molotov).

¹² Pis'ma I. V. Stalina V. M. Molotovu (1995), 249-50.

¹³ APRF, 45/1/769, 159-160.

22mld was not enough, and, as can be seen, could not be enough. The increase in school building (+760 mil), light industry, timber, food industry and local industry (+900 mln rub and more), in defence (+1mld 100mln), in health, on the Moscow canal project and other items (over 400 mil r) determined the physiognomy and size of the control figures for 1936.¹⁴

On the day on which Stalin wrote this letter, the increased plan was promulgated in a Sovnarkom decree. In the final letter in this sequence, dated August 2, Molotov replied grudgingly accepting the fait accompli:

I would have preferred a smaller amount of capital construction, but I think that we shall cope if we put our shoulders to the wheel (ponatuzhivshis') even with the approved plan of 25 mld r..The possibility of increasing industrial production by 23-22% favours this outcome.¹⁵

As will be seen from Table 3, this was by no means the end of the matter. Further major increases were made in the plan in December 1935. The December revision continued to reflect the multiple criteria advanced by Stalin to justify a higher level of investment. It was essential to increase expenditure on defence. But it was also essential to increase expenditure which would improve the standard of life of the population: on consumer industries, education and health (and on agriculture, expenditure on which was increased, though this was not specifically mentioned by Stalin). The revised plan also included a substantially increased investment in a prestige project, the Moscow-Volga canal.

The published version of the 1936 plan, prepared by Gosplan and with a preface by Mezhlauk, made a virtue of the investment expansion imposed on Gosplan from above. A year previously, the 1935 plan stated that the 'stabilisation of the volume of finance for construction in comparison with 1934 corresponds to the tasks of 1935: the further strengthening of the ruble, the development of trade and the reduction of prices.'¹⁶ But the 1936 plan proclaimed that 'capital investment in 1936 alone amounts to 50% of total investment in the first three years of the second five-year plan'; '1936 is a year of the tremendous growth of construction'.¹⁷

Further increases in the investment plan in the first few months of 1936 seem to have been largely defence-oriented.¹⁸ But the switch to a much higher level of investment in 1936 does not seem to have been simply a result of the necessities of defence, or to have been dictated by bottlenecks in industry which imperatively required additional investment. It was rather an attempt to achieve several policy goals which, taken together, were incompatible with the resources available.

¹⁴ Pis'ma Stalina Molotovu, 251.

¹⁵ APRF, 45/1/769, 162-3.

¹⁶ Narodno-khozyaistvennyi plan na 1935 god (2nd edn, 1935), 301.

¹⁷ Narodno-khozyaistvennyi plan na 1936 god (1936), 269, 280.

¹⁸ Details to follow.

While the additions to the investment plan were still being made, it had already become obvious that the plan was too ambitious. The huge planned increase in investment would have been impossible in an 'ordinary' year. In 1936 the rapid expansion in the production of armaments competed with the capital investment programme for the resources of the capital goods industries. In a memorandum dated May 16, 1936, Mezhlauk reported that in April capital investment was lower than required by the plan.¹⁹ The gap between plan and actual investment increased throughout the year. In a report to Sovnarkom 'On the course of the fulfilment of the capital construction plan in 1936', dated October 15, 1936, Mezhlauk stated that in the first eight months of 1936 the amount of investment (ob'em rabot), measured in 1935 estimate prices, in the economy as a whole was only 47.2 per cent of the annual plan, whereas 'with a normal development of construction approximately 70% of the annual plan should have been fulfilled in eight months'.²⁰ In the outcome, the total achieved was reported at only 31750 million rubles, 87.4 per cent of the final plan.²¹ Narkomtyazhprom reported that its investment in 1936 amounted to 91.7 per cent of its final plan.²² The gap between investment plan and performance was far larger than in the previous years of the second five-year plan.

1937

By the summer of 1936 the Politburo had already agreed to a more moderate investment policy. On July 19, Sovnarkom and the party central committee issued directives for the 1937 plan which provided for investment finance amounting to 20 per cent less than the 1936 plan and as much as 30 per cent less than the revised 1936 plan. This figure was later increased, but in the final plan approved in March 1937 was still 8 per cent lower than the expected fulfilment in 1936 in terms of finance, and only 3 per cent above that level in real terms.²³ This was clearly a down phase in the cycle of investment policy.

¹⁹ RGAE, 4372/92/59, 102-119.

²⁰ GARF, 5446/20/62, 170.

²¹ Narodnokhozyaistvennyi plan Soyuza SSR na 1937 god (1937), 142-3 (preliminary figure, implying that the final plan was 36327 million rubles).

²² Tyazhelaya promyshlennost' za 1936 god (1937), 250 (measured in 1935 estimate prices).

²³ Narodnokhozyaistvennyi plan...1937 (1937), 36, 142-3.

Other aspects of economic policy in 1934-7

The sharp change towards a more ambitious policy in 1935-6 was not of course confined to investment. The year 1934 and the first six months of 1935, when investment plans were relatively moderate, were distinguished by the great deal of attention paid, in Narkomtyazhprom and elsewhere, to costs, prices and the use of economic as well as administrative levers to control the economy (see Benvenuti; Siegelbaum). These considerations were not abandoned in the second half of 1935 and in 1936, when the switch to more ambitious investment plans took place. But far more attention was devoted to the campaigns to push the economy forward by increased productivity, launched by Stakhanov at the end of August 1935. These campaigns were spread throughout the economy in the succeeding twelve months or so by the determined support of the Politburo. They were afforded greater priority than the drive to improve costs.²⁴

The problem

This chronological examination of investment policy and its results shows us major shifts in policy which do not appear to be imposed by objective constraints or some kind of systematic necessity. It is true that it could be argued that the downturns in investment in 1933 and 1937 were imposed on the political leadership by the need to overcome the difficulties caused by the previous expansionist policy. But even here it needs to be shown that the difficulties were so great that a more determined leadership could not have stuck to the expansionist course.

But why the switch to 'over-investment' in the second half of 1935 and in 1936? The evidence from policy makes this appear as a voluntary decision by the leadership - indeed, by Stalin himself. If Molotov had been in charge in the summer of 1935, would the high investment plan for 1936 have been adopted?

But obviously this is not just a matter of Stalin's personal role. Similar patterns of events - with much longer periods of 'overstrain' on the economy - occurred under those very different personalities, Khrushchev and Brezhnev. The political set-up was evidently such that the leaders moved towards an over-ambitious plan whenever they thought they had the opportunity. Ideology? Or system? Does economics have something to say to us about all this?

²⁴ However, the 'campaign approach' did not give way to the 'economic approach' with the switch to more moderate investment policies.