

# No pause in Russia's financial crisis: How long will monetarism survive?

by Rachel Douglas

Interest rates on Russian Treasury Bills, known as GKO's, climbed to 46% in the first week of February—back to the levels of early December, when the Central Bank and Finance Ministry scrambled to prevent the bankruptcy of state finances, which was only days away. Despite official assurances from the so-called “young reformers,” the agents and apologists for international financial institutions within the Russian government, that the worst of the financial turmoil was over with the end of last year, Russia faces new battering in 1998, with hardly a New Year's pause.

During January, Russian stock indexes fell 28%, reaching a level nearly 60% below their 1997 peak. Foreign speculators, as “investors” in the stock of Russian companies are better termed, led the pullout. Selling by foreigners hit the GKO market, driving interest rates to 35% the week of Jan. 26, then 46% on Feb. 3. Of the approximately \$55 billion GKO market, some \$15 billion is held by foreigners.

“Russia's financial market is on the brink of catastrophe,” Boris Jordan of MFK-Renaissance finance company said at his Jan. 28 Moscow press conference. Jordan, who as a CS First Boston operative was one of the first and fastest looters of Russian industry during the privatization process after 1992, warned that failure of the Russian government to come out with a unified crisis-management line within a matter of days, would mean a devaluation of the ruble and breakdown of the country's financial system. *Kommersant-daily* of Jan. 29 reported Jordan's dire forecast, that Central Bank reserves are insufficient to compensate for the flight of non-residents from the GKO market.

On Jan. 28, the Ministry of Finance cancelled the latest GKO placement, which has only happened once before—during the Russian banking crisis in August 1995.

Financial calm could not be delivered by the Russian government, nor could performance of President Boris Yeltsin's top-priority political promise, to pay all state-sector wage arrears by the end of last year. Yeltsin devoted his first weekly radio address after a winter vacation, given Jan. 23, to this “most painful issue.” He blamed local officials for the failure to disburse the wages in at least six major regions, but also held his government “to find out how this could happen and to punish the culprits.”

On Jan. 15, miners at all the mines in Kemerovo Province, in the Kuzbass coal area, Siberia, carried out a one-day warning strike over unpaid wages. In another region where the Jan. 1 wage promise was not kept, 2,000 people, including miners, defense plant workers, and municipal employees, blocked the Trans-Siberian Railroad near Vladivostok for two hours on Jan. 27.

## Political fallout, petroleum deals

Upon Premier Viktor Chernomyrdin's return from official meetings in Turkmenistan and Tajikistan, he failed to chair a scheduled Jan. 15 cabinet meeting, prompting rumors that he was ill. The next day, however, Chernomyrdin not only reappeared, but announced that he had Yeltsin's support for a reorganization of the government. The most prominent “young reformers,” the two first deputy prime ministers, are to relinquish powerful portfolios: Anatoli Chubais will no longer oversee the media or the Finance Ministry, nor Boris Nemtsov the fuel and energy sector. These are key areas, in which Chubais and Nemtsov have enforced the austerity and privatization agendas of the International Monetary Fund. Chernomyrdin said that he, the premier, will now be directly responsible for the Finance Ministry, budget and monetary policy, and the banking sector.

Chernomyrdin, instead of Nemtsov, will supervise the Fuel and Energy Ministry, according to ITAR-TASS. Chubais is still in charge of tax collection, and Nemtsov of utilities and housing reform.

The now very active Chernomyrdin also made a highly visible move in petroleum-sector corporate politics, which are in turmoil. Oil and natural gas are Russia's biggest source of export earnings, which the drop in world oil prices has hit hard. Recent corporate consolidations are related both to that, and to struggles over power and policy.

On Jan. 19, a new Russian oil giant called “Yuksi” was created, from the merger of Boris Berezovsky's Sibneft with YUKOS, the oil company within the Menatep-Rosprom group of Mikhail Khodorkovsky. The merging firms produce 65 million tons of oil per year, including from major West Siberian deposits, which amount is more than the giant LUKoil. Yuksi becomes the world's largest company in

terms of oil reserves, and the third largest in oil extraction.

Khodorkovsky's press conference, announcing the merger, was chaired by Chernomyrdin, just three days after his reassertion of control over the fuel and energy sector. Berezovsky was present at the press conference, along with Vladimir Gusinsky of Most Bank and SBS-AGRO's Aleksandr Smolensky.

The Sidanco oil company, owned by V. Potanin's Oneksimbank, formed a partnership last year with British Petroleum. While Khodorkovsky confirmed that Yuksi plans to bid for the largest remaining unprivatized oil company, Rosneft, Oneksim-controlled *Russky Telegraph* of Jan. 16 charged there was a plot to keep Sidanco-BP out of the Rosneft bidding. On Jan. 15, *Russky Telegraph* reported, Gazprom head Rem Vyakhirev told journalists that "foreign companies may be forbidden to participate in the Rosneft auction." *Russky Telegraph* suggested that this statement revealed a deal between Gazprom-Lukoil and Sibneft-Menatep (or, rather, between Chernomyrdin and Berezovsky) to keep "Oneksimbank's only partner," BP, out of the bidding. On Jan. 26, Nemtsov announced that Chernomyrdin himself will select the final privatization plan for Rosneft.

## National security

If the contest for control of assets such as Rosneft were limited to warfare among financial clans, it would be fatal for Russia, but there is another agenda coming into view. Can the country's leadership be reshaped, to uphold its national interests? Yeltsin has indicated that he is not finished shaking up the government. The option for a "national unity" government, including parliamentary opposition figures for key economic policy areas, continues to be discussed in the State Duma (the parliament).

Academician Dmitri Lvov raised the question of national economic security in connection with the ouster of Boris Brevnov as head of United Energy Systems (UES), the Russian electric power utility. Anatoli Dyakov, chairman of the UES board, used evidence of embezzlement by Brevnov (evidence collected by the watchdog Accounting Chamber and published in *Pravda-5* newspaper), as the reason to dismiss Brevnov in late January. The 29-year-old Brevnov, former director of the Nizhny Novgorod Banking House, made his career as a member of Nemtsov's team. According to NTV, Nemtsov reacted in fury, using "non-normative" language and threatening Dyakov with retaliation. A government spokesman said that UES personnel decisions could only be finalized after Chernomyrdin returns from his trip to the Davos World Economic Forum in Switzerland.

NTV also interviewed advocates and opponents of Brevnov, which was the occasion for Academician Lvov — among the opponents — to make a strong statement on national security. Lvov, deputy director of the Central Mathematical Economics Institute (CEMI) of the Russian Academy of Sciences, told NTV that UES is an entity of great strategic

significance for Russia's economic future and the physical survival of the people, and therefore must be headed by persons having high professional skills and moral qualities. The first deputy premier (Nemtsov), said Lvov, should draw conclusions from the situation.

Academician Lvov's receiving air time for such remarks on a Russian national TV network is one sign of the times in Moscow. Another was the flap over George Soros's attack on Anatoli Chubais, whom he accused of allying with "gangster capitalism." Speaking Jan. 11 at the Second American-Russian Symposium on Investments, held at Harvard University, global speculator Soros startled his listeners by suddenly claiming that Chubais — the darling of Western speculators and the International Monetary Fund — had sullied Russian democracy by his deal-making during the 1996 Presidential elections, and that only the appointment of Nemtsov as another first deputy premier had averted a "gangster capitalism" takeover in Russia. The ensuing hub-bub, which featured Berezovsky defending his recent foe, Chubais, occasioned statements by Moscow Mayor Yuri Luzhkov, that speak to the looming changes in Russia — orderly or chaotic, under one or another clan or faction.

It is more and more evident that Luzhkov, who also attended the Harvard function, is running for President. (Nemtsov, smarting from recent demotions of himself and his team, said in late January that he hoped Yeltsin would run again, but otherwise he would back Luzhkov against Premier Chernomyrdin.) At a Jan. 15 press conference, back in Moscow, the mayor said that as far as Berezovsky's defense of Chubais was concerned, "it rather meets the description of the Russian proverb, 'A raven will never peck out another raven's eye.'"

In any event, Luzhkov said, things have come to the end of the "monetarism in contemporary Russia," begun in February 1992. "This monetarism is to end soon," said Luzhkov. "This playing with money must stop in Russia. Monetarism immediately switched the interest of banks to short money, to short-term credits given at tremendous interest rates," which made productive investment a losing proposition.

Later, Luzhkov replied to a question: "You're asking when the era of monetarism will end? Well, I think it is approaching its end. . . . There is a sobering-up now in society, among economists, among businessmen and economic managers, among representatives of numerous structures of the Executive branch of government who have to deal with economic matters as well. In the regions, this has already set in. The epoch is coming to an end. I think that we cannot, of course, name any date, but its end is coming. . . ."

"We say that the first thing that will save our economy is the restoration of the potential of our industry, agriculture, the systems in the social sphere. This will save our economy, and not playing with money. The latter has ended for Russia."