

Russia attempts policy shift in middle of world financial earthquake

by Rachel Douglas

Russian Premier Yevgeni Primakov has stated more than once, his preference for a Franklin Delano Roosevelt-style economic mobilization policy to replace the failed prescriptions of the International Monetary Fund and related ideologues. The possibility for Russia to make a clean break in that direction, however, is hampered by the vagaries of trying to do business with international financiers and institutions in their current state of rapid decay.

Thus, Deputy Premier Aleksandr Shokhin could tell a Sept. 24 press conference, after the new cabinet's first full meeting, that while he "would not like to scare anyone by discussing the possibility of default on foreign debts," this is nonetheless the likely outcome, if previously negotiated foreign loans are not released. At the same time, Shokhin blurted out the truth, that "the IMF has been hit by a crisis, as well, . . . an ideological crisis: the collapse of the models that the Fund has been supporting in various parts of the world—in Asia, Latin America, and Russia." The next day, an IMF delegation left Moscow without clearing the hoped-for release of funds during September.

Both Shokhin and Primakov say they would like to reverse parts of the Aug. 17 decision by the Kiriyenko government, to freeze government GKO-OFZ bonds and let the ruble float—a decision which crashed the currency and left imports virtually paralyzed, along with the banking system. But, the post-Aug. 17 Russian meltdown has already served as one trigger for reverse-leveraged collapses in global derivatives speculation, leading to a credit and liquidity crisis that radically alters the entire world financial landscape. It is not so easy to turn back the clock.

Shokhin was put in charge of one of three teams, working on a revision of economic policy, according to a spokesman for Primakov. His assignment was emergency financial stabilization for the rest of this year. Already, this area of the government's work is in turmoil. London courts ordered the seizure of accounts belonging to Russian banks that defaulted on forward currency contracts. Seventeen Western banks protested preferential redemption terms, initiated for Russian GKO-holders. When Mikhail Zadornov, one of those who made the Aug. 17 decisions, was reappointed Finance Minister on Sept. 25, Interfax reported that Shokhin resigned—after one week in office.

A team under First Deputy Premier Yuri Maslyukov is working on a strategic economic line, and Doctor of Econom-

ics Primakov himself is presiding over a third team, studying policy options. The Sept. 24 cabinet session dealt with three priority matters: payment of wage arrears, the state of monetary circulation in the economy, and the reimposition of a state monopoly on liquor production and wholesaling—a revenue-raising measure.

There are emergencies in several parts of Russia, including a large area in the south, where over two-thirds of the summer crops were destroyed by drought. On Sept. 16, a Volga River area official spoke on national television about "the real threat of famine," and another local official told Agence France Presse that emergency food was required for 100,000 villagers near the Kazakstan border, where "there is no more bread." A bread-rationing system is in use in the Pacific port city of Vladivostok. The city of Moscow has introduced price controls for bread, flour, meat, fish, boiled sausages, eggs, vegetables, salt, along with washing powder, toothpaste, and matches.

In televised remarks on Sept. 18, Primakov said his government would introduce new, unspecified exchange controls, to protect the ruble. As for borrowing abroad, he said, "We have every reason to count on IMF support. However, we will not accept ultimatums from international organizations, and we will follow the path we regard as best."

Among the measures Primakov has announced or suggested, are several drawn from a policy draft by economists at the Russian Academy of Sciences (see *Documentation*). These include an injection of liquidity into the banking system, initially by means of lowering reserve requirements for relatively healthy banks; some of the rubles they held in their reserves may circulate in financial markets and for commercial payments. Several commentators rushed to complain that this was "cranking up the printing press," which newly reinstated Central Bank Chairman Viktor Gerashchenko denies. Gerashchenko told the Sept. 24 government press conference, that the central bank and the government "tend to think that internal sources should be found for the necessary investment programs and for injections in the real economy, that would not contain inflationary potential."

Academician Dmitri Lvov, deputy head of the Central Mathematical Economics Institute and a longtime critic of the monetarist "reform" policy as a dead end, is taking a high profile as one of the Academy experts advising Primakov. On the widely watched TV program, Itogi, on Sept. 20, he and

Warning: Bush league agitates for 'Pinochet' dictatorship in Russia

Sources in Moscow report a renewed campaign, from International Republican Institute outlets there, for a "Pinochet" dictatorship in Russia. The Chilean ex-leader's name is shorthand for a radical free trade policy, with vicious austerity for the population, imposed by a military regime. The IRI is the "Republican" wing of the U.S. National Endowment for Democracy.

Vitali Naishul, a Russian proponent of Friedrich von Hayek's free trade doctrine, is a leading promoter of the "Pinochet" model. In 1996, he was attached to the Presidential campaign of Gen. Aleksandr Lebed. In recent weeks, several Russian press revived Naishul's 1996 "Chilean" theme, using the occasion of the 25th anniversary of Pinochet's coup in Chile.

This past Labor Day weekend, Naishul was in attendance at the von Hayek-founded Mont Pelerin Society's conference in Washington, D.C., hosted by the Heritage Foundation. The event had two main themes: 1) how to counteract the growing move of nations to re-regulate financial affairs, and 2) the crisis in Russia.

Yegor Gaidar, the original von Hayekian radical who launched Russia's reform disaster as premier in 1992, was interviewed by the French daily *Libération* Sept. 23 under the title, "Russian Society Is Waiting for a Dictator." Gaidar outlined a "pessimistic" scenario for Russia's future: "If you read the press, you would have observed that we are witnessing the birth of a personality cult, that of General Pinochet. The vast majority of society is demoralized, and is waiting for a dictator who, with his strong hand, is going to restore order, and bring the country into the paradise of the market."

Dr. Sergei Glazyev debated former Premier Yegor Gaidar. Glazyev asserted that the Russian economic crisis resulted from "a primitive, erroneous and criminalized policy," and that a national economy that "has not withstood these monetarist experiments," now needs re-regulation in order to recover. "The issue is not whether to print money or not," said Glazyev, "but what to print money *for*? . . . The state has to guarantee science-related branches of industry, earmarking finances not for the GKO pyramid, but to protect enterprises and investment."

Academician Lvov, interviewed in *Rossiyskaya Gazeta* of Sept. 18, summed up his policy outline: "[Under] current conditions, it is necessary not to focus on portfolio invest-

ments, but to endeavor to make Russia into a huge assembly site and to produce competitive goods. Including by the use of Western technologies. We should galvanize our internal reserves and at the same time carry out structural transformations in the real economy. . . . If Gerashchenko puts money into competitive projects and the real economy, into production units that are now idle, growth would become a reality already this year, in 1998."

Documentation

Russian Academy of Sciences open letter

The members of the Economics Division of the Russian Academy of Sciences, for which Academician Dmitri Lvov is the academician-secretary, submitted their "Open Letter to the President, Federal Assembly, and Government of the Russian Federation" in mid-September. Kommersant-daily published it on Sept. 15, under the snide headline "Basic Directions for Economic Policy," which alludes to the title of Soviet five-year-plans. Passages in brackets are summaries.

Scientists from the Economics Division of the Russian Academy of Sciences have been and remain initiators and advocates of profound social and economic transformations in the public life of our country. They have always supported, and continue to do so, a thought-through and considered transition to a socially oriented and effectively regulated market economy, and the creation of the basis for a civil society and its comprehensive democratization.

At the same time, we distinguish the main highways leading to such transformations, from the clumsy, primitive, and at times unprofessional methods of so-called "shock therapy." We repeatedly warned both the President and the government of the danger of experimentation with the economy of such an enormous country as Russia, on the basis of recommendations from foreign consultants and experts, untested by our own science and without corroboration in practice. As a result, Russia has been thrown far backwards. The destruction of its scientific and technological, economic, and intellectual potential has commenced, the impoverishment of the population has assumed a gigantic scale, the moral principles of society have been subverted, and criminality is brazenly rampant.

Now, when Russia is on the brink of the abyss, once again, without any consultations with domestic science, the latest model is being proposed—now, the Latin American version. [Domingo Cavallo, ex-Finance Minister of Argentina, had just spent a week in Moscow to promote a version of the British imperial Currency Board scheme for Russia, in con-

sultation with the acting Chernomyrdin government.—ed.]

Under these conditions, the scientists of the Russian Academy of Sciences, Economics Division, consider it their professional and civic duty to appeal to the President of Russia, the Federal Assembly, and the Government of Russia, presenting our proposals for a policy of some minimal economic security for the population and the country, in the face of the real threats of a contagious financial crisis.

We must solve the pressing questions of defending our citizens against inflation, empty shop shelves, the collapse of the banking system, and the catastrophic fall of the ruble's exchange rate.

1. Defense against inflation. [The document recommends: indexation of wages, pensions, and other social payments; state guarantees for bank deposits, and state-backed credits for housing construction; a national food insurance fund, including emergency purchases “to eliminate the problem of famine”; moratorium on public events; and measures to maintain retail trade in imported goods.]

2. Stabilization of the currency market. [To stem capital flight: mandatory conversion to rubles of 100% of foreign currency earnings, by their sale to the Central Bank; limitation of the number of commercial banks allowed to deal in foreign exchange; accelerated mandatory repatriation of foreign currency export earnings; limitation of foreign exchange trading to transactions associated with real import contracts and supplying cash for authorized exchange locations; and a state foreign-currency loan to the population, to pull dollars out of circulation and into the state banks.]

3. Clearing financial blockages. [Automatic controlled issue of money, when the federal government cannot pay for goods received or services rendered; cancellation of enterprise indebtedness, by amnesties and mutual offsets.]

4. The banking system. [Higher capital requirements for banks; expansion of directed Central Bank credits to commercial banks; and an interbank pool for deposit insurance, to maintain banking system liquidity, and stabilize the ruble.]

5. Financing state spending. [Draft of an emergency fourth-quarter 1998 state budget; and new terms for the issue of Central Bank credits for budget financing.]

6. Restructuring domestic bonded debt. [Correction of flaws in the Aug. 17 GKO-OFZ debt moratorium, so that Central Bank- and Sberbank-held GKO debt is restructured for 5-10 years, while GKO debt, held by commercial banks, insurance companies, pension funds, and individuals, should be redeemed either at Aug. 1 market prices, or at the purchase price; establishment of new types of long-term state securities; requirement that foreign purchasers of state securities hedge their investments with the Central Bank, which should limit yields to no higher than 15% per annum.]

7. Relations with world financial institutions.

7.1. It must be clearly affirmed at all levels of the state leadership, that even under current circumstances, Russia will make all current payments on its contractual obligations and

service state credits and Eurobonds. [Russian banks and commercial borrowers should negotiate terms with foreign lenders, even during the announced three-month moratorium.]

7.2. On a strategic level, foreign borrowing policy must be significantly adjusted. Its basic guidelines:

- orientation to attracting direct investment from abroad, rather than portfolio (which, under Russian conditions, is speculative). . . . It will be necessary to speed up the entry into force of laws on production-sharing and concessions, as well as precise and strict guarantees for foreign investments;

- definition of a long-term program for servicing the accumulated foreign state debt, including the possibility of restructuring and conversion into other types of obligations. . . ;

- obtaining new foreign state loans only for investment projects, which create sources for repayment.

[7.3: Development of trade and economic ties with the CIS countries.]

8. Shift to economic growth.

8.1. It is necessary to revise the erroneous position of the ideologues of the reforms, under which economic growth has traditionally been linked exclusively with investments. . . . The initiation of growth is possible through an expansion, in the first stage, of utilization of idle production capacities, by stimulating current consumer spending. . . .

[Price controls on the output of natural monopolies, allowing a moderate growth of prices for manufactured goods; protection for domestic production, and directed credits for them; tax relief for industrial producers.]

8.5. Finances and credit must be reoriented to servicing the production of real goods and services. This requires limiting the possibilities for speculative middlemen. . . .

9. Political conditions to avoid catastrophe. The main condition, capable of saving Russia from destruction, is the restoration of trust. . . . The path lies through a direct and extremely honest discussion with the people, in which mistakes and miscalculations in economic and social policy are admitted. . . . The basis for trust needs to be a precise long-term strategy for transformations. Our children and grandchildren should see clearly, what tomorrow will be like. . . .

The organic connection of the authorities with science, culture, and all spheres of the intellectual life of society has weakened. . . . It is a disgrace for Russia, that the country's rich and in many ways unique scientific and intellectual potential has been ignored, in favor of primitive recommendations by specialists who knew little about the history and culture of this outstanding country.

We, members of the Economics Division of the Russian Academy of Sciences, state once again, that we have developed serious projects, both for a social and economic development strategy for the country, and on urgent questions of bringing the country out of the looming catastrophe. We hope that our voice will finally be heard by the authorities and by the entire country. We are prepared for a constructive dialogue and to take part in carrying out a new reform policy.