

The Ides of March: Russia crisis breaks

by Rachel Douglas

Viktor Chernomyrdin sounded shocked to have gotten the boot, along with his entire Cabinet, the morning of March 23, but he was not perplexed about the reasons. President Boris Yeltsin acted now, said the outgoing Russian Prime Minister, because the country has been “hit from behind” by the global financial crisis. No sooner had his government secured parliamentary approval for a 1998 Federal budget, than, “Here comes the next blow,” said Chernomyrdin, “a new collapse of the world economy. . . . There are also the financial cataclysms, that are still continuing.” And, finally, “the drop of oil and gas prices. Those are the main sources of our budget [revenues]. This will generate a huge strain.”

In November-December 1997, as international speculators fled “emerging markets” on the first shock wave from Asian currency collapses and a worldwide plunge of stock prices, Russian convertible currency reserves were falling at a rate that would have achieved state bankruptcy in a matter of days. First Deputy Prime Minister Anatoli Chubais, the former privatization chief and former Finance Minister, led a scramble for means to keep foreign money in the Russian GKO (Treasury bill) market, in particular, while also raising enough cash to carry out President Yeltsin’s key political promise, the payment of back wages to public-sector employees by the first of the year. The measures adopted then, set the timer ticking on several financial and political bombs. Now, they are exploding.

In December, and again during the first week of February, when a second shock wave from Asia hit the Russian markets, the Central Bank allowed three-month GKO yields to rise above 45%. Whereas approximately \$7.5 billion (about 15% of foreign GKO holdings) fled Russia in December-January, the high rates attracted funds back in. The GKO yield fell to 28%, and Chubais boasted that Russia had weathered the storm. But, the money flowing back into Russia has been “speculative money, which hopes for profitable takeovers and for a devaluation of the ruble,” an analyst at the German Institute of Eastern Studies told *EIR* in early March.

In the March 9 issue of *Forbes* magazine, Prof. Steve Hanke asked, “Is the ruble next?” The Mont Pelerin Society’s zealous promoter of that old imperial looting mechanism, the currency board, took time between trips to Indonesia, to pen an article that read like an attempt to stampede speculators out of Russian state securities. Russia would be “a prime candidate” for “the next country whose currency blows up,”

according to Hanke, who predicted that by mid-1998, Russian foreign reserves would be drained, “structural reforms to restore investor confidence” would be politically impossible, and the only means to defend the ruble would be for interest rates “to go to the Moon.”

Advising speculators to shun the GKO’s, Hanke concluded with a scenario: “Beyond this, a ruble devaluation will send shock waves into central and eastern Europe. It will also motivate more repricing of emerging market risk and a further deterioration of the international financial environment. The danger of a full-scale international financial meltdown has by no means passed.”

During March, the ruble in neighboring Belarus did come under attack, plunging 25% before President Alyaksandr Lukashenka put the Central Bank under direct government control and mandated emergency measures to defend the currency.

Debt blows

The high-interest, three-month GKO’s, which have to be serviced, and rolled over, or paid off with interest, turned the Russian Federal budget on its ear. As economist Dr. Sergei Glazyev has reported (*EIR*, March 27, 1998, p. 53), debt service on the Russian state debt is running double the level of tax revenues. On Feb. 11, A. Shokhin of Chernomyrdin’s “Our Home Is Russia” party was asked about rumors that GKO-related foreign exchange demands were about to knock out several Moscow banks. It is not the banks, replied Shokhin, but “it is the budget that is in trouble”—because of the skyrocketing debt service on those state obligations.

In mid-February, an IMF delegation that had spent two weeks in Moscow approved continuation of the Fund’s three-year, \$10-billion Extended Fund Facility for Russia, “until 2000.” Doled out in quarterly tranches, contingent upon Russian adherence to conditionalities, the enlarged EFF is to continue at the rate of \$700 million per quarter. Russian sources cited by Itar-TASS, said that “a mass of problems” arose in the talks with the IMF, including IMF demands for tariff reductions on imports and other tax breaks for foreign investors. The IMF also demanded adjustments in 1998 Russian spending commitments, although the 1998 budget had not yet been approved. IMF Managing Director Michel Camdessus, meeting with Chernomyrdin on Feb. 19, hailed the IMF-Russia relationship as “a major element of the world economic system,” without which the end-1997 Asia shock would have been even worse than it was.

On March 4, the State Duma (parliament) approved the 1998 budget in its fourth reading, voting 252-129 in favor of a document that incorporated amendments demanded by the IMF. One alteration that was rejected, would have said that 27.9 billion rubles (\$4.6 billion) of recently added spending could only be paid out, if sufficient revenue were received to cover it; in the final version, the government will be allowed to cut spending, with three days’ notice to the Duma, if it

makes the cuts evenly across the board. Other IMF-designed austerity measures include the so-called “Kudrin-Fischer plan,” named after the Russian Deputy Finance Minister and IMF official Stanley Fischer, to sack 10-15% of public sector employees within the next four months; 208,000 layoffs, including thousands of teachers and medical personnel, were announced by Kudrin on March 25, even after the dismissal of the Cabinet.

Asked about prospects for performance on the 1998 budget, Chernomyrdin told a Feb. 26 press conference that it would be a lot easier to ensure performance, “if I knew what were in store for us this year.” But that is unknown, he cried: “Look at the crisis in the world! I mean the Asian crisis in the financial markets. It hit those who never thought it would hit them.” By mid-March, international oil prices had fallen to a level that would mean \$4.3 billion in lost revenue for the Russian oil sector, if they stayed depressed all year.

The public sector wage arrears, even those that were paid off with Chubais’s commercial borrowings and the December

release of World Bank loans, after the Russian government agreed to IMF austerity demands, began to mount again. Communist Party of the Russian Federation leader Gennadi Zyuganov claimed, on March 26, that those arrears already stand at 58 billion rubles (\$9.6 billion).

On March 12, journalist Pavel Felgenhauer leaked a report in the English-language *Moscow Times*, about a Defense Ministry briefing by Marshal Igor Sergeev some days before, on crumbling morale in the Russian Armed Forces. Felgenhauer often conveys the views of high-ranking Russian military sources, in his numerous interviews to Western reporters and articles in the English-language Russian press.

According to Felgenhauer, the Defense Minister “said the situation is ‘critical’ and that servicemen are deserting the Army, harassing local civilians and killing each other in the barracks. Officers and soldiers are committing suicide; commissioned officers committed 18,000 felonies in 1997; and in [three military districts], the number of felonies doubled in 1997. Many commanders are losing control of their units.”

‘New Bretton Woods’ presented in Russia

Prof. Taras Muranivsky spoke at a session of the Economics Division of the Russian Academy of Sciences on March 24, in Moscow. The meeting was chaired by Academician Dmitri Lvov, secretary of the Economics Division, and also deputy director of the Academy’s Central



Prof. Taras Muranivsky

Mathematical Economics Institute (CEMI). In attendance were 100 economists and other scientists from various institutions, who heard Professor Muranivsky speak about the science of physical economy, and the current worldwide financial and monetary crisis. The speaker urged that Russian representatives to the April 16 conference of the Willard Group in Washington, work out and present constructive proposals to make possible a New Bretton Woods system, instead of continuing the politics of the International Monetary Fund (IMF).

On March 26, issue #13 of the Russian weekly *Ekonomicheskaya Gazeta* came out, with a half-page article by Professor Muranivsky, titled “The Onset of the Second Phase.” It surveyed the barrage of criticism of the IMF

from around the world, the growing recognition of the systemic nature of the financial crisis, and the possibilities for serious deliberations on a New Bretton Woods, when 22 nations convene as the Willard Group, for talks on the global financial system.

Muranivsky informed Russian readers about:

- Bundesbank President Hans Tietmeyer’s Feb. 7 article in the German daily *Die Welt*, on the inadequacy of the IMF to deal with the current situation of the global markets;
- the Feb. 9-11 Group of 24 meeting in Caracas, where Venezuelan Central Bank President Antonio Casas González stated that the “Asia crisis” was a systemic one, that had struck the entire world, and that the IMF could not handle it;
- U.S. Treasury Secretary Robert Rubin’s Feb. 10 speech at Georgetown University, on the need for a conference to develop a “new architecture” for the international financial system;
- the growing “criticism of the IMF in the U.S. Congress, and academic circles,” which set the stage for IMF Managing Director Michel Camdessus’s own existentialist musings on March 12: “Should the IMF exist? . . . We should ask ourselves this, from time to time.”

Sources such as the Swiss bankers’ *Neue Zürcher Zeitung*, reported Muranivsky, “warn that the ‘Asian crisis’ is entering its ‘second phase,’ ” in which Western firms will experience “its devastating effect.”

In this situation, “Russia is between the hammer of the West and the anvil of the East. The time has come to listen carefully to the evaluations and recommendations of Asian, as well as European and American statesmen, politicians, and economists.” For example, Malaysian Prime

Still-unpaid wage arrears are a key factor that has morale “nearing the breaking point.” The arrears were not paid by Jan. 1, 1998, as promised. Now, there is a promise of “partial” payment by June 1.

Felgenhauer asserted that “an increasing number of officers and generals, including those in active service and in high-ranking positions in the Defense Ministry, are openly saying — even to journalists — that Sergejev is not fit to command Russia’s military. Russia’s conventional fighting forces — Army, Airborne Troops, Air Force and others — are being run down.” Gen. Lev Rokhlin, despite scant media attention, has officially registered his movement to defend the Armed Forces. “Rokhlin believes,” wrote Felgenhauer, “the Army will revolt some time this year and send Yeltsin packing.”

When Yeltsin returned from a week’s sick leave, and fired the Cabinet, the social-economic situation in the country was the one factor he cited as a reason. Over the preceding weekend, the President had received reports from government officials on the reappearance of state sector wage arrears. In a

Minister Mahathir bin Mohamad has blasted the hypocrisy of the advocates of “market forces” and globalization, who attacked his country’s currency. Now, Mahathir speaks in defense of Indonesia against the IMF, and is working on regional economic self-defense efforts.

The concluding section of Muranivsky’s *Ekonomicheskaya Gazeta* article dealt with the New Bretton Woods: “Lyndon LaRouche has noted, that the crisis is ready to take a new turn, of greater force and scale of destruction, than in the October-January period. The new phase will begin in March-April. All the so-called financial and economic reforms in Southeast Asia are failing. . . . Therefore, LaRouche proposes to abandon the hopelessly bankrupt world monetary system and to return to those forms of an international protectionist order, which were incorporated in the Bretton Woods system of the 1950s. The second modification . . . should be the replacement of the current, hopelessly bankrupt central banking system, with a new system of national banks, in the form successfully initiated by U.S. Treasury Secretary Alexander Hamilton, at the end of the 18th century.”

Muranivsky quoted Japanese Deputy Finance Minister Eisuke Sakakibara on the growing number of leaders who are considering the benefits of a new Bretton Woods type of agreement.

“In a word,” ended the Russian article, “the world monetary crisis is continuing, and effective measures to get out of it have not yet been adopted. There are great hopes for the 22-nation conference in Washington, scheduled for April 16. On March 18, at Lyndon LaRouche’s initiative, a scientific seminar was held to elaborate recommendations for that conference.” — *Rachel Douglas*

televised address, Yeltsin charged that the cabinet “did not cope with a number of key issues,” with an especially serious “lagging behind in the social sphere.”

Yeltsin moved in a flurry of byzantine palace politics, leaving open several possible courses of action. With two supplementary decrees, signed on March 23 alongside his main one disbanding the Cabinet, he secured the resignations of Chubais and of Minister of Internal Affairs Anatoli Kulikov, while all other ministers, except for ex-Prime Minister Chernomyrdin, were to stay at their posts. Minister of Fuel and Energy Kiriyenko, 35 years old and in office for only a few months, was named “acting Prime Minister” by Yeltsin and instructed to draw up a list of new government ministers.

Yeltsin appointed First Deputy Internal Affairs Minister Pavel Maslov as acting Minister of Internal Affairs. Maslov’s interim appointment was singled out by Chernomyrdin, in his own press conference, as of special significance, being at one of the “force” ministries — those with armed units at their disposal; there have been recurrent rumors about coup schemes, involving Kulikov, in light of his build-up of the Internal Troops, and much recent attention in the media, to his cultivation of a political partnership with Moscow Mayor Yuri Luzhkov.

Has Yeltsin been advised by his economics aide, Aleksandr Livshits, that the place to find relative competence, without a major shift in policy, is with First Deputy Premier Boris Nemtsov and his associates? Sergei Kiriyenko worked under Nemtsov when the latter was governor of Nizhni Novgorod, and came to the Fuel and Energy Ministry at Nemtsov’s behest. Livshits, at a press conference on March 25, spoke confidently about his plans, “together with the government, together with Boris Yefimovich Nemtsov,” to solve certain pressing military funding questions.

Or, is businessman Boris Berezovsky, former deputy secretary of the Security Council and lately the foe of Chubais, the *éminence grise* of these events? On the eve of the government’s dismissal, Berezovsky, just home after a month of medical treatment and business negotiations in Switzerland, told a TV interview show that the country should get ready for new faces in the government. He described himself as an unpaid “adviser to the President’s chief of staff” — Valentin Yumashev, who works closely with Yeltsin’s daughter, Tatyana Dyachenko.

Or, is Yeltsin preparing for the failure of any appointment from within his previous government? If the Duma rejects his nominee three times, there are supposed to be new Duma elections, leading to even more turmoil. Or, Yeltsin could seek a government of national unity, under a figure such as Yegor Stroyev, leader of the Federation Council (upper house of Parliament).

Those were three of the leading lines in Moscow, in the days after Yeltsin’s March 23 bombshell. Under any political course of action that might be attempted, Russia’s circumstances are ripe for a drastic change of economic course. The world financial crisis will continue to force the issue.