PERSONAL VIEW - RUSSIA - IMF GIVES TOO LITTLE, TOO LATE.

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The International Monetary Fund last week stared into the Russian abyss and for the first time saw the horrors. After withholding a $1.5bn loan from the Russian reformers in the second half of 1993 on the grounds that the budget deficit was too high, it finally freed the loan, in spite of a vastly larger deficit today. IMF inaction in the past contributed to Russia's gathering storm. Its action last week was a desperate move to help head off Russia's descent into chaos.

Russian reformers are understandably nonplussed. Last year, with reformers in the cabinet, the IMF withheld financing when the budget deficit was about 10% of gross domestic product; now it lends money to a 'cabinet of lobbies' with a deficit about 15% of GDP and rising. Tax collections appear to have dropped by at least 5% of GDP so far this year. The draft budget on which the IMF agreement is based is dubious.

And yet the IMF's move was understandable. The Russian central government teeters on the edge of a disaster, as it no longer collects adequate revenues needed to run the state. Tax evasion and arrears are rife; inflation eats into the real value of tax collections; revenues collected regionally are often not sent to central government. Under such circumstances, the government cannot feed and house the army, or provide for public order, much less cover social needs.

If the IMF had continued to withhold the funds, it would have amounted to the west's abandonment of Russia's reform hopes. Prime Minister Victor Chernomyrdin's new-found fiscal prudence, whether feigned or real, would have been buried immediately by a political avalanche. He knew it, and therefore courted the IMF chief, Michel Camdessus. The reformers are furious, but their anger would be better directed at past western inaction and poor IMF advice.

The real problem is not the IMF's action, but a much deeper malaise. The $1.5bn means little, since it covers less than two weeks of Russia's budget deficit. Only a much larger aid programme, with a wiser stabilisation strategy, could do the job.

IMF incantations of budget cutting and tight monetary policy are insufficient. Almost no stabilisation programme in history has worked the way that the IMF recommends in Russia. Real stabilisation programmes, whether in Israel, Bolivia, Poland, Estonia, Argentina, or the classic stabilisation programmes of the inter-war period, start from the proposition that a country needs a stable convertible currency as the first step towards ending high inflation, not the last. After currency stability is achieved, and inflation is lowered as a direct result, then cuts in the budget deficit become politically and economically more likely.

To move first on the currency typically requires large-scale help from the outside world to back the currency and to help finance the budget deficit, as well as immediate relief on debt servicing. The foreign help should surely come together with significant deficit cutting, but well before the fundamental budgetary problems are fully resolved.

The IMF has blundered badly on these points. It delayed introduction of a separate Russian currency in 1992. As a result, Russia was bombarded with inflation from the other states. The IMF has argued constantly against pegging the exchange rate until several months after inflation is ended, so guaranteeing a vicious circle of currency depreciation and rising deficits, not a virtuous circle of currency stability and falling budget deficits.

The IMF has failed to mobilise international assistance to help Russia fund its budget deficit, and to back its currency. It is poignant, and ironic, to compare Russia's shoddy treatment with the protections received by Macy's department store in the US when both Russia and Macy's went into default in January 1992. Macy's received an immediate standstill on all debt servicing under Chapter 11 of the US bankruptcy code. Two weeks later, in February 1992, it received a $600m working capital loan, also under Chapter 11. The
Russian government received its first working capital loan, from the World Bank, also for $600m, nearly one-and-a-half years later! Even debt service relief is not yet fully in place.

It is time for a serious, professional, external review of IMF operations in Russia. More important, it is time - if it is not already too late - for western governments to design a real support programme for Russia in return for a real stabilisation strategy. This would surely cost closer to the $28bn already announced, but not delivered, by the Group of Seven leading industrial countries, than the IMF’s $1.5bn. At least the IMF’s modest action gives a few more weeks to move on the more basic agenda.

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