Western governments and institutions are finally getting their act together over Ukraine. The Group of Seven industrial nations wisely announced at their recent summit that Ukraine could expect more than $4bn once it adopts meaningful economic reforms. When Ukraine's voters ditched do-nothing President Leonid Kravchuk and elected Leonid Kuchma, the G7 announcement suddenly opened the way to concrete actions.

While International Monetary Fund managing director, Michel Camdessus, has rightly opted to press the western case by making an early call in Kiev on the new president, one big problem remains: the IMF advice itself, in particular its monetary policy.

The most urgent question facing the IMF - whether in Ukraine, Russia, Kazakhstan or elsewhere - is how to help a bankrupt government trying to end high inflation. The IMF's approach is straightforward - sharp cuts in the budget deficit, a low target growth of the money supply, high real interest rates, and a floating exchange rate. But while these policies will end high inflation in the long run, they almost invariably lead to an unnecessarily deep recession; indeed, often to a reversal of the policies themselves, as recent history in Ukraine and other former Soviet Union countries confirms. The IMF has always blamed the governments for not following through, not recognising that its advice has played a significant role in these failures.

There is a better way. Stabilisations in Israel in 1985, Bolivia in 1986, Mexico in 1987, Poland in 1990, Argentina in 1991 and Estonia in 1992 have been based on a different principle. These governments recognised that low money growth was not enough. It was also necessary to bolster expectations of low inflation and to raise confidence in the money, in order to raise money holdings and to reverse capital flight. This was accomplished by a strong government commitment to a stable exchange rate, at least for several months, together with other fiscal, monetary and privatisation measures along normal IMF lines.

Exchange rate stabilisation serves several key functions in ending high inflation. It directly limits price increases in tradeable goods, thereby providing a 'nominal anchor' to the price level. It ties the government to a highly visible target. It co-ordinates future price expectations around a common standard. It raises confidence in the currency, especially when the pegged rate is backed by international resources or gold, as in the case of most of the highly successful programmes.

Countries making a clear commitment to a pegged exchange rate have done much better than countries simply allowing their exchange rate to float. Most recently, in the Baltics, the pegger, Estonia, outperformed the floaters, Latvia and Lithuania, until the latter countries relented and adopted Estonia's approach earlier this year.

The notable stabilisation programmes of the past decade - Israel, Bolivia, Poland, Argentina - were usually carried out despite the IMF, not because of it. Estonia's currency board system was launched over the heated initial objections of the IMF staff, though finally with IMF support when Estonia went ahead undeterred.

The IMF's poor monetary advice continues on seeming auto-pilot. Last week, it approved a bizarre programme for Kyrgyzstan. The Kyrgyz budget deficit is a respectable 4% of gross domestic product but inflation is above 100%, because of a lack of confidence in, and a continuing flight from, the new national currency. Remarkably, the Kyrgyz money supply is 3% of gross domestic product, so slight is the confidence in the money! The situation cries out for a defence of the currency, backed by an international stabilisation fund. Instead, the IMF plan calls for more budget cuts, and a further decline in the ratio of money to GDP. Even the IMF's own research department concluded last December that the 'exchange rate anchor' can 'enhance the credibility of stabilisation initiatives'.

There are still chances, though. Ukraine, Russia, Kazakhstan, Kyrgyzstan and elsewhere are all led by
presidents prepared to push strong reforms, and to wrestle with parliamentary resistance. The G7 and Mr Camdessus have taken important steps to make the western support more active and timely. Now the goodwill must be backed up with good ideas - currency stabilisation supported by IMF and international resources. Renewed confidence in the national currencies in these countries would be a crucial step to a renewed confidence in economic reforms and in a democratic future.

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