

On the Russian Collapse

An interview with Boris Kagarlitsky

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Kagarlitsky's books in English include: *The Thinking Reed* (Verso, 1988); *The Disintegration of the Monolith* (Verso, 1993); *The Mirage of Modernization* (Monthly Review Press, 1995); *Square Wheels* (Monthly Review Press, 1995); and *The Restoration in Russia* (Verso, 1995). Kagarlitsky is a regular contributor to several Russian newspapers and journals.

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Multinational Monitor: *Can you provide a brief snapshot of the state of the Russian economy?*

Boris Kagarlitsky: Probably for the first time in Europe since the first World War, a major economy is just falling apart.

It is not just a consumer issue. The ruble collapsed. Because of the collapse of the ruble, the price system became unorganized, and the exchange rate became unclear and imports are halted. People do not import because they do not know how to sell.

The ruble is now the worst currency in the world. In one month, the ruble went from 6.2 to 22 to the dollar. At the same time, salaries remained exactly the same. And the inflation rate is only 15 percent.

If you import goods, you cannot sell them. Trucks arrive at the border and they have to go back, because the importer just refuses to pick up the goods which are imported and they cannot

pay compensation to the foreign companies which sent the goods.

That is really dramatic, because in certain major cities, like Moscow or St. Petersburg, about 70 percent of the food is imported (versus 10 percent in the Soviet period), which means we are literally running out of food. The shops are empty and there are queues. So the market economy created the same problems which were attributed to Soviet-style central planning, with its inefficiency and inability to deliver the goods to the right places.

But that is only part of the problem. With the financial crisis, the state debt pyramid collapsed.

In order to keep the ruble stable, as advised by the IMF, the Russian government had to make state debt more attractive as an investment for the private sector and that was calculated in rubles. When the ruble was in danger of falling for the first time, the interest went to as high as 200 percent. Because of high interest rates, most of the private banks had their assets in rubles, not in dollars. They knew the debt pyramid was going to collapse but nobody knew when.

When the state debt pyramid did collapse, the banking system also collapsed. Most of the banks lost most of their assets, so they were not able to pay their customers. When the financial system collapsed, transactions halted.

Of course the official media will represent this as the Russian central bank's inefficiency. It is true. It is completely inefficient, and they managed the crisis in the worst possible way. But the key issue is that the Russian economy starting falling about

The reforms failed to create an entrepreneurial class. The privatizers really thought that if you get private property, and give it to someone, then this someone will automatically become capitalist, or entrepreneurial, just because of the fact that he possesses this property. Instead, we developed something that is sometimes called a lumpenbourgeoisie, which uses property, but not in a capitalist sense.

a month before the financial collapse.

It was in April-May, when the growth stopped. In June-July, the decline started. Industrial decline was about 9 percent in July. This is very important, because in Russia the economy is seasonal. In the summer, the economy usually grows faster.

The decline was quite natural, because there were no resources for economic growth. Private managers had exhausted the potential of the enterprises, and they failed to invest.

On the one hand, they wanted everything to be private. On the other, they didn't want to invest, but they wanted the economy to grow.

It was the decline of the real economy which pulled down the value of the ruble, not the mistakes of the bankers. The only mistake of the bankers was that they thought they were totally independent of the real economy.

Now, everything is disintegrating. It is more or less like 1916, without war. This time there was no major war, but the situation is exactly the same thanks to the free market reforms.

MM: How did the free market reforms do that?

Kagarlitsky: Almost every enterprise which was profitable under the Soviet system was privatized. Even the enterprises which were prohibited from being privatized were privatized. So the Russian economy became one of the most privatized economies in the world — and definitely the most private in Europe by far. It could be compared to the United States. Most European countries still have public phone companies; Russia doesn't. Europe still has public airlines; in Russia, most local airlines are privatized.

There was not enough money available in the country to cover more than 1 percent of the public assets. Given the black market, given the mafia money and so on, that could be another 5 percent. International capital was prepared to pay for perhaps another 10 percent. So if the assets were sold for a real price, you could sell something like 15 to 20 percent of the economy, and the rest would have remained public. If the entire Russian economy was privatized, the only possibility was to give the enterprises away for nothing or for some symbolic price.

Those who received the property, usually the people who were close to the top functionaries who distributed the property, became the oligarchs.

In giving the enterprises away, the state undermined its own income base — originally these enterprises produced profits which went directly into the state budget, which also went into investment and welfare and so on. With the enterprises private, the state just sits down and waits for taxes to come. But they never came, first because there

was no tax system. When they established a tax system, they discovered that when the enterprises became private, their performance declined immediately.

The new owners were completely unable to manage the enterprises properly. They didn't and couldn't invest in upkeep, let alone improvements. So they were either loss-making, or they didn't show their profits.

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By contrast, Byelorussia, instead of privatizing started modernizing. They invested money into infrastructure, into equipment. While Russia, before the current crisis, had a 9 percent decline in industry, and the previous year Russia had zero growth, Byelorussia the same year had 10 percent growth.

[Byelorussian President] Lukashenko is the bad boy of Central Europe, because he didn't privatize. He is authoritarian — that is absolutely true. But he is no more authoritarian than, say, Yeltsin in Russia. The difference is elsewhere.

Byelorussia did not privatize the economy. They had only some enterprises privatized, and they only had enterprises privatized for which there were real investors who came with real money — real investment projects which were realistic according to the market estimate of the value of the assets. In all other cases, it was public investment, which went to diversifying production. Production was realigned to more exports. They had inflationary policies to keep the price of the labor force cheap. They have low wages, but wages were paid, and they have full employment.

While they kept the Byelorussia ruble low, as compared to the Russian ruble, at the same time they maintained the system of social security — free health care, free education, holidays for workers and so on. People did not protest against the low wages, because they knew what was going on in Russia and the Ukraine, where wages were theoretically high, but the social system collapsed.

Russia has declined. Byelorussia has grown.

MM: You describe the essential problem as one of the real economy. How does the collapse of finance fit into the story?

Kagarlitsky: The point is that while the real economy didn't work, the concentration of wealth was tremendous. The enterprises didn't work in the

sense that performance declined. If you use the enterprise as a source of cash, then you end up with a lot of cash that you don't want to reinvest. But then the money must be placed somewhere. A lot was put into real estate. It was exported in huge quantities, ending up in American, Swiss and British banks. A lot of money accumulated in forms of so-called financial capital — state debt, state bonds — which didn't go into production but was recirculating in the banking system. That is why the financial system became so important. All of this money just disappeared when the ruble pyramid collapsed.

MM: *When International Monetary Fund (IMF) money comes into Russia, where does the money go?*

Kagarlitsky: I think quite a lot of this money is back in America in the private accounts — maybe most of this money is there. In that sense, you are not risking much; the money returns faster than you think.

Basically, the money goes to just one project: keeping Yeltsin in power. The IMF money is usually not linked to specific projects; it goes into the central bank.

The World Bank was different; it tried to link its credits to particular projects, many of which were not realized. For example, there was a scandal surrounding a World Bank project to restructure the Russian coal industry. The first tranche was \$500 million for the restructuring of the coal industry. It never reached the miners — it disappeared in Moscow. That was in the press, everyone knew, the head of finance personally tried to find the money, but failed. That is good: because of that, our coal industry was saved. The idea was to close down most of the coal industry and to use this money to compensate the workers to move elsewhere — but elsewhere means nowhere, because there were no jobs anywhere. So it was take \$500 million, shut up, and eliminate the industry. The losses for Russia would be billions of dollars in the long run. I think the guys who stole the money did a very patriotic thing for the country.

The IMF didn't try even that. The IMF just gave money to the central bank, mainly to keep the ruble stable. The philosophy of the IMF was if you have a good, stable currency, everything else will be OK; investment will come, the economy will grow, etc.

But what happened with this money? Russian hard currency reserves by the end of 1997 were around \$40 billion. These were central bank reserves. When the Spring crisis erupted and the ruble was on the brink of collapse, the Russian government spent about \$500 million a day to

keep the ruble stable. As a result of that, hard currency reserves were reduced to \$17 billion and then \$14 billion.

At the same time, the central bankers asked the IMF to give them more money to make up for the hard currency reserves lost in their attempts to keep the ruble stable. Some IMF money arrived. That didn't prevent the ruble from collapsing, but the money was spent on currency exchange.

We are now left with no money, and a huge international debt. That money just evaporated.

It is like a black hole, you can spend whatever you want. Finally, the central bank just gave up, when they lost most of their hard currency reserves and lost most of their IMF credit.

MM: *How are the miners or other popular movements responding to the crisis?*

Kagarlitsky: One thing that is very depressing is the left wing. The level of popular protest has been very low during the whole period. It is very interesting in the sense that discontent is almost universal, but open protest is very low. And that is very much thanks to the Soviet tradition. The Soviet experience taught them that you cannot do anything. For example, when the ruble collapsed, instead of going into the streets, people rushed into the shops, many to buy before their credit cards were cut off. It was like shooting at anything that moves, it was buying anything they saw.

In a certain sense Russian workers are very declassé. Because in the enterprises, they work half a year and for half a year they stop working, though they are not laid off. The enterprises do not pay them wages, but they give them products. If your enterprise produces china or glass, for example, instead of wages you get these products. Then you go to the nearest big city and sell it. So you are a worker but also a salesperson, a kind of petty bourgeois. It means people's social identities are mixed. People look for individual solutions.

The miners are a special case. They are the best organized of the Russian working class population. Miners work permanently. They have to. The Russian economy needs a lot of coal. So they have to stay there, they have to survive, they have to protest, because they have no other way. The conditions are terrible, especially in the North. The mines in the North were developed as labor camps in the Stalinist years. The people there are usually grandchildren of the people who were sent to Stalinist prisons. They are very militant. They always say, what can they do — send us to the North?

MM: *What are the miners asking for, beyond the immediate demand to have wages paid?*

Kagarlitsky: It is not just a corporatist project.

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the mines. They called for regulation of tariffs on railways, with more planning. Coal from Malaysia or the UK is cheaper than Russian coal because of the costs of railroads and transport in Russia. So instead of closing down the mines, rail tariffs should be reduced.

There is no clear project, but the tendency is very visible. They now even discuss the possibility of establishing a broader labor movement, to connect miners to other workers.

MM: What direction would you like to see things go in a near or medium-term sense?

Kagarlitsky: We've come to a point where it makes no sense to discuss where somebody wants things to go. We have reached a point where we face a national collapse. The minimal agenda is to avoid famine, to avoid starvation and to avoid final destruction of the economy, in the sense that the enterprises must remain functional, or otherwise they will turn into piles of useless metal, stone and brick.

So now the agenda is survival. By the way, I think we will survive. Russia survived through terrible periods.

The Russian economy, I think, has now reached the stage where no free market approaches are possible. To make enterprises productive, you must get supplies, resources and money. There is no money, the resources are elsewhere. The goods do not get to the customers. The banking system does not exist any more. The market infrastructure does not exist anymore. So you have to use administrative measures to make sure things work, to guarantee that people will be fed tomorrow and that they will not starve. And you have to print money — when people do not have enough money to buy food and to survive, it is much better to print money and increase salaries, while at the same time establishing price controls to guarantee that inflation does not rise too fast.

Getting out of the present bottleneck will require renationalization in some key areas. Now people speak about nationalization of banks, because either there will be public banks or no banks. People speak about nationalization of Gazprom and oil companies and proper control over the railways, which are formally public, but behave like a private company. There must be renationalization of domestic-flying airlines, which are private but completely disinvested. They have no capital to buy new aircraft, and as a result we have this terrible record of air crashes.

Oil and gas must be nationalized to produce money for the budget, otherwise we'll never have enough money for the budget. And vodka must be nationalized. In Soviet times, vodka production and sales covered 60 percent of the budget.

MM: Sixty percent of the budget?

Kagarlitsky: Yes. Now it is totally private. So if you renationalize vodka, oil and gas, your budget problem will be solved. Through the whole history of Russia, vodka was crucial for the state budget. Vodka was the public monopoly under the czars, and it was also one of the main aspects of the state budget. That may seem shocking, but it is true.

MM: How do you see the economy evolving over the longer term?

Kagarlitsky: In the long run, some kind of mixed economy will emerge, with a larger and more decentralized public sector. An interesting development which is happening now is that failing private enterprises are renationalized locally — not by the central government but by local governments. They understand that the only way to make enterprises work is to nationalize them; and they really put them back to work. In many cases enterprises which failed under private management are renationalized and restarted and are working properly. They are paying wages, they have restarted investment.

There is some external control needed, to prevent managers from stealing everything and putting it into their pockets. I don't want to say the new managers are extremely good, just that the previous managers were so bad that it is very easy to be better.

The more diversified and decentralized public sector will be more connected to community and provincial economies than the old, centralized private sector.

In the long run, some kind of bureaucratic planning will emerge, with a local emphasis. That means national planning will be more like some kind of coordination of different localities.

Small business must also be encouraged. With the large-scale privatization of the Russian economy, small business was completely destroyed. There was a growth of small private business during the Gorbachev period through the beginning of the Yeltsin period. Then during the Yeltsin period, small business was suppressed, because everything was done in the interests of these huge oligarch empires, which were not interested in small business, except for those few which provided services to the rich.

What we need is to encourage small private business at the level of community.

Even if we don't want it, we will end up with some of these enterprises closing down. So there must be some local policies to help people to be self-employed. We need a public sector which will subcontract, which will create this self-employment. It will not emerge spontaneously. ■