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Russia – a Partner Sui Generis for the IMF?

Early in 1994, the Government of the Russian Federation negotiated with the International Monetary Fund the disbursement of the second tranche of “only” US\$ 1.5 billion of a previously pledged standby loan. A year later the talks were about a new standby loan of as much as US\$ 6.4 billion. In February of this year the volume of lending under discussion was US\$ 10.2 billion. In all three cases the official spokesmen of the delegations let the world public know that the Fund would not be making any concessions in its conditionalities and that it was quite within the realm of possibility that negotiations could fail. And every time there was a happy ending when the IMF’s Managing Director Michel Camdessus turned up for the final round in Moscow and the tough talks conducted with such a sense of responsibility by both sides ended with a recommendation to the Board of Directors of the International Monetary Fund to grant the loan to the Russian Federation. All the IMF ever received in return was a promise by the government of Russia to take on the responsibility for seeing that certain stability and regulative objectives were achieved.

When, against its own better judgement in view of the economic situation and development trends in Russia, the Fund approved disbursement of the agreed loan in 1995, this raised the question of whether its patently politically motivated decision did not demolish the credibility of its own hitherto strict lending yardsticks – i.e. the principle of conditionality – and thus jeopardize its monetary policy authority. In view of the current political and social situation and the likely destabilisation of the Russian economy, there is a need to take another, and even harder, look at decision-making in the Fund even though its politically biased decision to grant the loan in March 1995 appears warranted in hindsight by the relatively stable development of the budget, prices, the rouble and the balance of payments during 1995. The Fund evidently acted under even heavier political pressure in 1995 than in the previous year. After German Chancellor Helmut Kohl and US President Bill Clinton made plain their wish that the loan be granted, even the most convincing economic arguments against it would have fallen on deaf ears.

So despite the widespread doubts about the economic outlook in Russia this year and despite the dubious character of various decisions on budget spending by President Boris Yeltsin and the Duma in February, Camdessus appeared before the press and announced the granting of a new credit worth US\$ 10.2 billion for a three-year term. The Fund explicitly gave the Russian government to understand that the first annual tranche would amount to about US\$ 4 billion and the disbursement of the first monthly instalment could begin as early as April, well aware that the Russian Ministry of Finance had already earmarked US\$ 3 billion of the loan for its 1996 budget. In order to pre-empt the many question marks about the soundness of its decision, the Fund stated that it assumed a stabilisation of the general economic situation in Russia in 1996 and 1997, with 2-4% economic growth, and even expected a growth rate of 6% as of 1998.

In the credit negotiations the Russian Federation vowed to continue with economic reform, explicitly including privatisation, a promise readily given by many Russian politicians faced with the country’s dire financial predicament. The Fund places particular stress on the stability conditionalities, on cutting the monthly inflation rate to 1% by the end of 1996, on not allowing the budget deficit for 1996 to rise to more than 4% of gross domestic product and to curtail it to as little as 3% and then 2% in the next two years. To cut the budget deficit by this much the inefficient tax system will have to be overhauled at last. Even before the conclusion of the loan negotiations Moscow had declared its basic willingness to abolish export duties on gas and oil. The IMF failed again this time to have the granting of the loan tied to effective steps to stem capital flight from Russia.

But can the Fund really rely on Russia to keep its promises and realistically expect its key economic targets to be met given the unpredictable political and economic situation in the Russian Federation? Surely the IMF cannot have failed to notice that political opposition to its forced austerity policy has mounted so much that Yeltsin, particularly in view of the coming presidential elections, cannot help but make extensive spending commitments to the people and to insolvent firms. Neither the inflation rate target nor the strict budget deficit ceiling are now likely to be met. Yeltsin is in the process of undermining the realisation of the pledges made to the Fund himself by handing out electoral presents throughout the country to secure his own political survival. Long-term tax deferrals, from which large-scale state-run enterprises profit in particular, will alone place an estimated US\$ 6.5 billion burden on the government budget. On top of this are promises to pay outstanding wages to miners and teachers and to raise pensions and scholarships. The development programme for Chechnya will also devour several billion dollars.

Not only the dismissal of deputy prime minister Chubays, in effect the last determined reformer in the Chernomyrdin cabinet, casts doubt on whether the government will resolutely press ahead with economic reform. Official announcements about slowing the pace of privatisation and even of renationalising some already privatised enterprises point in the same direction. Furthermore, there is an open discussion over whether Russia should orientate itself toward Western European social market models. The Communists, who emerged triumphant from the last elections to the Duma, are not reticent to make their opinions about economic reform and in particular privatisation public in statements to the press. Maslyukov, the former head of planning in the Soviet Union, would like to nationalise all areas of key importance for the development of the economy or bring them under full government control by means of regulations.

In response to misgivings about its decision to grant credit to Russia, the Fund has given its assurance that it will continually monitor the adherence to the fiscal and economic policy conditionalities and if necessary stop payments of any further tranches. After the recent declarations of intent by the Communist Party and the decision of the Duma to reinstate the old Soviet Union, the IMF could actually save itself the trouble, if Zyuganov took over the presidency, of sounding out to what extent the transition from a centrally planned to a market economy would proceed.

Not just the influence exerted by Western heads of state and government on the IMF but also other developments in connection with Russian foreign debt indicate that the Fund is under heavy political pressure in its decision-making. President Yeltsin and cabinet ministers are trying to misuse the Fund for their own purposes. During the negotiations with the London Club on the now agreed debt rescheduling arrangement covering about US\$ 33 billion – underpinned by no collateral whatsoever – Moscow stirred up fears that it might not ratify the rescheduling agreement if the IMF did not grant the new loan; this would have increased the uncertainty of creditor banks with regard to the repayment of their outstanding loans. Similar considerations may well have played a part in the rescheduling agreement recently negotiated with the Paris Club for a sum of about US\$ 40 billion.

The indirect influence of the Russian Federation over financial policy decisions appears to have grown recently. The Fund, Western governments and the Western creditor banks should keep in mind, however, that Russia badly needs them and other Western finance institutions. Both the IMF loan and the two debt rescheduling agreements are essential preconditions for Russia to return to the international financial markets to bolster the government budget for 1996 with additional foreign funds. President Yeltsin recently termed the possible refusal of support by the IMF and the European Bank for Reconstruction and Development betrayal; but he ought to know that a lax attitude towards the Fund's conditionalities governing its financial commitments could very quickly be tantamount to breach of contract. Only if it sticks to the path of reform will Russia be able to count on further funds from public coffers in the West.

Klaus Bolz