The IMF and Russia in the 1990s

John Odling-Smee

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A remarkably wide range of views has been expressed about the role of the IMF in Russia in the 1990s. Some people believe that most of the economic problems of Russia were attributable to the economic reform policies of successive Russian governments and that those policies were in turn pressed on them by the IMF.[2] Others believe that the IMF's influence in Russia was minor. Both Russian and foreign commentators can be found in both camps. The purpose of this paper is to explain the role of the IMF in Russia, as seen by a senior member of the IMF staff team working on Russia. It focuses on where and how the IMF made a difference to economic policies rather than on the quality and relevance of all the economic policy advice and technical assistance given by the IMF.

IMF policy advice

The IMF's basic view of the necessary economic reforms was that it was important to move as quickly as possible with all the key changes, especially macroeconomic stabilization, liberalization, and privatization. The IMF recognized that many reforms would take years to complete, especially the construction of the legal infrastructure for a market economy, privatization and restructuring of large enterprises, and the creation of a market system for banking and finance.[3] But this was not seen as a reason for postponing the main stabilization

[1] John Odling-Smee was Director of the European II Department of the IMF from 1992 to 2003. He thanks Gérard Bélanger, José Fajgenbaum, Yegor Gaidar, Oleh Havrylyshyn, Ernesto Hernández-Catá, David Owen, Emil Sunley, Poul Thomsen, Siddharth Tiwari, Thomas Wolf, and Mikhail Zadornov for many helpful comments. Aidar Abdychev and Franziska Ohnsorge provided valuable assistance. The author is responsible for the views expressed here and any errors. See Odling-Smee (2004) for a more detailed version of this paper.

[2] For example, Stiglitz (2002) wrote, "The IMF strategy did not work: GDP in post-1989 Russia fell, year after year" (p. 146).

[3] Camdessus (1992) noted that the process of basic economic transformation would take many years. Odling-Smee and Wolf (1994) classified reforms according to whether they could be undertaken over short-, medium-, or longer-term time horizons.

and liberalization measures, with some specific exceptions, such as gradually rather than suddenly raising the prices of public utilities and housing rents.[4]

Throughout the 1990s, the Russian government's public position was to pursue liberal economic reforms that would lead to the rapid establishment of a market economy. Thus IMF views were similar to those of Russian reformers and many foreign observers. As a consequence, the IMF was often in the position of endorsing policies proposed by reformers with little need to push for major changes in them.[5] However, the reformers and technicians in the CBR and government did not necessarily know how to give operational meaning to their policy choices, or how to handle many of the detailed issues that arose. The IMF played a major role in transferring knowledge about such issues, all within a context of market-oriented macroeconomic policies aimed at producing low inflation and a favorable environment for growth.

This picture of the IMF and the Russian government working harmoniously together on a program of liberal economic reforms has to be qualified because of three factors: the lack of consensus in favor of liberal economic reforms within the Russian leadership and the weakness of the Russian state; the difficulty Russia had in accepting foreign advisors; and the influence of the G7.

Lack of consensus in Russia and weak state

Consider, first, the opposition to economic reforms within government. The strongest strand of alternative thinking came initially from those who saw the primary economic function of government as being to support production. They did not wish to return to central planning, but they sought to use the government's fiscal and regulatory powers, and the allocation of Central Bank of Russia (CBR) credits, to encourage the continuation and growth of production, even in sectors that objectively had little future. The opposition to the reformers not only had different ideas about economic reforms; in many cases, they also had more operational experience and knew how to make the bureaucracy work in pursuit of their interests or to impede the reformers' policy initiatives. This was especially true in 1992 when the reformers underestimated the bureaucratic and other obstacles in their way, and placed too much faith in Yeltsin's ability to make things happen.

Economic policymaking suffered not only from differences of view within the government, but also from the weakness of the state itself. There was a vacuum created by the collapse of the coercive communist system and the Communist Party network, which together had

[4] The earliest official statement of the IMF's views about economic reforms are in IMF and others (1990). See, especially, Chapter V (pages 16–19) for a discussion about the speed and sequencing of reforms.

[5] Vladimir Mau, a leading reformer, explained the situation as follows: "A good part of the "IMF conditions" were developed in Moscow, not Washington. Russian politicians are the ones who initiated many of these conditions" (Mau (2000) p. 108).

ensured that government policy was implemented. This was filled by various business and interest groups as well as by criminals. In the early 1990s, enterprises were finding it difficult to adapt to the new environment in which they had to react to financial signals (e.g., changes in profitability and prices) rather than instructions from economic planners. They therefore sought protection or financial assistance from the government and the CBR to help them through the adjustment phase. From the mid-1990s, a small group of businessmen, the oligarchs, became increasingly powerful. They used their power to influence both the economic policy agenda, including the preparation of legislation, and the implementation of policy. They made special arrangements with the government about the amount of taxation that they would pay. They were not opposed to market-oriented reforms in principle and, indeed, provided a bulwark against a return to a planned, state-owned economy. But they sought to ensure that their own businesses were protected from competition and had favorable financial dealings with the government. Once other businessmen saw what the major oligarchs were able to get away with, they all tried to emulate them, further weakening the state.[6]

The lack of consensus in favor of liberal economic reforms within the Russian leadership and the weakness of the Russian state were the two most important reasons why economic reforms did not progress more smoothly, despite the stated policies of the government and the efforts of the IMF.

Foreign advisors in Russia

While the official policy was to request technical and financial assistance from the IMF, and many individual Russian officials benefited from discussions with IMF counterparts, it was not easy for Russians, individually or collectively, to seek and accept advice from IMF staff members. This is the second qualification to the picture of harmonious IMF/Russia relations. Russia is a strong, independent nation with centuries of history as a major European power and recent experience as a technically sophisticated world superpower. Many Russians, especially older and more nationalistic ones, felt that it was humiliating to have to negotiate with the IMF for loans and to adjust economic policies to IMF requirements. IMF staff tried to be sensitive to this need for country "ownership" of economic policies, which is an issue in the IMF's relations with all sovereign member states, albeit magnified in the case of Russia. But there was inevitably some tension in the relationship between the IMF and Russia arising from Russia's self-image and history.[7]

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[6] See Nagy (2000) and Graham (2002) for more discussion of the weak state. Nagy focused primarily on the implications for economic reforms and the economy.

[7] Yevgeny Primakov, prime minister from September 1998 to May 1999 and previously a senior member of the Soviet foreign policy establishment, was representative of those who found it most difficult to accept the IMF's role in Russia. In his memoirs, he said that he was boiling inwardly when he thought that Gérard Bélanger, IMF mission chief in 1999–2002, was "moralizing" (Primakov, 2001). Earlier in a November 1998 meeting with Jorge Márquez-Ruarte, IMF mission chief in 1997–99, he had accused the IMF of dictating to Russia and acting like Bolsheviks.

Influence of the G7

The third qualification relates to the role of the G7. The major western nations hoped for a smooth transition to a market economy in Russia. But they were very reluctant to spend large sums of money to assist it, in part because of a deep skepticism about whether Russia really was ready to implement major reforms. Instead, they turned to the international financial institutions (IFIs), which had the capacity to apply conditionality to any lending, as well as significant sums of money. By not providing large scale financial support themselves to Russia, the G-7 were effectively assigning two tasks to the IFIs that were sometimes contradictory.[8] First, the IFIs were expected to perform their usual function of lending on the basis of economic policies or projects that met the normal standards of the institutions. In insisting that Russia had to agree its economic policies with the IMF, the G-7 caused Russia to take the IMF's views more seriously than it might otherwise have done. Second, the G-7 sometimes wanted the IFIs to lend in order to show support for the government (or President Yeltsin), even at times when economic policies or projects were not up to the standard normally required by the IFIs.

This situation was unsatisfactory for both the Russians and the IMF. Russian governments thought that the West should be prepared to make available large sums of money without difficult policy conditions attached. This was a small price to pay for ensuring that Russia never returned to communism or confrontation with the West. The Russians resented the need to negotiate with the IMF and the delay this involved. The IMF was unhappy because it feared that the political concerns of the G-7 to make IMF money available to Russia, even when the normal economic policy conditions were not met, might cause the G-7 to push the IMF to lend with insufficiently strong conditionality. Although this never happened in an overt way, an atmosphere was sometimes created, for example in early 1994 and in 1996–98, in which the IMF felt that it should err on the side of supporting weak policies rather than interrupt disbursements altogether. This was not only because of the G7's views: many within the IMF believed that its influence over Russian economic policies was greater when there was an active dialogue without lengthy interruptions of lending. The Russians understood the situation and sometimes saw negotiations with the IMF as a charade since they believed that the G-7 would ultimately insist that the IMF should go ahead with the loans.

The result was that, during the years before the 1998 crisis, while the G-7 helped to create an important role for the IMF in Russia, its political and bilateral interests at the same time caused a weakening of the IMF's influence. After 1998, and especially after the newspaper stories suggesting money laundering scandals and the renewed fighting in Chechnya in 1999,

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[8] In fact, quite large sums of money were provided by the G-7, although most of it was tied to particular imports (suppliers' credits) or expenditures (e.g., housing for troops returning from Germany), or was debt relief. In 1992 and 1993, all bilateral creditors provided a total of US$36 billion of financial assistance, with the G-7 accounting for the bulk of it (Citrin and Lahiri, 1995, Table 7.5).

the G-7 took a much harder line on IMF lending. This too was reflected in the IMF's behavior.

Limited influence of the IMF

Once these three qualifications are taken into account, it is clear that the IMF's impact on economic policies in Russia in the 1990s was much less than the apparent similarity of views between the IMF and the government's leading reformers might suggest. By far the most important determinants of economic policies were the Russian leadership and the many economic agents who were in a position to support or thwart the leadership. It is not surprising that the IMF's influence was limited in this context.

Fiscal policy

The remainder of this paper discusses the impact of the IMF in the various areas of economic policy. The most prominent consequence of the IMF's limited influence was Russia's failure to raise government revenues and reduce fiscal deficits, which led to the 1998 crisis. Had the fiscal consolidation that was agreed between the government and the IMF in every year up to 1996 (when the medium-term program to 1998 was agreed) been achieved, it is very unlikely that the crisis would have occurred. It is even possible that a tougher stance by the IMF might have caused the authorities to bring about enough of a consolidation to avert the crisis. The crisis did, however, teach the important lesson that fiscal prudence is important, just as Black Tuesday (October 11, 1994) had taught the lesson that monetary prudence mattered.

Structural and institutional reforms

Another consequence of the IMF's relative weakness was that it had to focus its efforts on key monetary and fiscal policy issues rather than attempt to affect the whole range of reform policies. Thus, in practice, it had very little influence over structural and institutional reforms outside areas closely linked to the design and implementation of monetary and fiscal policies. In addition, it did not have the mandate or expertise to have an impact on the detailed implementation of the wider agenda of structural and institutional reforms. Its main contribution was to help keep such reforms on the agenda and to emphasize their importance. Its most ambitious effort in this direction was its work, together with the World Bank, on the government's structural reform agenda for 1996–98 in preparation for the EFF. The protection of social expenditures also received a relatively low weight in decisions about how to exert the IMF's influence. A special case of this was the increase in arrears in 1995, which met with undue tolerance from the IMF because the overall fiscal situation had been brought under control for the first time.

There was quite a contrast between the IMF's limited influence on structural and institutional reforms and the public perception in Russia and elsewhere that the IMF was responsible for policy advice in these areas and, indeed, for what actually did or did not happen. This perception was reasonable given that the programs that the IMF supported with loans, notably the 1996 program, had a large structural component, and that speeches by IMF leaders stressed the importance of structural reforms. The media focus on the drama of IMF-Russia negotiations added to the image of the IMF having influence across a much wider range of policies than was the case. The role of the World Bank, the EBRD, and others who were actively involved in advising on structural and institutional reforms received less public attention. While a general perception that the IMF was responsible for advice and outcomes in the structural and institutional area was understandable, it is surprising that some people who knew what the IMF's role actually was have continued to hold the IMF accountable for problematic outcomes.[9]

Monetary policy

Turning now to areas in which the IMF had more of an influence, the most important was monetary policy. The IMF repeatedly presented the case to the authorities for directing monetary policy at producing low inflation and, just as importantly, provided technical assistance on how the CBR should do this operationally. Although the political conditions in 1992–94 were not conducive to the sustained implementation of a serious disinflation strategy, the IMF was laying the foundations for later policies through debates with the CBR and government and operational advice. After conditions changed and the CBR and government economic policy came under new leadership in late 1994, the ground was ripe for the implementation of disinflationary monetary policies. The IMF continued to provide close support during 1995 and subsequent years, and the general success of the policies is seen in the decline in inflation in the years before the 1998 crisis.

Specific fiscal issues

Even in fiscal policy the IMF had some impact. Despite the failure at the macroeconomic level, much of the specific advice of the IMF was taken up and implemented by the government. For example, the long struggle to get rid of offsets would probably not have been successful so early if the IMF had not been pushing. And some components of the tax reforms of 2001 were derived in part from technical advice from the IMF in the mid-1990s. However, the IMF's influence was not always positive. It was, for example, a mistake to push for early abolition of the oil export duty and liberalization of the treasury bill market.[10]

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[9] For example, Stiglitz (2002) has strongly criticized the IMF for insisting on rapid privitization, whatever the price, and without being concerned about whether market institutions, such as a competitive system, were in place first. This led, he argued, to IMF acquiescence in the loans-for-shares scheme and to corruption, state capture, and growing income inequalities. (See below for more on the loans-for-shares scheme.) As Chief Economist at the World Bank in 1997-2000, he knew that the World Bank rather than the IMF was in the lead in advising on these issues and that the IMF had little influence. Similarly, Lopez-Claros (2002), who represented the IMF in Moscow in 1992–95, deplored the fact that the IMF did not stop the loans-for-shares scheme.

[10] See Owen (2004) for a more detailed discussion of these issues.

Exchange rate policy

Given what we now know about fiscal policy, it might have been better not to have introduced the pegged exchange rate regime in 1995. But the IMF could not have easily prevented it in the face of the government's insistence, as it was in principle open to such arrangements, and it did not expect fiscal policy to be so weak. Similarly, a devaluation before March 1998 might have been better than what actually happened.[11] But this was not obvious at the time, and the government might have resisted any IMF attempts to persuade it to change policy in this direction. Less ambiguous was the positive assistance that the IMF gave to the unification and liberalization of the exchange rate regime in 1992.

Transfer of knowledge

This mixed picture of the IMF's impact on specific policies and reforms is only part of the story of the IMF's role in Russia in the 1990s. Another part was the transfer of knowledge to individual officials and experts in the CBR and the government. This took place almost continuously through ongoing discussions about policy issues between the authorities and IMF missions, Moscow office representatives, and resident experts. It occurred at every level, from Camdessus' interactions with Chernomyrdin to discussions about data spreadsheets between economists. What came out of it were, in addition to specific policy improvements, a large number of officials and experts with a fine understanding of macroeconomic policy issues. As time has passed, more of these people have reached senior positions, and the knowledge has spread widely through the key agencies and public bodies. This has ensured that the CBR and the government as a whole now design and manage macroeconomic policies in ways recognizably similar to those in western industrial countries. There has also been a related improvement in the quality of the public debate about macroeconomic issues. While the IMF was only one of the elements in this critical transformation of the government's role from central planning to managing a market economy, the transfer of knowledge it brought about may stand as its major legacy from the turbulent 1990s.

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[11] It should be noted that many commentators, for example Berglöf and Vaitilingam (1999), Kharas, Pinto, and Ulatov (2001) and Stiglitz (2002), have argued that the exchange rate was overvalued before the crisis and an earlier devaluation would have been beneficial. But see the comments of Summers (2001) and Fischer (2001) on the paper by Kharas and others for an excellent exposition of the case for supporting the government's attempts to retain the exchange rate anchor.

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