Stated Meeting Report

Russia's Economic Prospects

Jeffrey Sachs

I want to talk to you tonight about the nature of the economic crisis in Russia and to give you a somewhat personal perspective on Russia's prospects for reform. It is very hard to gain enough distance to make a sound judgment about those prospects during these historic and tumultuous times—to have a good sense of whether Russia can get through its current crisis peacefully, with a civil society intact and with democracy as the outcome. Those are the standards of success that I would pose for the economic reforms under way, as well as for the broader political and social reforms.

Obviously, Russia's transformation now, like that of so many other countries in the region—the other fourteen countries of the former Soviet Union and more than a dozen countries of Eastern Europe emerging from communism, many in East Asia—is a tumultuous process that involves not merely economics but also the most fundamental and wrenching political and social changes. There is the move from brutal dictatorship to at least an attempt at a fragile and nascent democracy; the move from empire to a nation hopefully not commanding the neighboring states; and the attempt, of course, to create an economy that meets basic human needs, which Russia so miserably failed to accomplish under the Communist regime of the last seventy-five years.

Putting aside the great changes from dictatorship to democracy, from empire to nation-state, it is clear that the economic processes

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alone are of a complexity, scope, and depth virtually unrivaled in history. Russia is battling at least three fundamental economic crises now—three fundamental parts of economic change.

The first, in some ways the easiest to understand and also in some ways the most dangerous in the short term, is a financial crisis—essentially, the bankruptcy of the state, which was bequeathed to the new democracy by the Communist regime at the end of 1991. This is where most of my own energies as economic adviser were devoted in the past two years. As I'll explain, the financial crisis threatens virtually every other aspect of reform in its ferocity and its ability to throw the entire process into political turmoil.

The second process, the one that is most commonly discussed, is the process of institutional change—the creation of a market economy. This is distinct from overcoming the financial bankruptcy of the state. Some countries, like the Czech Republic, have solvent governments that still face the task of institutional change but fortunately don't have to try to manage financial bankruptcy at the same time. The combination of the two, which would be a stunning overload for any political system, is particularly perilous for Russia's, which is in a state of such tremendous change and uncertainty today.

The third fundamental part of the economic crisis could be called, in very broad terms, structural change or structural adjustment. Russia is not only financially bankrupt—it is not only a country that arrived in 1994 with defunct economic institutions and without a history or legacy of workable market institutions or market capitalist institutions—but it also has a specific legacy of resource development and resource allocation from the Communist regime, which adds tremendously to the burden of the adjustment process. As I'll discuss, that legacy was, essentially, Stalin's dream and intention to build a powerful military state backed by powerful heavy industry. And that specific task was the centerpiece of all the economic planning of the central-command system of the last fifty years. And so, on top of financial bankruptcy and the need to develop basic market institutions, Russia has the very specific problem of being a country that spans eleven time zones, that could be considered one vast rust belt of heavy industry once geared toward military production—and that we hope will never again be called upon to produce the output for which it was designed.

It's this constellation of three fundamental tasks that makes the Russian reform almost surely the most complex, challenging, and dangerous in history. Certainly, when one thinks about the tasks of economic restructuring in the twentieth century, whether in postwar Europe or postwar Japan, or about the collapse of the Ottoman Empire, or about other great economic revolutions of this century, nothing compares in either scope or danger with what Russia is facing. In view of that, it's easy to become thoroughly pessimistic about the prospects.

Indeed, I believe that one of the great dangers today is the overwhelming pessimism, both within Russia and internationally, about Russia's economic prospects. In many ways it has paralyzed needed actions and made the last two years far less productive than they might otherwise have been—especially, as I'll describe, in our own Western response to giving support for the changes through which Russia is now passing. But I think that the pessimism can be vastly overdone as well. It is not the case that we lack markers of what to do; it is not the case that we must operate blindly in the face of these challenges merely because of their enormity. It's my contention (and, as many of you know, it constantly gets me into trouble, or at least into conflict, with many of my colleagues) that it is possible to discern a way ahead for Russia, an appropriate path—obviously, a path of some significant uncertainty, but one that can be defined and pursued despite the magnitude of the challenges.

Russia therefore does have the prospect of successful change. These crises, however large they are, can still be overcome. But that will require a tremendous coordination of effort, both within the country and internationally. And I would assert that the current lack of coordination, the lack of Western response, and the obviously profound political instability inside Russia are the greatest hindrance to reform, not the underlying economic challenge itself. To some extent, I think, I can demonstrate that this is so by looking at similar, albeit smaller-scale, changes under way in Eastern Europe. There we can see more than a glimmer of hope; we can even see countries that have crossed the essential path and are, in my view, making enormously rapid progress in the "return to Europe" (their favorite phrase)—particularly Poland, where I've worked, and the Czech Republic and Hungary—although the road has been bumpier than expected. Those three countries, and at least a couple of the Baltic states, show that there are possibilities on the economic front for addressing the triad of crises shared by all of the former Soviet empire and Eastern Europe—the financial crisis, the crisis of institutions, and the crisis of structural change.

To understand how one can begin to formulate a policy response to this enormous challenge, it's important to understand where Russia was at the end of 1991, with the collapse of the Soviet Union. It's worth taking a couple of moments to try to clarify what has become in the public discussion, and certainly in the journalistic accounts, a hopelessly muddled description of which problems are due to reform, which problems were inherited from the old system, which problems are addressable in the short term, and which problems are inherently long-term problems. The point I would like to stress is that the Communist regime that collapsed in 1991 in Russia (like the Communist regime that collapsed with great similarity in Eastern Europe in 1989, particularly in Poland) left the nascent-democratic post-Communist country with a financial crisis of remarkable proportion and intensity. And it is, more than anything else, the financial conflagration that threatens to undermine civil order, to so weaken the state that it cannot possibly address the second and third crises—those of institution building and structural change.

When Gorbachev left office in December 1991, the budget deficit of the Soviet Union, as it was just ending, was on the order of about 25 percent of the gross national product (GNP). I hasten to emphasize "about," because in truth we have no idea what the GNP was, or what the budget deficit was—but thanks to the good services of the International Monetary Fund, we can take the ratio of two random variables and come up with an estimate that has a certain plausibility and at least a range that is descriptive of the size of the crisis. Twenty-five percent of the former Soviet Union's GNP, of course, is about five times the size of the United States's budget in proportion to national income. But far more important in the Russian context or the Polish context or the context of many other countries is the fact that the only way the budget deficit was being paid for was by printing money. Of course, this meant not merely the physical running of the printing presses; it meant the issuing of credit from the central bank in favor of large budget deficits that were covering a 2.5-million-man army and other vast expenditures of the state.

Throughout history, budget-deficit financing of 25 percent of a GNP has been more than enough to produce hyperinflation. According to the technical definition, hyperinflation is that extraordinary phenomenon of prices rising at a rate of 50 percent or more per month, which cumulates to 13,000 percent a year. Russia was already in repressed hyperinflation, one might say, by the end of 1991—repressed in the sense that official prices were more or less fixed. Earlier in the year they had been administratively raised three times on a wide range of consumer goods, but they were generally repressed by bureaucratic price controls, which made official prices completely irrelevant. This meant that the inflation, as it existed at that point, was in the black market, where goods could actually be purchased—not in the official market, where the official prices were a small fraction of what one actually had to pay under the counter or behind the shop or in the flagrant and ever-growing black markets throughout the country. The official distribution system had collapsed.

Most important, the danger of hunger in Russia, reported in the winter of 1991–92, was a macroeconomic phenomenon. It was not a farming phenomenon; it was not due to a sudden crisis in truck driving or bread baking or other things to which we directed our technical assistance, interestingly, that winter. It was simply due to the fact that because prices of wheat in the black market were five or six times the official price, farmers hoarded or sold in the black market or exported their wheat illegally to neighboring countries—and even reexported wheat that Western nations were sending for emergency humanitarian assistance—rather than sell to the official grain procurement agency, which was trying to buy the grain at one-fifth of the market price.

When Yegor Gaidar became head of the economic team in November 1991, and Boris Yeltsin announced the beginnings of so-called radical economic reform (also referred to by the awful term "shock therapy"), the fact was that the granaries had purchased only about 15 percent of the target procurement because of the incredible and rapidly widening discrepancy between black-market and official prices. The need to get the grain was urgent. The only choices were implementing Stalin's choice of 1928 or liberalizing prices—and that, of course, was not a choice at all. The idea of obtaining the grain by force, by requisition, by order, by law, by administrative action other than market pricing was not only morally horrendous but also practically impossible to carry out. Thus, the need for rapid price liberalization was at hand, but feeding the price pressure was an underlying hyperinflationary situation.

On top of this, Russia quickly found itself in one of the most perplexing and dangerous monetary arrangements ever concocted by the Communist mind: a monetary system in which the fifteen successor states of the Soviet Union were all simultaneously declaring themselves to be using a common ruble currency. Fifteen independent central banks were freely issuing the ruble to their hearts' content, with the understanding that their ruble credit issues would be honored in cross-border transactions.

Obviously, this was an invitation to mayhem, and mayhem is exactly what resulted: every successor state was running large budget deficits and issuing a common ruble, understanding that the inflationary effects of its own actions would simply spill over into, and be absorbed by, the other fourteen countries. In the end, during 1992, Russia bore the brunt of the inflationary actions of the other states, to the tune of 10 percent of Russia's GNP. Mechanically, this meant that Russia extended credits that turned out to be gifts in the inflationary circumstance—loans that, when paid back under hyperinflation, meant grants of 10 percent of its GNP—making Russia, in its state of utter financial bankruptcy, the largest aid giver in the world by a full order of magnitude. The United Nations has called on nations to give 1 percent of their GNP in foreign aid; in 1992, Russia was in effect giving 10 percent of its GNP through this horrendous, absolutely dangerous, and unworkable monetary arrangement.

Two weeks after Gaidar became head of Russia's economic team, the G7 governments—that is, the governments of the world's seven leading industrial countries—arrived in Moscow to negotiate the payment schedule on Soviet debt. Throughout history, it has been demonstrated that governments with failing economies and without domestic legitimacy turn, in their waning days, to foreign capital markets for that last measure of hope and help. It's easy to explain why they do it, but it's considerably harder to explain why the bankers meet them on the other side. Yet between 1986 and 1989, Bulgaria—absolutely the least creditworthy regime one could ever invent—was able to borrow several billion dollars; so too was Gorbachev able to borrow about $50 billion between 1987 and 1991. This debt could obviously not be serviced on schedule, and Russia was heading toward massive default—a condition to which it has well arrived during the past two years.

But when the G7 governments visited Moscow in November 1991, they went not to discuss with Gaidar how to meet his three challenges, the greatest in world history, or how to stabilize the new Russian democracy before hyperinflation threatened to create political and social chaos; rather, they went to settle on how Russia was to continue the flow of interest payments on the foreign debt and the repayment of short-term credits falling due. And in one of the most remarkably shortsighted and painful episodes of Western malinvolvement with Russia in this century, they pressed the Russians to sign a document guaranteeing the continued servicing of the interest payments and the short-term debt, which the Russians dutifully did for the next three weeks—by which time they had fully run out of foreign exchange reserves.

In January 1992 I published an article in the *Economist*, bemoaning the behavior of the G7 governments. I contended that pressing Russia to pay its debt was a very ill-considered move, because Russia's monetary reserves covered merely three days of imports, whereas the norm internationally is to have reserves that cover three *months* of imports. I was then taken to task by the minister of foreign economic relations in Moscow for overrepresenting the solvency of the Russian state, because in fact he had only three *hours* of import coverage, not three days.

So this was the state of affairs that confronted the Gaidar team: hyperinflation, a multistate common currency guaranteed to stoke the fires of inflation, price controls that were not only distorting but causing the utter collapse of the entire distribution system of the old Soviet state, and foreign insolvency at hand. For those reasons, at the beginning of 1992, Russia instituted the liberalization of prices and attempted to stop the macroeconomic disaster by ending budget subsidies. Both actions were undertaken on the premise that they would be strong measures. Much is now heard about "shock therapy" in societal change—the phenomenon of moving quickly rather than slowly—and about whether it isn't too much strain for a society to undergo such rapid change.

Of course, the strain is monumental. But the reasons for moving fast are not reasons of economic machismo; they are not reasons of naive belief in the magical powers of the free market to solve seventy-five or a thousand years of economic crisis. The need for urgency arises first and foremost and most brutally in the depths of financial crisis, because hyperinflation is the beast at the door. And the maintained hypothesis, in both my own reasoning on economic advice and that of the Russian economic reformers, is that hyperinflation poses the single greatest risk to the continued peaceful change of Russian society. John Maynard Keynes, as you know, put it famously and wonderfully and never better in long sections of *The Economic Consequences of the Peace* concerning the degradation and the debauching of the currencies of Central and Eastern Europe and their implications for the future peace of the region. Keynes said, you'll remember, that "there is no surer, no subtler means of overturning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million is able to diagnose." And that is the frightening aspect of hyperinflation. The extent of social dislocation that comes with high inflation is vast and, I think, unequaled in peacetime by any other calamity that a society can confront. And the most remarkable and destabilizing aspect of hyperinflation is that it is not understood, or at best poorly understood, by almost the entire society. So the affliction becomes the target of every kind of scapegoating, every kind of pernicious attack, whether anti-Western or anti-reform or anti-Semitic or anti- any other minority group that one can imagine. And this is why the need for urgent action in Russia was so acute.

As I said at the beginning, one can see from the experience in Eastern Europe, and also from the vast experience of this century, that this particular part of the Russian economic reform puzzle can be addressed by identifiable, established, and suitable means. Indeed, one of the most remarkable facts of the Russian inflation—absolutely a happy coincidence from the point of view of pedagogy and instruction—is that the money supply is a remarkably strong predictor of the Russian inflation. The identification of where this inflationary beast is coming from is a solved problem; it is not a mystery. If one graphs the rate of price increase from month to month in Russia, one finds an extraordinary correlation between that and the rate of increase of the money supply four or five months before. And this is to be expected—not necessarily in periods when inflation is of our variety (between 0 and 10 percent per year), but when inflation is of the variety found in Russia (20 percent per month or higher) or in Poland (where it reached 50 percent per month in the fall of 1989).

Fortunately, we know a great deal about how to confront such a crisis. In Eastern Europe and in parts of the former Soviet Union (Estonia and Latvia), and in Slovenia alone among the successor states of Yugoslavia, this particular kind of crisis has been confronted well, directly, and with fully satisfactory results. Poland also faced hyperinflation. At the beginning of 1990 Poland's budget deficit was cut sharply; cheap credits from the central banks to industry were restrained; and the Western world lent money to Poland to help stabilize its currency—both directly, through a reserve fund, and indirectly, by helping the Polish government to pay some of its bills by using Western money rather than by printing its own money. The results—as expected, given similar economic results throughout the world during the twentieth century—were rapid and successful. Poland ended its black markets. And Poland ended its high inflation, which went from an annual rate of thousands of percent down to about 40 percent within a year after the start of the program. The inflation rate in Poland is now about 2 percent per month, or about 26 percent per year.

In Estonia, which also used the ruble but introduced its own currency and then applied the same basic precepts of ending the rapid printing of money, stabilizing the value of the currency, and closing the budget deficit, inflation has come down to about 1 percent per month. This demonstrates that it's not the underlying structure of the economy or the Communist legacy per se, but the identifiable financial conditions, that can be addressed. In order to address them, however, a country almost always needs strong internal actions and outside help. That combination, as I'll explain, has not come together as well as it might have, and hence we have a serious shortfall of results in Russia.

As I've noted, the other two deep and fundamental processes of institution building and structural adjustment must inevitably be addressed. The structural adjustment goes forth willy-nilly, because with the end of the military-industrial state, there comes the inevitable collapse of the military-industrial complex, out of anybody's control and out of anybody's policy ken. When you hear about the decline of production in Russia, the most dramatic reason for this is straightforward. In Russia, as in the rest of Eastern Europe, the economy is fundamentally lopsided in its emphasis on heavy industry, and there simply is no way to keep such industry alive without the full devotion of the resources of the state. And if Russia were to keep heavy industry alive, it would, unfortunately, be keeping alive an industry that would be producing output with virtually no human value.

This is most dramatically evident in the manufacture of steel. In 1988 the Soviet Union had a steel production of 160 million metric tons. That same year, the United States produced 90 million metric tons of steel. In terms of purchasing power, our economy was perhaps eight times as large as Russia's, yet the steel industry in Russia was almost twice as large as ours. The number of tons of steel per dollar of GNP was seventeen times larger in Russia than in the United States. And since the steel mills find it very hard to market their ingots on the sidewalk and have people carry them home to their living rooms, they inevitably face an extremely sharp decline in production as soon as the military state, with all of the force required to draw on such resources, is ended. That is why every country in the region—whether it's going through so-called shock therapy or gradual reform or no reform or simply chaos—has had an enormously sharp decline in industrial production. The decline is primarily related not to the reform but to the economic structure.

The counterpart of Russia's excess of heavy industry is its famous dearth of consumer goods and services. The Russians illustrate it with a story of a man who goes to the purchasing bureau with bushels of useless rubles to buy a car. An apparatchik counts the rubles and tells the man that he's got enough money for the car and that the car will be delivered ten years from that date. The man asks, "Will that be in the morning or the afternoon?" The apparatchik says, "It's ten years from today—what difference could it possibly make?'' And the man replies, ''Oh, no, no—the plumber is coming in the morning!''

The number of shops in Russia is remarkably low; one observes their lack of physical presence in any Russian city. In a survey undertaken by the International Monetary Fund in 1988, Russia had 20 retail outlets per 10,000 population, whereas the United States had an average of 60 retail outlets per 10,000 population; Italy, as you might guess, had 175 retail outlets per 10,000. As the old authoritarian state fails, and as resources are no longer pumped into the heavy industry, there inevitably begins a period of very sharp structural change, marked by the collapse of the old heavy industry and the extremely rapid growth of the so-called service sector—the realm of traders, wholesalers, and even bankers. There are two thousand banks—most of them very small, probably bankrupt, and corrupt—in the new financial system of the Russian state.

That process of decline of industry and rise of the service sector is fundamental and occurring everywhere in Eastern Europe, including Russia. Millions of people, whose incomes are unrecorded, are moving out of the industrial sphere and into new activities. If at the same time the financial system is controlled so that cheap credits do not simply go to pay the wages of workers in the now-defunct heavy industrial sphere, unemployment inevitably rises sharply. Those changes are the core of the structural adjustment process. To minimize pain and maximize the possibility of cushioning society and creating conditions for sustained development in the future, it's crucial to put that inevitable structural change in a context of institutional change as well. The combination of institutional work and financial control becomes the core of the reform process, to the extent that the reform cabinet can carry it forward.

The institutional change process consists of three steps. The first is to dismantle the impediments to market activity that are most pernicious in the short term, such as price controls, which prevent the legal exchange of goods, both domestically and internationally, and lead to massive corruption and the breakdown of economic activity.

The second step of institutional change is the construction of a system of private property, including both the construction of a legal system and the transfer of ownership of state assets to private hands. This is the one area in which Russia has indisputably made remarkable progress, by essentially giving the workers and managers title to the enterprises and "selling" the minority of shares in the open market in return for voucher tickets, which are a kind of Monopoly money. Through this method, Russia has already privatized about 7,000 medium and large enterprises, and overall about 80,000 enterprises, in a period of two years. This establishes at least the legal foundation for future private development. Already, cadres of young Russian investment bankers are discovering the joys of hostile takeovers, management buyouts, and every other kind of mischief that is an important adjunct to a private ownership system and a private capital market system.

The third step of the institutional change process is the development of a social safety net. This is a very complex problem. Contrary to the perception of some observers, Russia did not embark upon the transition without a social safety net. In fact, the socialist state had not just a social safety net but a social cocoon of such density that it contributed to the state's bankruptcy and therefore poses one of its greatest challenges. The step of developing a social safety net is not a matter of creating social protection; it's actually a matter of removing social protection from some parts of the population and redirecting it to the truly vulnerable. The social protection that now exists in Russia is both comprehensive and a fiction, because it cannot be afforded. So the reconstruction of the present system, rather than the construction of a new system, is the challenge. And as you know from our own debates on reform, whether it concerns health care or welfare or unemployment insurance, such challenges are tremendously difficult—not only because of their technical and social aspects but also because of vested interests.

The interests in Russia are vested universally, which makes it all the more complex. Facile comparisons to Chinese reform seem even more off the point if one looks at the social area. China, regardless of its reforms, is a society in which 80 percent of the population is completely without social protection. It is an agrarian society in which the vast hinterland is separated from the cities. There is no social protection for the 800 million Chinese peasants. Those of you who have gone there know that in a downtown city in China, you can see one of the most extraordinary sights on our planet: at three o'clock in the morning, rural laborers, who have come in to work for fifteen cents an hour, are erecting buildings by spotlight. The Chinese system produces growth—but do not, ladies and gentleman, believe that it is a social welfare system, or that it is a "soft" way of economic reform, as is sometimes said. China is an agrarian society attempting to develop industry for the first time. Russia is an industrial society with a hypertrophied social welfare system that is so completely bankrupt and untargeted as to be unworkable. And the construction of a targeted system is the profound challenge to be faced.

In Eastern Europe these challenges can be met, given a modicum of political and social stability. It is easy to overemphasize, however, the degree of consensus about the reforms, even in Eastern Europe. It is often said, for example, that reform in Poland can work because there's consensus in Poland, yet the closer one looks, the less consensus one finds, certainly on the tactics of reform. Therefore, the successful reforms, as they have been achieved, have not been those based primarily on consensus; rather, they have been those based on the legitimacy of a government that, to put it frankly, imposes strong reform measures on the population and then faces the consequences at the next poll. And in Poland the consequences for every government have been, "Let's try a new government." Each successive government finds that there is no room for maneuver, and so continues, thankfully, on the same reform path. But even though Poland is in fact on a workable path, nobody's too happy about it; the Poles are still looking for that miracle that is not going to be found.

Indeed, Poland is a country that has returned to economic growth. It was the fastest-growing country in all of Europe in 1993, after being the basket case of Europe in 1989. It has ended hyperinflation. The shortages in Poland now exist only in the realm of history, after being at the core of the society for forty years. The private sector now employs 60 percent of the population and produces about 55 percent of the GNP. There is one private firm for every ten workers in the labor force. Poland has undergone a social revolution of private ownership, private economic activity, and a resumption of growth, and is likely to attain full membership in the European community by the end of this century. In fact, it seems likely that Germany will propose just that during its presidency of the European Union.

Russia, obviously, has seen nothing of the kind of dramatic success that has been evident in Eastern Europe—success, of course, with high cost and high risk, but success nonetheless. In Russia the problem has been that from the start, in the area of institutional reform and, most important, in the area of financial stabilization, the results have been at most partial, halting, and subject to tremendous political reversal. And then, of course, the main reformers in the government were pushed out in a cabinet reshuffling in January of this year, after the December elections, in which the reform parties did very poorly and the post-Communist parties, both the agrarian and the general Communist blocs, did well, together with the extreme right-wing parties. It's too early to predict disaster, but thus far the reform process has unfortunately been quite painful and fraught with lost opportunities. The essence of financial stabilization is to move quickly and decisively. That, unfortunately, Russia did not do, and so it finds itself in a continuing perilous financial condition, even as other changes go forward. Life at the edge of hyperinflation continues, and continues to be the pernicious factor in the social life of the country.

I'll conclude by stressing that we contributed, at least, to Russia's missed opportunities of the past two years—even though it's fortunately not yet time to say that there is no chance for that country to achieve economic reform in the future. Maybe some of the lessons of the past two years will be applicable in the coming months. The key to stabilization is to move decisively. Inflation feeds upon itself. It undermines tax collections, it undermines budgeting, it invites flight from the currency, it undermines the holdings of real money balances, so governments have to print money ever more rapidly, simply to get the same real resources from their printing. History shows that in order to move decisively, it's almost always necessary to get a measure of international help—at least forbearance on debt servicing, to start—typically, balance-of-payment support in the form of the outside world helping the government to pay its bills through loans and grants rather than through money printing. Often, as in the case of Poland, or in the case of the Israeli stabilization of 1985, a fund is directly dedicated to supporting the international value of the currency.

None of these things was done in the case of Russia, despite much talk and posturing by this administration, by the G7 governments, and by the international institutions. During the past two years, Russia has received very little in actual grants—perhaps two billion dollars in total—from the entire Western world. We have given one-year loans and two-year loans, which are now being repaid, and we are calling that financial aid—even though the burdens on the budget are immediate and sometimes even more adverse than not having gotten the loans, because of the peculiar ways these loans have been delivered. The IMF has given assistance of a most bizarre and surrealistic sort by lending money with the instruction that it cannot be touched. It must be held in the bank as "reserves" if the government ever wants to get more (presumably for the same purpose of holding it in the bank)! This too is added to the bill of international assistance.

A pertinent illustration of how financial workouts should and shouldn't be done may be drawn from a comparison of the Russian financial workout with another famous workout—that of Macy's Department Store, which declared bankruptcy in January 1992, just as Gaidar did. On the day that Macy's filed for Chapter 11, all creditors were by law immediately estopped from any further attempts at debt collection. There was, in technical terms, a full standstill. Two weeks later, under Chapter 11 court supervision, Macy's borrowed $600 million through a so-called debtor-in-possession loan, which enabled Macy's to keep its showrooms filled with goods. Macy's is now leaving bankruptcy, having been allowed to operate normally during this period.

In the case of Russia, it took fourteen months to get a legal standstill on the official debt. To this moment, Russia has not yet signed an agreement with the commercial banks for a standstill. And it took Russia sixteen months to get a $600 million debtor-in-possession loan from the World Bank—the same size loan that Macy's was able to get in two weeks. That gives you an indication of the scale of real assistance that has been going to Russia in the past two years.

Now Russia's inflation is about 25 percent per month. The Duma (parliament) is overwhelmingly represented by conservative forces (which means Communist old guard) or by right-wing forces (the meaning of which is not yet clear). The government is heavily represented by the ministers of the late Gorbachev era—people who contributed to the financial collapse of the system the first time around.

If there is good news in this, I would point to two developments. First, and I think it may prove to be important, was the adoption of a constitution, which may channel at least some of the political conflict through legal and institutional means. Even when Aleksandr Rutskoi left prison last week, he spoke of challenging for the presidency under the constitution in 1996. The members of the new Duma speak about its constitutional prerogatives, and this may prove to be important as well. Another point of some hope is that the past two years have certainly not been all lost. There has been tremendous and positive structural change beneath the surface, together with great tumult, great burdens, and great pain. There are positive developments in private ownership (even in terms of legal structure) and in the extent of the commercialization of the society. And with respect to the financial crisis, which I contend is the most important and most urgent of all the crises facing Russia, the good news is that the current government is fearful of the crisis, and maybe fear is the beginning of understanding. We can only hope.