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## THE IMF'S \$22.6 BILLION FAILURE IN RUSSIA

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On August 17, just three days after President Boris Yeltsin unequivocally stated that the ruble would not be devalued, Russia's Prime Minister announced that the government would allow the ruble to be devalued by 34 percent by the end of this year. He also declared a 90-day foreign debt moratorium. It is now painfully clear that the \$22.6 billion bailout package orchestrated by the International Monetary Fund (IMF) has not rescued Russia.

Commenting on the Russian devaluation and debt moratorium on August 17, Michel Camdessus, the Fund's Managing Director, concluded that "Implementation of [Russia's economic] program has been satisfactory." Camdessus, however, never explains how something as disastrous as a currency devaluation of this scope can be deemed "satisfactory." Even he admits that, despite the IMF bailout, "confidence in financial markets has not been reestablished and as a result Russia has continued to lose reserves, and asset prices have fallen sharply." If this is "satisfactory," Camdessus must have a very high tolerance for failure.

What was the purpose of the July IMF bailout of Russia, and who is responsible for its failure?

### THE PURPOSE OF THE IMF BAILOUT

On July 20, the IMF Executive Board approved its portion (\$11.2 billion) of a \$22.6 billion international bailout. This emergency package was intended to help Russia maintain the value of the ruble while the government implemented reforms necessary to create long-term stability. IMF First

Deputy Managing Director Stanley Fischer outlined this strategy on July 13:

The underlying problem [in Russia] is the budget and the financing needs. So if you devalue, you sort of relieve the pressure on the markets for a while, causing difficulties, but unless you got the budget in shape, and the devaluation wasn't going to do anything for the budget, you would be back in this situation.

Indeed, the IMF plan specifically stated that "exchange rate policy should remain broadly unchanged during the remainder of 1998." After only four weeks, however, it is clear that the massive bailout failed in both of its missions: The ruble was devalued, and reforms are not likely to be implemented.

On August 17, Prime Minister Sergei Kiriyenko announced that the government would allow the ruble to fall from the former official rate of 6.3 to the U.S. dollar to 9.5 to the dollar. This devaluation and a 90-day foreign debt moratorium amount to

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an expensive policy debacle for Russia. The devaluation will make it much more expensive to repay foreign currency-denominated debt. The moratorium has frightened already leery investors and likely will dampen foreign investment for years to come.

The Russian Duma, moreover, is not likely to adopt the bulk of the IMF-sanctioned reform agenda. In fact, the Duma's communist majority already is urging the Russian government to backpedal on budgetary cuts, increase domestic spending instead of paying foreign debt, or nationalize the dollar-denominated debt of Russian banks.

### WHO IS RESPONSIBLE?

Both Russia and the IMF are responsible for the Russian debacle. Russia's fault lies in the government's chronic refusal to reform. The Russian government has been aware of the problems in its economy and what is needed to fix them for at least five years. Because of mismanagement, inertia, and outright corruption, such vital changes as trimming the budget, overhauling the tax code and tax collection, land reform, and otherwise providing conditions to stem capital flight and attract foreign investment have not been implemented.

The fault of the IMF lies in its willingness to provide successive bailouts regardless of whether they achieve the desired results. When asked at a July 13 press conference whether the IMF would refrain from new lending because of reduced liquidity, IMF Treasurer David Williams responded, "[W]e never say no."

Russia is a prime example of how this can lead to disastrous results. Since 1992 (and before the most recent \$22.6 billion bailout), the IMF lent Russia over \$18 billion. With each loan, the IMF required Russia to adopt economic reforms. Even though Moscow rarely fulfilled its promises, the IMF continued to disperse tranche after tranche. In other words, the cheap credits allowed Russia to delay reforms, while the IMF rewarded Moscow for not reforming.

This pattern is being repeated in the current bailout. Despite the devaluation of the ruble and the

Duma's refusal to pass the majority of IMF-mandated reforms, Michel Camdessus' August 17 statement merely remarked that

[Russia's] measures and their potential impact will immediately be analyzed by the staff and management of the IMF... I hope that the government's economic program will continue to be implemented in full, so that the economic and financial situation will improve and the IMF can be in a position to disburse the second tranche....

### CONCLUSION

Russia is now in an economic morass. The achievements of the Yeltsin administration—a stable currency and low inflation—have gone down the drain. The political cost to the Yeltsin government will be tremendous, as millions of workers and pensioners have not been paid for months and the price inflation will escalate. Before August 17, Russia had asked whether the international community were prepared to provide some additional financial support beyond the \$22.6 billion finalized on July 20. Thus far, the G-7 leading industrial countries have prudently declined.

Both the IMF and Russia share the blame for the country's current crisis. Despite ample advice on how to shore up its economy, Russia has refused to implement the changes necessary to resolve the current crisis and create long-term economic health. The IMF has consistently permitted Russia to borrow despite Russia's refusal to reform its economy.

Congress should send a message to Russia that the United States will no longer send good money after bad. It can do so by refusing to approve additional funding for the IMF. An organization that cannot say "no" should not be given additional money to waste.

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