PART 3

1998: A YEAR OF UPHEAVAL

9

"War on the Rails"

A government crisis in Russia in March–April 1998 was followed in May by a wave of social protest on an unprecedented scale. The decline in living standards (which began in 1990–91 and has continued to the present day), the constantly delayed payment of wages, and the growing threat of unemployment brought millions of industrial and office workers in Russia's many different economic regions to the point of extreme desperation. The "war on the rails"—that is, the blocking of rail lines by protesting workers—which broke out in the coal-mining regions of the country, proved to be a powerful and effective way of pressuring the government.

It was also a profoundly symbolic action. Back in 1991, when Boris Yeltsin was elected president of Russia, he made a promise —to "lay his head on the rails" if his government were ever to allow living standards in the country to fall. What we have seen "on the rails" has not been Yeltsin's head, but hungry miners, with their wives and children. And other working people, teachers and students, doctors and retired people, scientists and farmers, have been speaking out more and more loudly about their difficulties.

Many economists called the situation in Russia not so much a "crisis" as a "catastrophe." Even UN reports referred to Russia and Ukraine as "countries with ruined economies," like Iraq or Yugoslavia.

The miners' protests were a surprise not only to the authorities but to the leaders of the unions themselves. One of the new officials of the Russian government stated that a nationwide labor organization like Poland's Solidarnosc would be a good thing for Russia because, as things stood, it was necessary to negotiate separately with the workers at each mine.

CHUBAIS'S BLUFF

In early 1997 the progovernment press in Russia was full of optimistic predictions and upbeat pronouncements. "The economy is entering a period of growth and the situation is being normalized," wrote Sergei Pavlenko, director of the Russian government's Working Center on Economic Reforms. After a long illness Yeltsin returned to work. One of his first actions was to appoint three vice premiers and to place them in charge of Russia's economy. The three were Anatoly Chubais, Boris Nemtsov, and Oleg Sysuyev. Commentators spoke of a "second liberal revolution." Western experts referred to the threesome as a "dream team." Chubais declared, "We are convinced we will be able to realize the goals we first set for ourselves in 1991."

But there was no revolution. By draining the government budget, this "new" administration was able to reduce the backlog of unpaid wages a little. Inflation was held down to only 11 percent for 1997. For the first time in seven years, a rise in the GDP was announced, though it was only 0.4 percent; average per capita income increased by 0.8 percent; and the number of people below the poverty line was reduced by 0.7 percent. However, these improvements were barely noticeable in the daily lives of ordinary citizens.

On the other hand, the deeper, more fundamental economic processes showed no positive gains in 1997. Instead, they continued to evolve in a direction quite dangerous for Russia. Investments in actual production, which were already insignificant, declined by a further 6 percent. Unemployment rose 3 percent. Total profits for industrial enterprises fell by 15 percent, but losses increased by 140 percent.

Foreign debt went up by $5–6 billion, reaching a total of nearly $140 billion. The government's domestic debt rose even more quickly during 1997, increasing from 330 to 530 billion "denominated" rubles. When Russia's currency was "denominated" in 1997 the last three zeros were removed from all bank notes. Thus, one million (1,000,000) rubles became one thousand (1,000).

Vitaly Tretyakov, editor in chief of *Nezavisimaya Gazeta*, wrote:

> I consider 1997 the greatest year in modern Russian history. It was great in that during this year all the internal, material, and intellectual reserves of the present regime were exhausted completely. Yes, it is true that not a single question was given a constructive answer. Yes, as before, Russia may fall apart. Yes, the economy is in a state of stable stagnation and the government is completely bankrupt. But 1997 was good in that now, by all indications, the authorities, the ruling elites, have themselves become aware of this.
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> (*Nezavisimaya Gazeta*, December 31, 1997)

In fact, neither the government authorities nor the "ruling elites" understood anything. An article by an adviser to Chubais, the economist Andrei Illarionov (*Izvestia*, December 30, 1997), contained the following assertions: Yeltsin has enjoyed "successes of a kind that have not existed in all the years of his presidency"; 1997 was "the best year of the past decade"; "the results of the government's activities during the year just expired" had been "magnificent" and there were "brilliant possibilities" ahead.

An article by the economist Mikhail Delyagin, an adviser to Vice Premier Boris Nemtsov, declared that "Russia has overcome its downward slide and is gathering its strength for the upward pull. Our country is heading uphill, and not toward Golgotha." Aleksandr Frolov, a doctor of political science, wrote: "Exerting all their strength and exhausting themselves in the struggle for survival, overcoming fear and despair, the people of Russia have literally carried our country on their backs out of the abyss of economic crisis" (*Novoye Vremya*, 1998, no. 1, pp. 14, 15).

Chubais outdid all the others in professions of optimism:

> In our country the decline of production has ended and a turnaround has begun, which can be seen quite well by people who

> analyze seriously. It seems to me that nothing can stop Russia from a long, steep, powerful upward trajectory of growth, constantly gaining in strength. This will be evident not only to specialists in economics and statistics but will also be felt within the family of every Russian breadwinner: from his wages, from his income, from his ability to buy a new car and go on a full-fledged summer vacation
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> (*Argumenty i Fakty*, 1997, no. 47. p. 3)

All these assertions turned out to be nothing but bluff.

TWO STEPS BACK

In January 1998 the cautious and concerned predictions of more objective observers were drowned out by the chorus of optimistic official commentary. Even a confidential World Bank report predicted that the Russian economy would have a 6 percent growth rate in 1998 because 70 percent of GDP was being produced by private firms. The Organization for Economic Cooperation and Development foresaw a growth rate for Russia of 3 percent in 1998 and 5 percent in 1999. Russia's Central Bank promised a growth rate of 1–2 percent, with investment increasing by 6–7 percent and inflation dropping to 5–8 percent for the year.

The first months of 1998, however, gave Russians nothing to cheer about. Capital investment in the economy shrank by 7.1 percent compared to the early months of 1997. Industrial production was 0.3 percent less than in the first quarter of 1997. The consumer price index rose 3.1 percent, and real income declined by 6.8 percent. The total indebtedness of industry, construction, agriculture, and transport reached the level of 1.5 trillion denominated rubles. (These figures were reported by the government's Economic Conjuncture Center and other institutions engaged in economic analysis.)

Budget revenue was reduced, and once again the government could not promptly meet its obligations for the payment of wages and pensions to millions of Russian citizens. Wage payments were widely delayed in the private sector as well. The government of Chernomyrdin and Chubais had exerted itself greatly to try to integrate Russia into the world economic and financial system, and as a result not only had Russia been formally recognized as a country with a market economy but also Russia's president was included on a nominally equal basis at a summit of leaders of the most developed countries (the so-called Group of Eight). Integration into the global system, however, also resulted in some heavy blows to the weakened Russian economy.

While capitalism today has little resemblance to what it was a century ago, the inner nature of "post-industrial" capitalism has not changed fundamentally. Such features as competition and the anarchy of production, the constant striving for the maximization of profits, periodic crises of overproduction(with accompanying financial crashes and massive unemployment) have all persisted, although in different form.

Sometimes these economic and financial crises affect the entire world. The first signs of a new global crisis appeared in Asia during 1997. A chain of seemingly unrelated events in Thailand, Malaysia, Indonesia, the Philippines, and South Korea culminated in financial upheavals and stock-market disasters in September–October 1997. For a decade or more these countries had demonstrated steady and rapid economic growth, earning them the nickname "the Asian Tigers." Western investment in the region was nearly $100 billion per year.

But in the fall of 1997, the Hong Kong and Japanese stock markets were hit by the biggest drop in prices in recent years. Stock exchanges all over the world, not just in Singapore or New Zealand, but also New York, were affected.

In December 1997 it also became evident that there was a worldwide glut of oil and of some other raw materials, a crisis of overproduction. The price for a barrel of oil had fallen since the late 1970s, when it stood at $40, to around $17–20 in the period 1991–1997. But in January 1998 the price per barrel fell to $11. And in some cases, only $8–10 was being paid.

For Western industrial countries, lower oil prices made up in part for losses as a result of the downturn in Asia. But the big losses experienced by the oil-producing countries were bound to be reflected in the state of the world economy. Western consumers, out of caution if nothing else, began to buy less, especially in the case of luxury goods. A number of jewelry firms and tourist agencies experienced difficulties, including some bankruptcies. Reduced commodity circulation led to greater unemployment, especially in Germany and France.

Russian officials reassured the public that the Asian crisis would not become a threat to Russia. Deputy Finance Minister Kudrin declared that the crises in the financial markets were "no cause for concern." Russia's Central Bank promised to maintain stability on the Russian securities market.

Again, Chubais outdid all others in his professions of optimism. He asserted that Russia could win, rather than lose, from the Asian crisis "because Russia today is the most attractive of the emerging markets. It is entirely possible that we will again create a situation in which Russia, in comparison to other developing markets, will prove to be the most stable and profitable" (*Obzor Mezhdunarodnoi i Rossiyskoi Informatsii. Yezhenedelny Byulleten* [Review of International and Russian Information: Weekly Bulletin], 1997, no. 48, p. 17).

Several experts predicted heightened interest in Russian securities among foreign investors, but these expectations proved unfounded. In late October 1997 prices on Russian stock markets began to fall. In November and December foreign investors, to whom Russia's capital market had been opened hastily and without any restrictions, began to withdraw their funds just as hastily. At first they turned to the more profitable and reliable Russian market in short-term government bonds, but many soon pulled out of Russia altogether.

The Central Bank, in order to avoid devaluation of the ruble so soon after its "denomination," was forced to make substantial outlays from its foreign currency and gold reserves, which fell from $25 billion in the early fall of 1997 to $18 billion in January 1998. Russia's central savings bank also suffered substantial losses.

Falling world market prices for raw materials also had a painful effect on the Russian economy. In the years 1995–97 Russia exported 100–110 million tons of oil annually, earning substantial profits, with 40–50 percent of those profits in the form of hard currency. "For now, oil and gas are feeding Russia," wrote *Novoye Vremya* in July 1997.

This was nothing new. Petrodollars had also nourished the Brezhnev regime, and to many politicians this cash flow seemed inexhaustible. But everything changed quickly and, it seems, will remain changed for a long time to come. In Russia the prime cost, or production cost, of oil is not just $2–$3 per barrel, as in the Persian Gulf countries, but $13–$14. Oil exports were suddenly bringing not profit but loss.

Russia cannot abruptly curtail its production and export of oil, for that would leave hundreds of thousands of people in its northern and eastern regions without jobs. For such "oil cities" as Surgut, Noyabrsk, and Nefteyugansk, the social consequences of stopping production would be worse than the already serious crisis in the more habitable coal-mining regions.

There is another reason why Russia cannot stop producing and selling oil, even though at a loss. It would be unwise to risk losing the traditional customers that Russia supplies. Almost all the energy needs of the Baltic region are met by exports from Russia; for Ukraine, the figure is 80 percent; for Eastern Europe, 50 percent; for Germany, 15–20 percent. Besides, with oil production you can't just close a valve on a pipeline and wait for better times, as you can with natural gas.

Thus it was necessary to start planning for ongoing losses from oil sales. From January through March 1998, because of the fall in world oil prices, the Russian treasury lost $1.5 billion, according to the State Duma's budget committee. Thus, the many hopes for a quick upward flight of the Russian economy had been dashed as early as the first quarter of 1998. All attention was now focused on trying to maintain economic and social stability against the threat of a new wave of difficulties.

THE FALL OF CHERNOMYRDIN

The new problems in the economy, already troubling the top politicians and government officials, aroused the dissatisfaction of Russia's business elite, those who are called "the oligarchs." The orientation toward the raw materials sector, which had been the basis of economic policy for many years, now proved to have been mistaken. Huge parcels of state property, now in the hands of a few private owners, had stopped bringing in the earnings they had previously brought. With the ruble more stabilized, commercial banks were making less profit from currency speculation in general and from operations involving foreign currency in particular. Disputes among the various oligarchical groups, or "clans," intensified. The question of governmental continuity troubled everyone. Only two years remained until the next presidential elections, and only a year and a half until the elections for a new Duma.

During January and February 1998 Yeltsin seemed little concerned with the new problems that had arisen. He postponed several times his administration's report to the Duma, and when the report was finally given, he walked out of the proceedings at the end of the first hour. In early March he came down with a cold. To his entourage the president's new illness seemed more of a problem than the deepening ills of the Russian economy.

At the same time Chernomyrdin began to display signs of unaccustomed independence. In previous years the premier had hardly ever interfered in the activities of the vice premiers, allowing them to decide matters in direct consultation with the president. It was this passivity that enabled Chernomyrdin to observe the fifth anniversary of his premiership in December 1997, while Yeltsin might well have ousted a more combative individual long before. The average stay in office for *vice* premiers had been no more than one year.

In early 1998, however, Chernomyrdin began issuing statements that the press viewed as rather "daring." He also reorganized the duties of the three vice premiers, reducing the powers of Chubais, Nemtsov, and Sysuyev while increasing his own. When talks were held in the United States within the framework of the Gore-Chernomyrdin Commission the Russian premier conducted himself as though he expected in the near future to be the president of his country. Within the "party of power" and among "the oligarchs" there were many who had linked their fortunes with a Chernomyrdin victory in the elections scheduled for 2000.

Several Russian newspapers ran special features on Chernomyrdin as the candidate of the party in power. In one interview in mid-March Chernomyrdin not only acknowledged a qualitative rise in his authority in the government but actually declared that the political situation in Russia, as he saw it, had reached an adequate level of stability and would probably not change essentially before the elections (*Mir. Ekonomika i Politika* [The World: Economics and Politics], 1998, no. 10, p. 23). People got the hint.

In the first weeks of March 1998, Chubais was active in the public eye to an unprecedented extent, observing with much fanfare the first anniversary of his appointment as vice premier. Many observers agreed that, as one publication stated, this was a "precise and reliable indication that the political process has passed through a period of great strain and has returned to normal, stable channels and will flow smoothly without whirlpools or blockages into the straight-line phase of the election campaign" (*Politicheskaya Nedelya v Rossii. Informatsionno-Analitichesky Monitoring* [The Political Week in Russia: Informational-Analytical Monitoring], March 11–18, 1998, p. 12).

In mid-March, Georgy Kleiner, a doctor of economic sciences, wrote: "The political situation in Russia has taken on new features of predictability, and international politics in relation to Russia have lost their menacing character" (*Nezavisimaya Gazeta*, March 31, 1998). Only a few days after these observations were written Yeltsin showed how little the assessments of such learned experts were worth.

On Monday, March 23, having recovered from his illness and returned to work at his office in the Kremlin, Yeltsin made an early morning announcement that Chernomyrdin, Chubais, and the interior minister, Anatoly Kulikov, were being retired. Under Russian law this meant the resignation of the entire cabinet. Yeltsin gave no reason for this sudden decision. Not until later did he make explanations of some sort. Two months afterward he said he had retired Chernomyrdin "not because he was a poor prime minister or had made any mistakes. It's just that times had changed, and after five, six, seven years society had begun to get tired of this particular leader . . . . It was necessary to seize the time, release him from his duties, and make a change" (*Rossiyskiye Vesti*, May 27, 1998).

Yeltsin's action was a complete surprise to Chernomyrdin, especially because under a new law such action required a statement by the prime minister himself. It was as much a surprise to Chubais, who was getting ready to act as Russia's representative to a meeting of the International Monetary Fund in New York. Kulikov refused to comment about being retired. Of the generals heading the "power ministries" he was considered the one most devoted to Yeltsin.

At noon on March 23 Yeltsin announced that a previously little-known official, Sergei Kiriyenko, would become acting prime minister. It had been only a few months, since November 1997, that this 35-year-old businessman from Nizhny Novgorod had occupied the post of minister for fuel and energy, and he had not distinguished himself in any way.

Hardly anyone could explain or even comment intelligently on Yeltsin's action. A few journalists and "expert commentators" who are generally considered to be in the pay of Yeltsin's administrative apparatus tried to portray this sudden move as part of a carefully considered plan of action, intended to speed up the pace of reform. Most observers, however, agreed that Yeltsin's action was not thought out, but was an emotional decision guided by a single desire and a single aim—to show everyone in Russia and beyond its borders "who was really the boss."

The government crisis continued for more than a month and did considerable damage not only to the participants in this artificially provoked conflict but also to Russia as a whole. Uncertainty in regard to the government probably resulted in several billion dollars worth of harm to the economy. The "party of power" obviously suffered from the crisis, for no major political figures remained in it besides Yeltsin. As *Nezavisimaya Gazeta* observed on March 24, "with a single blow Boris Yeltsin has removed three of the most powerful political figures from the game."

NO WINNERS

For more than a month economists and political experts wrote about the negative consequences of the sudden change of government. The new cabinet, which was finally formed in mid-May, came out of the crisis greatly weakened, although more than half of the cabinet ministers retained the positions they had held in the previous government. Several promising younger politicians refused to enter the new administration, which looked transient and unstable to them. "I don't want to find a paper grave for myself in the White House," said Vladimir Ryzhkov, vice speaker of the Duma, in reply to a proposal that he take a position in the new cabinet.

Two provincial governors, Konstantin Titov and Mikhail Prusak, were even more emphatic in declining positions as cabinet ministers or vice premiers. Top-ranking officials in several different ministries chose this moment to leave the Russian White House rather hurriedly to take jobs in private business. They didn't wish to wait for further "reductions in staff."

No one knew much about the new vice premier, Sergei Khristenko, or such new cabinet ministers as Sergei Generalov, Ilya Yuzhanov, Sergei Frank, Viktor Semyonov, and Pavel Krashennikov. Some described the new government as one of "professionals with a pragmatic orientation"; others spoke of the "revolution of unknown middle-level managers."

In Russia today a government minister needs not just professional expertise but also political and practical experience. This was shown by the events of mid-May when the negotiations with protesting miners in the Kuzbass and Shakhty regions were headed by the "retired" leaders Nemtsov and Sysuyev, who were well known in those troubled regions, having held important political positions there in earlier times.

Within a few weeks Sergei Kiriyenko had become well known, but he had not gained respect. His complete dependence on President Yeltsin was obvious to all, and he himself did not try to hide it. His inexperience and lack of preparation for the high responsibilities of the premier's job were flagrantly obvious.

Where, after all, could he have gained the kind of experience needed for his new job? He had graduated in 1984 from the Gorky Institute of Water Transport Engineering and had worked for a short time as a foreman at the Krasnoye Sormovo shipyard in the city of Gorky (which has retaken its pre-Soviet name of Nizhny Novgorod). At the Gorky Institute, he had been active in the Communist Party and the Komsomol (the Communist Youth organization), and at the shipyard he was elected Komsomol organizer, first for his shop and then for the workplace as a whole. Soon after that we find him as a member of the Central Committee of the nationwide Komsomol organization and first secretary of the Nizhny Novgorod regional committee of the Komsomol.

It was through the "Komsomol economy" that Kiriyenko entered the oil business and joined the board of directors of the Garantiya commercial bank. Boris Nemtsov, whose career had also begun in Nizhny Novgorod, invited the young "banker" Kiriyenko to go to work for the government at the Russian White House.

Such was Kiriyenko's entire biography in a nutshell. An analytical memorandum distributed to government offices and the press in mid-May had this to say about him: "He is ambitious, arrogant, and capricious. Not stupid, but superficial in his opinions and actions. He knows how to avoid responsibility by moving to a new position at the right time. He will take on any job at all, even if he doesn't understand a thing about it. He will consult endlessly with everyone, especially those of equal rank or in positions above him, which allows him to place the blame on them if things go wrong." The people of Russia soon had ample opportunity to judge the accuracy of this characterization.

The change of government meant an especially heavy political and moral loss for Chernomyrdin. In front of the TV cameras on March

23 he was unable to hide that he felt both dismayed and offended. Booted out of his lofty position by a swift kick from the president, Chernomyrdin within two weeks was accepting a medal "For Services to the Fatherland" from that same president. Instead of a triumphal celebration of his sixtieth birthday, he received this honor on the occasion of his retirement from office.

Soon after that Chernomyrdin announced quite loudly that he would be running for president in 2000. But his ratings as a potential presidential candidate were quite low in January and February 1998, and they did not rise any higher in May and June. His status as an influential politician fell very quickly: in a May 1998 listing of Russia's top political figures, instead of his usual position as third or fourth, the place he held was No. 34 (as reported by *Nezavisimaya Gazeta*, June 2, 1998).

Chernomyrdin's political party, Our Home Is Russia (which uses the initials NDR, for Nash Dom—Rossiya), held a "renewal congress" at the end of April, endorsing Chernomyrdin as its candidate for the presidential elections in 2000. But this party had been built as the "party of power" under his protective wing while he was premier and with Yeltsin's support. After Chernomyrdin's ouster, this party's prospects were not at all clear. Instead of a "renewal," there was an intensification of internal conflict and intrigue within the party's top leadership. The NDR sought in vain to obtain some important posts in the new cabinet formed after March 1998. Its regional structures were weak, and in all local elections during the preceding year it had gone down to defeat. "Regionally we are still being taken into account only because of inertia," one of the party's analysts commented. "Regional governors have not yet gotten used to the fact that Chernomyrdin is no longer premier. He no longer has much influence on the economy. . . . Our movement may not survive up to the 1999 Duma elections" (*Itogi*, May 5, 1998, p. 21).

Chernomyrdin did not have many possibilities for strengthening his political movement, or for financing and organizing an election campaign. He has a strong personality, but at the same time he is passive; he does not typically express emotions vividly. He was always more of a businessman than a politician and kept his distance from the play of political passions. It is difficult for a person like him to perform in public. Even his indirect way of speaking, which the Russian press has often joked about, becomes a hindrance for him, because the ability to speak effectively and to sway an audience is one of the main qualities required of a public political figure today.

It was difficult for Chernomyrdin to seek sympathy as a leader who had been mistreated and wrongly cast aside. He bore a large share of the responsibility for all the difficulties Russians have experienced in recent years, and outside of his native Orenburg province he was not likely to win much support from impoverished voters. Although he was no longer leader of "the party of power," he could hardly join the ranks of the opposition. The ex-premier defined his position in relation to the government as one of "critical solidarity."

His slogan was, "I am running for president in order to be No. 1 in the government." But what does the voter gain by that? In what way would the "new" Chernomyrdin differ from the premier of yesterday? Chernomyrdin and the NDR were likely to suffer the same fate as Gaidar and his party with their very poor showing in the polls.

The government crisis also dealt a substantial blow to the authority of the Duma and the left-wing parties who held a majority in it. Twice the Duma rejected Kiriyenko as a candidate for premier, but in the end it approved his nomination. If it had voted a third time to reject Kiriyenko's candidacy, the lower house of the Duma would have been dissolved and new elections held. Most deputies feared the possibility of losing their relatively privileged positions as Duma members in the event of new elections, and therefore voted for Kiriyenko the third time around. Many deputies joked, "Better to have a degraded Duma, than a dissolved one."

The supposedly oppositional character of the left-wing parties, in particular the Communist Party of the Russian Federation (CPRF), turned out to be quite toothless. The "oppositional" Duma deputies apparently hoped that by retaining their relatively comfortable positions as incumbents, they would have an advantage in the 1999 Duma elections.

Another group that gained nothing from the government crisis was the one usually referred to as "the oligarchs." The feuding among them rose while profits fell. Many banks, including some of the largest, found themselves in straitened circumstances. One, which goes by the name Tokobank, had enjoyed great confidence among Western investors and held ninth place among Russian banks in amount of capital owned. But during the government crisis, it was placed under temporary receivership and a new management was brought in from the outside. The credit ratings of other Russian banks were lowered. Some banks, fearing a loss of clientele, raised their interest rates on deposits. But the cost of credit also went up. The "oligarchs" were feeling the need for stability, for government regulation, for the game to be played by fixed rules. The Kiriyenko government, however, was too new and weak to be of much help in solving these problems. Russia's banking and financial crisis continued.

It was Boris Yeltsin who lost the most in the first half of 1998. In December 1992, as we recall, Yeltsin had accepted Chernomyrdin as premier in place of his first choice, Gaidar. Yeltsin came to appreciate the advantages of this compromise. For years he was able to distance himself from the not very successful activities of the government. By retaining Chernomyrdin as premier while changing vice premiers and ministers as he pleased, Yeltsin could let the premier take much of the blame for failed policies.

As for Chernomyrdin, he had agreed, perhaps not fully consciously, to play along with this game. He did not make the main decisions, but took upon himself, at least in part, responsibility for all the disastrous "reforms" of recent years.

Now the situation had changed. Yeltsin could no longer so easily distance himself from the actions of the cabinet. To be sure, Yeltsin requested that Kiriyenko resolve virtually all problems of government, including the appointment of personnel, without submitting his decisions to the executive branch for approval. In 1995 many cabinet decisions and decrees had been endorsed or authorized by the president's administrative apparatus. In 1996, when Chubais joined the presidential apparatus, all documents from the cabinet began to be submitted to him as the head of the president's staff. The head of the presidential apparatus acquired powers and responsibilities that were almost equal to those of the premier. Later this procedure was eliminated by a special decree of the president—except in the case of documents concerning national security and defense. "Let the cabinet answer for its own actions," said Yeltsin. "Let Kiriyenko make the decisions."

The cabinet, however, did not have political authority commensurate with its powers and responsibilities. At the end of May 1998, public confidence in the Kiriyenko-led cabinet was only about 10 percent. On the other hand, in December 1997 confidence in the Chernomyrdin cabinet had been only 9 percent (*Argumenty i Fakty*, 1998, no. 23, p. 6).

During May and June 1998 Yeltsin felt obliged several times to place his own authority on the line in support of decisions made by Kiriyenko. The new premier could not assume all responsibility for the situation in the country, nor was he inclined to do so.

Yeltsin's relations with "the oligarchs" deteriorated significantly. Vladimir Gusinsky, head of the influential MOST Bank and the information conglomerate Media-MOST, stated bluntly that Yeltsin could no longer count on support from the newspapers and television companies belonging to his conglomerate. The most complete coverage about the coal miners' protests was provided to Russia's viewing audience by the NTV channel, which placed the strikers' political demands in the forefront. Every evening Russians heard and saw the striking miners demanding Yeltsin's resignation. Some officials accused the television companies not just of giving excessive coverage to the "war on the rails" but of actually *organizing* it.

During April, many observers commented with good reason that Yeltsin himself had become a chief source of instability in Russia. For example, the political scientist Pavel Tsepura wrote at the end of April:

> On March 23, Yeltsin killed the party of power. Without stopping to consider, he thus lost a considerable part of his electorate. Even wealthy people, who own something in Russia and have something to lose here, are less and less inclined to link their future with our homeland, and still less with Yeltsin and his present team. . . . Yeltsin's "revolution" of March 23 destroyed the objective prerequisites for the establishment of some sort of national harmony or concord. Virtually the entire population has ceased to believe in the reliability or stability of the political regime established by Yeltsin. Fear of the president's unpredictability, his dependence on opinions inside his own family, has spread since March 23 to all regions and all strata of our society. . . . It is beside the point now to say that no one believes in the president's ability to make adequate decisions and be guided by the national interest. He has swept from the political scene a group of political figures who could have ensured the stability of the political system and the democratic continuity of power through the presidential elections of the year 2000.
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> (*NG-Stsenarii*, April 1998, no. 4, p. 1.)

Many people in Russia and the West were wondering who would be able to maintain government authority in the event of mass disturbances. As Yeltsin had lost the remnants of his former government team, without having acquired a new one, only a few people could still be regarded as team members. Among them were Valentin Yumashev, a former journalist; Sergei Yastrzhembsky, a former Interior Ministry official; and Yeltsin's own daughter, Tatyana Dyachenko, a specialist in computer mathematics. None of these people had experience in administering governmental and economic structures. True, a more experienced figure, Sergei Stepashin, had returned to the government. And then there was Sergei Kiriyenko, who could also be counted as part of the team, although not a very valuable addition.

Criticism of Yeltsin rose sharply in both volume and intensity in almost all the mass media during April and May 1998. Even Yeltsin's former press secretary, Vyacheslav Kostikov, published a major article in the popular weekly *Moskovskiye Novosti* ("Moscow News," 1998, no. 23, p. 6), in which he called his former boss a "buffoon."

GROWING THREAT OF CHAOS

Several groups of economists and political scientists, including a group at Gaidar's Institute of Economic Problems, drafted a program for Kiriyenko of renewed economic reforms, which he then presented to the Duma. There is no point in analyzing this program, because the heated events of May quickly rendered it obsolete. The Russian White House at the end of May resembled a major fire department that had to hastily deal with the outbreak of more and more new blazes. Dangerous political and economic complications kept arising and had to be overcome. Besides the coal miners' protests, there were disasters in the northern regions of the country and armed clashes in Dagestan and Abkhazia and on the border between Dagestan and Chechnya. The downfall of the Suharto regime in Indonesia indicated the kind of social upheavals that could result from the spreading "Asian crisis." All these events increased the uneasiness of Western investors and hastened their flight from Russian financial markets and the Russian economy.

More doubts about the stability of the Yeltsin regime arose after the victory of Gen. Aleksandr Lebed in elections for governor of the

Krasnoyarsk region in east-central Siberia, an event which drew favorable commentary in much of the Russian and Western press. I personally was confident that Lebed would win and considered his victory preferable. But I did not expect the incumbent governor, V. Zubov, to be so soundly defeated, especially when Zubov had been endorsed by many prominent political figures, such as the mayor of Moscow, Yuri Luzhkov; the journalist Alla Pugachova; the head of the Communist Party of the Russian Federation (CPRF), Gennady Zyuganov; and the speaker of the lower house of the Duma, Gennady Seleznyov. In spite of these endorsements, Lebed was able to rally behind his banner the entire protest vote in the Krasnoyarsk region, including those who had voted for the CPRF in the first round. Lebed's political opponents in Moscow, it seems, had been too preoccupied with their own governmental crisis.

Lebed's victory resounded throughout Russia and further weakened the standing of the CPRF, which had claimed to be the chief oppositional force. Lebed's overall political influence increased substantially. He was again ranked among the ten most influential politicians in Russia, and his chances as a candidate in the 2000 presidential elections were much higher. In all opinion polls on this question in early June 1998, Lebed's ratings put him right up next to Zyuganov and were twice as high as Yuri Luzhkov's.

Nervousness in Russia's financial markets persisted throughout May. Hundreds of Western investors withdrew from the Russian market during that month, and experts estimated the losses to the market at $12–15 billion. Not everyone mourned the loss of foreign-currency speculators and other sharp operators of dubious merit who had already made a lot of money out of Russia's economic woes. There were signs, however, that large amounts of native capital, including profits from the shadow economy, were flowing out of the country at a significantly higher rate. For example, at the end of May Vladimir Gusinsky, who we mentioned above as owner of the Media-MOST conglomerate, bought a 25 percent share in the second largest newspaper . . . in Israel! Gusinsky offered $85 million for this purchase, twice as much as anyone else bidding for shares in the newspaper *Ma'ariv*. This kind of money could have helped a dozen different operations run more successfully in the depressed coal-mining regions of Russia. Gusinsky's business deal was indicative. It showed not only that there were large amounts of capital in Russia, but also that the owners considered it unwise to invest in the unstable domestic economy.

So great was the economic instability that when the state-owned oil company Rosneft was put up for auction in May, no bidders came forward. Preparations for this auction had been under way for eight months, and the government had hoped to add no less than $2 billion to the budget, with its looming deficit of as much as $12 billion.

PANIC ON THE MOSCOW STOCK EXCHANGE

News of the difficulties at Tokobank, the failure to auction off Rosneft, and a variety of alarming predictions and rumors led to a fall in prices on the Moscow stock exchange on May 27 that turned into a panic. The *Washington Post* reported on May 28: "What happened was reminiscent of Wall Street in 1929, but this time the crash was on the Moscow stock exchange. During the day prices fell another 11 percent, which meant they had lost half their value since the beginning of the year. Russia's inability to restore order in its economy has forced foreign investors to take their money and head for the exit . . . Nervous investors are fleeing the Russian securities markets partly out of fear of an Asian-type crisis and partly out of fear of investing in Russia's capitalist jungle, where lawlessness reigns."

It was impossible without big losses to get out of the situation that had developed in Russia's financial markets. The only question was, Who would have to pay for those losses? Many economists were proposing a 15–20 percent devaluation of the ruble. This would ease the situation for the main Russian banks, for exporters of oil and other raw materials, and for foreign investors. It would also help the government by artificially reducing the value of its domestic debt. But it would be a hard blow to the population as a whole. Inflation would inevitably take a new upward leap that would be hard to stop at just 15–20 percent. Moreover, the value of people's savings would again be slashed. Devaluation would render pointless the whole fiscal policy of Russia's Central Bank during the preceding year, including denomination of the ruble. Also among the sufferers would be importers, as well as Russian businessmen who depended on Western technology and equipment for the conduct of their business inside Russia.

Most of the press in Moscow was calling for a "soft devaluation." The advantages of this move, as presented in the press, did not seem convincing to the nonspecialist. *Nezavisimaya Gazeta*, May 27, 1998, for example, urged Kiriyenko to move ahead with devaluation even though its consequences might be comparable to those of the "shock therapy" of 1991–92. Among specialists, Yegor Gaidar, Russia's chief expert in "shock therapy," rejected the idea. "Only semi-literates could imagine our having a 'controlled devaluation,' that today the exchange rate could be 6.2 rubles to the dollar and tomorrow, 7.3. In fact, tomorrow the rate would be 25 rubles to the dollar. That is, there would be an uncontrollable fall in the value of the ruble, exhaustion of all the Central Bank's reserves, a very harsh blow to the whole banking system, and general panic" (*Moskovskiye Novosti*, 1998, no. 21, p. 3).

Newspaper commentators favoring a "controlled devaluation" of the ruble as a solution to the crisis angrily declared that Yeltsin was the only one preventing this operation from being carried out. And sure enough, the man whose surprise action of March 23 really provoked the crisis of spring 1998 made no attempt to bring it under control. Perhaps for the first time since 1992 Yeltsin was refusing to go further down the road of "shock therapy."

Even Western observers took an understanding attitude. A CBS correspondent reported from Moscow that for Yeltsin "the worst nightmare would be the collapse of Russia's ruble. That would send the Russian economy, which has barely been staying afloat, plunging to the bottom and bring on the danger of political chaos. The Kremlin had a whiff of what that would be like last week when thousands of miners who hadn't been paid blocked rail lines as a sign of protest. The government succeeded in turning them back, but just imagine what they would be capable of if it suddenly became clear that the miserably few rubles they did have were worth nothing." (This report was printed in the Moscow publication *Mir. Ekonomika i Politika* [The World: Economics and Politics], 1998, no. 21, p. 5.)

With Yeltsin's support the Russian government and Central Bank made the decision to raise interest rates on short-term government refinancing bonds up to 150 percent annually! This decision, which was rather incomprehensible to the man in the street, succeeded in stopping the panic on the Moscow stock market. With such high rates, however, the banking system was unable to conduct even ordinary credit transactions let alone engage in large-scale speculative operations.

Everyone began holding onto money whose value had so greatly increased, and the market froze at the low level it had fallen to. By May 28 and 29 it was obvious that the ruble had survived only for the time being.

At the same time a decision was made to introduce harsher tax policies—with the rich generally being favored over the poor once again, except for some taxes that were imposed on highly profitable banking operations and on gambling. These measures were condemned by newspapers of the most varied orientation, from the strongly pro-market *Kommersant* and *Moskovsky Komsomolets* to the formerly Communist *Pravda-Pyat*. "The Bleeding Has Been Stopped—All the Patient's Blood Has Been Drained," declared a headline in *Moskovsky Komsomolets*. And *Nezavisimaya Gazeta* proclaimed, "The Hunt for Speculators Is a Witch Hunt."

The population remained calm despite the outcry in the press, because for the time being prices of everyday consumer goods remained the same. There was a sharp increase in the demand for gold, the free sale of which had been legalized in Russia only two years earlier. The purchase of foreign currency also rose markedly at the end of May and in early June.

A LULL

The first week of June in Russia passed more calmly than the last weeks of May. The crisis, while not overcome, had been brought within acceptable limits. It was generally understood, though, that changed tax policies and financial regulation by themselves would not overcome the crisis. In order to surmount it, the real, underlying causes had to be understood. All economists and politicians of a left persuasion were agreed that the crisis was one of the political system itself and that only a change of social and economic policies could overcome it.

Kiriyenko, who in late May and early June had been showered with praise by President Yeltsin and the Western press, declared that the crisis had been artificially provoked by a group of financial speculators and sharp operators. Such figures were known to exist, although no one named them by name. Deputy Finance Minister Oleg Vyugin said that four major foreign players on the Russian stock market were specifically to blame. They were supported, he said, by some Russian commercial banks that had accumulated a lot of foreign currency and wanted to sell it at a higher price. They wanted to "push through" a devaluation, from which they could profit handsomely (*Argumenty i Fakty*, 1998, no. 3, p. 7).

The events of May 1998 showed rather clearly that there are predatory operators who have played and will continue to play a ruthless game against the Russian ruble and against Russia's economy, whose growth and development is not to their advantage. This is no new discovery, for predators live not only in the forests but also in the jungle of the market economy, wherever it may be. The weak and the unhealthy are their usual prey. The real question, however, is this: Why is Russia now so weak economically, and who made it that way?

Big-time speculators themselves rarely panic. When others panic, selling off their stocks and bonds at low prices, the speculators clean up. The new director of Russia's tax collection agency was Boris Fyodorov. He had taken quite a lenient attitude toward the speculators. "How can you blame people who are playing the market for wanting to save their endangered money?" (*Izvestia*, May 29, 1998). It is true that the stock market is a form of gambling, and no one wants to lose. But the game should be played according to rules, and cheaters should be penalized and ousted.

On June 2, in an attempt to restore his good standing with "the oligarchs," Yeltsin invited Russia's wealthiest businessmen to meet with him in the Kremlin. He did not ask anything of his guests, let alone accuse them of anything. He asked for their political support and complained that Russian bankers had been investing very little in the domestic economy. The oligarchs signed a general declaration on this point, although it did not oblige them to take any action. The weekly *Nezavisimaya Gazeta* reported (June 6, 1998) that one of "the oligarchs" commented quite agreeably: "We have all made so much money that it is time to think about our country." Andrei Bagrov wrote in the daily paper *Kommersant* (June 3, 1998): "Yeltsin finds himself in political isolation. Both politicians and financiers had already been rather contemptuous of the head of state, but during the current financial crisis they became completely disillusioned with him. The meaning of yesterday's meeting, therefore, was that Yeltsin was appealing to the oligarchs for political support at a time that for him was especially difficult."

Many proposals were being made on how to strengthen and develop Russia's economy and finances, and some of them deserved to be adopted. The bureaucratic machinery of state, which had swollen out of all proportion, needed to be cut back. Tighter control was needed over foreign trade and the sale of alcohol. And the tax system needed to be reformed. But current problems could not be solved by reducing government spending on science and education, as some economists were proposing with the argument that there were "too many instructors and professors" in Russia. It is true that investment in the system of science and education does not produce immediately tangible profits. But this system is one of Russia's most important acquisitions, no less than its natural resources. Support for science and education would help assure the prosperity of Russia in the twenty-first century.

Even Western experts were expressing the desire for greater government regulation of the Russian economy and for the development of a real economy (not just speculation or raw materials export). In the final analysis this would improve prospects for cooperation between Russia and the West as well as for increased strategic investment.

Many financiers, stock brokers, and financial analysts were sure that Russia could not overcome the difficulties of spring 1998 without major new loans from the West. "Only Bill Clinton and Helmut Kohl can stop the financial crisis in Russia," wrote Andrei Serov and Yelena Stanova in *Russky Telegraf* (June 2, 1998). Anatoly Chubais was sent to Washington to talk with his "personal friends" at the IMF (as he himself phrased it). Russian newspapers carried such headlines as "Help Is on the Way," "The West Will Help Us," "Chubais Will Bring New Credits from the U.S.," and "Chubais Is Close to Bringing It Home."

One newspaper wrote: "Again the role of savior of the Russian economy has been assigned to Chubais. If he brings home new credits from the U.S., the Kremlin will have a breathing space" (*Delovoi Vtornik* [Business Tuesday], 1998, no. 21, p. 1). The commentator Konstantin Sorokin, writing in the newspaper *Tribuna* (June 2, 1998), observed that without IMF aid the Finance Ministry and Central Bank could keep the situation under control only until mid-June. "After that the bankruptcy of the government will become more and more obvious. The only salvation is to obtain major stabilizing credits from abroad, a loan on the order of $10–15 billion."

Yeltsin, too, gave in to these fears and warnings and personally requested help from Clinton and Kohl. It must be said in Kiriyenko's favor that at first he did not take this road. In April and May he refrained from asking the West for new credits and said repeatedly that Russia should "live within its means." (Once the credits were obtained, however, Kiryenko spoke in favor of them and claimed them as a success for his administration.)

Actually the new loans and credits created a greater problem. Russia's debt to Western governments and financial institutions was already quite large. In 1997 approximately 20 percent of the budget went to servicing the foreign debt. It was expected that in 1998 no less than 30 percent of the budget would go for the same purpose. Russia's debts are structured in such a way that the biggest payments don't even begin until 2002! If present trends continue, the government will be paying as much as 70 percent of its budget just to service the foreign debt. On top of that, there is internal debt, which by some estimates is even larger than the foreign debt.

The only way out of this situation is for actual production, the "real economy," to grow. Most likely, however, 1998 represented another year lost on the way to achieving that goal.

It seemed that by the summer of 1998 the acute phase of the latest crisis in Russia had passed. Once again, though, the autumn would become a difficult time. A group of political analysts of the Gorbachev Foundation had worked out four different scenarios for possible developments in Russia for the period from 1996 through 2000. Not even the most pessimistic of those scenarios envisaged such a sharp and stormy crisis as Russia had experienced from March through May 1998. The general conclusion of the Gorbachev Foundation experts was that a fundamental change for the better was unlikely before the 2000 elections.