Russia

Financial panic hits, as LaRouche forecast

by Rachel Douglas

Two springs ago, in April 1996, Lyndon H. LaRouche, Jr. spent a day as the guest speaker at a Round Table seminar, hosted by Academician Leonid Abalkin and Academician Gennadi Osipov of the Russian Academy of Sciences. The theme was "Russia, the U.S.A., and the Global Financial Crisis." LaRouche opened his remarks by saying, "We are in the middle of the worst international and financial crisis of the century. The financial crisis has two dimensions: its severity, and the efforts of many leading institutions in the world, to pretend it doesn't exist. But that is characteristic of every major crisis in history. Leadership consists of not denying the crisis, in the first place."

Not all of the Round Table participants were prepared to believe LaRouche. One scholar, from a leading Russian economics institute, countered that the world financial market events since 1987 were "not very serious; . . . the collapse of one major British bank and one large American investment house. As the saying goes: If only we had *your* problems!"

Now, Russia does. The May 1998 meltdown of Russian financial markets, "can be described in one word—'panic,' " suggested Deputy Finance Minister Oleg Vyugin at his May 28 press conference. The fright unfolded through the very interplay of insane policies inside Russia and on the global scene, about which LaRouche has warned since the moment, in 1991, when President Boris Yeltsin put radical free-marketeer Yegor Gaidar, an intimate of the Mont Pelerin Society's Lord Harris of High Cross, in charge of Russian economic reform.

In 1995, LaRouche gave testimony to the Russian State Duma (Parliament), at the request of its Committee on Economic Policy, which began:

"In my estimate, the most crucial facts posed by the present economic situation in Russia, and in eastern Europe and the former Soviet Union generally, are in the following order of descending strategic weight:

"**1.0** Russia is trapped in the new phase of a worldwide monetary and financial collapse.

"**1.1** The present global monetary and financial order has recently entered a new phase of collapse, as marked by such prominently discussed examples as (a) the long slide downward in bond markets, (b) the waves of collapse caused by 'derivatives' speculation, such as the Mexico crisis, and (c) other impending, similar crises in nations of South America, Italy, and some former Comecon-member countries in eastern Europe. (Contrary to the hysterical, and demonstrably futile attempts to deny this fact, the current, new round of bankruptcies or near-bankruptcies of both governmental and private institutions is not a mere coincidence of separate and distinct local problems, but, rather, this pattern of increasing local crises is the result of an epidemic: a systemic disorder of the worldwide financial and monetary system as a whole.)

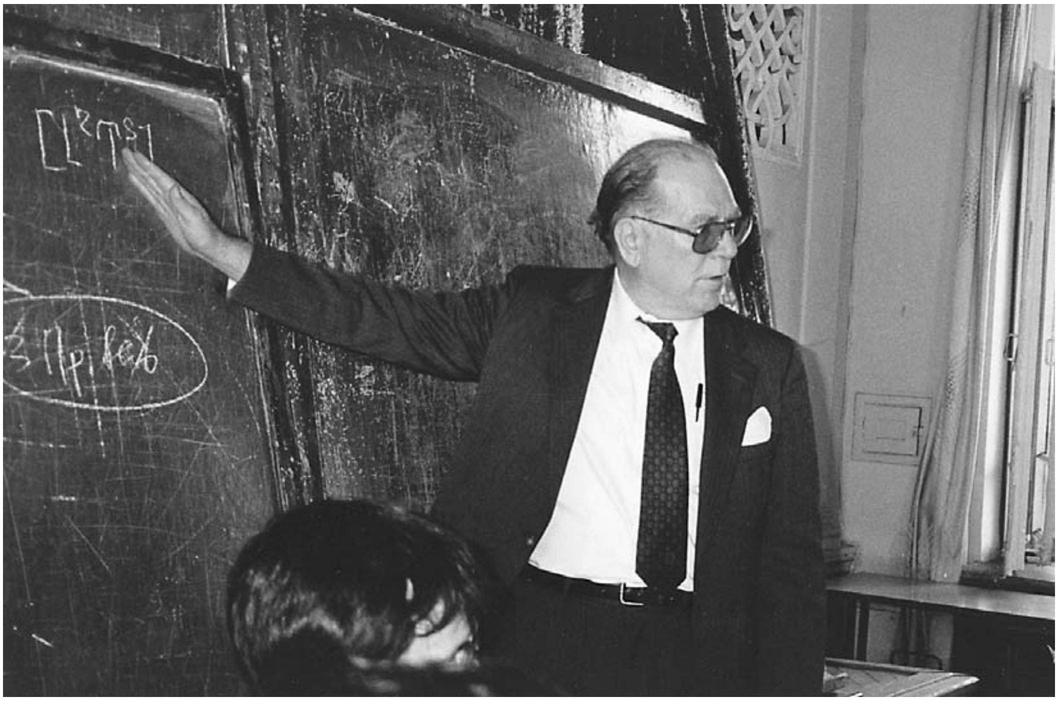
"**1.2** The present phase of the economic crises inside Russia and nearby countries is the result of the interaction between the ongoing, new phase of collapse in the world monetary and financial systems, and the relative exhaustion of Russia's ability to deliver a stream of loot to Western financier interests. Thus, the shrinking of the relatively depleted economy of Russia is an important feature of the current downward pressures upon London-centered world financial markets. This has a reciprocal effect: At the same time, the so-called reform-process in Russia is put on its death-bed by the inability of the Western side of the financial system to supply sufficient assistance to keep the Russia reform-process alive in its present form.

"**1.3** For related reasons, there exists no possible solution to this crisis, either for Russia or for the world, within the bounds of the previously accepted terms of dominant international economic and financial institutions. The present world system, as derived from the post-1971 form of 'floating exchange-rate' international monetary system, and present doctrines of International Monetary Fund (IMF) and related 'conditionalities,' is doomed to extinction during the near- to medium-term. The present system will either be brought to an end in an orderly way, through governments acting responsibly to put existing central banking and financial systems under state-controlled reorganization in bankruptcy, or through a chain-reaction form of rapid, 'thermonuclear' implosion of that speculative financial bubble which the world's financial system has become."

The memorandum that followed, was published under the title "Prospects for Russian Economic Revival," and widely circulated in Russian by the Schiller Institute for Science and Culture (Moscow), as well as in English (*EIR,* March 17, 1995).

An emerging disaster

Throughout the Byzantine twists and turns of the personnel configuration in the upper echelons of the Russian leadership in the Yeltsin years, almost all government officials there have considered it a success, when more foreign participants came into the country's new financial markets. Former Finance Minister and Deputy Premier Anatoli Chubais, who pushed through the fire-sale privatization of Russian industry, was particularly fond of crowing about how Russia was becoming a member of the club, in a globalized free trade economy. It was the "best-performing emerging market," some manic investment advisers trumpeted in mid-1997.



Lyndon LaRouche lectures in Moscow, April 1994, at the Russian Academy of Sciences. LaRouche has repeatedly warned Russian policymakers that the greatest danger to their nation's well-being, would be to give the radical free-marketeers control over economic reforms. Unfortunately, some people did not want to listen, and now LaRouche's forecast has been fully confirmed.

The financial boom, as *EIR* readers know from the writings of Dr. Sergei Glazyev, was divorced from real economic performance, except within the sector producing raw materials for export. "In effect," Glazyev wrote in the March 27, 1998 *EIR,* "the country's economy decomposed into two loosely connected spheres—the speculative financial one, and the productive—the former being characterized by rapid growth and the concentration of wealth and capital, while the latter, playing the role of donor for the former, is in a state of deep depression and decline."

The financial sphere almost fatally exploded in the October 1997 to January 1998 round of global financial crisis. Out of approximately $15 billion in foreign investments in Russian state treasury bonds (GKOs and OFZs) at that time, as much as one-third belonged to South Korean and Brazilian institutions. In a ten-day period in mid-November 1997, foreign "investors" pulled approximately $5 billion out of the Russian GKO market, of which $3 billion was withdrawn by South Koreans and about $1 billion by Brazilians.

On March 24, 1998, in "A Coup from Above," about Yeltsin's latest purge of the Russian government, LaRouche reviewed how the fuse on the Russian financial time-bomb was re-set, at the end of 1997. "At the time, last Autumn, the global systemic financial-monetary crisis was targetting Korea, Japan, and Indonesia. Russia had postponed a similar collapse by an hysterically inflationary bailout, through short-term international financing at loan-shark interest-rates. Come March, as the end of the first quarter of calendar year 1998 approached, the financial, economic, and social pressures of this bailout financing terrified Russia's leading political circles. In such circumstances, whatever might be likely to occur under such circumstances, were likely to begin building up now, echoing the scenario which began during October of 1997" (see *EIR,* April 3, 1998).

Going into the late-1997 crisis phase, Russia had more than $24 billion in gold and convertible currency reserves. At the beginning of May 1998, those reserves were $16 billion, of which approximately $4 billion is in gold. By May 28, some $2 billion had reportedly been spent in defense of the ruble and to pay out GKO liquidations. The Central Bank hiked interest rates from 30% up to 50%, on May 19, and then to 150% on May 27, after GKO yields rocketted through the previous ceiling and the stock market had fallen a cumulative 40% since the beginning of the month.

Looting of real production

The steepest collapse of Russian stock and bond prices, on May 27, came just days after the interim settlement of a two-week labor action by Russian coal miners. They blocked rail transportation, demonstrating not only for months of unpaid wages, but for the government to take action to save their industry and their regions.

Finance Minister Mikhail Zadornov maintained on May 27 that the financial collapse will not affect the ordinary citizen of Russia. Even apart from the fact that the state savings bank, Sberbank, is the largest single holder of the increasingly worthless GKO paper, Zadornov's ministry has outlined austerity measures, which were adopted on an emergency basis by Yeltsin and Prime Minister Sergei Kiriyenko, that will reach deep into Russian society. *Izvestia* of May 28 sketched the contours of the 12% cut in planned budget spending (the equivalent of $10 billion), to hit across the board. *Izvestia* leaked that the package incorporates the notorious "Kudrin" plan, named after the Deputy Finance Minister, for cutting 200,000 people from the state payroll. Two months ago, Yeltsin repudiated that plan as "a provocation," when it was said to include firing teachers and doctors. *Izvestia* claims that it doesn't—rather, "hundreds and thousands of employees from the Ministry of Food and Agriculture, Forestry Service, Medical Division of the Russian Academy of Sciences, the Siberian Division of the RAS, and even the government centers for economic analysis and reforms." The railroads would be reorganized: "Whole sections and junctions would be eliminated."

All this is supposed to save 3-4 billion rubles in the third quarter and 7-10 billion rubles in the fourth quarter of this year. For comparison, spending on GKO-OFZ debt service during 1998 was planned to be about 100 billion rubles, with interest rates averaging 25% through the year. GKO yields even in the 40-50% range, never mind the 80% or higher they hit on May 27, would mean debt service far exceeding the gains from the new austerity.

Will the social fabric hold?

Speaking from prison, on Dec. 28, 1991, LaRouche issued a Presidential campaign statement, "On the Subject of the Threat of Chaos in the Economies of Russia and Its Associated Member-States of the New Commonwealth of Independent States."

LaRouche warned, "The ironical fact is, that in the present stage, the only likely source of a nuclear crisis coming out of the former area of the Soviet Union today, aside from a special situation in the Transcaucasus region, is the danger that Boris Yeltsin, the President of the Russian Federation, might follow, to some degree or other, the pathway toward bankruptcy which the Polish government pursued for a while, up until most recently, at the instruction of Harvard's lunatic professor, Jeffrey Sachs. If Yeltsin, for example, and his government, were to go with a reform of the type which Sachs and Sachs's co-thinkers demand—chiefly from the Anglo-American side—then the result in Russia would be chaos. In such a case, the overthrow of Yeltsin, or somebody, by a dictatorship and the restoration of a form of what is called totalitarianism would probably occur. In that case, then we have a strategic threat."

Addressing the same matter, five years later, LaRouche wrote in "Russia's Relation to Universal History" (*EIR,* Nov. 29, 1996), "A so-called 'Reform' policy, was jointly imposed upon post-Soviet Russia, Ukraine, and Belarus, by Britain's Prime Minister Margaret Thatcher and the man she has described as her dupe, U.S. ex-President Sir George Bush. That 'Reform' policy, not reversed under U.S. President Clinton, has driven Russia presently to existential extremes, at which some sort of explosion is imminent. 'Explosion' does not signify 'global thermonuclear war,' but the ignition, and spread of chaos, out from Russia, to engulf much of the planet. It appears, that official diplomatic Washington is more concerned with clinging to the appearance of defending a failed British-designed 'Reform' policy, than replacing London's and the U.S. Republican Party's bankrupt policy with a sane American one."

On May 22, after meeting with President Yeltsin, Russian Prosecutor-General Yuri Skuratov said the President wanted an investigation of the coal miners' leaders for violating the Constitution when they blockaded rail traffic of national importance. Skuratov quoted Yeltsin as saying that the miners had "gone too far," and that they "have not yet learned to work in a market economy."

Vitali Tretyakov, founding editor-in-chief of Russia's first big post-Soviet daily paper, *Nezavisimaya Gazeta,* wrote a May 21, 1998 editorial, titled "The History of the Economic Reforms in Russia Has Been Written to the End." Hoping that "reforms, as such, (in forms that will better correspond to the sense of this word) sooner or later will be continued," Tretyakov took stock of the latest turn in Russia's economic and social crisis, as "the finale of a whole historical period, which is coming to an end. This finale is unfortunate. The reforms in Russia did not just fail. They failed shockingly. They collapsed. The question is if this collapse will mean the simultaneous collapse of the country. It cannot be ruled out."