

Testimony to the
Subcommittee on International Development,
Finance, Trade, and Monetary Policy
of the
Committee on Banking, Finance, and Urban Affairs

by

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I would like to thank the Committee for the opportunity to testify on the issue of Western financial assistance to Russia. As you know, Russia is engaged in a struggle for economic reform. Success will make possible the transformation of Russia's economy to the market system, the integration of Russia into the world economy, and the democratization of Russian society. Failure would mean a new round of financial chaos that would pose threats to democratization and even to global security.

On Monday, the International Monetary Fund took an historic step by giving formal approval to Russia's economic reform program. It voted to support Russia's "Economic Memorandum." This memorandum will be converted in April into a formal IMF program that will be the basis for a one-year standby credit, as soon as Russia becomes a member of the IMF at the end of April. Part of the Memorandum identifies the urgent need for Western financial support to accompany Russia's reform measures.

In its oversight of the international financial institutions and the U.S. Eximbank, this committee therefore faces urgent issues of how to use best to use U.S. resources, prudently but adequately, to support the economic reforms now underway.

I will begin with some economic and political background to underscore Russia's urgent need for Western financial assistance. I will then describe the package of multilateral Western support that should be mobilized in the nearest future to support the Russian reform program. I also include an annex that clarifies the

debate concerning the levels of Western support that have been extended to the former Soviet Union in previous years.

At the outset let me stress several of the most important points.

- First, IMF has identified the need for multilateral support for calendar year 1992. According to the IMF, the minimally necessary support is \$12.3 billion of balance of payments assistance, and \$6 billion in a stabilization fund for the ruble;
- Second, in addition to the \$12.3 billion, there is a need, acknowledged by the IMF, to secure support from Western export credit agencies, including the U.S. Eximbank, for credits and credit guarantees for urgently needed investment projects, particularly in agro-industry, energy, and military conversion;
- Third, as explained below, the timetable for mobilizing this support is tight, for both economic and political reasons;
- Fourth, the financial risks to the Western nations of providing this aid are much less than sometimes alleged. The aid should all come with strong conditionality, linking the support to implementation of the reform program. Moreover, as shown in the annex, the widely bruited notion that \$40 - \$50 billion of aid was squandered last year is totally mistaken, and is based on a simple misunderstanding of EC data.
- Fifth, the U.S. share of this multilateral package should be roughly as follows: (1) \$1 billion in appropriations for technical assistance and humanitarian assistance; (2) approximately \$1.2 billion as the U.S. share of a \$6 billion stabilization fund

(the budgetary implications of the U.S. contribution would depend on the exact specification of the fund, as a grant versus a line of credit); (3) new credit guarantees for purchase of U.S. grain products; (4) increased Eximbank support for U.S. exports to Russia, made possible by repeal of the Stevenson-Byrd Amendment.

Economic Background

Russia is suffering from an acute balance-of-payments crisis, that threatens to undermine its economic and democratic reforms. Export earnings have fallen sharply since 1990, as shown in Table 1, particularly in the hydrocarbon (oil and gas) sector, but in other sectors as well. At the same time, as of early 1991, most creditors stopped extending new loans to Russia, and on the contrary, began withdrawing credit lines as rapidly as possible. The combination of falling exports and heavy debt servicing resulted in a collapse of imports and a depletion of foreign exchange reserves. Imports fell from \$US 81.6 billion in 1990 to only \$US 44.3 billion in 1991, an astounding drop of 46 percent. Foreign exchange reserves were essentially depleted, falling to a few hundred million dollars, or the equivalent of a few hours of import coverage.

The fall of exports and the withdrawal of financial credits has led to an intense scarcity of foreign exchange in Russia, which has been reflected in the collapse of the real purchasing power of the ruble vis-a-vis foreign exchange. Consider, for example, an average worker's ability to purchase dollars (or dollar-priced

items) using ruble wage earnings. The average industrial worker earns about 1,900 roubles per month in March 1992. Since dollars are so scarce and therefore so expensive, this wage translates into only \$16 per month at the current cash-market exchange rate of 120 roubles per dollar.

According to extensive evidence at the enterprise level as well as the sectoral level, the cutback of imports is a major cause of the ongoing collapse of industrial production. In 1991, industries were subjected to sharp cutbacks in centralized allocations of imported inputs, including raw materials, intermediate goods, and spare parts, resulting in a fall of GDP of about 11 percent compared with 1990.

In 1992, the intense shortage of foreign exchange continues, but it is now hitting the enterprises through market mechanisms rather than through central allocations of foreign exchange. Specifically, enterprises cannot afford to purchase imported inputs at the current free-market exchange rate, since they cannot pass the high costs of imported inputs on to their domestic consumers, in view of \$15 per month average wages. Similarly, the enterprises cannot afford to purchase domestically produced tradeable goods, such as metal ores, since the prices of such goods are determined by world market prices in the same way as imported goods.

The individual enterprise is therefore caught in a jackknife between soaring input costs and falling purchasing power of customers. The result is a wave of plant closings, sharply rising unemployment, and sharply falling industrial production. While the

individual enterprise might blame its fate on tight credit, or bad government policies, or the withdrawal of subsidies, the fact is that the balance of payments squeeze is the most relentless and powerful single factor in Russia's intense industrial crisis.

The crisis is further intensifying in 1992 as enterprises deplete their inventories of imported inputs. In 1991, imports fell far more sharply than output. Now, in 1992, the output decline is catching up with last year's collapse of imports. There are widespread reports that machinery is breaking down, and that factories are continuing to close, for lack of imported spare parts.

The economic consequences of the balance-of-payments crisis are severe. First, unless there is a partial reversal of the 1991 decline of industrial goods imports, the output shortfall in 1992 will exceed even the pessimistic estimate of a 20 percent GDP drop. Second, the import shortfall is also causing serious human distress, as the country lacks the normal financial means to import urgently needed foodstuffs and medicines. Imports of medicines fell by an estimated 47 percent between 1990 and 1991. Third, the lack of foreign exchange reserves at the Russian Central Bank also threatens the anti-inflation efforts of the Yeltsin government. Since the government lacks foreign exchange reserves, it is unable to commit itself to defending a stable nominal exchange rate. But without a commitment to a stable exchange rate, it is difficult to prevent an on-going wage-price-exchange rate spiral.

Some Political Implications of the Balance-of-Payments Crisis

The shortage of foreign exchange is perhaps the major immediate threat to the Yeltsin government and to the economic and political reforms more generally. In broad terms, the balance-of-payments crisis is a major cause of the ongoing industrial collapse and the precipitous fall of living standards, both of which threaten the viability of the reforms. More specifically, the reactions of the Parliament, the politicians, and the bureaucracy, to the foreign exchange crisis, may seriously undermine the key measures of the reform.

Because of the foreign exchange crisis, several adverse trends are possible:

- there is pressure to restore the central rationing of foreign exchange, thus undermining the basic step towards liberalization of the economy;
- there are powerful separatist movements of the raw-materials-producing regions, which are fighting to keep control over their high-valued products;
- there is a pressure in key ministries to reimpose export controls and state orders between enterprises, to try to ensure that industrial enterprises can afford to buy the inputs of tradeable goods that they need to keep operating.
- there are pressures undermining the use of the ruble, not only in the non-Russian republics, but also in Russian autonomous regions. These tendencies are fueled by the continuing instability of the value of the ruble and its lack

of proper convertibility.

Of course, while none of these trends would solve the basic balance-of-payments crisis, and indeed would actually reduce Russia's exports still further, these trends are likely to intensify in the absence of Western financial assistance.

The pressures on the reform are reaching an important stage. The program will be under attack in April and May, for the following reasons:

- the People's Congress comes into session on April 6, with many populist politicians intent on undermining the government;
- the pressures for wage increases and strikes are rising (partly linked to the political timetable);
- parts of the bureaucracy are putting on pressures for a reimposition of central controls (foreign exchange rationing, export controls, and state orders);
- the Government is embarking on a necessary, but high-risk, round of new price increases, especially energy price increases. Unless there is confidence in the currency, this new round of price increases could unleash a new round of a wage-price spiral.

There is also the growing risk of an anti-Western backlash, provoked by opponents of the government. The next round of policy measures is explicitly part of an IMF-approved program. Therefore, the IMF and the West more generally, will bear the blame for the

measures -- if there is no Western financial support to accompany this round of policy actions.

The Necessary Scale of Western Support

The IMF has made an estimate of Russia's financial needs for the calendar year 1992. In essence, the IMF has made an estimate of the minimal level of foreign exchange that Russia will need in 1992 to pay for imports of goods and services (including interest payments on the foreign debt). It then examined the level of Russian export earnings that are likely to be available to pay for the imports. Since the import needs exceeded the anticipated export earnings, there is a financing gap, which should be filled by grants and loans from the West.

The IMF has determined that Russia needs \$12.3 billion of balance-of-payments support, as well as a \$6 billion stabilization fund to support the ruble, hence a total of \$18.3 billion. The balance-of-payments support can come in the form of grants (e.g. food deliveries), loans, or postponement of interest servicing of the foreign debt. Note that the calculation of the \$12.3 billion financing gap already assumes that Russia will be granted a full rescheduling of all principal payments on medium and long-term debts taken on by the Soviet Union before 1991.

The IMF estimate of \$12.3 billion should be regarded as a absolutely minimum estimate of Russia's needs, since the number was already selected with a view towards political acceptability to the G-7. In particular, the underlying assumption of the IMF estimates

is that import levels will remain very low in 1992, more than \$US 30 billion below the level of 1990, as shown in Table 2. The IMF recognizes that the continuing extreme squeeze of imports will contribute to the 20 percent GDP decline forecasted for 1992, and that a greater level of financing would make possible a higher level of imports and thereby a smaller drop of GDP.

Nor does the \$12.3 billion include financing for new large-scale investments, such as in military conversion, energy or agro-industry, which will require financing in addition to the \$12.3 billion. (This last point is made clear in the IMF discussion of the financing gap, where the IMF says that Russia's capacity to "absorb imports" may "turn out to be larger than expected . . . This may occur for example in energy or agriculture, where new investment projects are now being examined by the World Bank"). In this case, the IMF advises that additional financing "would be beneficial." Most of that additional financial should then come from the export credit agencies of the G7 countries, including the U.S. Eximbank, and from the new European Bank for Reconstruction and Development.

It should also be noted that the IMF estimate of exports (\$49.4 billion for 1992), which underlies the calculation of the financial gap, may also be overly optimistic, since exports have been running at an annual rate of only \$36 billion in the first two months of 1992. If exports are lower than expected, then of course additional financial assistance would be needed to maintain the targeted level of imports.

In sum, the IMF estimate of \$12.3 billion in financial needs is somewhat higher than the G7 wished to acknowledge -- and in this sense, the IMF has played a useful role in mobilizing international support for Russia -- but the estimate is lower than the West ought to put forward at this crucial stage of Russia's economic and democratic reforms. Financing of at least \$12.3 billion will be needed simply to avoid an utter balance of payments collapse. Additional financing should be extended to moderate the fall of GDP, and to make it possible for Russia to begin undertaking crucially needed investment projects in key sectors.

In addition to \$12.3 billion of balance of payments needs, the IMF identified another \$6 billion as required for a ruble stabilization fund. The idea of a stabilization fund is straightforward. The fund is a pool of foreign exchange reserves, made available to the Russian Central Bank, that can be drawn upon in order to maintain a stable market exchange rate of the ruble. If the exchange rate of the ruble begins to weaken from a targeted level, the Central Bank can sell dollars into the foreign exchange market, thereby stabilizing the ruble value. The target exchange would be set in consultation with the International Monetary Fund.

The idea of the fund is to act as an insurance policy. Monetary and fiscal policies are to be set sufficiently tightly so that, in expectation, the stabilization fund would not have to be used by the Russian Central Bank. Rather, the goal would be to stabilize the exchange rate purely through market forces and disciplined macroeconomic policies. If an unexpected shock hits

the economy, however, or if citizens start to panic and try to convert their rubles into dollars, then the fund would be drawn upon to maintain the exchange rate.

Why have a fund if, in expectation, it won't be used? Because the knowledge of the fund will actually help to forestall a panic, or a loss of confidence. Since citizens and firms will know that the money is available, they will also know that they don't have to join a run on the ruble the moment it breaks out. By calming the public's nerves, the panic is much less likely to ever arise. Incidentally, Russia would be barred from drawing down the \$6 billion fund (which would be set up as a line of credit maintained at the IMF or Bank for International Settlements) if its macroeconomic policies were out of compliance with the IMF-monitored program.

This mechanism has recently proved its merit in the case of Poland, where a \$1 billion stabilization fund set up by the G7 at the start of 1990 was instrumental in helping to stabilize the zloty. In the event, the zloty stabilized as a convertible currency, and Poland never had to draw upon the stabilization fund.

IV. Timetable of Western Support

In late February, the IMF and Russia reached agreement on an Economic Memorandum, and this economic memorandum was formally approved by the Executive Board of the IMF [yesterday]. Russia is already carrying out actions based on the economic memorandum (such as the freeing of milk and bread prices), and it will carry out

further major actions (such as the freeing of energy prices and the unification of the foreign exchange market) shortly after the IMF program is approved (in April and May).

It is anticipated that this Economic Memorandum will be converted to a full-fledged standby loan of the IMF soon after Russia becomes a member of the IMF at the end of April. Assuming that the IMF and G7 put in the effort, the IMF lending program could start in the middle of May. The IMF estimate of the \$12.3 billion financing gap, and the need for the Stabilization Fund, are described in an annex to the Economic Memorandum.

In order to implement the financial support needed to back up Russia's reforms, a timetable such as the following should be envisioned:

- March 30: IMF votes approval of economic program
G-7 should declare intention of filling financial needs of Russia, including \$12.3 billion of financial support, plus \$6 billion stabilization fund.
- April 1: Paris Club meeting on Russia. The Paris Club should postpone Russia's interest payments for 1992, leading to savings in calendar year 1992 of approximately \$3.0 billion in interest payments (including interest owed to commercial banks, which should be rescheduled on the same terms as the Paris Club.
- Mid-April: IMF mission in Moscow, to convert the Economic Memorandum into a full standby agreement. The new agreement would be sent to the Board of Directors of the IMF for expedited approval
- April 6: Opening of the People's Congress in Russia. The G7 should have made clear, and the Russian Parliamentarians should understand clearly that the West has committed at least \$12.3 billion to support the economic program, as well as \$6 billion for a stabilization fund.

Late April: Russian membership in IMF and World Bank

Mid-May: Standby Agreement of IMF begins
World Bank lending begins ("Critical Imports Loan")

May 22-23 Lisbon Conference, completion of \$12.3 billion financial support package

June-July Stabilization Fund begins operation, exchange rate is pegged.

July Munich Summit reaches agreement on structural issues regarding Russian-G7 economic cooperation

Several important comments should be made about this suggested timetable.

Most importantly, the West (in the form of the G7) should commit publicly to meet Russia's financial needs soon after the IMF Executive Board approves Russia's program, and before the April 6 start of the People's Congress. It will be very important for the Russian Government to be able to put the IMF agreement and its own current policies in the framework of financial cooperation with the West.

The first measure towards meeting the financial gap should be relief on foreign interest payments in the Paris Club on March 31. The Paris Club should postpone 100 percent of principal and interest payments owed on all debts taken on before 1991, for a period that lasts until the end of 1992.

Next, the IMF should be ready to start its own lending program immediately upon Russian membership at the end of April. To accomplish that, the IMF must have a new mission in Russia in early

April, to make the necessary preparations.

Similarly, the World Bank should be ready to start its lending program immediately upon World Bank membership (which will come at about the same time as IMF membership). It should start with a \$1 billion loan for "critical import needs."

The stabilization fund should start up in June or the start of July, so that the Russian Government can make an early commitment to defending the exchange rate. This commitment to exchange rate stability will be important in preventing the April and May price increases from turning into a new wage-price-exchange rate explosion. The exact date for the start-up of the stabilization fund will depend to some extent on financial measures agreed to with the other republics (for instance, the timing for the introduction of a new currency in Ukraine).

The Lisbon Aid meeting at the end of May can be the occasion when the overall \$12.3 billion financing package is committed. (Much of it will already have been committed by the IMF, World Bank, and other lenders, but the overall package can be confirmed in Lisbon).

It will be very valuable for the G7 and Russia to have the overall financing arranged before the Munich Summit, precisely so that the Summit is not a "pledging session." Expectations might be raised too high if there are still unmet financial needs by the time of the Summit. Rather, the Summit should concentrate on "structural" issues regarding Russia, such as: energy, agriculture, private sector development, military conversion, nuclear safety,

etc.

Sources of Western Financial Support

The precise parameters of the financing gap must be clearly understood. The \$12.3 billion refers to calendar year 1992. Thus, almost all of the required financing must be mobilized during the period April - December, 1992, since little has come in the first three months of 1992. Moreover, the \$12.3 billion includes humanitarian assistance, new loans and grants, and relief on interest payments on the debt. It does not include, however, the stabilization fund (an additional \$6 billion), nor deferment of principal repayments (since a deferral of principal has already been assumed by the IMF).

At this point, it is possible to give only an approximate idea of possible financing of the \$18.3 billion:

IMF standby loan (drawn down in 1992)	\$2.5 ²
World Bank	\$1.5
Paris Club	\$3.0
Bilateral Grants and Credits (including humanitarian aid)	\$5.3
Stabilization Fund (bilateral donors)	\$6.0
Total	\$18.3

For the bilateral grants and credits, and for the stabilization fund, there is a need for burden sharing among the

²Note that the IMF standby program will be a loan of about \$4 billion, but only about \$2.5 billion will be available in calendar year 1992.

advanced industrial countries. One formula for burden sharing would be:

	Bilateral credits (\$5.3 billion)	Stabilization Fund (\$6 billion)
U.S. (20% of total)	\$1.1	\$1.2
Japan (20% of total)	\$1.1	\$1.2
EC (50% of total)	\$2.6	\$3.0
Other (10% of total)	\$0.5	\$0.6
Total	\$5.3	\$6.0

"Other" countries might include South Korea, Saudi Arabia, Australia, New Zealand, Scandinavia, etc. Another possibility might be to take the shares of the Poland Stabilization Fund as an adequate basis for burden sharing.

Some comments about the funding are in order. First, the IMF and the World Bank must be pressed hard to contribute an adequate amount of financing. The World Bank should be pressed to begin its assistance program with a \$1 billion loan for critical import needs. Currently, the World Bank is considering a much smaller loan (around \$500 million), which would be too small to meet the financing needs of the program.

Second, the Paris Club must give generous rescheduling of interest, if the financial package is to be secured. This decision should be taken in the first week of April, when the Paris Club is scheduled to meet on Russia. The Paris Club has hinted at the notion of rescheduling interest for three months only. This would leave too much uncertainty on Russia's financial situation. The

rescheduling should apply for at least six months, with the intention of later making it coterminous with the IMF standby program that will start in Mid-May.

Third, it is important to "fill the gap" only with real resources, not with empty pledges. Export credits are in general difficult to use, and not very flexible. Thus, it is not enough to pledge export credits, as evidenced by the fact that there were credits of more than \$10 billion that remained untouched in 1991.

Fourth, it should be remembered that the \$12.3 billion does not include financing for large-scale investment projects in critical sectors (military conversion, energy, and agro-industry). Special projects, supported by the World Bank, EBRD, and the export credit agencies, should be developed -- in addition to the \$12.3 billion -- to support investment efforts in these areas.

In order to justify the aid package, and to support the Russian reforms, all aid should be conditional on compliance with the economic package agreed to with the IMF. This conditionality should apply to the export credit agency lending, stabilization funds, Paris Club rescheduling, funds from the international financial institutions, etc.

The U.S. Role in the Financing Package

As I have already stressed, the U.S. should participate in the financial package as part of a multilateral effort that is at least sufficient to meet the needs identified by the IMF. There are four areas of assistance that have been identified.

- U.S. participation via the IMF, World Bank, and EBRD
- U.S. humanitarian and technical assistance of \$1 billion for 1992
- U.S. contribution to the Stabilization Fund of \$1.2 billion
- U.S. opening of export credit lines from the Eximbank, and further credit guarantees for grain purchases.

To mobilize Eximbank credits, the so-called Stevenson-Byrd Amendment must be repealed. This 1974 amendment puts a ceiling on Eximbank credits to Russia of only \$300 million. This ceiling should be repealed, and Eximbank funding of Russia should rise to around \$1 billion per year in the next few years, with a special emphasis placed on military conversion, energy, and agro-industry.

Russian Issues at the Munich Summit

The G7 leaders have pledged to make economic reform in the CIS one of the three central topics at the Munich Summit on July 6-8 (in addition to the world economy and third world economic problems). Chancellor Kohl has confirmed that President Yeltsin will be invited to participate in the summit. Nonetheless, the G7 has not yet settled on a specific agenda regarding Russia and the other new states of the Commonwealth.

One possibility is to make financial assistance a centerpiece of the discussions. Such a use of the Summit would be disappointing and even problematic. One reason is that the financial package should be settled far in advance of the Summit,

to coincide with the Russian Government's economic and political timetable for macroeconomic stabilization. The ruble stabilization fund should be set up and operating no later than July 1, 1992 (and probably no later than June 1). Therefore, the fund should be arranged, and confirmed, in the Spring. Similarly, the \$12.3 billion balance-of-payments support for 1992 can and should be arranged in the Spring as well.

If the financial package is not settled before the Summit, there would be a danger of the Summit turning into a "pledging session," in which expectations in Russia and the other republics could well get out of hand. It would be highly deleterious for Yeltsin to go home from the Summit "disappointed" compared with exaggerated financial expectations that build up in the Russian public in the weeks leading up to the Summit. Similarly, there is no way that the Summit would be able to make financial commitments to the other republics that have not yet reached financial and economic accords with the IMF.

Perhaps most importantly, if the Summit focusses on the financial aid issues, it will miss an important opportunity to deepen the Western cooperation and support of Russia's reforms in ways that will be of even greater significance in the long term. Rather than focussing on the 1992 balance-of-payments needs, the Summit should be used to push forward Russia's reforms in various structural areas.

The Summit should be used to set out a basic framework to guide the process of Russia's integration into the world economic

system. The framework, which might be called a Compact on Economic Cooperation, would spell out Russia's long-term goal to become a "normal" and prosperous member of the world economic community, and would commit the G7 to providing financial, political and technical assistance to help Russia achieve that goal. In addition to laying out general precepts, the Compact could establish a number of specific projects, which would be incorporated into the G7 process during the coming year.

The project areas might include: trade liberalization between Russia and the G7 countries; energy sector development; military-industrial conversion; agro-industrial development; and small business development. Special projects in these areas would become part of the regular agenda of G7 Ministerials, and the Russian Deputy Prime Minister for Economy would be invited to several of the meetings for purposes of discussing the progress of the reforms. The Summit leaders would also announce that they will undertake a comprehensive review of the Compact at the following Summit.

Annex: G7 Assistance Extended to Former Soviet Union in 1990-91

This annex summarizes the information available about Western financial assistance extended to the former Soviet Union in the recent past. It is well known that substantial assistance was given, mostly in the form of credits and guarantees from export credit agencies, particularly Hermes (FRG). Nonetheless, there is considerable, and understandable confusion about the actual extent of assistance, and there has been a tendency in public debate for opponents of balance-of-payments assistance to Russia to magnify the flows that have went to the former Soviet Union in the past couple of years.³ In fact, in 1990 and 1991, inflows of credits and grants barely exceeded the outflows of debt servicing (amortization and interest payments).

According to preliminary and partial data collected by the EC, the CIS states received commitments of assistance of \$52.6 billion during 1990 and 1991.⁴ This includes \$2.3 billion of grants, \$7.6 billion of untied loans, and \$42.7 billion of tied loans. In addition, Germany extended approximately \$11 billion in assistance for the withdrawal of Soviet troops from East Germany.

About two-thirds of these commitments were actually disbursed,

³For example, see Bandow (NYT, 3/27) and Gelb (NYT, 3/30) for particularly extreme exaggerations. Gelb writes that about \$50 billion in the last 20 months "has virtually disappeared without a trace or a dent on the economic picture."

⁴In fact, the data refer to all of 1990 and 1991 for Germany, but only September 1990 - December 1991 for the other donor countries. Since Germany extended the vast bulk of assistance in this period, and since the other donors extended little in grants and credits during January - August 1990, the data give fairly good coverage for all of 1990 and 1991.

so that disbursements amounted to \$28.1 billion. Only \$1.7 billion of the disbursements came in the form of grants; the rest were credits (of which \$7.6 billion were untied, and \$18.8 billion were tied). As a rough estimate, Russia's share of the overall disbursements was about 0.6 (approximately the share of the Russian economy in the former Soviet Union), or about \$17 billion over 1990 and 1991. Germany provided about half of the total disbursements (\$14.6 billion). A large part of the German credits involved credits to East German industrial firms to continue to ship goods to the Soviet Union after the breakdown of COMECON and the unification of Germany.

The IMF has presented independent estimates of the capital flows to the Soviet Union and Russia for these two years, that are slightly lower than the EC estimates (see Table A1). There is, as yet, no careful accounting of the differences in the estimates of the two sources.⁵

The net flows to the Soviet Union and Russia were substantially less than the gross flows, since there were substantial amortizations (repayments of debt principal) during this period, as shown in Table A2. For the Soviet Union as a whole, the IMF records that total amortizations due were \$16.3 billion for 1990 and 1991, with Russia's share of amortizations of

⁵Technically, the IMF estimates refer to total flows recorded in the balance of payments, including private capital sources as well as official sources, while the EC data refer to official flows only. It is therefore surprising that the IMF magnitudes are actually smaller than the EC estimates, despite the fact that the IMF category of resource flows is more inclusive.

\$9.9 billion. In fact, some of the amortizations were not paid. The Soviet Union accumulated arrears of about \$3.7 billion, and had \$0.3 billion of debt formally deferred at the end of 1991. Russia accumulated arrears of about \$2.2 billion, and had \$0.2 billion of debt deferral. Thus, actual amortizations were \$12.3 billion (\$16.3 - \$4.0 billion) for the Soviet Union and \$7.5 billion (\$9.9 - 2.4 billion) for Russia.

Net flows actually paid are calculated as gross resource inflows minus actual amortizations. The net flows, according to the IMF, amounted to \$ 13.7 billion for the Soviet Union, and \$8.1 billion for Russia (Table A2).

If we subtract off the interest payments on the foreign debt in order to calculate the net resource transfer to the Soviet Union and to Russia from foreign creditors, the financial transfers are de minimus. Russia paid \$5.6 billion in interest payments for 1990 and 1991, and the Soviet Union as a whole paid \$9.1 billion. Thus, the net resource transfer from the creditors (net flows minus interest payments) equalled \$4.6 billion for the entire Soviet Union, and \$2.5 billion for Russia (Table A2, final line).

There is no doubt that the Gorbachev regime squandered a great deal of borrowing since the mid-1980s. Imports of machinery and grains led to a heavy debt accumulation in the second half of the 1980s, which started to come due in 1990 and 1991. Foreign borrowing also was used to cushion the blow of falling oil prices and oil production after 1985. By 1990 and 1991, however, outflows on debt servicing were simply absorbing almost all of the inflows

of new money from abroad. There is no mystery, therefore, about \$50 billion of "disappeared" funds in the past 20 months. Such funds never came. The much smaller credits that were in fact issued were simply balancing the outflow of debt servicing.

Table A1. Gross Resource Flows to the Soviet Union and Russia
(\$US billion, disbursed)

	1990 - 91	
	EC	IMF
Soviet Union	28.1	26.0
Russia	16.9 ¹	15.6
of which grants:		
Soviet Union	1.7	2.6
Russia	1.0 ¹	1.2

¹The EC does not make a separate estimate for Russia. The figure shown in the table is simply 0.61 multiplied by the estimate for the entire Soviet Union.

Table A2. Resource Transfers to Russia, 1990 and 1991
(\$ billion)

	1990	1991	Total
Gross Flows:	6.6	9.0	15.6
Credits	6.6	7.8	14.4
Grants	0.0	1.2	1.2
Amortization due	4.9	5.0	9.9
minus:			
Arrears ¹	2.7	-0.5	2.2
Deferrals	0.0	0.2	0.2
Amortization paid	2.2	5.3	7.5
Interest Payments ¹	2.9	2.7	5.6
Net Flows (gross flows minus amortization paid)	4.4	3.7	8.1
Net Resource Transfer ¹ (net flows minus interest payments)	1.5	1.0	2.5

1

For purposes of presentation, the table assumes that all arrears fell on principal repayments, and none fell on interest due (that is, the table assumes that all interest was paid). The final calculation of net resource transfer would remain unchanged if in fact the arrears fell partly on interest and partly on principal, since the NRT is based on total debt service actually paid, and not on the division of principal versus interest payments.

Source: IMF estimates of balance of payments

Table 1. Russian Exports, \$US billion, 1990-92

	1990	1991	1992 (IMF projection)
<u>Exports</u>	80.9	56.8	49.4
oil and gas	36.7	21.4	19.3
other	44.2	35.4	30.1

Source: IMF balance of payments estimates.

Table 2. Russia's Imports, \$US billion, 1990-92

	1990	1991	1992 (IMF estimate ¹)
Imports	81.6	44.7	50.0
Food and medicine	14.0	12.1	14.9
Other	67.6	32.6	35.1

¹The IMF estimate of imports is judged to be the minimum level of imports necessary to limit the 1992 decline in Russian GDP to 20 percent.