

## **Russia's Economy: Back to the Third World or Ahead to the First Soltan Dzasarov**

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*This article is the abbreviated text of a piece published in the March 10, 1999 issue of the Russian publication, "Slovo." Prof. Dzasarov is chair of the department of economic theory and business at the Russian Academy of Sciences and an active member of the Board of ECAAR-Russia.*

Probably most Russians have little doubt that there is just one goal: a free market and democracy. But the path is less clear. The choice is between reforms in the interest of the oligarchs, or policies in the interest of the majority of the Russian people.

The seven years of "reform accomplishments" seem to have been inefficient and even pernicious for the present and for the future of the country and its people. Whatever is said about modern Russia, realistically the majority of Russians have found the promises of an economic miracle to be a cynical deception.

The question is not whether to implement reforms. The question is how to do it right. Neoclassical economics and the accompanying monetary models have led the economy to full bankruptcy. This result is unique in world history. In all other cases such market reforms had positive effects: in post-war Germany, in modern China, and even in our own history of the NEP (new economic policy of the 1920s). Hungry, Poland and the Czech Republic are gradually finding their way out of crisis.

### **Declaring One Thing and Doing the Opposite**

Why is Russia such an exception? The answer is very simple: We have been declaring one thing, but doing the complete opposite. Under the motto of market reforms, we have created something extremely different from a real market economy. We have constructed a criminal social system, which has no analog in world history and is incompatible with civilized free market enterprise. This is an economy where:

- 1) one can't take a step in business without a bribe for criminal "krysha" (cover);
- 2) it is "unnecessary" to compensate employees with salaries or pay contractor's bills;
- 3) pricing is subject to negotiation in order to artificially decrease the revenues and hence avoid certain tax levels;
- 4) only 25 percent of all accounted transactions are made with actual money exchange; the rest being by barter deals;
- 5) lack of competition is replaced with a system of personal connections and privileges granted by the state.

An economy in such a form can not and will not provide a step toward the development of conventional free market terms and conditions. Furthermore, in some ways the former centrally planned economy was more market oriented than the current one, although a true market system was not achieved then either.

Our economy is not a free market, both because of these clear indicators, and also because of its processes. Instead of the past command-administrative economy that was obsolete and inefficient, but did have an organized structure, we now have a "criminal-voluntary" economy. Its completely arbitrary criteria of action are not limited

by law or ethics. Instead, the thirst for gain has become the main motive leading to a system of destructive economic imbalance. If this scenario is continued, the formation of any truly free market or normal economic development are excluded not only today, but also in the future.

### **Free Market Competition and Criminal Private Property**

The advantage of a free market compared to a centrally planned economy relates to free competition that can create a mechanism to define the value of accumulated resources so they tend to go to those who can use them most efficiently. In contrast, the nomenclature privatization in Russia has excluded efficient business people. The majority of people who have succeeded have not done so by market efficiency, but by the power of the criminal world and by using bribes and other “services.”

As a result, large-scale property has not been separated from the state, the prerequisite of a free market; it is closely interwoven with the state through criminal agreements. Thus the normal process for developing free market conditions of capital accumulation has been precluded. Profits and gains are achieved not by the skills of business people, but by misappropriation, i.e. by distribution and redistribution of resources by means of bribes, connections and other forms of criminal business practices.

### **Service Industries and Manufacturing Industries**

The disparity between the service and manufacturing sectors in the modern Russian economy led to a scandalous situation with no parallel in economies elsewhere. A striking illustration is the over ten-fold greater profits in banking and trade compared with manufacturing. In normal free market countries, the level of gains in manufacturing sectors is at least twice as high as the bank interest rate. Otherwise, the manufacturing business people simply could not afford to apply for credit.

The recent “crisis” of the Russian banking sector provides a clear example of its exploitative nature. Banks isolated themselves, not looking after manufacturing and its timely modernization, and by simply robbing it, which did not even permit normal growth. Thus the role of private banking in our economic situation has been exceptionally negative.

### **Raw Materials Industries and Manufacturing**

The Soviet economy’s imbalance in favor of raw materials extraction as opposed to manufactures has been surpassed in the current economy. A market system should stimulate high-tech development and increase the share of manufacturing and production in the economy. Arms reduction processes created opportunities for military conversion to increase our export potential and move a variety of domestic products into the worldwide marketplace.

But “radical-destructive” elements (individuals) did not need this “light at the end of the tunnel,” seeing their interests from a different perspective.

Manufacturing industries, especially high-tech and efficient organizations of the military-industrial complex, underwent purposeful and severe reductions as high-quality professionals were denied regular salaries or unceremoniously fired from their jobs.

Today, production has stopped in those industries, and high levels of unemployment and poverty are typical. As a result, the share of raw material industries in total production has risen from 11.6 percent to 33.4 percent while manufacturing has decreased. This can be seen as a substantial decrease in the efficiency of the economy.

## **Domestic and Foreign Economic “Hero Strata”**

In the course of the recent seven years, the top strata of the Russian economy has been very proud of the results of its transformation, explaining it as the “destruction of the command-administrative economic system.” In reality, their “reforms” have led the country to an unprecedented collapse of production, investment, commodity usage, levels of employment and living standards.

The facts lead many of us to the thought that the important cause of failure of our “reforms” (contrary to the Chinese experience), is the conclusion that the reforms were conceived not by us and not in our best interests, but by others in their own interest. So that those thoughts not be seen as extreme leftist fantasies, I would refer to an article in the New York Times (September, 1998), which called our economy an “Oligarchy of Thieves.” A substantial number of the West’s independent and competent economists understand the failure of Russian reforms as showing that they were implemented not in the best interests of the country and its people, but mainly in the interests of the West.

Thus, American scientist James Angresano, has compared the free market reforms in China with those of Central and Eastern Europe. He explains the success of the first and the failure of the second by uncovering substantial differences in the concepts and strategies. He shows that China has been implementing its reforms in conformity with an advanced concept of a “planned-market economy” based on the best interests of the nation and the needs of its population.

In contrast, the Eastern European countries, including Russia, followed the recommendations of the international organizations. Angresano wrote: “From the early 90’s, those countries’ objectives for transformation were based on the interests of the West and were guided by ideological postulates of neoclassical theory with an aspiration to provide new markets for Western exports, secure access to raw materials, and increased political influence in the entire region.” Consequently, as China achieves new heights in its GDP and finds its way into the ranks of developed countries, Russia has followed IMF recommendations and is sinking to the level of countries of the third world.

Recently, Prof. M. Chosudovsky of Canada published “The Globalization of Poverty” where he shows the negative role of IMF activity on the fate of its client countries. One chapter of the book devoted to Russia has the title, “Transformation of the Russian Federation to a Third World Country.”

Our current situation should not be considered a result of near-sighted and incompetent political activity of the Russian government. It is a consequence of the fact that its policy was developed and implemented on the basis of recommendations of international organizations and a range of Western consultants and specialists. Dissenting from this chosen policy, qualified domestic professionals were not even allowed into the reform process. Also, by tradition from the Soviet past, they were put under pressure and discredited by most of the mass media.

## **Using Our Own Experience with that of Others**

When government leadership was given to Yevgeny Primakov, there was new hope for the development and implementation of truly free market reforms in the best interests of the country and its people. To accomplish this, we will need to make a larger effort than yet envisioned. We will need new solutions, which will incorporate our own experience with the experiences of others.

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