Currency Tribulations

In Search of...the "Ruble Zone"

By Lynda L. Maillet

The once Soviet, now Russian, ruble has fallen dramatically in value over the past year, from R30 to the dollar only last summer to as low as R350 to the dollar in October 1992. Much of the blame for this falls on the monetary authorities of Russia and other republics, who have overseen a sharp jump in money creation. The prime beneficiaries of this, the large state enterprises in Russia and elsewhere, have emerged as a powerful political force; the growing influence of a coalition favoring expansion has added considerable unease into Russia's negotiations with the International Monetary Fund.

Although the ruble remains an inconvertible currency, a first step towards convertibility was taken on 1 July, when the Russian government introduced a single exchange rate for the ruble set by domestic currency markets (the official rate is now based on the ruble's trading price at the Inter-Bank Currency Exchange, which holds auctions twice a week). Up to that point, the government had set several different rates for the ruble (commercial, tourist, etc.), most of them artificially overvalued. The ruble is also convertible domestically, meaning that domestic firms may purchase foreign exchange in order to finance imports or to remit profits to a foreign parent firm. At a later date, the rate of the ruble will be pegged, probably to the dollar (the date, however, continues to be put off). Though domestic convertibility has been largely achieved, convertibility in international payments—meaning that the ruble is accepted as payment for foreign trade and debts—will be a very long time in coming. Only twenty or so countries' currencies are accepted worldwide; a more limited convertibility could be in the ruble's future if its exchange rate is stabilized and there is more confidence in the Russian economy.

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The continued fall of the ruble has been a result of the lax monetary policy of the Russian Central Bank (RCB) and the irresponsible policies of the other former Soviet republics which continue to use the ruble. Much of the blame for this recent drop has fallen on the shoulders of the new chairman of the RCB, Viktor Gerashchenko. His predecessor, Georgiy Matyukhin, had succeeded, with a fairly strict monetary policy, in stabilizing the ruble to some extent through mid-summer. In contrast, Gerashchenko has greatly expanded credit to failing state industries in order to thwart a looming fall in production and the consequent unemployment. At the same time, the new chairman said that the RCB could no longer afford to prop up the ruble by intervening in hard currency auctions. While inflation had subsided somewhat over the summer to about 10% a month, wages rose about 35% a month over the same period, paid for by RCB credits. The flood of new money into the economy triggered the recent fall of the ruble and will most likely accelerate inflation this fall.

The ruble zone

The Russian ruble continues to serve as the official currency of fourteen of the fifteen former Soviet republics so that the RCB's decisions affect all of these republics without their input. Only Estonia has introduced its own currency, the kroon, and follows a completely independent monetary policy. Despite the fact that they all use the ruble, most republics follow their own monetary policies without any central coordination. While the Russian Central Bank had been attempting to bring inflation under control and stabilize the ruble rate, many republics have taken actions which directly undermine the RCB's efforts. Most have been printing their own bank notes or coupons to make up for a deficiency of rubles; they blame Russia for not supplying them with enough ruble notes. They have also been issuing ruble credits to their enterprises who, in turn, use them to pay Russian enterprises (and the RCB feels politically obliged to make good on these fabricated credits). The net effect of these policies has been to weaken the ruble.

The economies of the former Soviet Union are unusual in that nearly all transactions—especially those made by workers and consumers—are made in cash; bank checks and debit cards are quite rare. As a result, a loose monetary policy usually involves actually printing currency notes; deficits cannot be financed in any effective way at the moment. On the other

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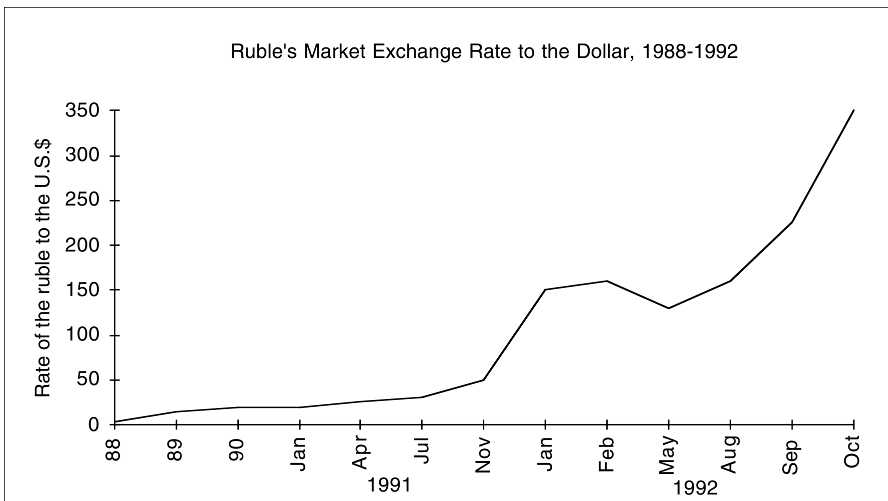
hand, a tight monetary policy requires reductions in the amount of currency produced, leading to note shortages which make it difficult to meet payrolls and which put a brake on economic activity.

Russian officials have had no mechanism by which they can impose discipline on the policies of the other republics; by withholding cash, they have merely exacerbated the careless manner in which many of the other republics have issued their own coupons to be used alongside the ruble. At the same time, the Russians do not want to provide the republics with an unlimited supply of rubles for fear of further devaluing their own currency.

Even though they all use the ruble, most republics follow their own monetary policies without any coordination.

Under pressure from the International Monetary Fund, Russian Central Bank officials are forcing the other republics to choose whether or not they want to remain in the "ruble zone." Remaining in the zone would mean the republic would have to obey the dictates of the RCB. If they decide to opt out, they must negotiate with the RCB conditions for establishing a separate currency, to be coordinated by the Interbank Coordination Council of Central Banks formed in May 1992 in Bishkek. Most republics have already stated their desire to remain in the ruble zone, but except for Belarus they have not yet agreed to abide by RCB policies. Uzbek and other officials are still concerned about the shortage of rubles, which has already resulted in many workers going unpaid. As in other republics, they are threatening to print coupons to make up the deficiency. Many of the republics have not completely eliminated the option of introducing their own currency. A national currency would mean political and economic independence from Russia; they would not have to subordinate their economic policies to coordination by the RCB. However, it would greatly hinder interrepublic trade and may cause hardships in the republics which rely on energy exports from Russia.



Ruble stabilization fund

Once certain conditions are met, the IMF has promised to provide a $6 billion ruble stabilization fund as the third stage of a larger $24 billion aid package. The stabilization fund would serve mostly as psychological support for the ruble, giving the RCB the means to intervene to support it in times of crisis. The recently approved first stage of credits (about $1 billion) is intended to help reduce inflation and reinforce structural reforms. One of the primary terms of the agreement is to bring the RCBs liberal lending policies under control—which will help bring down the budget deficit (from 17% of GDP to 5%) and inflation (from 15% a month to less than 10%). Russia must also have an agreement on monetary coordination with other states of the ex-USSR remaining in the ruble zone in order to have access to the next stages of financial support. The ruble stabilization fund will not become available until the beginning of next year at the earliest and not until the exchange rate has stabilized. Once the fund is in place, Russians are hoping that it will restore badly needed confidence in their economy and attract foreign investors.

Plans for convertibility of the ruble have been set aside, at least for this year. The government will be focusing on privatization plans which may help with ruble stabilization by giving investors opportunities to spend their rubles on assets other than hard currencies. ◊

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