

The Coming Unemployment Crisis in Russia

Stephen Hanson

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University of Washington

There can be little doubt that open unemployment in the Russian Federation is going to rise dramatically over the next few years. Currently, approximately 10% of the Russian population is out of work--a figure about triple the rate in 1992 at the outset of Yeltsin's market reforms, and comparable to unemployment rates in Western European countries such as France and Germany that are experiencing considerable social unrest about the problem. However, even this serious rate of unemployment in Russia could easily double, given the continuing need for extensive layoffs to increase Russia's productive efficiency in both industry and agriculture. Proposed substantial cuts in the military, while welcome in most respects, will add to this problem. Yet few analysts seem aware of the potentially dramatic effects that the predictable increase in joblessness might have on Russian domestic politics, Russian foreign policy, and the US-Russian relationship. Thinking through some of these effects in advance may help Western policymakers to avoid some rather unpleasant political shocks.

The problem of unemployment has thus far been a low priority for analysts of Russia's democratic and market transitions. Unlike in East-Central Europe, where (except in the Czech republic) the percent of the labor force looking for work has been stuck in the mid-teens through most of the 1990s, Russia has been able to limit unemployment to single digit rates. The seriousness of other economic and social problems, such as inflation, crime, and the growing power of various "mafias," has until recently captured most of the attention of both policymakers and the Russian public. However, Russia's "success" in dealing with unemployment has been achieved through temporary expedients that are not economically sustainable. The structural legacies of the Stalinist economic system that have inhibited the formation of a fully functioning labor market are only now being confronted directly.

From the 1930s until the late Gorbachev era, managers of Soviet enterprises and farms were judged according to the simple criterion of gross output to "fulfill and overfulfill" plan targets. Since efficiency in the utilization of inputs was rarely taken into consideration by the planning authorities, there was no incentive to fire unproductive or poorly-trained workers; in fact, factories and farms benefitted from the presence of large numbers of excess workers who could be called upon to contribute to the monthly and yearly "storming" efforts to meet production goals, and whose wages were in any case paid by the state. Additionally, possession of a large labor force in the Soviet period tended to increase a manager's political clout with his Communist Party bosses. Soviet workers, while suffering both from the arbitrary hierarchical rule of state and party bureaucrats and the generally low standard of living characteristic of Soviet-type economies, nevertheless did enjoy significant bargaining power due to the endless demand for labor generated by the Stalinist system. Skilled laborers could bid up their compensation--primarily nonwage benefits such as subsidized housing, health care, child care, and vacation facilities sponsored by individual enterprises--while unskilled (and even drunk or

apathetic) workers could rest assured that they would not be kicked out onto the street. Thus, the vast majority of enterprises and farms entered the post-Soviet period with bloated, largely undisciplined workforces, huge welfare budgets, and hopelessly outdated technologies. Clearly, genuine market competition would necessitate an unprecedented wave of "downsizing" throughout the Russian economy.

However, from 1992-1993, during the political struggle between Yeltsin and the Russian Congress of People's Deputies, layoffs at most enterprises and farms were rendered unnecessary due to massive monetary subsidies from the Central Bank of Russia (CBR), then under the control of forces opposed to Western-style economic reforms. The round-the-clock printing of rubles by the CBR led to near-hyperinflation, but also held official joblessness to just 3% of the workforce. After Yeltsin's defeat of the Congress in 1993, a policy of relative monetary and fiscal austerity was adopted in close consultation with the International Monetary Fund (IMF). Yet even after 1994 formal dismissal of workers has remained much rarer than might have been expected. Many enterprises threatened with bankruptcy did not undergo serious restructuring, but instead managed to carry on through such expedients as barter transactions, nonpayment of taxes, nonpayment of energy bills, and, most crucially, nonpayment of wages.

Meanwhile, many workers continued to show up for work even after not being paid for months at a time, in order to remain eligible for the continuing welfare services still provided by enterprises--including hot meals at the workplace. In many cases, too, workers continued to expect that at some point back wages would be paid to those who were still around to demand them. Such expectations were sustained by the opaque privatization process adopted in many old Soviet state enterprises, the majority of which were simply officially handed over to their "workers' collectives," guided in most cases by their old Soviet management. Since privatization had been portrayed in the media as a great boon to the public, it was hard to explain to workers that their new status as "owners" of factories made their jobs more, not less, vulnerable. Nor was public awareness of the necessity of job losses under capitalism heightened by Yeltsin's continual high-profile campaigns to pay back all wage arrears--a pledge which, it was rarely emphasized, did not apply to the two-thirds of the Russian economy that had been officially "privatized."

Only now it is finally becoming clear to many workers throughout the Russian Federation that their old jobs are gone for good. Of course many younger, more skilled, more educated, and more mobile workers left the old Soviet sector long ago to find work in new businesses, in Moscow, in joint ventures with foreign concerns, and abroad. Unfortunately, this means that it is precisely the least adaptable workers who are going to bear the brunt of the job losses in the years to come. For this group--perhaps 10% of the Russian workforce--open unemployment will come on top of years of failed perestroika reforms that destroyed the Soviet Union, years of high inflation that wiped out personal savings, and years of unfulfilled promises that Yeltsin's regime would stop the wage arrears crisis. It would be surprising indeed if the final blow of mass firings did not produce enormous, and concentrated, social unrest. This wave of anger is likely even if, as is forecast, Russia's economy at last returns to positive growth in 1998. Growth in postcommunist economies generally begins in the big cities, in the service sector, in small businesses, and in foreign trade; throughout the former Soviet bloc, agriculture and medium-sized industrial towns have continued to suffer long after the rest of the economy recovers. Given

the age, training, and cultural background of post-Soviet workers in the most distressed regions, it seems unlikely that many of them will find employment in the leading economic sectors, which tend to look for young, English-speaking, and culturally-flexible employees.

Why does the coming unemployment crisis in Russia matter to the US? To begin with, it is important to emphasize that many of the blue-collar workers who will be most affected by unemployment have been, until now, staunch supporters of Boris Yeltsin in national elections. In almost every industrial region of the Russian Federation, the Communist Party challenger Zyuganov lost the second round of balloting by significant margins; the Communists achieved majorities only in predominantly rural areas. Urban voters in medium-sized cities have, in short, rejected the past regime quite decisively. They know perfectly well from experience that "revolutionary" state planning does not work, that a system that eliminates the market ends up rewarding the corrupt and the lazy, and that an ideology mandating a single political "truth" produces a society based on lies. However, these voters cannot be assumed to favor Westernization at all costs to their own families' livelihood--particularly if "Westernization" appears to involve a continuous attack on the security of the poor while the sleaziest and most violent members of society become rich and powerful. Indeed, voters who are officially unemployed--as opposed to being semi-employed in semi-privatized industries--have tended to favor explicitly anti-democratic candidates such as Alexander Lebed and, even more disturbingly, Vladimir Zhirinovskiy, whose 5.8% of the presidential vote in the first round remains more worrisome than is generally recognized. The upper class, educated young people, and most intellectuals, it is true, can probably be counted on to vote for Westernizers. But these groups make up at most 25% of the population. A swing of 10% of the electorate toward an anti-Western, anti-communist candidate in the year 2000 could easily result in a run-off between Zyuganov and a fascist challenger, especially given continuing divisions among self-identified "liberal" candidates for the presidency in the wake of Yeltsin's departure. Considering that Russia is still a nuclear power--however militarily weak at present--such a scenario should provoke genuine concern.

Is there really anything the United States and Western Europe can do about this situation? The wave of open unemployment coming to Russia cannot be remedied by a return to the failed policies of the Soviet past, nor will resuming the inflationary rouble-printing of 1992-93 help anyone (other than corrupt bankers). The sad fact is that Russians will be paying for Stalinism for a long time to come, regardless of what macroeconomic policies are adopted by Moscow or advocated by the West. Still, the above analysis suggests that there are some obvious mistakes Western policymakers must avoid.

First, it is a mistake for international financial institutions such as the IMF and the World Bank to push Yeltsin and his team to end all remaining housing subsidies by the year 2002, as is currently planned. Economically, of course, continuing the inefficient heating of old Soviet flats at almost no cost to consumers is an enormous waste. But socially, it is one of the best investments imaginable. The ability to stay in one's apartment and keep warm, as well as to grow fruits and vegetables on one's private plot or dacha, has kept many impoverished Russians from total catastrophe. The public demand of Western advisors to Yeltsin that such subsidies be quickly eliminated thus reinforces the most extreme Russian conspiracy theories about the West's ultimately "genocidal" goals. New housing, of course, must be constructed with

individual meters for gas and electricity; those who can afford to buy private residences must be made to pay their utilities in full. But the effort to force the part of the population now faced with mounting job losses to do the same is both wrongheaded and shortsighted.

Second, the US and the EU must work harder to lower trade barriers to Russian manufactured goods and agricultural products. If there is any hope for a successful market restructuring of former Soviet firms and farms that might eventually generate good new jobs in the places they are most needed, the process will have to begin with increased sales of Russian goods abroad. The Russian domestic market has the potential for enormous expansion in ten to twenty years, but for the next decade or so the lack of disposable income of so many Russians will sharply limit sales of Russian goods at home. The chief comparative advantage of Russian producers, then, for the time being, will be their ability to charge low prices due to shrinking labor costs. If this advantage is nullified by Western protectionism, charges of hypocrisy leveled at Western advocates of the "free market" would be quite understandable.

Finally, foreign aid to Russia must be directed in such a way as to maximize its welfare effects. Support for small business, especially in the Russian regions, is extremely important in this regard. Aid for the reconstruction of outdated Soviet nuclear power plants and gas and oil pipelines would serve the twin goals of reducing the danger of an environmental cataclysm as well as lowering the price of energy for homes and businesses. Efforts to help Russians move from dying industrial cities, particularly in the Far North, would help to increase labor mobility as well as demonstrating Western concern for ordinary people's fates. Indeed, even a minimal effort by Western leaders publicly to address the problems facing poorer Russians might be crucial in undermining the potentially growing support for anti-liberal politicians in the years to come.