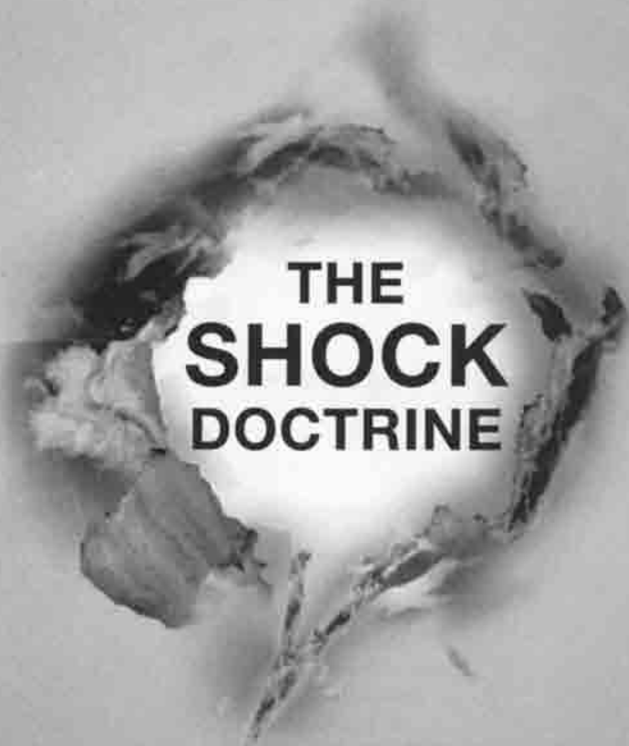

THE SHOCK DOCTRINE

THE RISE OF DISASTER CAPITALISM

. . .

NAOMI KLEIN

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Pieces of a living city cannot be auctioned off without taking into consideration that there are indigenous traditions, even if they seem odd to foreigners. . . . But these are our traditions and our city. For a long time we lived under the dictatorship of the Communists, but now we have found out that life under the dictatorship of business people is no better. They couldn't care less about what country they are in.

—Grigory Gorin, Russian writer, 1993[1]

Spread the truth—the laws of economics are like the laws of engineering. One set of laws works everywhere.

—Lawrence Summers, chief economist of the World Bank, 1991[2]

When Soviet president Mikhail Gorbachev flew to London to attend his first G7 Summit in July 1991, he had every reason to expect a hero's welcome. For the previous three years, he had seemed not so much to stride across the international stage as to float, charming the media, signing disarmament treaties and picking up peace prizes, including the Nobel in 1990.

He had even managed to do the previously unthinkable: win over the American public. The Russian leader so thoroughly challenged Evil Empire caricatures that the U.S. press had taken to calling him by a cuddly nickname, "Gorby," and in 1987, *Time* magazine took the risky decision of making the Soviet president their Man of the Year. The editors explained that unlike his predecessors ("gargoyles in fur hats"), Gorbachev was Russia's own Ronald Reagan—"a Kremlin version of the Great Communicator." The Nobel Prize committee declared that thanks to his work, "It is our hope that we are now celebrating the end of the Cold War."[3]

By the beginning of the nineties, with his twin policies of *glasnost* (openness) and *perestroika* (restructuring), Gorbachev had led the Soviet Union through a remarkable process of democratization: the press had been freed, Russia's parliament, local councils, president and vice president had been elected, and the constitutional court was independent. As for the economy, Gorbachev was moving toward a mixture of a free market and a strong safety net, with key industries under public control—a process he predicted would take ten to fifteen years to be completed. His end goal was to build social democracy on the Scandinavian model, "a socialist beacon for all mankind."[4]

At first it seemed that the West also wanted Gorbachev to succeed in loosening up the Soviet economy and transforming it into something close to Sweden's. The Nobel Committee explicitly described the prize as a way of offering support to the transition—"a helping hand in an hour of need." And on a visit to Prague, Gorbachev made it clear that he couldn't do it all alone: "Like mountain climbers on one rope, the world's nations can either climb together to the summit or fall together into the abyss," he said.[5]

So what happened at the G7 meeting in 1991 was totally unexpected. The nearly unanimous message that Gorbachev received from his fellow heads of state was that, if he did not embrace radical economic shock therapy immediately, they would sever the rope and let him fall. "Their suggestions as to the tempo and methods of transition were astonishing," Gorbachev wrote of the event.[6]

Poland had just completed its first round of shock therapy under the IMF's and Jeffrey Sachs's tutelage, and the consensus among British prime minister John Major, U.S. president George H. W. Bush, Canadian prime minister Brian Mulroney and Japanese prime minister Toshiki Kaifu was that the Soviet Union had to follow Poland's lead on an even faster timetable. After the meeting, Gorbachev got the same marching orders from the IMF, the World Bank and every other major lending institution. Later that year, when Russia asked for debt forgiveness to weather a catastrophic economic crisis, the stern answer was that the debts had to be honored.[7] Since the time when Sachs had marshaled aid and debt relief for Poland, the political mood had changed—it was meaner.

What happened next—the dissolution of the Soviet Union, Gorbachev's eclipse by Yeltsin, and the tumultuous course of economic shock therapy in Russia—is a well-documented chapter of contemporary history. It is, however, a story too often told in the bland language of "reform," a narrative so generic that it has hidden one of the greatest crimes committed against a democracy in modern history. Russia, like China, was forced to choose between a Chicago School economic program and an authentic democratic revolution. Faced with that choice, China's leaders had attacked their own people in order to prevent democracy from disturbing their free-market plans. Russia was different: the democratic revolution was already well under way—in order to push through a Chicago School economic program, that peaceful and hopeful process that Gorbachev began had to be violently interrupted, then radically reversed.

Gorbachev knew that the only way to impose the kind of shock therapy being advocated by the G7 and the IMF was with force—as did many in the West pushing for these policies. *The Economist* magazine, in an influential 1990 piece, urged Gorbachev to adopt "strong-man rule . . . to smash the resistance that has blocked serious economic reform."[8] Only two weeks after the Nobel Committee had declared an end to the Cold War, *The Economist* was urging Gorbachev to model himself after one of the Cold War's most notorious killers. Under the heading "Mikhail Sergeevich Pinochet?" the article concluded that even though following its advice could cause "possible blood-letting . . . it might, just might, be the Soviet Union's turn for what could be called the Pinochet approach to liberal economics." *The Washington Post* was willing to go further. In August 1991, the paper ran a commentary under the headline "Pinochet's Chile a Pragmatic Model for Soviet Economy." The article supported the idea of a coup for getting rid of the slow-going Gorbachev, but the author, Michael Schrage, worried that the Soviet president's opponents "had neither the savvy nor the support to seize the Pinochet option." They should model themselves, Schrage wrote, after "a despot who really knew how to run a coup: retired Chilean general Augusto Pinochet."[9]

Gorbachev soon found himself facing an adversary who was more than willing to play the role of a Russian Pinochet. Boris Yeltsin, though holding the post of Russian president, had a much lower profile than Gorbachev, who headed all the Soviet Union. That was to change dramatically on August 19, 1991, one month after the G7 Summit. A group from the Communist old guard drove tanks up to the White House, as the Russian parliament building is called. In a bid to halt the democratization process, they threatened to attack the country's first elected parliament. Amid a crowd of Russians determined to defend their new democracy, Yeltsin stood on one of the tanks and denounced the aggression as "a cynical, right-wing coup attempt."[10] The tanks retreated, and Yeltsin emerged as a courageous defender of democracy. One demonstrator who stood in the streets that day described it as "the first time I felt that I could really affect the situation in my country. Our souls soared. It was such a feeling of unity. We felt invincible."[11]

And so did Yeltsin. As a leader, he had always been a kind of anti-Gorbachev. Where Gorbachev had projected propriety and sobriety (one of his most controversial measures was an aggressive anti-vodka-drinking campaign), Yeltsin was a notorious glutton and a heavy drinker. Prior to the coup, many Russians harbored reservations about Yeltsin, but he had helped save democracy from a Communist coup, and that made him, at least for the time being, a people's hero.

Yeltsin immediately parlayed his triumphant showdown into increased political power. As long as the Soviet Union remained intact, he would always have less control than Gorbachev, but in December 1991, four months after the aborted coup, Yeltsin pulled off a political masterstroke. He formed an alliance with two other Soviet republics, a move that had the effect of abruptly dissolving the Soviet Union, thereby forcing Gorbachev's resignation. The abolition of the Soviet Union, "the only country most Russians had ever known," was a powerful shock to the Russian psyche—and as the political scientist Stephen Cohen put it, it was the first of "three traumatic shocks" that Russians would endure over the next three years.[12]

Jeffrey Sachs was in the room at the Kremlin on the day Yeltsin announced that the Soviet Union was no more. Sachs recalled the Russian president saying, "'Gentlemen, I just want to announce that the Soviet Union has ended. . . .' And I said, 'Gee, you know, this is once in a century. This is the most incredible thing you can imagine; this is a true liberation; let's help these people.'"[13] Yeltsin had invited Sachs to come to Russia to serve as an adviser, and Sachs was more than game: "If Poland can do it, so can Russia," he declared.[14]

But Yeltsin didn't just want advice, he wanted the kind of gold-plated fund-raising that Sachs had pulled off for Poland. "The only hope," Yeltsin said, "was the promises of the Group of Seven quickly to grant us large sums of financial aid."[15] Sachs told Yeltsin he was confident that if Moscow was willing to go with the "big bang" approach to establishing a capitalist economy, he could raise something in the area of $15 billion.[16] They would need to be ambitious, and they would need to move fast. What Yeltsin did not know was that Sachs's luck was about to run out.

Russia's conversion to capitalism had much in common with the corrupt approach that had sparked the Tiananmen Square protests in China two years earlier. Moscow's mayor, Gavriil Popov, has claimed that there were really only two options for how to break up the centrally controlled economy: "Property can be divided among all members of society, or the best pieces can be given to the leaders. . . . In a word, there's the democratic approach, and there's the nomenklatura, apparatchik approach."[17] Yeltsin took the latter approach—and he was in a hurry. In late 1991, he went to the parliament and made an unorthodox proposal: if they gave him one year of special powers, under which he could issue laws by decree rather than bring them to parliament for a vote, he would solve the economic crisis and give them back a thriving, healthy system. What Yeltsin was asking for was the kind of executive power enjoyed by dictators, not democrats, but the parliament was still grateful to the president for his role during the attempted coup, and the country was desperate for foreign aid. The answer was yes: Yeltsin could have one year of absolute power to remake Russia's economy.

He immediately assembled a team of economists, many of whom, in the final years of Communism, had formed a kind of free-market book club, reading the basic texts of the Chicago School thinkers and discussing how the theories could be applied in Russia. Though they had never studied in the U.S., they were such devoted fans of Milton Friedman that the Russian press took to calling Yeltsin's team "the Chicago Boys," a knock-off of the original title, and fitting in the context of Russia's thriving black market economy. In the West they were dubbed "the young reformers." The group's figurehead was Yegor Gaidar, whom Yeltsin named as one of his two deputy prime ministers. Pyotr Aven, a Yeltsin minister in 1991–92 who was part of this inner circle, said of his former clique, "Their identification of themselves with God, which flowed naturally from their belief in their all-round superiority, was, unfortunately, typical of our reformers."[18]

Surveying the group that had suddenly ascended to power in Moscow, the Russian newspaper *Nezavisimaya Gazeta* observed the rather astonishing development that "for the first time Russia will get in its government a team of liberals who consider themselves followers of Friedrich von Hayek and the 'Chicago school' of Milton Friedman." Their policies were "quite clear—'strict financial stabilization' according to 'shock therapy' recipes." At the same time as Yeltsin made these appointments, the newspaper noted, he had also put the notorious strongman Yury Skokov "in charge of the defense and repressive departments: the Army, the Ministry of Internal Affairs and the State Security Committee." The decisions were clearly connected: "Probably the 'strong' Skokov can 'ensure' strict stabilization in politics while the 'strong' economists guarantee it in the economy." The article ended with a prediction: "It will come as no surprise if they attempt to construct something like a homegrown Pinochet system, in which the role of the 'Chicago boys' will be played by Gaidar's team."[19]

To provide ideological and technical backup for Yeltsin's Chicago Boys, the U.S. government funded its own transition experts whose jobs ranged from writing privatization decrees, to launching a New York–style stock exchange, to designing a Russian mutual fund market. In the fall of 1992, USAID awarded a $2.1 million contract to the Harvard Institute for International Development, which sent teams of young lawyers and economists to shadow the Gaidar team. In May 1995, Harvard named Sachs director of the Harvard Institute for International Development, which meant that he played two roles in Russia's reform period: he began as a freelance adviser to Yeltsin, then moved on to overseeing Harvard's large Russia outpost, funded by the U.S. government.

Once again a group of self-described revolutionaries huddled in secret to write a radical economic program. As Dimitry Vasiliev, one of the key reformers, recalled, "At the start, we didn't have a single employee, not even a secretary. We didn't have any equipment, not even a fax machine. And in those conditions, in just a month and a half, we had to write a comprehensive privatization program, we had to write twenty normative laws. . . . It was a really romantic period."[20]

On October 28, 1991, Yeltsin announced the lifting of price controls, predicting that "the liberalization of prices will put everything in its right place."[21] The "reformers" waited only one week after Gorbachev resigned to launch their economic shock therapy program—the second of the three traumatic shocks. The shock therapy program also included free-trade policies and the first phase of the rapid-fire privatization of the country's approximately 225,000 state-owned companies.[22]

"The country was taken by surprise by the 'Chicago School' program," one of Yeltsin's original economic advisers recalled.[23] That surprise was deliberate, part of Gaidar's strategy of unleashing change so suddenly and quickly that resistance would be impossible. The problem his team was up against was the usual one: the threat of democracy obstructing their plans. Russians did not want their economy organized by a Communist central committee, but most still believed firmly in wealth redistribution and in an activist role for government. Like the Polish supporters of Solidarity, 67 percent of Russians told pollsters in 1992 they believed workers' cooperatives were the most equitable way to privatize the assets of the Communist state, and 79 percent said they considered maintaining full employment to be a core function of government.[24] That meant that if Yeltsin's team had submitted their plans to democratic debate, rather than launching a stealth attack on an already deeply disoriented public, the Chicago School revolution would not have stood a chance.

Vladimir Mau, an adviser to Boris Yeltsin in this period, explained that "the most favorable condition for reform" is a "weary public, exhausted by the previous political struggle. . . . That is why the government was confident, on the eve of price liberalization, that a drastic social clash was impossible, that the government would not be overthrown by a popular revolt." The vast majority of Russians—70 percent—were opposed to lifting price controls, he explained, but "we could see that the people, then and now, were concentrating on the yields of their private [garden] plots and in general on their individual economic circumstances."[25]

Joseph Stiglitz, who at the time was serving as chief economist at the World Bank, summarized the mentality that guided the shock therapists. His metaphors should by now be familiar: "Only a blitzkrieg approach during the 'window of opportunity' provided by the 'fog of transition' would get the changes made before the population had a chance to organize to protect its previous vested interests."[26] In other words, the shock doctrine.

Stiglitz called Russia's reformers "market Bolsheviks" for their fondness for cataclysmic revolution.[27] However, where the original Bolsheviks fully intended to build their centrally planned state in the ashes of the old, the market Bolsheviks believed in a kind of magic: if the optimal conditions for profit making were created, the country would rebuild itself, no planning required. (It was a faith that would reemerge, a decade later, in Iraq.)

Yeltsin made wild promises that "for approximately six months, things will be worse," but then the recovery would begin, and soon enough Russia would be an economic titan, one of the top four economies in the world.[28] This logic of so-called creative destruction resulted in scarce creation and spiraling destruction. After only one year, shock therapy had taken a devastating toll: millions of middle-class Russians had lost their life savings when money lost its value, and abrupt cuts to subsidies meant millions of workers had not been paid in months.[29] The average Russian consumed 40 percent less in 1992 than in 1991, and a third of the population fell below the poverty line.[30] The middle class was forced to sell personal belongings from card tables on the streets—desperate acts that the Chicago School economists praised as "entrepreneurial," proof that a capitalist renaissance was indeed under way, one family heirloom and second-hand blazer at a time.[31]

As in Poland, Russians did, eventually, regain their bearings and began to demand an end to the sadistic economic adventure ("no more experiments" was a popular piece of graffiti in Moscow at the time). Under pressure from voters, the country's elected parliament—the same body that had supported Yeltsin's rise to power—decided it was time to rein in the president and his ersatz Chicago Boys. In December 1992, they voted to unseat Yegor Gaidar, and three months later, in March 1993, the parliamentarians voted to repeal the special powers they had given to Yeltsin to impose his economic laws by decree. The grace period had expired, and the results were abysmal; from now on, laws had to go through parliament, a standard measure in any liberal democracy and following the procedures set out in Russia's constitution.

The deputies were acting within their rights, but Yeltsin had grown accustomed to his augmented powers and had come to think of himself less as a president and more as a monarch (he had taken to calling himself Boris I). He retaliated against the parliament's "mutiny" by going on television and declaring a state of emergency, which conveniently restored his imperial powers. Three days later, Russia's independent Constitutional Court (the creation of which was one of Gorbachev's most significant democratic breakthroughs) ruled 9–3 that Yeltsin's power grab violated, on eight different counts, the constitution he had sworn to uphold.

Until this point, it had still been possible to present "economic reform" and democratic reform as part of the same project in Russia. But once Yeltsin declared a state of emergency, the two projects were on a collision course, with Yeltsin and his shock therapists in direct opposition to the elected parliament and the constitution.

Nevertheless, the West threw its weight behind Yeltsin, who was still cast in the role of a progressive "genuinely committed to freedom and democracy, genuinely committed to reform," in the words of then U.S. president Bill Clinton.[32] The majority of the Western press also sided with Yeltsin against the entire parliament, whose members were dismissed as "communist hardliners" trying to roll back democratic reforms.[33] They suffered, according to the *New York Times* Moscow bureau chief, from "a Soviet mentality—suspicious of reform, ignorant of democracy, disdainful of intellectuals or 'democrats.'"[34]

In fact, these were the same politicians, for all their flaws (and with 1,041 deputies there were plenty), who had stood with Yeltsin and Gorbachev against the coup by the hardliners in 1991, who had voted to dissolve the Soviet Union and who had, until recently, thrown their support behind Yeltsin. Yet *The Washington Post* opted to cast Russia's parliamentarians as "antigovernment"—as if they were interlopers and not themselves part of the government.[35]

In the spring of 1993, the collision drew closer when parliament brought forward a budget bill that did not follow IMF demands for strict austerity. Yeltsin responded by trying to eliminate the parliament. He hastily threw together a referendum, supported in Orwellian fashion by the press, which asked voters if they agreed to dissolve parliament and hold snap elections. Not enough voters turned out to give Yeltsin the mandate he needed. He still claimed victory, however, maintaining that the exercise proved the country was behind him, because he had slipped in an entirely non-binding question about whether voters supported his reforms. A slim majority said yes.[36]

In Russia, the referendum was widely seen as a propaganda exercise, and a failed one at that. The reality was that Yeltsin and Washington were still stuck with a parliament that had the constitutional right to do what it was doing: slowing down the shock therapy transformation. An intense pressure campaign began. Lawrence Summers, then U.S. Treasury undersecretary, warned that "the momentum for Russian reform must be reinvigorated and intensified to ensure sustained multilateral support."[37] The IMF got the message, and an unnamed official leaked to the press that a promised $1.5 billion loan was being rescinded because the IMF was "unhappy with Russia's backtracking on reforms."[38] Pyotr Aven, the former Yeltsin minister, said, "The maniacal obsession of the IMF with budgetary and monetary policy, and its absolutely superficial and formal attitude to everything else . . . played not a small role in what happened."[39]

What happened was that the day after the IMF leak, Yeltsin, confident that he had the West's support, took his first irreversible step toward what was now being openly referred to as the "Pinochet option": he issued decree 1400, announcing that the constitution was abolished and parliament dissolved. Two days later, a special session of parliament voted 636–2 to impeach

Yeltsin for this outrageous act (the equivalent of the U.S. president unilaterally dissolving Congress). Vice President Aleksandr Rutskoi announced that Russia had already "paid a dear price for the political adventurism" of Yeltsin and the reformers.[40]

Some kind of armed conflict between Yeltsin and the parliament was now inevitable. Despite the fact that Russia's Constitutional Court once again ruled Yeltsin's behavior unconstitutional, Clinton continued to back him, and Congress voted to give Yeltsin $2.5 billion in aid. Emboldened, Yeltsin sent in troops to surround the parliament and got the city to cut off power, heat and phone lines to the White House parliament building. Boris Kagarlitsky, director of the Institute of Globalization Studies in Moscow, told me that supporters of Russian democracy "were coming in by the thousands trying to break the blockade. There were two weeks of peaceful demonstrations confronting the troops and police forces, which led to partial unblocking of the parliament building, with people able to bring food and water inside. Peaceful resistance was growing more popular and gaining broader support every day."

With each side becoming more entrenched, the only compromise that could have resolved the standoff would have been for both sides to agree to early elections, putting everybody's job up for public review. Many were urging this outcome, but just as Yeltsin was weighing his options, and reportedly leaning toward elections, news came from Poland that voters had rained down their decisive punishment on Solidarity, the party that had betrayed them with shock therapy.

After they witnessed Solidarity get pounded at the polls, it was obvious to Yeltsin and his Western advisers that early elections were far too risky. In Russia, too much wealth hung in the balance: huge oil fields, about 30 percent of the world's natural gas reserves, 20 percent of its nickel, not to mention weapons factories and the state media apparatus with which the Communist Party had controlled the vast population.

Yeltsin abandoned negotiations and moved into war posture. Having just doubled military salaries, he had most of the army on his side, and he "surrounded the parliament with thousands of Interior Ministry troops, barbed wire and water cannons and refused to let anyone pass," according to *The Washington Post*.[41] Vice President Rutskoi, Yeltsin's main rival in parliament, had by this point armed his guards and welcomed proto-fascist nationalists into his camp. He urged his supporters to "not give a moment of peace" to Yeltsin's "dictatorship."[42] Kagarlitsky, who participated in the protests and wrote a book about the episode, told me that on October 3, crowds of supporters of the parliament "marched to the Ostankino TV center to demand that news be announced. Some people in the crowd were armed, but most were not. There were children in the crowd. It was met by Yeltsin's troops and machine-gunned." About one hundred demonstrators, and one member of the military, were killed. Yeltsin's next move was to dissolve all city and regional councils in the country. Russia's young democracy was being destroyed piece by piece.

There is no doubt that some parliamentarians showed antipathy for a peaceful settlement by egging on the crowds, but as even the former U.S. State Department official Leslie Gelb wrote, the parliament was "not dominated by a bunch of right-wing crazies."[43] It was Yeltsin's illegal dissolution of parliament and his defiance of the country's highest court that precipitated the crisis—moves that were bound to be met by desperate measures in a country that had little desire to give up the democracy it had just won.*

A clear signal from Washington or the EU could have forced Yeltsin to engage in serious negotiations with the parliamentarians, but he received only encouragement. Finally, on the morning of October 4, 1993, Yeltsin fulfilled his long-prescribed destiny and became Russia's very own Pinochet, unleashing a series of violent events with unmistakable echoes of the coup in Chile exactly twenty years earlier. In what was the third traumatic shock inflicted by Yeltsin on the Russian people, he ordered a reluctant army to storm the Russian White House, setting it on fire and leaving charred the very building he had built his reputation defending just two years earlier. Communism may have collapsed without the firing of a single shot, but Chicago-style capitalism, it turned out, required a great deal of gunfire to defend itself: Yeltsin called in five thousand soldiers, dozens of tanks and armored personnel carriers, helicopters and elite shock troops armed with automatic machine guns—all to defend Russia's new capitalist economy from the grave threat of democracy.

This is how *The Boston Globe* reported on Yeltsin's parliamentary siege:

* In one of the most remarkable bits of sensational reporting, *The Washington Post* noted, "About 200 demonstrators then surged to Russia's Defense Ministry, where the nation's nuclear controls are located and its top generals were meeting"—raising the absurd prospect that the crowd of Russians attempting to defend their democracy might start a nuclear war. "The ministry locked its doors and kept the crowd out without incident," reported *The Post*.

"For 10 hours yesterday, about 30 Russian army tanks and armored personnel carriers encircled the parliament building in downtown Moscow, known as the White House, and pelted it with explosive rounds, while infantry troops sprayed machine-gun fire. At 4:15 p.m., about 300 guards, congressional deputies and staff workers marched single-file out of the building with their hands up."[44]

By the end of the day, the all-out military assault had taken the lives of approximately five hundred people and wounded almost a thousand, the most violence Moscow had seen since 1917.[45] Peter Reddaway and Dmitri Glinski, who wrote the definitive account of the Yeltsin years (*The Tragedy of Russia's Reforms: Market Bolshevism against Democracy*), point out that "during the mopping-up operation in and around the White House, 1,700 persons had been arrested, and 11 weapons seized. Some of the arrested were interned in a sports stadium, recalling the procedures used by Pinochet after the 1973 coup in Chile."[46] Many were taken to police stations, where they were severely beaten. Kagarlitsky recalls that while he was being struck on the head, an officer shouted, "You wanted democracy, you sons of bitches? We'll show you democracy!"[47]

But Russia wasn't a repeat of Chile—it was Chile in reverse order: Pinochet staged a coup, dissolved the institutions of democracy and then imposed shock therapy; Yeltsin imposed shock therapy in a democracy, then could defend it only by dissolving democracy and staging a coup. Both scenarios earned enthusiastic support from the West.

"Yeltsin Receives Widespread Backing for Assault," read a headline in *The Washington Post* the day after the coup, "Victory Seen for Democracy." *The Boston Globe* went with "Russia Escapes a Return to the Dungeon of Its Past." The U.S. secretary of state, Warren Christopher, traveled to Moscow to stand with Yeltsin and Gaidar and declared, "The United States does not easily support the suspension of parliaments. But these are extraordinary times."[48]

The events looked different in Russia. Yeltsin, the man who had risen to power by defending the parliament, had now literally set it on fire, leaving it so badly charred that it was nicknamed the black house. A middle-age Muscovite told a foreign camera crew in horror, "People supported [Yeltsin] because he promised us democracy, but he shot up that democracy. Not only did he violate it, but he shot it up."[49] Vitaly Neiman, who had stood guard at the entrance of the White House during the 1991 coup, put the betrayal this way: "What we got was entirely the opposite of what we dreamed of. We went to the barricades for them, laid our lives on the line, but they didn't keep their promises."[50]

Jeffrey Sachs, lauded for proving that radical free-market reforms could be compatible with democracy, continued to publicly support Yeltsin after his assault on the parliament, dismissing his opponents as "a group of former communists intoxicated by power."[51] In his book *The End of Poverty*, in which he gives his definitive account of his involvement in Russia, Sachs completely glosses over this dramatic episode, not mentioning it once, just as he left out the state of siege and attacks on labor leaders that accompanied his shock program in Bolivia.[52]

Following the coup, Russia was under unchecked dictatorial rule: its elected bodies were dissolved, the Constitutional Court was suspended, as was the constitution; tanks patrolled the streets, a curfew was in effect, and the press faced pervasive censorship, though civil liberties were soon restored.

So what did the Chicago Boys and their Western advisers do at this critical moment? The same thing they did when Santiago smoldered, and the same thing they would do when Baghdad burned: liberated from the meddling of democracy, they went on a law-making binge. Three days after the coup, Sachs observed that up to this point "there was no shock therapy" because the plan was "only incoherently and fitfully put into practice. Now there is a chance to do something," he said.[53]

And do something they did. "These days, Yeltsin's liberal economic team is on a roll," reported *Newsweek*. "The day after the Russian president dissolved Parliament, the word came down to the market reformers: start writing decrees." The magazine quoted a "jubilant Western economist working closely with the government" who made it absolutely clear that in Russia, democracy was always a hindrance to the market plan: "With Parliament out of the way, this is a great time for reform. . . . The economists around here were pretty depressed. Now we're working day and night." Indeed, there seems to be nothing quite as cheering as a coup, as Charles Blitzer, the World Bank's chief economist for Russia, told *The Wall Street Journal*. "I've never had so much fun in my life."[54]

The fun was just beginning. With the country reeling from the attack, Yeltsin's own Chicago Boys rammed through the most contentious measures in their program: huge budget cuts, the removal of price controls on basic food items, including bread, and even more and faster privatizations—the standard policies that cause so much instant misery that they seem to require a police state to stave off rebellion.

After Yeltsin's coup, Stanley Fischer, first deputy managing director of the IMF (and a 1970s Chicago Boy), advocated "moving as fast as possible on all fronts."[55] So did Lawrence Summers, who was helping to shape Russia policy in the Clinton administration. The "three '-ations,'" as he called them—"privatization, stabilization and liberalization—must all be completed as soon as possible."[56]

Change was so rapid that it was impossible for Russians to keep up. Workers often did not even know that their factories and mines had been sold—let alone how they had been sold or to whom (a profound confusion I would witness a decade later in the state-owned factories of Iraq). In theory, all this wheeling and dealing was supposed to create the economic boom that would lift Russia out of desperation; in practice, the Communist state was simply replaced with a corporatist one: the beneficiaries of the boom were confined to a small club of Russians, many of them former Communist Party apparatchiks, and a handful of Western mutual fund managers who made dizzying returns investing in newly privatized Russian companies. A clique of nouveaux billionaires, many of whom were to become part of the group universally known as "the oligarchs" for their imperial levels of wealth and power, teamed up with Yeltsin's Chicago Boys and stripped the country of nearly everything of value, moving the enormous profits offshore at a rate of $2 billion a month. Before shock therapy, Russia had no millionaires; by 2003, the number of Russian billionaires had risen to seventeen, according to the *Forbes* list.[57]

That is partly because, in a rare departure from Chicago School orthodoxy, Yeltsin and his team did not allow foreign multinationals to buy up Russia's assets directly; they kept the prizes for Russians, then opened up the newly privatized companies, owned by so-called oligarchs, to foreign shareholders. The returns were still astronomical. "Looking for an investment that could gain 2,000 per cent in three years?" *The Wall Street Journal* asked. "Only one stock market offers that hope . . . Russia."[58] Many investment banks, including Credit Suisse First Boston, as well as a few deep-pocketed financiers, quickly set up dedicated Russian mutual funds.

For the country's oligarchs and foreign investors, only one cloud loomed on the horizon: Yeltsin's plummeting popularity. The effects of the economic program were so brutal for the average Russian, and the process was so self-evidently corrupt, that his approval ratings fell to the single digits. If Yeltsin was pushed from office, whoever replaced him would likely put a halt to Russia's adventure in extreme capitalism. Even more worrying for the oligarchs and the "reformers," there would be a strong case for renationalizing many of the assets that had been handed out under such unconstitutional political circumstances.

In December 1994, Yeltsin did what so many desperate leaders have done throughout history to hold on to power: he started a war. His national security chief, Oleg Lobov, had confided to a legislator, "We need a small, victorious war to raise the president's ratings," and the defense minister predicted that his army could defeat the forces in the breakaway republic of Chechnya in a matter of hours—a cakewalk.[59]

For a while at least, the plan seemed to work. In its first phase, the Chechen independence movement was partially suppressed, and Russian troops took over the already abandoned presidential palace in Grozny, allowing Yeltsin to declare glorious victory. It would prove to be a short-term triumph, both in Chechnya and in Moscow. When Yeltsin faced reelection in 1996, he was still so unpopular and his defeat looked so certain that his advisers toyed with canceling the vote altogether; a letter signed by a group of Russian bankers published in all the Russian national newspapers strongly hinted at this possibility.[60] Yeltsin's privatization minister, Anatoly Chubais (whom Sachs once described as "a freedom fighter"), became one of the most outspoken proponents of the Pinochet option.[61] "In order to have a democracy in society there must be a dictatorship in power," he pronounced.[62] It was a direct echo of both the excuses made for Pinochet by Chile's Chicago Boys and Deng Xiaoping's philosophy of Friedmanism without the freedom.

In the end, the election went ahead and Yeltsin won, thanks to an estimated $100 million in financing from oligarchs (thirty-three times the legal amount) as well as eight hundred times more coverage on oligarch-controlled TV stations than his rivals.[63] With the threat of a sudden change in government removed, the knockoff Chicago Boys were able to move to the most contentious, and most lucrative, part of their program: selling off what Lenin had once called "the commanding heights."

Forty percent of an oil company comparable in size to France's Total was sold for $88 million (Total's sales in 2006 were $193 billion). Norilsk Nickel, which produced a fifth of the world's nickel, was sold for $170 million—even though its profits alone soon reached $1.5 billion annually. The massive oil company Yukos, which controls more oil than Kuwait, was sold for $309 million; it now earns more than $3 billion in revenue a year. Fifty-one percent of the oil giant Sidanko went for $130 million; just two years later that stake would be valued on the international market at $2.8 billion. A huge weapons factory sold for $3 million, the price of a vacation home in Aspen.[64]

The scandal wasn't just that Russia's public riches were auctioned off for a fraction of their worth—it was also that, in true corporatist style, they were purchased with public money. As the *Moscow Times* journalists Matt Bivens and Jonas Bernstein put it, "a few hand-picked men took over Russia's state-developed oil fields for free, as part of a giant shell game in which one arm of government paid another arm." In a bold act of cooperation between the politicians selling the public companies and the businessmen buying them, several of Yeltsin's ministers transferred large sums of public money, which should have gone into the national bank or treasury, into private banks that had been hastily incorporated by oligarchs.* The state then contracted with the same banks to run the privatization auctions for the oil fields and mines. The banks ran the auctions, but they also bid in them—and sure enough, the oligarch-owned banks decided to make themselves the proud new owners of the previously public assets. The money that they put up to buy the shares in these public companies was likely the same public money that Yeltsin's ministers had deposited with them earlier.[65] In other words, the Russian people fronted the money for the looting of their own country.

As one of Russia's "young reformers" put it, when Russia's Communists decided to break up the Soviet Union, they made an "exchange [of] power for property."[66] Just like his mentor Pinochet's, Yeltsin's own family grew exceedingly rich, his children and several of their spouses appointed to top posts at large privatized firms.

With oligarchs firmly in control of the key assets of the Russian state, they opened up their new companies to blue-chip multinationals, who snapped up large portions. In 1997, Royal Dutch/Shell and BP entered into partnerships with two key Russian oil giants, Gazprom and Sidanko.[67] These were highly profitable investments, but the principal share of the wealth in Russia was in the hands of Russian players, not their foreign partners. It is an oversight that the IMF and the U.S. Treasury would successfully rectify in future

* The two major oligarch-connected banks were Mikhail Khodorkovsky's Bank Menatep and Vladimir Potanin's Uneximbank.

privatization auctions in Bolivia and Argentina. And in Iraq after the invasion, the U.S. would go even further, attempting to cut the local elite out of lucrative privatization deals entirely.

Wayne Merry, the chief political analyst at the U.S. embassy in Moscow during the key years of 1990 to 1994, has admitted that the choice between democracy and market interests in Russia was a stark one. "The U.S. government chose the economic over the political. We chose the freeing of prices, privatization of industry, and the creation of a really unfettered, unregulated capitalism, and essentially hoped that rule of law, civil society, and representative democracy would develop somehow automatically as a result of that. . . . Unfortunately, the choice was to ignore popular will and to press on with the policy."[68]

So much wealth was being made in Russia in this period that some of the "reformers" couldn't resist getting in on the action. Indeed, more than anywhere else up to this point, the situation in Russia exposed the myth of the technocrat, the egghead free-market economist supposedly imposing textbook models out of pure conviction. As in Chile and China, where rampant corruption and economic shock therapy went hand in hand, several of Yeltsin's Chicago School ministers and deputy ministers ended up losing their posts in high-profile corruption scandals.[69]

Then there were the whiz kids from Harvard's Russia Project, tasked with organizing the country's privatizations and the mutual fund market. The two academics who headed the project—Harvard economics professor Andrei Shleifer and his deputy Jonathan Hay—were discovered to have been directly profiting from the market they were busily creating. While Shleifer was the lead adviser to the Gaidar team on privatization policy, his wife was investing heavily in privatized Russian assets. Hay, a thirty-year-old graduate of Harvard Law School, also made personal investments in privatized Russian oil stocks, allegedly in direct violation of Harvard's USAID contract. And while Hay was helping the Russian government to set up a new mutual fund market, his girlfriend, later wife, was awarded the first license to open a mutual fund company in Russia, which, when it started, was managed out of the U.S. government–funded Harvard office. (Technically, as head of the Harvard Institute for International Development, which housed the Russia Project, Sachs was Shleifer's and Hay's boss for part of this time. However, Sachs was no longer working on the ground in Russia and has never been implicated in any of the questionable actions.)[70]

When these tangles came to light, the U.S. Department of Justice sued Harvard, alleging that the business dealings of Shleifer and Hay violated contracts they had signed agreeing not to profit personally from their high-level work. After a seven-year investigation and legal battle, the U.S. District Court in Boston found that Harvard had breached its contract, that the two academics "conspired to defraud the United States," that "Shleifer engaged in apparent self-dealing," that "Hay attempted to launder $400,000 through his father and girlfriend."[71] Harvard paid a settlement of $26.5 million, the largest in the institution's history. Shleifer agreed to pay $2 million, and Hay agreed to pay between $1 and $2 million, depending on his earnings, though neither admitted any liability.*[72]

Perhaps this kind of "self-dealing" was inevitable, given the nature of the Russian experiment. Anders Åslund, one of the most influential Western economists working in Russia at the time, claimed that shock therapy would work because "the miraculous incentives or temptations of capitalism conquer more or less anything."[73] So if greed was to be the engine for rebuilding Russia, then surely the Harvard men and their wives and girlfriends, as well as Yeltsin's staff and family, by taking part in the frenzy themselves, were simply leading by example.

This points to a nagging and important question about free-market ideologues: Are they "true believers," driven by ideology and faith that free markets will cure underdevelopment, as is often asserted, or do the ideas and theories frequently serve as an elaborate rationale to allow people to act on unfettered greed while still invoking an altruistic motive? All ideologies are corruptible, of course (as Russia's apparatchiks made abundantly clear when, during the Communist era, they collected their abundant privileges), and there are certainly honest neoliberals. But Chicago School economics does seem particularly conducive to corruption. Once you accept that profit and greed as practiced on a mass scale create the greatest possible benefits for any society, pretty much any act of personal enrichment can be justified as a contribution to the great creative cauldron of capitalism, generating wealth and spurring economic growth—even if it's only for yourself and your colleagues.

George Soros's philanthropic work in Eastern Europe—including his funding of Sachs's travels through the region—has not been immune to controversy.

* Unfortunately, the money didn't go to the Russian people, the true victims of the corrupt privatization process, but back to the U.S. government—the same way that the "whistle-blower" lawsuits against U.S. contractors in Iraq divvy up the settlement between the U.S. government and the American whistle-blower.

There is no doubt that Soros was committed to the cause of democratization in the Eastern Bloc, but he also had clear economic interests in the kind of economic reform accompanying that democratization. As the world's most powerful currency trader, he stood to benefit greatly when countries implemented convertible currencies and lifted capital controls, and when state companies were put on the auction block, he was one of the potential buyers.

It would have been perfectly legal for Soros to profit directly from the markets he—as a philanthropist—was helping to open up, but it would not have looked particularly good. For a time, he dealt with the appearance of conflict of interest by barring his companies from investing in countries where his foundations were active. But by the time Russia went up for sale, Soros could no longer resist. In 1994, he explained that his policy "has been modified due to the fact that markets are really developing in the region and I have no rhyme or reason or right to deny my funds, or my shareholders, the possibility of investing there, or to deny those countries the chance to get hold of some of these funds." Soros had already purchased shares in Russia's privatized phone system in 1994, for example (a very bad investment, as it turned out), and acquired a piece of a large food company in Poland.[74] In the early days of the fall of Communism, Soros, through Sachs's work, had been one of the prime movers behind the push for the shock approach to economic transformation. By the late nineties, however, he had an apparent change of heart, becoming one of the leading critics of shock therapy and directing his foundations to fund NGOs that focus on putting anticorruption measures in place before privatizations occur.

That epiphany came much too late to save Russia from casino capitalism. Shock therapy had cracked it open to flows of hot money—short-term speculative investment and currency trading, which are highly profitable. Such intense speculation meant that in 1998, when the Asian financial crisis (the subject of chapter 13) started spreading, Russia was left wholly unprotected. Its already precarious economy crashed definitively. The public blamed Yeltsin, and his approval rating dropped to an utterly untenable 6 percent.[75] With the futures of many of the oligarchs in jeopardy once again, it was going to take yet another major shock to save the economic project and stave off the threat of genuine democracy coming to Russia.

In September 1999, the country was hit with a series of exceedingly cruel terrorist attacks: seemingly out of the blue, four apartment buildings were blown up in the middle of the night, killing close to three hundred people.

In a narrative all too familiar to Americans after September 11, 2001, every other issue was blasted off the political map by the only force on earth capable of doing the job. "It was this sort of very simple fear," explains the Russian journalist Yevgenia Albats. "All of a sudden, it appeared that all these discussions about democracy, oligarchs—nothing compared to this fear to die inside your own apartment."[76]

The man put in charge of hunting down the "animals" was Russia's prime minister, the steely and vaguely sinister Vladimir Putin.*[77] Immediately after the apartment bombings, in late September 1999, Putin launched air strikes on Chechnya, attacking civilian areas. In the new light of terror, the fact that Putin was a seventeen-year veteran of the KGB—the most feared symbol of the Communist era—suddenly seemed reassuring to many Russians. With Yeltsin's alcoholism making him increasingly dysfunctional, Putin the protector was perfectly positioned to succeed him as president. On December 31, 1999, with the war in Chechnya foreclosing serious debate, several oligarchs engineered a quiet handover from Yeltsin to Putin, no elections necessary. Before he left power, Yeltsin took one last page out of the Pinochet playbook and demanded legal immunity for himself. Putin's first act as president was signing a law protecting Yeltsin from any criminal prosecution, whether for corruption or for the military's killing of pro-democracy demonstrators that took place on his watch.

Yeltsin is regarded by history more as a corrupt buffoon than a menacing strongman. Yet his economic policies, and the wars he waged in order to protect them, contributed significantly to the Chicago School crusade death toll, which has been mounting steadily since Chile in the seventies. In addition to the casualties of Yeltsin's October coup, the wars in Chechnya have killed an estimated 100,000 civilians.[78] The larger massacres he precipitated have taken place in slow motion, but their numbers are much higher—the "collateral damage" of economic shock therapy.

In the absence of major famine, plague or battle, never have so many lost so much in so short a time. By 1998, more than 80 percent of Russian farms had gone bankrupt, and roughly seventy thousand state factories had closed, creating an epidemic of unemployment. In 1989, before shock therapy, 2

* Not surprisingly, given the defiant criminality of Russia's ruling class, conspiracy theories swirl around these events. Many Russians believe that Chechens had nothing to do with the apartment bombings and that they were a covert operation designed to turn Putin into Yeltsin's heir apparent.

million people in the Russian Federation were living in poverty, on less than $4 a day. By the time the shock therapists had administered their "bitter medicine" in the mid-nineties, 74 million Russians were living below the poverty line, according to the World Bank. That means that Russia's "economic reforms" can claim credit for the impoverishment of 72 *million people in only eight years.* By 1996, 25 percent of Russians—almost 37 million people—lived in poverty described as "desperate."[79]

Although millions of Russians have been pulled out of poverty in recent years, thanks largely to soaring oil and gas prices, Russia's underclass of extreme poor has remained permanent—with all the sicknesses associated with that discarded status. As miserable as life under Communism was, with crowded, cold apartments, Russians at least were housed; in 2006 the government admitted that there were 715,000 homeless kids in Russia, and UNICEF has put the number as high as 3.5 million children.[80]

During the Cold War, widespread alcoholism was always seen in the West as evidence that life under Communism was so dismal that Russians needed large quantities of vodka to get through the day. Under capitalism, however, Russians drink more than twice as much alcohol as they used to—and they are reaching for harder painkillers as well. Russia's drug czar, Aleksandr Mikhailov, says that the number of users went up 900 percent from 1994 to 2004, to more than 4 million people, many of them heroin addicts. The drug epidemic has contributed to another silent killer: in 1995, fifty thousand Russians were HIV positive, and in only two years that number doubled; ten years later, according to UNAIDS, nearly a million Russians were HIV positive.[81]

These are the slow deaths, but there are fast ones as well. As soon as shock therapy was introduced in 1992, Russia's already high suicide rate began to rise; 1994, the peak of Yeltsin's "reforms," saw the suicide rate climb to almost double what it had been eight years earlier. Russians also killed each other with much greater frequency: by 1994, violent crime had increased more than fourfold.[82]

"What have our motherland and her people gotten out of the last 15 criminal years?" Vladimir Gusev, a Moscow academic, asked at a 2006 democracy demonstration. "The years of criminal capitalism have killed off 10 percent of our population." Russia's population is indeed in dramatic decline—the country is losing roughly 700,000 people a year. Between 1992, the first full year of shock therapy, and 2006, Russia's population shrank by 6.6 million.[83] Three decades ago, André Gunder Frank, the dissident

Chicago economist, wrote a letter to Milton Friedman accusing him of "economic genocide." Many Russians describe the slow disappearance of their fellow citizens in similar terms today.

This planned misery is made all the more grotesque because the wealth accumulated by the elite is flaunted in Moscow as nowhere else outside of a handful of oil emirates. In Russia today, wealth is so stratified that the rich and the poor seem to be living not only in different countries but in different centuries. One time zone is downtown Moscow, transformed in fast-forward into a futuristic twenty-first-century sin city, where oligarchs race around in black Mercedes convoys, guarded by top-of-the-line mercenary soldiers, and where Western money managers are seduced by the open investment rules by day and by on-the-house prostitutes by night. In the other time zone, a seventeen-year-old provincial girl, asked about her hopes for the future, replied, "It's difficult to talk about the twenty-first century when you're sitting here reading by candlelight. The twenty-first century does not matter. It's the nineteenth century here."[84]

This pillage of a country with as much wealth as Russia required extreme acts of terror—from the torching of the parliament to the invasion of Chechnya. "Policy that breeds poverty and crime," writes Georgi Arbatov, one of Yeltsin's original (and ignored) economic advisers, ". . . can survive only if democracy is suppressed."[85] Just as it had been in the Southern Cone, in Bolivia under the state of siege, in China during Tiananmen. Just as it would be in Iraq.

When in Doubt, Blame Corruption

Rereading Western news reports on Russia's shock therapy period, it is striking how closely discussions at that time paralleled debates about Iraq that would unfold more than a decade later. For both the Clinton and Bush Sr. administrations, not to mention the European Union, the G7 and the IMF, the clear goal in Russia was to erase the preexisting state and create the conditions for a capitalist feeding frenzy, which in turn would kick-start a booming free-market democracy—managed by overconfident Americans barely out of school. In other words, it was Iraq without the explosives.

When the zeal for shock therapy in Russia was at its peak, its cheerleaders were absolutely convinced that only total destruction of every single institution would create the conditions for a national rebirth—the dream of the blank slate that would recur in Baghdad. It is "desirable," wrote the Harvard historian Richard Pipes, "for Russia to keep on disintegrating until nothing remains of its institutional structures."[86] And the Columbia University economist Richard Ericson wrote in 1995, "Any reform must be disruptive on a historically unprecedented scale. An entire world must be discarded, including all of its economic and most of its social and political institutions, and concluding with the physical structure of production, capital, and technology."[87]

Another Iraq parallel: no matter how baldly Yeltsin defied anything resembling democracy, his rule was still characterized in the West as part of "a transition to democracy," a narrative that would change only when Putin began cracking down on the illegal activities of several of the oligarchs. Similarly, the Bush administration has always portrayed Iraq as on the road to freedom, even in the face of overwhelming evidence of rampant torture, out-of-control death squads and pervasive press censorship. Russia's economic program was always described as "reform," just as Iraq is perennially under "reconstruction," even after the U.S. contractors have mostly all fled, leaving the infrastructure in a shambles, as the destruction roars on. In Russia in the mid-nineties, anyone who dared question the wisdom of "the reformers" was dismissed as nostalgic for Stalin, just as critics of Iraq's occupation were, for years, met with accusations that they thought life was better under Saddam Hussein.

When it was no longer possible to hide the failures of Russia's shock therapy program, the spin turned to Russia's "culture of corruption," as well as speculation that Russians "aren't ready" for genuine democracy because of their long history of authoritarianism. Washington's think-tank economists hastily disavowed the Frankenstein economy they helped create in Russia, deriding it as "mafia capitalism"—supposedly a phenomenon peculiar to the Russian character. "Nothing good will ever come of Russia," *The Atlantic Monthly* reported in 2001, quoting a Russian office worker. In the *Los Angeles Times*, the journalist and novelist Richard Lourie pronounced that "the Russians are such a calamitous nation that even when they undertake something sane and banal, like voting and making money, they make a total hash of it."[88] The economist Anders Åslund had claimed that the "temptations of capitalism" alone would transform Russia, that the sheer power of greed would provide the momentum to rebuild the country. Asked a few years later what went wrong, he replied, "Corruption, corruption and corruption," as if corruption was something other than the unrestrained expression of the "temptations of capitalism" that he had so enthusiastically praised.[89]

The entire charade would be replayed a decade later to explain away the billions of missing reconstruction dollars in Iraq, with the disfiguring legacy of Saddam and the pathologies of "radical Islam" standing in for the legacy of Communism and czarism. In Iraq, U.S. rage at the apparent inability of Iraqis to accept their gift of gunpoint "freedom" would also turn abusive—except that in Iraq the rage would not be found only in nasty editorials about "ungrateful" Iraqis but would also be pounded out on the bodies of Iraqi civilians by U.S. and British soldiers.

The real problem with the blame-Russia narrative is that it pre-empts any serious examination of what the whole episode has to teach about the true face of the crusade for unfettered free markets, the most powerful political trend of the past three decades. The corruption of many of the oligarchs is still spoken of as an alien force that infected otherwise worthy free-market plans. But corruption wasn't an intruder to Russia's free-market reforms: quick and dirty deals were actively encouraged by Western powers at every stage as the fastest way to kick-start the economy. National salvation through the harnessing of greed was the closest thing Russia's Chicago Boys and their advisers had to a plan for what they were going to do after they finished destroying Russia's institutions.

Nor were these catastrophic results unique to Russia; the entire thirty-year history of the Chicago School experiment has been one of mass corruption and corporatist collusion between security states and large corporations, from Chile's piranhas, to Argentina's crony privatizations, to Russia's oligarchs, to Enron's energy shell game, to Iraq's "free fraud zone." The point of shock therapy is to open up a window for enormous profits to be made very quickly—not despite the lawlessness but precisely because of it. "Russia Has Become a Klondike for International Fund Speculators," ran a headline in a Russian newspaper in 1997, while *Forbes* described Russia and Central Europe as "the new frontier."[90] The colonial-era terms were entirely appropriate.

The movement that Milton Friedman launched in the 1950s is best understood as an attempt by multinational capital to recapture the highly profitable, lawless frontier that Adam Smith, the intellectual forefather of today's neoliberals, so admired—but with a twist. Rather than journeying through Smith's "savage and barbarous nations" where there was no Western law (no longer a practical option), this movement set out to systematically dismantle existing laws and regulations to re-create that earlier lawlessness. And where

Smith's colonists earned their record profits by seizing what he described as "waste lands" for "but a trifle," today's multinationals see government programs, public assets and everything that is not for sale as terrain to be conquered and seized—the post office, national parks, schools, social security, disaster relief and anything else that is publicly administered.[91]

Under Chicago School economics, the state acts as the colonial frontier, which corporate conquistadors pillage with the same ruthless determination and energy as their predecessors showed when they hauled home the gold and silver of the Andes. Where Smith saw fertile green fields turned into profitable farmlands on the pampas and the prairies, Wall Street saw "green field opportunities" in Chile's phone system, Argentina's airline, Russia's oil fields, Bolivia's water system, the United States' public airwaves, Poland's factories—all built with public wealth, then sold for a trifle.[92] Then there are the treasures created by enlisting the state to put a patent and a price tag on life-forms and natural resources never dreamed of as commodities—seeds, genes, carbon in the earth's atmosphere. By relentlessly searching for new profit frontiers in the public domain, Chicago School economists are like the mapmakers of the colonial era, identifying new waterways through the Amazon, marking off the location of a hidden cache of gold inside an Inca temple.

Corruption has been as much a fixture on these contemporary frontiers as it was during the colonial gold rushes. Since the most significant privatization deals are always signed amid the tumult of an economic or political crisis, clear laws and effective regulators are never in place—the atmosphere is chaotic, the prices are flexible and so are the politicians. What we have been living for three decades is frontier capitalism, with the frontier constantly shifting location from crisis to crisis, moving on as soon as the law catches up.

And so, far from acting as a cautionary tale, the rise of Russia's billionaire oligarchs proved precisely how profitable the strip mining of an industrialized state could be—and Wall Street wanted more. Immediately following the Soviet collapse, the U.S. Treasury and the IMF became much tougher in their demands for instant privatizations from other crisis-racked countries. The most dramatic case to date came in 1994, the year after Yeltsin's coup, when Mexico's economy suffered a major meltdown known as the Tequila Crisis: the terms of the U.S. bailout demanded rapid-fire privatizations, and *Forbes* announced that the process had minted twenty-three new billionaires. "The lesson here is fairly obvious: to predict whence the next bursts of billionaires will issue, look for countries where markets are opening." It also cracked Mexico open to unprecedented foreign ownership: in 1990, only one of Mexico's banks was foreign owned, but "by 2000 twenty-four out of thirty were in foreign hands."[93] Clearly the only lesson learned from Russia is that the faster and more lawless the transfer of wealth, the more profitable it will be.

One person who understood that was Gonzalo Sánchez de Lozada (Goni), the businessman in whose living room the Bolivian shock therapy plan had been drafted in 1985. As president of the country in the mid-nineties, he sold off Bolivia's national oil company, as well as the national airline, railway, electricity and phone companies. Unlike what transpired in Russia, where the biggest prizes were awarded to locals, the winners of Bolivia's fire sale included Enron, Royal Dutch/Shell, Amoco Corp. and Citicorp—and the sales were direct; there was no need to partner with local firms.[94] *The Wall Street Journal* described the Wild West scene in La Paz in 1995: "The Radisson Plaza Hotel is crammed with executives from major U.S. companies like AMR Corp.'s American Airlines, MCI Communications Corp., Exxon Corp. and Salomon Brothers Inc. They have been invited by the Bolivians to rewrite laws governing the sectors to be privatized and to bid on the companies on the block"—a tidy arrangement. "The important thing is to make these changes irreversible and to get them done before the antibodies kick in," said President Sánchez de Lozada, explaining his shock therapy approach. To make absolutely sure those "antibodies" didn't kick in, Bolivia's government did something it had done before under similar circumstances: it imposed yet another prolonged "state of siege" that banned political gatherings and authorized the arrest of all opponents of the process.[95]

These were also the years of Argentina's notoriously corrupt privatization circus, hailed as "A Bravo New World" in an investment report by Goldman Sachs. Carlos Menem, the Peronist president who came to power promising to be the voice of the working man, was in charge during those years, downsizing and then selling the oil fields, the phone system, the airline, the trains, the airport, the highways, the water system, the banks, the Buenos Aires zoo and, eventually, the post office and the national pension plan. As the country's wealth moved offshore, the lifestyles of Argentina's politicians grew increasingly lavish. Menem, once known for his leather jackets and working-class sideburns, began wearing Italian suits and reportedly making trips to the plastic surgeon ("a bee sting" is how he explained his swollen features). María Julia Alsogaray, Menem's minister in charge of privatization, posed for the cover of a popular magazine wearing nothing but an artfully draped fur coat, while Menem began driving a bright red Ferrari Testarossa—a "gift" from a grateful businessman.[96]

The countries that emulated Russia's privatizations also experienced milder versions of Yeltsin's coups-in-reverse—governments that came to power peacefully and, through elections, found themselves resorting to increasing levels of brutality to hold on to power and defend their reforms. In Argentina, the rule of unfettered neoliberalism ended on December 19, 2001, when President Fernando de la Rúa and his finance minister, Domingo Cavallo, tried to impose further IMF-prescribed austerity measures. The population revolted, and de la Rúa sent in federal police on orders to disperse the crowds by whatever means were required. De la Rúa was forced to flee in a helicopter, but not before twenty-one protesters were killed by police and 1,350 people were injured.[97] Goni's last months and days in office were even bloodier. His privatizations sparked a series of "wars" in Bolivia: first the water war, against Bechtel's water contract that sent prices soaring 300 percent; then a "tax war" against an IMF-prescribed plan to make up a budget shortfall by taxing the working poor; then the "gas wars" against his plans to export gas to the U.S. In the end, Goni was also forced to flee the presidential palace to live in exile in the U.S., but, as in de la Rúa's case, not before many lives were lost. After Goni ordered the military to put down street demonstrations, soldiers killed close to seventy people—many of them bystanders—and injured four hundred others. As of early 2007, Goni was wanted by Bolivia's Supreme Court on charges relating to the massacre.[98]

The regimes that imposed mass privatization on Argentina and Bolivia were both held up in Washington as examples of how shock therapy could be imposed peacefully and democratically, without coups or repression. Although it's true that they did not begin in a hail of gunfire, it is surely significant that both ended in one.

In much of the Southern Hemisphere, neoliberalism is frequently spoken of as "the second colonial pillage": in the first pillage, the riches were seized from the land, and in the second they were stripped from the state. After every one of these profit frenzies come the promises: next time, there will be firm laws in place before a country's assets are sold off, and the entire process will be watched over by eagle-eyed regulators and investigators with unimpeachable ethics. Next time there will be "institution building" before privatizations (to use the post-Russia parlance). But calling for law and order after the profits have all been moved offshore is really just a way of legalizing the theft ex post facto, much as the European colonizers locked in their land grabs with treaties. Lawlessness on the frontier, as Adam Smith understood, is not the problem but the point, as much a part of the game as the contrite hand-wringing and the pledges to do better next time.

CHAPTER 12

THE CAPITALIST ID

RUSSIA AND THE NEW ERA OF THE BOOR MARKET

You have made yourself the trustee for those in every country who seek to mend the evils of our condition by reasoned experiment within the framework of the existing social system. If you fail, rational change will be gravely prejudiced throughout the world, leaving orthodoxy and revolution to fight it out.

—John Maynard Keynes in a letter to
President Franklin D. Roosevelt, 1933[1]

On the day I went to visit Jeffrey Sachs in October 2006, New York City was under a damp blanket of gray drizzle punctuated, every five paces or so, by a vibrant burst of red. It was the week of the grand launch of Bono's (Product) Red brand, and the city was getting the full blitz. Red iPods and Armani sunglasses loomed from billboards overhead, every bus shelter featured Steven Spielberg or Penélope Cruz in a different red garment, every Gap outlet in the city had given itself over to the launch, and the Apple store on Fifth Avenue was emitting a rosy glow. "Can a tank top change the world?" asked one ad. Yes it can, we were assured, because a portion of the profits was going to the Global Fund to Fight AIDS, TB and malaria. "Shop till it stops!" Bono had pronounced, in the midst of a televised shopping spree with Oprah a couple of days earlier.[2]

I had a hunch that most of the journalists wanting to talk to Sachs that week would be looking for the superstar economist's view on this fashionable new way to raise aid money. After all, Bono refers to Sachs as "my professor," and a photo of the two men greeted me as I entered Sachs's office at Columbia

University (he left Harvard in 2002). In the midst of all this glamorous charity, I felt like a bit of a spoiler, because I wanted to talk about the professor's least favorite topic of all, one that has prompted him to threaten to hang up on reporters mid-interview. I wanted to talk about Russia and what went wrong there.

It was in Russia, after the first year of shock therapy, that Sachs began his own transition, from global shock doctor to one of the world's most outspoken campaigners for increasing aid to impoverished countries. It is a transition that, in the years since, has put him in conflict with many former colleagues and collaborators in orthodox economic circles. As far as Sachs is concerned, he isn't the one who changed—he was always committed to helping countries develop market-based economies bolstered by generous aid and debt forgiveness. For years he had found it possible to achieve these goals by working in partnership with the IMF and the U.S. Treasury. But by the time he was on the ground in Russia, the tenor of discussion had changed and he came up against a level of official indifference that shocked him and pushed him into a more confrontational stance with Washington's economic establishment.

Seen with hindsight, there is no doubt that Russia marked the beginning of a new chapter in the evolution of the Chicago School crusade. In earlier shock therapy laboratories of the seventies and eighties, there had been some desire at the U.S. Treasury and the IMF to make the experiments at least superficially successful—precisely because they were experiments, meant to serve as models for other countries to follow. The Latin American dictatorships of the seventies were rewarded for their attacks on trade unions and their open borders with steady loans, which were granted despite such departures from Chicago School orthodoxy as Chile's continued state control over the world's largest copper mines and the Argentine junta's slow action on privatizations. Bolivia, as the first democracy to adopt shock therapy in the eighties, was granted aid and had a portion of its debt erased—well before Goni moved ahead with privatization in the nineties. In Poland, the first Eastern Bloc country to impose shock therapy, Sachs had no trouble securing substantial loans, and, once again, major privatizations were slowed and staggered when the original plan encountered strong opposition.

Russia was different. "Too much shock, not enough therapy" was the widespread verdict. Western powers were totally unyielding in their demand for the most painful "reforms," at the same time as they were assiduously stingy in the amount of aid they would offer in return. Even Pinochet had cushioned the pain of shock therapy with food programs for the poorest children; Washington lenders saw no reason to help Yeltsin do the same, pushing the country instead into its Hobbesian nightmare.

Having a substantive discussion about Russia with Sachs isn't easy. I was hoping to take the conversation beyond his initial defensiveness ("I was right and they were completely wrong," he told me. Then, "Ask Larry Summers, don't ask me; ask Bob Rubin, ask Clinton, ask Cheney how happy they were with the way Russia went"). I also wanted to get beyond the genuine despondency ("I was trying to do something at the time, which proved to be completely useless"). What I was aiming to understand better was why he was so unsuccessful in Russia, why Jeffrey Sachs's famous luck ran out at that particular juncture.

Sachs now says that he knew something was different as soon as he arrived in Moscow. "I had a sense of foreboding from the first moment . . . I was furious from the first moment." Russia was facing "a first-class macroeconomic crisis, one of the most intense and unstable I had ever seen in my life," he said. And as far as he was concerned, the way out was clear: the shock therapy measures he had prescribed for Poland "to get basic market forces working quickly—plus a heck of a lot of aid. I was thinking of $30 billion a year, roughly divided, $15 billion for Russia and $15 billion for the republics, in order to be able to pull off a peaceful and democratic transition."

Sachs, it must be said, has a notoriously selective memory when it comes to the draconian policies he pushed in both Poland and Russia. In our interview, he repeatedly glossed over his own calls for swift privatization and large cutbacks (in short, shock therapy, a phrase he now disavows, claiming he was referring only to narrow pricing policies, not wholesale country makeovers). The way he remembers his role, shock therapy played a minor part, and he was almost exclusively focused on fund-raising; his plan for Poland, he says, was a "stabilization fund, debt cancellation, short-term financial help, integration with the Western European economy. . . . When I was asked by Yeltsin's team to help them, I proposed basically the same thing."*

There is no debate about the key fact in Sachs's account: securing a major aid infusion was a central pillar of his plan for Russia—that was Yeltsin's

* As John Cassidy noted in a 2005 *New Yorker* profile, "The fact is that in both Poland and Russia Sachs favored large-scale social engineering over gradual change and institution-building. The disastrous privatization policy is one example. Although most of the privatization took place after Sachs left Russia, at the end of 1994, the original policy framework was put in place in 1992 and 1993, when he was still there."

incentive for submitting to the entire program. Sachs based this vision, he says, on the Marshall Plan, the $12.6 billion ($130 billion in today's dollars) that the U.S. allotted for Europe to reconstruct its infrastructure and industry after the Second World War—a scheme widely regarded as Washington's most successful diplomatic initiative.[3] Sachs says the Marshall Plan showed that "when a country is in disarray, you can't just expect it to get back up on its feet in a coherent way by itself. So, for me the interesting thing about the Marshall Plan . . . is how a modest amount of monetary infusion created a base for [Europe's] economic recovery to take hold." At the start, he had been convinced that there was a similar political will in Washington to transform Russia into a successful capitalist economy, just as there had been a genuine commitment to West Germany and Japan after the Second World War.

Sachs was confident that he could shake a new Marshall Plan out of the U.S. Treasury and the IMF, and not without reason. "Probably the most important economist in the world" is how *The New York Times* described him in this period.[4] When he was an adviser to Poland's government, he recalled that he "raised $1 billion in one day in the White House." But, Sachs told me, "when I suggested the same thing for Russia, there was absolutely no interest at all. None. And the IMF just stared me down like I was crazy."

Although Yeltsin and his Chicago Boys had plenty of admirers in Washington, no one was willing to come up with the kind of aid they were talking about. That meant Sachs had urged wrenching policies on Russia, and he couldn't keep up his end of the bargain. It was in this period that he came close to self-criticism: "My greatest personal mistake," Sachs said in the midst of the Russia debacle, "was to say to President Boris Yeltsin, 'Don't worry; help is on the way.' I believed deeply that the assistance was too important, and too crucial to the West, for it to be messed up as significantly and fundamentally as it has been."[5] But the problem wasn't only that the IMF and the Treasury hadn't listened to Sachs, it was that Sachs had pushed hard for shock therapy before he had any guarantee that they would—a gamble for which millions paid dearly.

When I revisited the question with Sachs, he reiterated that his real failing was in misreading Washington's political mood. He recalled a discussion with Lawrence Eagleburger, U.S. secretary of state under George H. W. Bush. Sachs made his case: if Russia was allowed to descend further into economic chaos, it could unleash forces no one could control—mass famine, resurgent nationalism, even fascism, surely unwise in a country where virtually the only product held in surplus was nuclear arms. "Your analysis may be just right, but it's not going to happen," Eagleburger replied. Then he asked Sachs, "Do you know what year this is?"

It was 1992, the year of the U.S. election in which Bill Clinton was about to defeat Bush Sr. The core of Clinton's campaign was that Bush had neglected economic hardship at home to pursue glory abroad ("It's the economy, stupid"). Sachs believes that Russia was a casualty of that domestic battle. And, he says, he now sees that there was something else at work: many of Washington's power brokers were still fighting the Cold War. They saw Russia's economic collapse as a geopolitical victory, the decisive one that ensured U.S. supremacy. "I had none of that mind-set," Sachs told me, sounding, as he often does, like a Boy Scout who has stumbled into an episode of *The Sopranos*. "For me it was just, 'Great, this is the final end of this abominable regime. Now, let's really help [the Russians]. Let's throw everything into it. . . .' I'm sure that in retrospect, in the minds of the policy planners, that was viewed as crazy."

Despite his failure, Sachs does not feel that the policy toward Russia in this period was driven by free-market ideology. It was mostly, he said, characterized by "sheer laziness." He would have welcomed a heated debate about whether to offer aid to Russia or leave it all to the market. Instead, there was a collective shrug. He said he was amazed by the absence of serious research and debate informing momentous decisions. "To me, it was just the lack of effort that was the dominant thing. Let's at least spend two days and debate this—well, we never even did that! I never saw the hard work of 'Roll up your sleeves, let's get down and solve these problems, let's figure out what's really going on.' "

When Sachs talks passionately about "hard work," he is harking back to the days of the New Deal, the Great Society and the Marshall Plan, when young men from Ivy League schools sat around commanding tables in their shirt sleeves, surrounded by empty coffee cups and piles of policy papers, having heated debates about the interest rate and the price of wheat. That is how policy makers behaved in the heyday of Keynesianism, and that is the kind of "seriousness" that Russia's catastrophe clearly deserved.

But attributing the abandonment of Russia to a bout of collective laziness in Washington offers little by way of explanation. Perhaps a better way to understand the episode is through the lens favored by free-market economists: competition in the market. When the Cold War was in full swing and the Soviet Union was intact, the people of the world could choose (at least theoretically) which ideology they wanted to consume; there were the two poles, and there was much in between. That meant capitalism had to win customers; it needed to offer incentives; it needed a good product. Keynesianism was always an expression of that need for capitalism to compete. President Roosevelt brought in the New Deal not only to address the desperation of the Great Depression but to undercut a powerful movement of U.S. citizens who, having been dealt a savage blow by the unregulated free market, were demanding a different economic model. Some wanted a radically different one: in the 1932 presidential elections, one million Americans voted for Socialist or Communist candidates. Growing numbers of Americans were also paying close attention to Huey Long, the populist senator from Louisiana who believed that all Americans should receive a guaranteed annual income of $2,500. Explaining why he had added more social welfare benefits to the New Deal in 1935, FDR said he wanted to "steal Long's thunder."[6]

It was in this context that American industrialists grudgingly accepted FDR's New Deal. The edges of the market needed to be softened with public sector jobs and by making sure no one went hungry—the very future of capitalism was at stake. During the Cold War, no country in the free world was immune to this pressure. In fact, the achievements of mid-century capitalism, or what Sachs calls "normal" capitalism—workers' protections, pensions, public health care and state support for the poorest citizens in North America—all grew out of the same pragmatic need to make major concessions in the face of a powerful left.

The Marshall Plan was the ultimate weapon deployed on this economic front. After the war, the German economy was in crisis, threatening to bring down the rest of Western Europe. Meanwhile, so many Germans were drawn to socialism that the U.S. government opted to split Germany into two parts rather than risk losing it all, either to collapse or to the left. In West Germany, the U.S. government used the Marshall Plan to build a capitalist system that was not meant to create fast and easy new markets for Ford and Sears but, rather, to be so successful on its own terms that Europe's market economy would thrive and socialism would be drained of its appeal.

By 1949, that meant tolerating from the West German government all kinds of policies that were positively uncapitalist: direct job creation by the state, huge investment in the public sector, subsidies for German firms and strong labour unions. In a move that would have been unthinkable in Russia in the 1990s or Iraq under U.S. occupation, the U.S. government infuriated its own corporate sector by imposing a moratorium on foreign investment so that war-battered German companies would not be forced to compete before they had recovered. "The feeling was that letting foreign companies come in at that point would have been like piracy," I was told by Carolyn Eisenberg, author of an acclaimed history of the Marshall Plan.[7] "The main difference between now and then is that the U.S. government did not see Germany as a cash cow. They didn't want to antagonize people. The belief was that if you come in and start pillaging the place, you interfere with the recovery of Europe as a whole."

This approach, Eisenberg points out, was not born of altruism. "The Soviet Union was like a loaded gun. The economy was in crisis, there was a substantial German left, and they [the West] had to win the allegiance of the German people fast. They really saw themselves battling for the soul of Germany."

Eisenberg's account of the battle of ideologies that created the Marshall Plan points to a persistent blind spot in Sachs's work, including his recent laudable efforts to dramatically increase aid spending for Africa. Rarely are mass popular movements even mentioned. For Sachs, the making of history is a purely elite affair, a matter of getting the right technocrats settled on the right policies. Just as shock therapy programs are drafted in secret bunkers in La Paz and Moscow, so, apparently, should a $30 billion aid program for the Soviet republics have materialized based solely on the commonsense arguments he was making in Washington. As Eisenberg notes, however, the original Marshall Plan came about not out of benevolence, or even reasoned argument, but fear of popular revolt.

Sachs admires Keynes, but he seems uninterested in what made Keynesianism finally possible in his own country: the messy, militant demands of trade unionists and socialists whose growing strength turned a more radical solution into a credible threat, which in turn made the New Deal look like an acceptable compromise. This unwillingness to recognize the role of mass movements in pressuring reluctant governments to embrace the very ideas he advocates has had serious ramifications. For one, it meant that Sachs could not see the most glaring political reality confronting him in Russia: there was never going to be a Marshall Plan for Russia because there was only ever a Marshall Plan *because of* Russia. When Yeltsin abolished the Soviet Union, the "loaded gun" that had forced the development of the original plan was disarmed. Without it, capitalism was suddenly free to lapse into its most savage form, not just in Russia but around the world. With the Soviet collapse, the free market now had a global monopoly, which meant all the "distortions" that had been interfering with its perfect equilibrium were no longer required.

This was the real tragedy of the promise made to the Poles and Russians—that if they followed shock therapy they would suddenly wake up in a "normal

European country." Those normal European countries (with their strong social safety nets, workers' protections, powerful trade unions and socialized health care) emerged as a compromise between Communism and capitalism. Now that there was no need for compromise, all those moderating social policies were under siege in Western Europe, just as they were under siege in Canada, Australia and the U.S. Such policies were not about to be introduced in Russia, certainly not subsidized with Western funds.

This liberation from all constraints is, in essence, Chicago School economics (otherwise known as neoliberalism or, in the U.S., neoconservatism): not some new invention but capitalism stripped of its Keynesian appendages, capitalism in its monopoly phase, a system that has let itself go—that no longer has to work to keep us as customers, that can be as antisocial, antidemocratic and boorish as it wants. As long as Communism was a threat, the gentlemen's agreement that was Keynesianism would live on; once that system lost ground, all traces of compromise could finally be eradicated, thereby fulfilling the purist goal Friedman had set out for his movement a half century earlier.

That was the real point of Fukuyama's dramatic "end of history" announcement at the University of Chicago lecture in 1989: he wasn't actually claiming that there were no other ideas in the world, but merely that, with Communism collapsing, there were no other ideas sufficiently powerful to constitute a head-to-head competitor.

So while Sachs saw the collapse of the Soviet Union as a liberation from authoritarian rule and was ready to roll up his sleeves and start helping, his Chicago School colleagues saw it as a freedom of a different sort—as the final liberation from Keynesianism and the do-gooder ideas of men like Jeffrey Sachs. Seen in that light, the do-nothing attitude that so infuriated Sachs when it came to Russia was not "sheer laziness" but laissez-faire in action: let it go, do nothing. By not lifting a finger to help, all the men charged with Russian policy—from Dick Cheney, as Bush Sr.'s defense secretary, to Lawrence Summers, Treasury undersecretary, to Stanley Fischer at the IMF—were indeed doing something: they were practicing pure Chicago School ideology, letting the market do its worst. Russia, even more than Chile, was what this ideology looked like in practice, a foreshadowing of the get-rich-or-die-trying dystopia that many of these same players would create a decade later in Iraq.

The new rules of the game were on display in Washington, D.C., on January 13, 1993. The occasion was a small but important conference, by invitation only, on the tenth floor of the Carnegie Conference Center on Dupont

Circle, a seven-minute drive from the White House and a stone's throw from the headquarters of the IMF and the World Bank. John Williamson, the powerful economist known for shaping the missions of both the bank and the fund, had convened the event as a historic gathering of the neoliberal tribe. In attendance was an impressive array of the star "technopols" who were at the forefront of the campaign to spread the Chicago doctrine throughout the world. There were present and former finance ministers from Spain, Brazil and Poland, central bank heads from Turkey and Peru, the chief of staff for the president of Mexico and a former president of Panama. There was Sachs's old friend and hero, Leszek Balcerowicz, architect of Poland's shock therapy, as well as his Harvard colleague Dani Rodrik, the economist who had proven that every country that had accepted neoliberal restructuring had been in deep crisis. Anne Krueger, future first deputy managing director of the IMF, was there, and although José Piñera, Pinochet's most evangelical minister, couldn't make it because he was trailing in Chile's presidential election, he sent a detailed paper in his place. Sachs, who was still advising Yeltsin at the time, was to deliver the keynote address.

All day long, the conference participants had been indulging in that favorite economists' pastime of strategizing how to get reluctant politicians to embrace policies that are unpopular with voters. How soon after elections should shock therapy be launched? Are center-left parties more effective than right-wing ones because the attack is unexpected? Is it better to warn the public or take people by surprise with "voodoo politics"? Though the conference was called "The Political Economy of Policy Reform"—so willfully bland a title that it seemed designed to deflect media interest—one participant remarked slyly that what it was really about was "Machiavellian economics."[8]

Sachs listened to all this talk for several hours, and after dinner he went to the podium to give his address, titled, in true Sachsian fashion, "Life in the Economic Emergency Room."[9] He was visibly agitated. The crowd was ready to hear a speech from one of their idols, the man who had carried the torch of shock therapy into the democratic era. Sachs was in no mood for self-congratulation. Instead, he was determined to use the speech, he later explained to me, to try to get this powerful crowd to grasp the gravity of what was unfolding in Russia.

He reminded his audience of the infusions of aid that had gone to Europe and Japan after the Second World War, "vital for Japan's later magnificent success." He told a story about getting a letter from an analyst at the Heritage Foundation—ground zero of Friedmanism—who "believed strongly in Russia's reforms but not in foreign aid for Russia. This is a common view of free-market ideologues—of which I am one," Sachs said. "It is plausible but it is mistaken. The market cannot do it all by itself; international help is crucial." The laissez-faire obsession was taking Russia into catastrophe, where, he said, "no matter how valiant, brilliant, and lucky are Russia's reformers, they won't make it without large-scale external assistance . . . we are close to missing a historic opportunity."

Sachs got a round of applause, of course, but the response was tepid. Why was he praising such lavish social spending? This crowd was on a global crusade to dismantle the New Deal, not to forge a new one. In the conference sessions that followed, not a single participant supported Sachs's challenge, and several spoke out against it.

What he was trying to do with the speech, Sachs told me, was "explain what a real crisis was like . . . to convey a sense of urgency." People who make policy from Washington, he said, often "don't understand what economic chaos is. They don't understand the disarray that comes." He wanted to confront them with the reality that "there's also a dynamic that things get farther and farther out of control, until you have other disasters, until Hitler comes back in power, until you have civil war, or mass famine or whatever it is. . . . You need to do emergency things to help, because an unstable situation definitely has a path of increasing instability, not just a path to normal equilibrium."

I couldn't help thinking that Sachs wasn't giving his audience enough credit. The people in that room were well versed in Milton Friedman's crisis theory, and many had applied it in their own countries. Most understood perfectly how wrenching and volatile an economic meltdown could be, but they were taking a different lession from Russia: that a painful and disorienting political situation was forcing Yeltsin to rapidly auction off the riches of the state, a distinctly favorable outcome.

It was left to John Williamson, the host of the conference, to steer the discussion back to those pragmatic priorities. Sachs was the one with the star power at the event, but it was Williamson who was the crowd's real guru. Balding and untelegenic but thrillingly politically incorrect, Williamson was the one who coined the phrase "the Washington Consensus"—perhaps the most quoted and contentious three words in modern economics. He is famous for his tightly structured closed-door conferences and seminars, each designed to test one of his bold hypotheses. At the conference in January, he had a pressing agenda: he wanted to test what he called the "crisis hypothesis" once and for all.[10]

In his lecture, Williamson offered no warnings of the imperative to save any country from crisis; in fact, he spoke rhapsodically of cataclysmic events. He reminded his audience of the indisputable evidence that only when countries are truly suffering do they agree to swallow their bitter market medicine; only when they are in shock do they lie down for shock therapy. "These worst of times give rise to the best of opportunities for those who understand the need for fundamental economic reform," he declared.[11]

With his unparalleled knack for verbalizing the subconscious of the financial world, Williamson casually pointed out that this raised some intriguing questions:

> One will have to ask whether it could conceivably make sense to think of deliberately provoking a crisis so as to remove the political logjam to reform. For example, it has sometimes been suggested in Brazil that it would be worthwhile stoking up a hyperinflation so as to scare everyone into accepting those changes. . . . Presumably no one with historical foresight would have advocated in the mid-1930s that Germany or Japan go to war in order to get the benefits of the supergrowth that followed their defeat. But could a lesser crisis have served the same function? Is it possible to conceive of a pseudo-crisis that could serve the same positive function without the cost of a real crisis?[12]

Williamson's remarks represented a major leap forward for the shock doctrine. In a room filled with enough finance ministers and central bank chiefs to hold a major trade summit, the idea of actively creating a serious crisis so that shock therapy could be pushed through was now being openly discussed.

At least one conference participant felt obliged to distance himself in his own speech from these risqué ideas. "Williamson's suggestion that it might be a good move to provoke an artificial crisis in order to trigger reform should best be read as an idea designed to provoke and tease," said John Toye, a British economist from the University of Sussex.[13] There was no evidence that Williamson was teasing. In fact, there was plenty of evidence that his ideas were already being acted on at the highest levels of financial decision making in Washington and beyond.

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The month after Williamson's conference in Washington, we caught a glimpse of the new enthusiasm for "pseudo crisis" in my country, although few understood it as part of a global strategy at the time. In February 1993, Canada was in the midst of financial catastrophe, or so one would have concluded by reading the newspapers and watching TV. "Debt Crisis Looms," screamed a banner front-page headline in the national newspaper, the *Globe and Mail*. A major national television special reported that "economists are predicting that sometime in the next year, maybe two years, the deputy minister of finance is going to walk into cabinet and announce that Canada's credit has run out. . . . Our lives will change dramatically."[14]

The phrase "debt wall" suddenly entered the vocabulary. What it meant was that, although life seemed comfortable and peaceful now, Canada was spending so far beyond its means that, very soon, powerful Wall Street firms like Moody's and Standard and Poor's would downgrade our national credit rating from its perfect Triple A status to something much lower. When that happened, hypermobile investors, liberated by the new rules of globalization and free trade, would simply pull their money from Canada and take it somewhere safer. The only solution, we were told, was to radically cut spending on such programs as unemployment insurance and health care. Sure enough, the governing Liberal Party did just that, despite having just been elected on a platform of job creation (Canada's version of "voodoo politics").

Two years after the deficit hysteria peaked, the investigative journalist Linda McQuaig definitively exposed that a sense of crisis had been carefully stoked and manipulated by a handful of think tanks funded by the largest banks and corporations in Canada, particularly the C. D. Howe Institute and the Fraser Institute (which Milton Friedman had always actively and strongly supported).[15] Canada did have a deficit problem, but it wasn't caused by spending on unemployment insurance and other social programs. According to Statistics Canada, it was caused by high interest rates, which exploded the worth of the debt much as the Volcker Shock had ballooned the developing world's debt in the eighties. McQuaig went to Moody's Wall Street head office and spoke with Vincent Truglia, the senior analyst in charge of issuing Canada's credit rating. He told her something remarkable: that he had come under constant pressure from Canadian corporate executives and bankers to issue damning reports about the country's finances, something he refused to do because he considered Canada an excellent, stable investment. "It's the only country that I handle where, usually, nationals from that country want the country downgraded even more—on a regular basis. They think it's rated too highly." He said he was used to getting calls from country representatives telling him he had issued too low a rating. "But Canadians usually, if anything, disparage their country far more than foreigners do."

That's because, for the Canadian financial community, the "deficit crisis" was a critical weapon in a pitched political battle. At the time Truglia was getting those strange calls, a major campaign was afoot to push the government to lower taxes by cutting spending on social programs such as health and education. Since these programs are supported by an overwhelming majority of Canadians, the only way the cuts could be justified was if the alternative was national economic collapse—a full-blown crisis. The fact that Moody's kept giving Canada the highest possible bond rating—the equivalent of an A++—was making it extremely difficult to maintain the apocalyptic mood.

Investors, meanwhile, were getting confused by the mixed messages: Moody's was upbeat about Canada, but the Canadian press contantly presented the national finances as catastrophic. Truglia got so fed up with the politicized statistics coming out of Canada, which he felt were calling his own research into question, that he took the extraordinary step of issuing a "special commentary" clarifying that Canada's spending was "not out of control," and he even aimed some veiled shots at the dodgy math practiced by right-wing think tanks. "Several recently published reports have grossly exaggerated Canada's fiscal debt position. Some of them have double counted numbers, while others have made inappropriate international comparisons. . . . These inaccurate measurements may have played a role in exaggerated evaluations of the severity of Canada's debt problems." With Moody's special report, word was out that there was no looming "debt wall"—and Canada's business community was not pleased. Truglia says that when he put out the commentary, "one Canadian . . . from a very large financial institution in Canada called me up on the telephone screaming at me, literally screaming at me. That was unique."*[16]

By the time Canadians learned that the "deficit crisis" had been grossly manipulated by the corporate-funded think tanks, it hardly mattered—the budget cuts had already been made and locked in. As a direct result, social programs for the country's unemployed were radically eroded and have never recovered, despite many subsequent surplus budgets. The crisis strategy was

* It must be said that Truglia is a rarity on Wall Street—bond and credit ratings are often influenced by political pressure, and are used to increase the pressure to enact "market reforms."

used again and again in this period. In September 1995, a video was leaked to the Canadian press of John Snobelen, Ontario's minister of education, telling a closed-door meeting of civil servants that before cuts to education and other unpopular reforms could be announced, a climate of panic needed to be created by leaking information that painted a more dire picture than he "would be inclined to talk about." He called it "creating a useful crisis."[17]

"Statistical Malpractice" in Washington

By 1995, political discourse in most Western democracies was saturated with talk of debt walls and imminent economic collapse, demanding ever-deeper cuts and more ambitious privatizations, with the Friedmanite think tanks always out front crying crisis. At Washington's most powerful financial institutions, however, there was a willingness not only to create an appearance of crisis through the media but also to take concrete measures to generate crises that were all too real. Two years after Williamson made his observations about "stoking up" crisis, Michael Bruno, chief economist of development economics at the World Bank, publicly echoed the same line, once again without attracting media scrutiny. In a lecture to the International Economic Association in Tunis in 1995, later published as a paper by the World Bank, Bruno informed five hundred assembled economists from sixty-eight countries that there was a growing consensus about "the idea that a large enough crisis may shock otherwise reluctant policymakers into instituting productivity-enhancing reforms."*[18] Bruno pointed to Latin America as "a prime example of seemingly beneficial deep crises" and to Argentina in particular, where, he said, President Carlos Menem and his finance minister, Domingo Cavallo, were doing a fine job of "taking advantage of the emergency atmosphere" to push through deep privatization. Just in case the audience missed the point, Bruno said, "I have emphasized one major theme: the political economy of deep crises tends to yield radical reforms with positive outcomes."

In light of this fact, he argued that international agencies needed to do more than just take advantage of existing economic crises to push through the Washington Consensus—they needed to preemptively cut off aid to make those crises worse. "An adverse shock (such as a drop in government

* Though Bruno did not attend the University of Chicago, he studied under and was mentored by the prominent Chicagoan Don Patinkin, quoted earlier comparing Chicago economics to Marxism for its "logical completeness."

revenue or in external transfers) may actually *increase* welfare because it shortens the delay [before reforms are adopted]. The notion that 'things have to get worse before they can get better' emerges naturally. . . . In fact, a high-inflation crisis may leave a country better off than if it had muddled along through less severe crises."

Bruno conceded that deepening or creating a serious economic meltdown was frightening—government salaries would go unpaid, public infrastructure would rot—but, Chicago disciple that he was, he urged his audience to embrace this destruction as the first stage of creation. "Indeed, as the crisis deepens the *government may gradually wither away*," Bruno said. "This development has a positive outcome; namely, at the time of reform the power of entrenched groups may have been weakened—and a leader who opts for the long-run solution over short-term expediency may win support for reform."[19]

The Chicago School crisis addicts were certainly on a speedy intellectual trajectory. Only a few years earlier, they had speculated that a hyperinflation crisis could create the shocking conditions required for shock policies. Now a chief economist at the World Bank, an institution funded, by this time, with tax dollars from 178 countries and whose mandate was to rebuild and strengthen struggling economies, was advocating the creation of failed states because of the opportunities they provided to start over in the rubble.[20]

For years, there had been rumors that the international financial institutions had been dabbling in the art of "pseudo-crisis," as Williamson put it, in order to bend countries to their will, but it was difficult to prove. The most extensive testimony came from Davison Budhoo, an IMF staffer turned whistleblower, who accused the organization of cooking the books in order to doom the economy of a poor but strong-willed country.

Budhoo was a Grenadian-born, London School of Economics-trained economist who stood out in Washington thanks to an unconventional approach to personal style: he let his hair stand straight on end, à la Albert Einstein, and preferred the windbreaker to the pinstripe suit. He had worked at the IMF for twelve years, where his job was designing structural adjustment programs for Africa, Latin America and his native Caribbean. After the organization took its sharp right turn during the Reagan/Thatcher era, the independent-minded Budhoo felt increasingly ill at ease in his place of work. The fund was packed with zealous Chicago Boys under the leadership of its managing director, the staunch neoliberal Michel Camdessus. When Budhoo quit in 1988, he decided to devote himself to exposing the secrets of his former workplace. It began when he wrote a remarkable open letter to Camdessus, adopting the *j'accuse* tone of André Gunder Frank's letters to Friedman a decade earlier.

Showing an enthusiasm for language rare for senior fund economists, the letter began: "Today I resigned from the staff of the International Monetary Fund after over twelve years, and after 1000 days of official Fund work in the field, hawking your medicine and your bag of tricks to governments and to peoples in Latin America and the Caribbean and Africa. To me resignation is a priceless liberation, for with it I have taken the first big step to that place where I may hope to wash my hands of what in my mind's eye is the blood of millions of poor and starving peoples. . . . The blood is so much, you know, it runs in rivers. It dries up, too; it cakes all over me; sometimes I feel that there is not enough soap in the whole world to cleanse me from the things that I did do in your name."[21]

He then went on to build his case. Budhoo accused the fund of using statistics as "lethal" weapons. He exhaustively documented how, as a fund employee in the mid-eighties, he was involved in elaborate "statistical malpractices" to exaggerate the numbers in IMF reports on oil-rich Trinidad and Tobago in order to make the country look far less stable than it actually was. Budhoo contended that the IMF had more than doubled a crucial statistic measuring the labor costs in the country, making it appear highly unproductive—even though, as he said, the fund had the correct information on hand. In another instance, he claimed that the fund "invented, literally out of the blue," huge unpaid government debts.[22]

Those "gross irregularities," which Budhoo claims were deliberate and not mere "sloppy calculations," were taken as fact by the financial markets, which promptly classified Trinidad as a bad risk and cut off its financing. The country's economic problems—triggered by a drop in the price of oil, its primary export—quickly became calamitous, and it was forced to beg the IMF for a bailout. The fund then demanded that it accept what Budhoo described as the IMF's "deadliest medicine": layoffs, wage cuts and the "whole gamut" of structural adjustment policies. He described the process as the "deliberate blocking of an economic lifeline to the country through subterfuge" in order to see "Trinidad and Tobago destroyed economically first, and converted thereafter."

In his letter, Budhoo, who died in 2001, made it clear that his dispute was over more than the treatment of one country by a handful of officials. He characterized the IMF's entire program of structural adjustment as a form of mass torture in which "'screaming-in-pain' governments and peoples [are] forced to bend on their knees before us, broken and terrified and disintegrating, and begging for a sliver of reasonableness and decency on our part. But we laugh cruelly in their face, and the torture goes on unabated."

After the letter was published, the government of Trinidad commissioned two independent studies to investigate the allegations and found that they were correct: the IMF had inflated and fabricated numbers, with tremendously damaging results for the country.[23]

Even with this substantiation, however, Budhoo's explosive allegations disappeared virtually without a trace; Trinidad and Tobago is a collection of tiny islands off the coast of Venezuela, and unless its people storm the headquarters of the IMF on Nineteenth Street, its complaints are unlikely to capture world attention. The letter was, however, turned into a play in 1996 called *Mr. Budhoo's Letter of Resignation from the I.M.F. (50 Years Is Enough)*, put on in a small theater in New York's East Village. The production received a surprisingly positive review in *The New York Times*, which praised its "uncommon creativity" and "inventive props."[24] The short theater review was the only time Budhoo's name was ever mentioned in *The New York Times*.