The New York Times
nytimes.com

August 15, 1999

The Russian Devolution

By JOHN LLOYD

Seated around the long table on the first floor of the modest dacha, the young men were relaxed, laughing a lot, talking excitedly, sometimes all together. They barely noticed as, guided by their chairman, I skirted the table and took a seat in a little room off their conference chamber to wait for a break in the proceedings. As I sat there, I marveled at the hilarity and occasional cacophony that fairly shook the wooden walls.

It was October 1991; the Soviet Union still existed. Yet next door, this little band of brothers was writing the economic program for an independent Russia. When the chairman joined me and began to describe what they were doing, I could not at first take it in. We were seated in a dacha in a little colony of state dachas some 30 miles from Moscow. The scope of the task contrasted oddly with the participants' youth and high spirits. Something graver seemed called for -- a hushed conference hall with graybeards attended by aides, perhaps. This seemed so . . . light.

In his soft voice, with the attitude of calm certainty that had made him the natural leader of these men, the chairman explained that the Soviet Union was finished. Any policy, whether organized by the West or pursued within the Soviet Union to save it from disintegration and collapse, would fail. The other 14 Soviet republics wished to go their own ways, and they should. Russia must find itself again, he said, and become a part of the modern, civilized world.

Within three months of the meeting, many of these men were ministers in the first Government of an independent Russia in more than seven decades. Pyotr Aven, an academic researcher, was Minister of Foreign Trade; Konstantin Kagalovsky, an academic researcher, was leading negotiations with the International Monetary Fund; Anatoly Chubais, a former academic researcher, was Minister for Privatization. My guide and their chairman, Yegor Gaidar, director of a small academic institute, was soon to become acting Prime Minister. Their mission: to make Russia a free, democratic, capitalist state.

For most of this decade, Russia has been consumed by the quest for these goals. Billions of dollars of aid have poured into reforms. Bitter struggles have been waged between free-market radicals and their Communist or nationalist foes, most significantly in 1993, when armed struggle broke out between the Parliament and the President. Great privations have been visited on the country in the name of necessary sacrifice. Yet what has changed for the better?

Russians, free to get rich, are poorer. The wealth of the nation has shrunk -- at least that portion of the wealth enjoyed by the people. The top 10 percent is reckoned to possess 50 percent of the state's wealth; the bottom 40 percent, less than 20. Somewhere between 30 and 40 million people live below the poverty line -- defined as around $30 a month. The gross domestic product has shrunk every year of Russia's freedom, except perhaps one -- 1997 -- when it grew, at best, by less than 1 percent. Unemployment, officially nonexistent in Soviet times, is now officially 12 percent and may really be 25 percent. Men die, on average, in their late 50's; diseases like tuberculosis and diphtheria have reappeared; servicemen suffer malnutrition; the population shrinks rapidly.

This is the Russia that many in the West now say we have lost. Lost not in the sense of having mislaid, by accident, but through our own actions and mistakes. Lost as a selfish, thoughtless man loses a woman who loves him -- through indifference or by pushing her away. Lost, the critics say, because we pursued agendas that were hopelessly wrong for Russia, and lost because we encouraged and supported precisely these men in the Government dacha, who were also hopelessly wrong for Russia.

These are the charges now being made in the West. Some of those who make them want the critique to be part of George W. Bush's election campaign. It is already becoming one of the most charged foreign-policy debates in America.

George Kennan, the venerable diplomat, former Ambassador to the Soviet Union and scholar, says in an interview in The New York Review of Books of Aug. 12 that "this whole tendency to see ourselves as the center of political enlightenment and as teachers to a great part of the rest of the world strikes me as unthought-through, vainglorious and undesirable." The case that we lost Russia begins with America's insistence on exporting the free market and takes in everything up to the NATO bombing of Serbia, an act that seems to have completed Russia's retreat from Washington -- a retreat with as many victims as Napoleon's from Moscow. The claim that we have lost Russia, in short, is a proxy for Clintonite failure to reshape Russia as an idealized America.

In Russia, the charge is that the New Russian reformers, abetted by the West, have destroyed the country's economy while enriching themselves. Many of those who make these charges (and who would like to see those they judge guilty locked up) will be candidates for the Duma (parliamentary) elections in December. And this critique may well be a major plank in the platform of one or more contenders for Boris Yeltsin's mantle in the presidential elections next summer. At the end of a century in which Russia has been raped by Bolsheviks, the country now seems to have been raped by capitalists. The stakes in this debate are very high.

The west's involvement in Russian reform was deep and early. Even before the reforms began, the big names in Western economics were debating how they should be managed. One issue overarched all others and would haunt the policy and its implementation down to the present. It was whether reform should push, hell for leather, the privatization of state assets or if institutions and a market infrastructure should be developed first.

"There was a debate about institutions and infrastructure back in 1990," says Joseph Stiglitz, the chief economist at the World Bank, whose earlier work on imperfect information and markets has put him in line for a Nobel. "I remember talking to a conference in Prague in 1991 on the theme of 'Quis Custodiet Ipsos Custodes?' (Who guards the guards themselves?') in a situation of rapid privatization. There were already differences between us then."

His major opponents were Jeffrey Sachs, a Harvard economics professor, and Lawrence Summers, a colleague of Sachs and now the Treasury Secretary. "They thought you needed to pursue privatization rapidly and that infrastructure would follow," Stiglitz says. "It was a divide then."

But it was Sachs and Summers who seemed to carry the argument. Sachs was at the height of his reputation following his success in breaking Bolivia's 24,000 percent inflation rate. In Warsaw in 1989, he explained market economics to the Solidarity activists about to be thrust into power. That December, the first post-Communist Government was quailing before price liberalization. Sachs got on the phone late at night in the office of Poland's Finance Minister, and harangued American officials until they promised to nudge the I.M.F. into providing $1 billion in support for the Polish currency. His myth as the economic liberator was born, and with it a mechanism known as "shock therapy." This was shorthand for a raft of measures -- price liberalization, budget stabilization, a slashing of subsidies -- undertaken more or less simultaneously to "shock" the economy into a therapeutic, market-driven recovery. The young reformers in Russia heard about it, and saw in Sachs and his mechanism their way forward.

When Bill Clinton came to the Presidency in early 1993, Summers was appointed Under Secretary of the Treasury for International Affairs. The official who covered the former Soviet Union and Eastern Europe was David Lipton, who had worked closely with Sachs on Polish and Russian reform. Sachs, on a leave of absence from Harvard, had installed himself and his team in the Finance Ministry -- where he spent a large part of one morning chiseling away a portrait of Lenin that had been embedded in the plaster of a colleague's office wall. Both men proselytized for shock therapy -- Sachs, vocally and impatiently, and Summers, behind the scenes, nagged and pushed the I.M.F. and the World Bank to lend, lend, lend. The money, tens and tens of billions of dollars, would be used for the essential first step in the reform, making the ruble convertible on world markets. Only with a hard currency, they believed, would investors commit the substantial sums needed to transform the Russian economy.

That never happened. Yegor Gaidar needed much more help than the Clinton Administration -- or any other Western government -- was willing to give him. He had come to Government at a time of collapse. At the end of 1991, as Mikhail Gorbachev left office and the Soviet banner was pulled down from the Kremlin tower, most Russians were lining up around the block for the basics. As Gaidar tells it, he had no choice but to let prices rise to increase supply and to scrap trade barriers so that foreign commodities could begin to fill store shelves.

Though Russia never did adopt the full menu of shock therapy, the release of prices and the soaring of inflation, with its effect of wiping out the average person's modest savings, was shock enough -- without, as the United States Deputy Secretary of State, Strobe Talbott, was to observe later, any therapy. The shock was such that by April 1992 the slender parliamentary majority the Government commanded for its measures evaporated. With that, Gaidar and Yeltsin began what has characterized Russian reform ever since -- a guerrilla struggle with a hostile, often violently hostile, legislature.

The reformers had hoped that the West would back them as soon as they took office. But it did not. This, for many insiders, was and remains the key mistake. Sachs ran himself ragged, zipping between Moscow, Cambridge and Washington, begging and demanding a big loan to stabilize the economy and give reform a chance. In retrospect, it was a fool's errand.

Here, at the very beginning of reform, is the first charge that we lost Russia -- and it is made by the economic radicals, East and West. They blame the Western Governments' lack of vision; Sachs loudly and bitterly, others still in Government more mildly and often unattributably. In Moscow, Yegor Gaidar has no doubt -- the West blew it. "There was a massive failure of imagination on the part of the West," he says. "There was no one statesman then in power who could grasp the enormity of the events happening here. The first delegation of high-level Westerners with whom I had to deal in office was that led by David Mulford, then the United States Under Secretary of the Treasury, on behalf of the Group of Seven richest countries in the world. He impressed on us backward Russians that our first responsibility was to repay the Soviet debt."

Says Sachs, who resigned as an adviser to the Russian Government in 1994: "I think in this debate the people with the power and the money, the governments of the West, must take the responsibility. It was going to be a major concerted effort to do anything, by the Russians and the West. I understood the challenge, I think, better than anybody. I never thought that the markets would do it by themselves -- never. We were never engaged. The dereliction of responsibility was massive. It does make you wonder. Were there people in the Administration who wanted Russia to fail, to be weak?"

Summers, who more than any other single official was in charge of Clinton economic policy on Russia, would not be interviewed for this article. But Lipton, who worked closely with him and has now left the

Government, says that "in '91-'92, it was Bush's last year. There surely was a failure to embrace the process of reform. I would agree that more could have been done. I think that people lacked the vision to see the consequences of the end of the cold war. The Bush Administration didn't grasp it. But it wasn't going to be a sure thing, whatever we did. The key thing was the Russians themselves -- the lack of people who knew what to do, the absence of a consensus on a Russian national identity. Poland wanted to be in Europe. Russia had no such consensus."

As the macroeconomic measures faltered for lack of foreign and domestic support, the first privatization program took off. Gaidar, assailed on every side by enterprise managers screaming for a continuation of subsidies, gave in inch by inch. But he was determined to proceed with the privatization of state assets, which all the reformers agreed would break the power of the Communist-era bosses and was, accordingly, at least as much a political as an economic policy. It was an article of faith that privatization would foster honest dealings and civic behavior by creating a middle class with a stake in the country, while cleaning out the Augean stables of the bureaucracy.

The opposition was ferocious. I went to one of the first auctions of state-owned shops, in the city of Nizhni Novgorod, in late 1992. Demonstrators organized by the local Communist Party jostled Government officials on their way in and protested that their common heritage was being taken from them. They carried banners with a slogan that would soon become a commonplace: "Privatisatsiya (privatization) = Prikhvatisatsiya (grabbing)."

As the auction got under way, a master of ceremonies dressed in a dinner jacket came on stage -- an exotic sight in a country where formal evening wear had been pronounced bourgeois and shunned for decades. He spoke fluent Russian, but he was a Czech who had developed his skills in his country's state property auctions. These, based on vouchers distributed to the population that entitled them to shares in the privatized companies, were the model for the Russian sell-off.

As each lot came up, the auctioneer described the shop in glowing terms and then threw it open to the audience. As he did so, it became obvious that the groups had already settled among themselves which was to bid for each shop under the hammer; there was little bidding up of the price. Some of the groups were men with darker skins than the fair Russians; a couple of matrons near me said, loudly, "Blacks!" (the Russian derogatory expression for people from the Caucasus), and then, "Mafia!"

I realized then, with a start, that the freedoms Russia had accomplished over the past few years were seen quite differently on the ground. This was no gathering of economically knowledgeable actors. The majority were puzzled and hostile citizens raised in a Soviet culture, with a few sharp customers thrown in -- perhaps already accustomed to cutting corners and wheeling and dealing in the many cracks in the command economy -- who were taking advantage of an incredible stroke of luck.

The politician who emerged to effect a privatization that still dwarfs every other such exercise many times over is one of the most remarkable figures of post-Communist politics. Anatoly Chubais, who had come to Moscow with little preparation, no money and not even an apartment, rose in the next seven years to become second in power only to Yeltsin himself. He also became, for the majority in the political class, the target of extraordinary hatred -- some of which, in less virulent form, has crossed to the West. He has retained the protection of Yeltsin and thus keeps a place in the informal power structure. On a trip to Washington in May, he saw Robert Rubin, then the Treasury Secretary, and Larry Summers; Secretary of State Madeleine Albright and Strobe Talbott; Stanley Fischer of the I.M.F., and the national security adviser, Sandy Berger -- a level of access that some Russian officials found disturbing. Yet no single figure is more vulnerable if power in Russia goes to one who owes him nothing, or wishes him ill.

In 1992, Chubais confronted an economy that was virtually wholly state owned (Gorbachev had permitted the growth of a few "co-operatives"), a distrustful Parliament and high-level managers who had effectively taken control of their enterprises and wished to enjoy their fruits undisturbed. "What is never remembered," Chubais said in a 1995 interview, "is that even before the collapse of the Soviet Union, the managers were stealing everything they could, in association with the state bureaucrats. You could not stop it. You could not get the managers -- the insiders -- out. They were powerful enough to block everything. The only way you could get the property into the private sector was to get the insiders motivated and rewarded. You could dream up 100 schemes that were better or purer than the ones we brought in, but this was actually the only way you could do it."

This huge and sudden transfer of assets is a major area of the debate on Western strategy toward Russia. It has attracted the most prestigious -- and for Western Governments and the international financial institutions the most embarrassing -- critique, coming as it does from within their own ranks.

That attack came in the spring of this year, from Joseph Stiglitz. In papers given in May and June, the World Bank's chief economist argued that much of the responsibility must be taken by the advocates of shock therapy. "The standard Western advice . . . the 'Washington consensus,'" he wrote, took "an ideological, fundamental and root-and-branch approach to reform-mongering as opposed to an incremental, remedial, piecemeal and adaptive approach. . . . Some economic cold warriors seem to have seen themselves on a mission to level the 'evil' institutions of Communism and to socially engineer in their place the new, clean and pure 'textbook institutions' of a private property market."

In a probably unconscious echo of the signs held by the demonstrators in Nizhni Novgorod, Stiglitz said that the Western and Russian radicals had a particular view of government -- that it was a "grabbing hand," always seeking rents from corporations, always interfering to make things worse. "The grabbing hand theory," he wrote, "sees the state as being irredeemably corrupt -- while the private sector is viewed through rose-colored glasses. Yet the resulting program of transferring assets to the private sector without regulatory safeguards has only succeeded in putting the 'grabbing hand' into the 'velvet glove' of privatization."

Stiglitz, with other critics of shock therapy and Western aid to economic reform, believes that assets should be put into private hands at a deliberate pace, and only after effective laws and working markets have been established. In a passage that infuriated reformers, he said that China, with no I.M.F. program and little outside advice, has achieved high growth rates over the past decade while Russia, with a number of I.M.F. programs and endless outside advice, has steadily declined.

"Sachs and Summers were right when they said that you can't live with hyperinflation," Stiglitz says now. "Though even the fight against inflation can be taken too far. But those who thought that macroeconomic changes alone were sufficient were wrong. And those who put privatization above all else were clearly wrong. Summers and Sachs and others thought that you had to pursue privatization, and infrastructural change would follow. They thought that the new owners of private property would demand that this happen. But instead they took their money out."

This is a direct challenge to the Clinton team. Stiglitz has used his prestige and his office to strike at the center of the strategy promoted by Summers and Talbott in the Government and by Sachs and others in their advisory roles. He has said they were fundamentally and damagingly wrong in the view he attributes to them -- that the first issue was putting state property into private hands.

Lipton will have none of this critique: "Anyone who says that privatization ignored the real conditions of Russia's reform is totally wrong. Russia needed what we tried to assist putting into place -- laws, property rights, banking institutions, capital markets. The privatization did give too much to insiders, but Chubais had to compromise. The first wave of privatization created a new class and a capital market, and these are achievements which have endured."

Yet for the most part, when the new Russian biznismeny got hold of the properties, their first thought was not how to spruce them up or extend their product lines or retrain the staff in post-Communist customer relations. Rather, it was how to realize the assets in cash, change the cash into dollars and get it out of the country. Capitalism became capital flight. Just how much money has left Russia in the past seven years isn't known precisely, but estimates vary from $200 billion to $500 billion.

"This process, we now know, is going to take a long time -- maybe a generation," says Harry Broadman, a World Bank economist. "Because of what's happened in the last seven years, vested interests have been created that were not present before and that make it more difficult to reform to get growth and economic democracy."

At the top, there was an increasing absence of authority. Yeltsin declined in health and in coherence. He drank in binges, as we know from the many memoirs of his courtiers. Even more disabling were his depressions, when he stared at the wall of his office, immobilized for hours, even days. His periods of triumph -- in 1991, over the coup plotters, and in 1993, over his own Parliament in a bloody shootout -- were followed by inaction and withdrawal.

In 1994, he seemed drunk in public at a solemn ceremony in Berlin to mark the Soviet Army's withdrawal. He then slept through a brief visit with a waiting Irish Cabinet on a stopover en route home from Washington. The memoirs of his bodyguard, Aleksandr Korzhakov, claim he suffered a heart attack. The intervention in the rebel province of Chechnya got under way in December 1994 and from the start went horribly wrong. Yeltsin's ratings slumped to low single figures and stayed that way into 1995.

Throughout these years, the Russians perceived the West as supporting what to most of them seemed a Government of criminality and inefficiency. After Yeltsin won the 1993 battle with Parliament by bringing in the tanks, Strobe Talbott -- the political counterpart on Russia policy to Summers in Treasury -- sent a message of congratulations that is still interpreted by the opposition as glorying in the blood of those who died as the Parliament building was shelled.

Much later than the radicals had hoped, the I.M.F. and the World Bank began substantial lending. So long as Yeltsin was President and a few reformers remained in Government -- Chubais was the constant figure until 1995, sporadically thereafter -- the official view in the West was that reform was on track and our money was keeping it so. In background briefings from World Bank and I.M.F. officials, I was told of the anguish they felt when money disappeared and public silk purses had to be made out of private sows' ears.

The officials knew what was happening, but the West was locked into a desperate struggle to preserve reform and to keep the Communists out of power. They would not give up as long as "our guys" had a chance. "The I.M.F. should have shown more guts in resisting political pressure," one official said. "The big mistake was not realizing soon enough that the reformers lacked the levers of power to do what they had agreed and to keep on lending. We should have been tougher."

On the ground in Russia, Western advisers worked with the reformers to set up market institutions. But it was a fraught undertaking: the Westerners themselves were caught in -- or constructed -- webs of patronage.

A key text in the critics' armory is a book by Janine R. Wedel, published late last year, called "Collision and Collusion." Wedel, an anthropologist at George Washington University, had worked for many years in Poland and moved east to Russia in 1994. She came to realize that the Western "clan," as Russians called it, around Chubais was a very close-knit group indeed. Most of the more than $300 million provided for privatization by the Agency for International Development went directly to or was controlled by the Harvard Institute of International Development, run by Chubais's aides. Two of its Western members, Andrei Shleifer and Jonathan Hay, both then of Harvard, are now under investigation for allegedly undertaking "activities for personal gain."

"In a country like Russia," Wedel says, "it was exactly the wrong thing to do to choose a particular group of people -- the New Russians in politics. They were seen as embodying our ideas. They talked the talk. They were very savvy operators. It was fascinating how people from the West latched on to the features in their Russian counterparts they wanted to see."

In this febrile atmosphere, as Russia veered between a success always just around the corner and the reality of a plunging economy, there emerged, in 1995, the bones of a plan that became the most important element in the reform process -- what has come to be called "loans for shares." Regarded today almost universally as an act of colossal criminality, it has defined the Russian economy and Russian business to the world. It completed Boris Yeltsin's retreat into an isolation from his country and created billionaires without the tedious process of building wealth from below. For Anatoly Chubais, it was a "pact with the devil."

Though most of the enterprises had been privatized by then, the richest pickings had not. These included the energy companies, the telecoms and natural-resource corporations like Norilsk Nickel, the biggest nickel producer in the world. The emerging financial class -- already building themselves streamlined glass and steel offices and roaring about the boulevards of the capital in armor-plated Mercedes flanked by armed guards -- wanted what they felt was their own. They wanted to be Morgans, Carnegies, Rockefellers. They wanted to transform Russia into a market they would dominate.

The loans-for-shares scheme was the brainchild of Vladimir Potanin, one of the new Russian businessmen. Potanin had built up a bank, Uneximbank, from the ruins of the Soviet Vneshtorgbank. Norilsk Nickel was a client, and he thought he could run it better than the managers who kept it going in the bleak Arctic Circle city that was its home. In the mid-1990's, he conceived the idea that the state would give him the right to manage it; in return, he would grant the state -- strapped for cash, as ever -- a large loan.

The idea had immediate appeal. The Government still controlled a dozen vast enterprises, mainly in the oil sector, that were abysmally managed. Potanin's fellow financiers, most of them fierce competitors, were eager to extend their empires. So, he proposed, why not offer loans for shares? He gathered them together for what became a series of exploratory meetings -- Mikhail Khodorkovsky of the Menatep group, Boris Berezovsky, who had made a fortune from car production and sales, Mikhail Fridman and Pyotr Aven (the former Foreign Trade Minister) of Alfa Group, Aleksandr Smolensky of Stolichny Bank and Vladimir Gusinsky of the MOST banking and construction group. These men were not accustomed to co-operating with one another. But the bonanza promised by Potanin's plan was too tempting to allow the usual rivalries and feuds to take precedence. If it worked, they would become masters of the land. Potanin was persuasive, and Chubais, at first scornful of the idea, agreed to it at a Cabinet meeting in March 1995.

But there was -- as always in Russia -- a catch. The deal presupposed a continuity of Government. By the end of 1995, Yeltsin remained deeply unpopular, as well as remote and ailing, and 1996 was a presidential election year. His rival for the presidency was Gennadi Zyuganov, leader of a Communist Party he had built up from near extinction to win a strong representation in the parliamentary elections of December 1993 and a dominant one in the elections of 1995. Zyuganov was scoring way above Yeltsin, and he was trying to talk the Yeltsin talk -- stressing the need to create an attractive business climate. This was the kind of Communist whom capitalists might grow to like.

In February 1996, with presidential elections looming in the summer, Zyuganov went off with a raft of Russian V.I.P.'s to Davos, where the world's high and mighty gather annually at the World Economic Forum. Everyone seemed to want to meet him, to shake his hand.

Things were looking grim for the Russian bankers. The financier George Soros reportedly told them over coffee that the Communists were going to win and that they should ready their private jets for takeoff. According to Chrystia Freeland, a journalist who is completing a book on the new Russian capitalists, the bankers say he turned to them and said: "Boys, your time is over. You've had a few good years, but now your time is up." The bankers were horrified. They had a habit of putting their money abroad, but they did not want to follow it. Yet what to do?

Hanging out in Davos was Anatoly Chubais, by now an out-of-work politician. Too hot, after a huge parliamentary victory by the Communists, to keep in the Government, he had seen his loyalty to Yeltsin rewarded by being fired. Sitting there, solitary and depressed, his spirits began to revive as he sensed a new political opening. He called a news conference in which he scolded the Western businessmen for flocking to Zyuganov. "If Zyuganov wins the Russian presidency in June, he will undo several years of privatization and this will lead to bloodshed and civil war," he said.

If the foreign businessmen were not overly impressed, the Russians were. There, at Davos, a pact was formed between the bankers and Chubais. Desperate to avoid a Government that would threaten their wealth, they made him an offer: lead the campaign against the Communists, and we will open our purses and our influence to you. He was paid, some of the bankers told Freeland, a $3 million fee in the form of an interest-free loan.

In the crucible of the 1996 election campaign, the shape of Russian power today was finally molded. The bankers controlled the main TV channels and newspapers; indeed, Berezovsky had been given control of the oil company Sibneft in order to help finance the main state TV channel ORT, which became a mouthpiece for the President. Gusinsky's NTV, a trenchant critic of Yeltsin during the Chechen war, turned on a kopeck to support him.

Yeltsin, who had sunk into inactivity and had all but decided to provoke a crisis in order to cancel the elections, was roused by Chubais and Yeltsin's daughter, Tatyana Dyachenko, who became and remained the main gatekeeper for her father. Money was poured into advertising campaigns, into regional tours, into bribing journalists. Yeltsin, through Chubais, called in the chips. And he won. Communism was confounded, for a second time in a decade, by the forces of freedom and democracy.

But that is not how it looked then to Russians, or looks now to anyone else. The bankers -- or oligarchs, as even they call themselves -- consolidated their power, but they did not invest, reverting to their past practice of asset stripping and banking abroad. Reforms, which Chubais and others pushed from a position of, at first, unrivaled power after the elections, once more foundered on a recalcitrant bureaucracy and a sullen country. Successive Governments grappled in vain with a tax system that could not develop a reliable framework for taxing the new capitalism.

Last August, the financial crises in Southeast Asia touched off a collapse in Russia; the currency fell 40 percent, and with it the Russians' already miserable living standards. Chubais was expelled from Government once more; he is now head of Unified Energy Systems, the main electricity utility -- an oligarch in his own right.

No one now defends the loans-for-shares scheme. One World Bank official called it a "tragedy." Lipton, choosing his words with obvious care, says that it was an "unwise political compromise -- to let a few of your guys have a lot of resources. It fed the asset-stripping instincts of the oligarchs. Because it was linked to the campaign contributions of the oligarchs, it cemented them into the state. But you must put yourself in the place of the policy makers. Chubais was fighting for a second phase of privatization like the first phase. He needed to make a deal. But I'm willing to condemn Chubais for this. He realizes it was unwise. His argument is, it was either that or no privatization."

But its effect has been to complete the corruption of the state. "The fish rots from the head," says the famous Greek proverb, and the head and heart of Russia are seen as deeply corrupt -- and worse, deeply ineffective. Boris Yeltsin's approval ratings have been in low single figures for more than a year. He is seen as a mixture between an invalid and a puppet, his strings jerked by masters behind his throne.

The domestic puppet masters are now simply -- if sourly -- accepted as a fact of Russian life. The circle around Yeltsin is tight and powerful; it comprises his daughter Tatyana Dyachenko; his former chief of staff, Valentin Yumashev, and Boris Berezovsky and his protege, Roman Abramovich, who controls his Sibneft oil company.

Berezovsky has been the main beneficiary of the "devil's pact" struck with Chubais (though the two are bitter rivals now). He, with Abramovich, had the major say in the naming of the present Russian Cabinet. They insisted on the appointment of their friend, the former railway boss Nikolai Aksyonenko, as First Deputy Prime Minister. Sergei Stepashin, the Prime Minister, was told to take it or leave: he stayed. Stepashin, whom Chubais promoted to American officials during his May visit as a future President, is at present hardly in command of his Cabinet. Nor is he, as the fourth Prime Minister within 12 months, secure in his office.

What happens in the Kremlin happens in the street. In Moscow researching this article, I was arrested for drunk driving, given a Breathalyzer test whose "positive" results I was not allowed to see and confronted with the threat of a disruption to my work so large that I took the usual way out for a foreigner or New Russian. I paid the fine on the spot -- with a $100 bill for which no receipt was issued -- and I was allowed to drive off in a "dangerously drunk" condition. (To add piquancy to the sting, I was lectured by the traffic policeman who "fined" me on NATO's criminality in bombing the Serbs.)

In Moscow, I went to see Konstatin Kagalovsky, one of the young men I had met in the state dacha eight years and a lifetime before. He was the first reformer I had got to know when I went to live in Russia early in 1991. Back then, he lived in a two-room, comfortless flat in one of the massive projects that ring Moscow. Thin and intense, he had sat me down at the kitchen table and, battling with his halting English and my halting Russian, talked of Adam Smith and Milton Friedman and Jeffrey Sachs (whom he asked to join the dacha group soon after I had met them). He told me of the futility of Gorbachev's reforms, the need for policies of the strictest monetarist provenance and of the pure evil of Communism.

The man who came out of his office to meet me -- after I had gone through two careful security checks and several soft-carpeted corridors in an expensively renovated 19th-century Moscow mansion -- had put on some weight and wore a well-cut suit and rich tie. On the wall behind him were photographs of him meeting with Margaret Thatcher and George Bush. On leaving Government service, he had joined Mikhail Khodorkovsky's Menatep -- then one of the biggest of the new banks -- and now was vice chairman of the Yukos oil company, which Menatep had acquired in the loans-for-shares deal.

"In 1991 and into 1992," he said, "we were still in our romantic period. Our views and feelings were based on our readings, discussions, ideas -- some of them childish, it seems now. After that" -- he smiled a little -- life changed all of us. It's very difficult to be effective in politics and keep your basic values. Even Yeltsin -- in the beginning the major decisions were based on these basic values he had. Not now, not now. After the 1996 elections, things changed fundamentally. Chubais was the best organizer of all of us, but what he did to win the 1996 election was to say, 'The aim is good -- anything goes.' Everyone closed their eyes. But in Government afterward, the main thing that had to be done was paying back the bankers, and economic reform got a low priority.

"We now see such simple truths: that a country that is based on stealing and corruption is much less efficient than a normal society. And that the end doesn't justify the means. After 1996, corruption became a systematic element of the state. It went to the core of the new Russian state." He paused and then said something that, coming from one for whom anti-Communism had been an article of faith, still gives me a shock. "If the Communists had won in 1996," he said, "I'm not sure we would be in a worse situation than now."

Corruption is seen by many as the greatest factor in Russia's loss, and those who see it most clearly (because they make a living studying it) are intelligence officers. Fritz Ermarth, who spent his professional life in the Central Intelligence Agency and did two tours with the National Security Council, now spends much of his time in Congress huddling with staff members over how to stop what he sees as the rot in Russia policy. He believes that Russia has become so corrupt that, in certain essential respects, business cannot be done with it at all, and he blames, in large part, the high officials whom he served.

"We followed the dictates of a theory that was made for countries with some trouble because of temporary government profligacy, not for a country melting down," Ermarth says. "In fact, what the United States Treasury and the I.M.F. were doing was financing and licensing a Great Grab and calling it reform. And there was so much in Russia to steal that was so precious: oil, diamonds, nickel. It was the kind of opportunity that comes once in a millennium."

In November last year, unnamed C.I.A. officials told The New York Times that in 1995 they had compiled a large dossier on Viktor Chernomyrdin, then the Russian Prime Minister. They sent the material to Vice President Al Gore, co-chairman of the Gore-Chernomyrdin Commission, in which much of the government-to-government business between the countries was handled. It came back, said the officials, with what was described as "a barnyard epithet" scrawled on it. The lesson they reportedly took away was that evidence of high-level corruption was not wanted. Thus, when they established that a German businessman had been asked for $1 million to see Chernomyrdin, they did not circulate the report.

But Chernomyrdin -- now back as president of Gazprom, the energy monopoly he created and partially privatized and whose huge revenues, vast holdings and large exemptions from taxes now make it a state within the Russian state -- was for years a key interlocutor with the man who seeks to prolong Democratic rule in the White House, Al Gore. Gore was deeply involved in Russian policy through the Gore-Chernomyrdin Commission, which dealt with economic issues. He was a strong advocate of more aid and assistance to Russia, harshly criticizing the World Bank and I.M.F.'s reluctance to lend. He exhorted American business to invest in the country and lauded Chernomyrdin, whose personal fortune, held abroad, is estimated by Russian security sources in the billions of dollars -- an allegation he denies. When this checkered record is eventually held up to the light during a Presidential campaign, Gore will have much to answer for.

Already, these issues are boiling up in political circles. Politicians like Curt Weldon, a Republican Representative from Pennsylvania, now barrage the Administration with questions and criticisms on their handling of Russia, drawing strength from an increasingly cohesive "Lost Russia" lobby.

And this lobby now looks as if it will have a powerful mouthpiece: the front-runner in next year's Presidential race. The main foreign-policy adviser to George W. Bush, Condoleezza Rice, former provost of Stanford University, is pressing to make the charge that the Clinton-Gore Administration lost Russia a major part of the Presidential campaign. Rice, who will shape Bush's policy and probe Gore's weak spots, poses a special danger for the Democrats -- she has been an expert on Russia for decades.

Rice admits to the difficulty of the transition from Soviet Communism, that the fault lies largely with the Russians. She also acknowledges the hazards of retrospective wisdom. "When all that's said," she says, "you are left with a policy that leaned very far toward accepting the mere rhetoric of reform. It didn't recognize how mercurial Yeltsin is. It didn't react to the fact that an awful lot of money has been siphoned off. This gave a false sense of security to the Russians. They felt that no matter what reforms they didn't do, they would get the I.M.F. money. No matter what behavior they showed, they would get friendship.

"I think what's called for now is a major disengagement from Russian domestic policies. The corruption reached into very high places, to people with whom we dealt and are dealing. I know that international politics has to deal with issues like corruption, but we should have confronted them with what we knew, and I doubt this was done. The Administration equated Boris Yeltsin with democracy, and you can't do that now.

"Russia is a huge country with foreign-policy aims that will sometimes coincide with ours and sometimes won't. Our big mistake was in assuming we would have a strategic partnership. In that regard, we were spoiled -- by getting so much from them so early. What we now face in international politics is a Russia more dangerous than it has been, because it is coming apart. And so one must ask, given what we tried to do and hoped for in 1991, What went wrong? How could it have happened? What is our responsibility?"

It is the same question again: Who lost Russia? Is it so lost that corruption has eaten into the very fabric of the state and that it is now doomed to repeat its past deep into its future? Has the President we in the West supported, feted, lauded become worse than the Communists we helped him to overcome? Have the market reforms that we promoted and helped pay for been so counterproductive that we have helped create a Frankenstein's monster of a state, which lost its way out of gradualist reformism in the 80's into a shock no society could bear?

The most dismal "proof" that Russia is lost is that Russians now proclaim that they wish to be lost to us. The NATO action in Kosovo has produced a bitter reaction, the more so for emphasizing to the Russians their relative weakness. In Moscow, I called on an old contact and friend, Boris Fyodorov, who though never one of Gaidar's gang had been a tough radical as the Deputy Prime Minister for finance. Kosovo came up, and his geniality vanished. He said that the bombing of Kosovo was a preparation for a NATO raid on Russia. "That's absurd!" I said. "NATO is absurd!" he shot back.

Strobe Talbott has had to take more Russian grief over Kosovo than anyone else in the West. In his time in office since 1993, he has reached deep into his command of superlatives to describe Western joy at the liberations we thought we were witnessing. Life is tougher now. On the night the Russian troops were dispatched to dash into the Kosovan capital of Pristina ahead of the NATO forces, Talbot was in the Russian Defense Ministry being harangued till dawn by the Defense Minister, Igor Sergeyev, and his colleagues on the impossibility of Russian troops submitting to NATO command. This was an argument he had heard for weeks, in his relentless shuttle to and from Moscow trying to get an agreed position on a settlement of the war. At 3 in the morning he was informed that CNN was reporting on the Russians' dash to Pristina -- something his hosts had not found time to mention.

In an interview, Talbott made his case: that Kosovo marks a breach, but not an unbridgeable one. Business has gone on, agreements keep being made and the I.M.F. is preparing a new program. Withdrawing -- as Condoleezza Rice advises -- would be to "put Russia in a corner with a dunce's cap on its head and ignore it, which is not an option for any Administration." Its re-entry into the world is indeed a vast endeavor, he says, but one to which we are if not central, not marginal either.

"Russia is a great, big, spiraling, complex country," Talbott continued. "It is undergoing perhaps the most extraordinary and comprehensive transformation of any country that did not lose a war. It is finding itself both in the modern world as an economy and in the planet as a physical entity. It is doing so in a way that is very much its own, and must be."

Talbott waxed a little poetic, quoting, he said, no one, not even himself. "Our policy toward Russia must be that of a lighthouse, because Russia is going through a very rough sea. They can locate themselves against this light. The real question is the overall direction. Nothing that has happened over the last seven years makes me think that they have reversed course or are about to be submerged in a red-brown tide of fascism. This is decades long. The judgment of history on any question is not yet."

But politics do not wait on history's judgment. The judgment that Russia was lost through Western action or inaction is being made now, and is increasingly politicized. Talbott, whose 1993 book (with Michael Beschloss), "At the Highest Levels," is a detailed and sympathetic account of United States-Soviet relations in the last years of the Soviet Union, had a first-rate training for Russia policy. Nevertheless, as Talbott himself says, "this was unprecedented. There was no recipe book or users' manual. We were experimenting as we went along. Yet, even now, Russia is not failing. It has moved and will keep on moving."

There must be a large element of hope in that last remark, but perhaps hope was all we could have offered in the first place. Russia's 20th century has been unimaginable in its horror, uniquely awful for any major country in modern times. "Oh children, if you only knew/The cold and gloom of days ahead," Alexander Blok wrote in 1914. At the end of the century, the "children" know it. They know that Communism worked best in destroying most remnants of civil society, leaving a people deeply distrustful of everything, especially one another.

Two last snapshots, one from near the beginning of Russia's century, one from nearer to its close: Isaac Steinberg, a uniquely freethinking Bolshevik who was briefly Commissar for Justice, noted in 1920 that the effect of the terror his party was waging on its fellow Russians was to produce a mutually hateful misery. "See . . . how this mass of humanity, accidentally chained together, seems to lack all sense of mutual sympathy and understanding, how everyone sees in his fellow man only a rival!"

The contemporary witness comes from Norilsk, where the oligarch Vladimir Potanin has his nickel works. Beginning in 1937, Jadwiga Malewicz served 10 years at Norilsk for "anti-Soviet activity," and she is there still. In an interview for Angus McQueen's limpid and horrifying documentary film "Gulag," she said: "We built Norilsk from nothing; truly, it was built on bones. Once, I told a girl working with me to stop working so hard, or she'd kill herself. Someone informed on me. I got 10 days in a freezing punishment cell, a piece of bread each day. I nearly died. I no longer trust anyone. I have never done a good deed since then."

Russia suffered from our mistakes and preconceptions but -- barring catastrophe -- ultimately will make its own accommodation. It never was ours to lose. Russia lost, not itself but the trust that makes societies civil and functioning.

The competing Western visions of how to bring it into the contemporary world are important more for what they have said about our hopes and fears than about Russia's possibilities. We can't know whether we have "lost" Russia by prescribing the wrong medicine or have helped save it by administering a nasty potion that, however unpleasant, will ultimately bring health.

It seems unlikely that the potion will be wholly rejected. Russia will make of it what its history allows. It must find itself; until then, we can do little more than watch, offering an occasional bit of encouragement from the sidelines.