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Recent Developments With Respect to the Ruble

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There have been two, or perhaps three, important developments with respect to the ruble since the publication in April 1960 in Staff Papers of "Russian Gold and the Ruble." This paper attempts to describe these developments and to appraise their significance.

In May 1960, a new "heavy" ruble was announced, with a value equal to ten existing rubles. The shift from light to heavy rubles is to be made on January 1, 1961, by exchanging existing paper and coins for new units. Secondly, on November 15, 1960, it was announced that the gold content of the heavy ruble is to be established, also effective January 1, 1961, at 0.987 grams of gold. Since the par value of the U.S. dollar, stated in terms of gold, is equal to 0.889 grams of gold, the new Soviet gold equivalent will give the heavy ruble (100 kopeks) a dollar value of $1.11. Third, on November 17, a newspaper item reportedly published in Ultima Hora, a left-wing newspaper in Brazil, stated that delegations from Brazil and the U.S.S.R. would soon confer in Geneva or Moscow to study the possibility of placing rubles on sale in the Brazilian Currency Exchange and of engaging in free exchange dealings in Soviet currency. The news item stated that the exchange of the ruble in the Brazilian market would result in an increase in trade, and that in the future any industrialist or businessman could buy or sell the required amount of rubles directly from Soviet commercial houses. This report has not been confirmed by official Brazilian sources, nor has it yet appeared in any other publication.

Background1/

Since the establishment of the U.S.S.R. in 1917, there has been a number of major changes in the Soviet money unit and money supply. There were far-reaching reforms of the Soviet domestic money supply in 1922-24 and in 1947, and substantial adjustments in the external value of the ruble (unaccompanied by changes in the domestic money supply) in 1934, 1936, and 1950. Only in 1924 did a domestic change in money unit coincide with an external one in the exchange value of the ruble.

1/ This background is largely based upon The Bank for International Settlements, The Revaluation of the Rouble, C.B. 218 (1950); V. Holubnychy, Ruble Foreign Exchange Rates, Bulletin of Institute of Study of U.S.S.R. (Munich), Vol. 5, No. 8 (1958); H. Schwartz, Russia's Soviet Economy, 2nd Ed. (1954), Ch. XII, and The Soviet Economy 1956-58, Conference Board Study No. 60; and "Ruble," Encyclopedia Brittanica.

Domestic changes in the ruble

Under the influence of war, revolution, and reconstruction, inflation developed at a terrific pace. Reform was undertaken in a number of steps in 1922-24. In 1922, a new unit (the chervonetz gold ruble) was established alongside the old ruble; its value was set at 10 prewar gold rubles, or 7.74 grams of gold. In March 1924, the rate of redemption was defined at 50 billion old rubles for one chervonetz ruble. Later in 1924, the old rubles were replaced with new rubles, at the rate of 10 new rubles to the chervonetz; the new rubles were thus equivalent to 0.774 grams of gold, and a dollar exchange rate of 1.94 rubles.

Inflationary pressures continued, however, and stringent rationing was imposed in the early 1930's and intensified during World War II. Prices continued to increase after the war. During all of this time, the liquidity of the Soviet economy, as reflected by holdings of cash, bank deposits, and holdings of government bonds, increased.

In December 1947, the Government announced its most important domestic monetary reform since 1924. All (old) rubles were to be exchanged for new rubles at the rate of one for ten; deposit accounts in government banks were revalued on a sliding scale, ranging from 1:1 for the first 3,000 rubles to 1:2 for amounts in excess of 10,000 rubles; government bonds were exchanged for new bonds at the ruble ratio of 1:3; and current accounts of collective farms and cooperative associations were revalued at the rate of 4 for 5. Taxes, obligations to the state, wages, and other fixed obligations were unchanged, and ordered to be paid at the same rates in the new currency as in the old. These actions reduced excessive Soviet liquidity and inflationary pressures. Hoards were uncovered and eliminated, and according to reports these corrections were accompanied by penalties and punishment in some cases. This reform was declared to have "restored the full value of the Soviet ruble."

In general, this monetary reform adversely affected peasants and others who had benefited from shortages and been able to accumulate hoards of cash; it improved the position of the urban population. This internal adjustment in the money supply and in bond holdings was not accompanied by any modification of the exchange rate.

External changes in the ruble

The last step in the currency reforms of 1922-24 established an exchange rate by which the dollar exchanged for 1.94 rubles (the prewar parity). When the United States increased its official price of gold in 1934, reducing the gold content of the dollar by 41 per cent, the U.S.S.R. cut the dollar's ruble value by the same proportion, from 1.94 rubles to 1.15 rubles. In 1936, apparently in recognition of the price effects that followed a relaxation of rationing, the gold content of the ruble was reduced from 0.774 grams to 0.177 grams, a devaluation of 77 per cent as measured in gold, and the dollar was made equivalent to 5.02 rubles. For three years, 1934-37, the foreign exchange value of the ruble was related to the French gold franc, but in 1937 the parity was shifted to a dollar base, with one dollar equal to 5.30 rubles. (Though the dollar-franc cross rate would have suggested a dollar equivalent of 5.02 rubles, there was no talk of a devaluation at the time.)

In 1950, the ruble was declared equal to 0.222 grams of gold--the announcement did not refer to any previous gold content of the ruble--and the stated parity was increased and set at 4 rubles to the dollar. The official explanation for this change was that the value of the ruble had risen since the war, the American dollar had become an unstable currency, and the ruble must therefore shift to a gold base. This increase of the dollar equivalent of the ruble was almost uniformly interpreted in the West as lacking economic justification, since the very large increases in Soviet prices should logically have led to a decrease in the dollar value of the ruble.

During the 1950's, the ruble exchange rates of currencies other than the dollar were related to the dollar cross rates of those currencies in free world markets. The U.S.S.R. authorities have in recent years quoted ruble equivalents of an increasing number of currencies.

Preferential exchange rates for the ruble

During World War II, diplomats and many other foreigners in the U.S.S.R. were allowed a preferential exchange rate of 12 rubles to the dollar. As of 1948, the extent of preference was reduced and the rate changed to 8 rubles. After the monetary reform of 1950 all preference was eliminated.

In the past few years, there has been an increase in tourist travel in the U.S.S.R., and much criticism of the expensiveness of such travel. Some tourists had been able to meet these high prices by buying rubles outside the U.S.S.R., but in 1955 the Soviet Union reacted strongly, reminding all potential buyers that it was a criminal offense to bring rubles into the U.S.S.R. The problem of high prices at the official rate was met by special package deals to tourists, which in one way or another worked out to implicit ruble exchange rates lower than the official one. Finally, in the spring of 1957, the Soviet Government began to sell rubles to tourists and foreign residents in the U.S.S.R. at rates ranging from about 5.3 to 10 rubles to the dollar (i.e., currency premiums of as much as 150 per cent above the official ruble rate) for non-commercial transactions, such as personal expenditure, payments of official levies, gift remittances from abroad, and the like. These rates do not apply to foreign trade or to payments made outside the U.S.S.R. The usual tourist rate was set at 10 rubles to the dollar.

The ruble and gold

The value of the Soviet ruble is officially linked to gold, but the nature of this linkage is unclear. Gold coin does not circulate in the Soviet Union. The official relationship between gold and the paper ruble is one of one-way convertibility, i.e., within the U.S.S.R., gold will buy paper rubles but paper rubles will not buy gold for monetary purposes. The official purchase price of gold in 1950-60 was 4.45 rubles per gram, but the Government has sold gold for industrial and dental purposes at prices as much as 22 times higher than the official price.1/

The ruble is not convertible into gold on external account. There is no official information on Soviet gold production or gold reserves, and the actual relationship between gold reserves and the money supply is not known.

The convertibility objective

It has for many years been an announced objective of Soviet monetary policy to make the ruble convertible and to increase its international importance. Some of the meanings that might be attributed to these objectives were analyzed in "Russian Gold and the Ruble" and need not be repeated here. The objective of ruble convertibility is not to "bury" the dollar and sterling as key currencies, but rather to share the world stage with them. The process of making the ruble convertible, and turning it into a key currency, alongside of the dollar and sterling, cannot but help increase the prestige of the ruble. This, according to Soviet expectation, would be widely interpreted as yet another indication of the great and growing strength of the U.S.S.R. As part of the cult of strength, the U.S.S.R. always tries to implant the notion that Soviet money is becoming stronger while capitalist monies are becoming weaker, that Soviet money is solidly based on gold, and that there is not, and there cannot be, any inflation in the country.

The Heavy Ruble and Its Gold Content

The recent adoption of the heavy ruble and of a higher gold content for this ruble are related. The effects of the two actions must, therefore, be considered together, though each action has, in part, its own rationale. The U.S.S.R. has tried hard--and not without some success--to explain that the two actions are independent.

The change to a heavy ruble was described2/ as having the following advantages: (1) It would bring the present scale (domestic value) of the ruble, which has become too small a unit, into conformity with the greatly increased money values of production, sales, and income, and thus simplify

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1/ In the United States, and many other countries, the relationship between gold and paper money is also that of one-way convertibility. In some countries, but not in the United States and the U.S.S.R., individuals may buy and hold gold. In the United States, unlike the U.S.S.R., gold for legitimate artistic and industrial purposes is sold at the official price.

2/ By Korovushkin, the Chairman of the Board of Directors of the U.S.S.R. State Bank, as reported in United Nations, Economic Bulletin for Europe, Vol. 12, No. 1, October 4, 1960. Korovushkin's statement was first published in Pravda in May 1960.

computations, record keeping, and costs of engraving and printing.1/ (2) The compulsory exchange of outstanding currency for heavy rubles would yield valuable data on the distribution of domestic hoards in various sections of the economy. The advantage to the monetary authorities is that of information, since it is officially stressed that there is no intention of expropriating holdings. (3) The conversion into heavy rubles will liquidate illegal foreign holdings. Although the export of rubles has been illegal for many years, there are undoubtedly stocks of ruble banknotes outside the U.S.S.R., as the existence of a free ruble quotation in Swiss markets indicates. Since December 1959, there has been provision for legally repatriating Soviet banknotes in limited amounts, so that it may be considered that there is now a case for demonetizing all of the banknotes that have not yet been repatriated. (4) The rate for the U.S. dollar might not automatically be cut by ten, i.e., from 4 rubles to 40 kopeks, but it would undoubtedly be adjusted (by reducing its command over dollars) and it might well be nearer to the historical rate of 2 rubles to the dollar that prevailed before World War I.2/ This would make it possible to compare production, trade, and national income magnitudes of the U.S.S.R. more accurately with those of other countries.

The adoption of the heavy ruble has thus been explained in independent terms which are superficially reasonable. But the major reason for the introduction of the heavy ruble is related to the level of prices in the U.S.S.R. and to the subsequent move to change the dollar-ruble exchange rate, i.e., the gold content of the ruble. Together, the two moves are designed to camouflage a reduction in the external value of the ruble.3/ It may also be that these changes may later help to cover up changes in the price relationships of different kinds of goods and in the level of taxes applicable to different economic sectors. These real objectives can be obscured to the maximum extent if the adoption of the heavy ruble and the change in the gold content of the ruble are treated--as Soviet news releases and explanations have invariably treated them--as separate and isolated events, each of which has its own economic justification. On the other hand, if these two actions are treated as two separate parts of one action, a more appropriate interpretation results.

1/ Nor should one overlook the Soviet radio comment that the new scale of prices and the issuance of metallic rubles and 50-kopek pieces will make it possible to introduce automatic vending machines widely.

2/ Adoption of the pre-1914 rate of 1.94 rubles to the dollar would have implied a devaluation of about 80 per cent, compared with that of 56 per cent which was finally effected.

3/ Paul Einzig, writing in Optima before the change in the gold content of the ruble was announced, suggested that devaluation of the ruble might be followed by an application for admission to the International Monetary Fund. He explained that "it has long been realized in Moscow that the decision immediately after the end of the war not to participate in that institution was a mistake." (Johannesburg), Vol. 10, September 1960, p. 166.

There is no doubt that the Soviet emphasis on two separate actions has been successful to a greater or lesser extent. In the Western press, these two actions are now considered together and interpreted as a devaluation of the ruble by 56 per cent. Early interpretations were much less clear. In many other parts of the world, however, the explanations of Soviet actions and objectives are sufficiently confusing to leave the impression that the increase in the gold content represents increased Soviet strength at a time when the dollar is universally recognized as being under pressure.

The change in the gold content of the ruble, considered by itself, means that the dollar, which formerly was equivalent to 4 light rubles, will now buy only 0.91 heavy rubles, and that the value of an unspecified ruble has increased from $0.25 to $1.11. The effect of the shift to a heavy ruble plus the increase in gold content works out differently. Prices within the U.S.S.R. are now stated in the heavy ruble and are, therefore, one tenth of what they were formerly. Consequently, it will now cost 11 cents to buy in the U.S.S.R. what would have cost 25 cents. This may be compared with the rate of 10 cents which has been available to tourists within the U.S.S.R. for the past three years. Since this preferential rate is to be abolished, tourist travel costs will increase by 10 per cent.

The adjustment in the exchange rate of the ruble has advantages for the U.S.S.R., even though the reasons for, or the direction of, the change are often inverted. The new rate is more realistic than the old, as the elimination of the preferential tourist rate suggests. Similar effects were achieved with respect to all exported and imported commodities. Accounting adjustments to record losses (in rubles) on exports and profits (in rubles) on imports will be greatly reduced. As Minister of Finance Garbuzov explained: "The ruble's new exchange rate will make it possible to compare world prices with wholesale prices in the USSR, since, through this exchange rate, mean world market prices will for the most part be brought to the level of mean wholesale prices in the USSR. This will make it possible to estimate more correctly the relative profitability of the exports and imports of separate commodities and the profitability of the Soviet Union's foreign trade as a whole, and its trade with separate countries."1/ These statements are reasonable provided that their limitations and inversions of logic are kept in mind, e.g., when the dollar-ruble rate was changed, Soviet prices were "adjusted" to world prices and not the other way around; price structures are so different in the U.S.S.R. and in the free world, that comparisons of mean prices have little meaning; Soviet foreign trade is conducted by monopolies, and each commodity does not have to pay its own way; and finally, the change in the ruble-dollar rate may be followed by changes in the ruble rates of the currencies of satellites, which have been paying more for Soviet exports and receiving less for Soviet imports than the countries of free Europe.2/

1/ As reported in Pravda, November 15, 1960, and Radioteletype in English to Europe. Also, New York Times, November 16, 1960.

2/ Horst Mendershausen, "The Terms of Soviet-Satellite Trade," Review of Economics and Statistics, May 1960, pp. 152-64.

Ruble Trading in the Cruzeiro Free Market

Since trade between Brazil and the U.S.S.R. is insignificant, it is interesting to speculate why the U.S.S.R. might undertake, according to a recent but unconfirmed report, to buy and sell rubles in the cruzeiro market. This report may be false; it may be premature; or it may be a trial balloon. A number of elements may be involved in such an undertaking. The U.S.S.R. may plan gradually to introduce the ruble to international trading in the next few years. It has to begin somewhere to see how trading will go, how the ruble will be priced in terms of the dollar and other currencies, and what kinds of market policies will be required. A relatively limited exchange market, such as that in Brazil, offers the opportunity to make these determinations with a minimum commitment. The U.S.S.R. has for a long time declared its aim to make the ruble a key international currency and even, as a measure of socialist competition, a currency stronger than the dollar. Buying and selling operations in the cruzeiro market offer the opportunity to do this on a limited scale in an area it regards as politically important.

The Brazilian authorities have in recent years intervened in the free market for cruzeiros to achieve and maintain the desired dollar-cruzeiro exchange rate. The exchange rates of the cruzeiro with currencies other than the dollar are largely determined by arbitrage. The U.S.S.R. could easily maintain a ruble-dollar cross rate equal to the official ruble-dollar parity. This by itself would have political significance, particularly since (in conjunction with the shift to a heavy ruble) it might eliminate existing black or grey markets in rubles. But the U.S.S.R. may possibly wish to do even more. It could offer relatively small amounts of rubles for sale and, at the same time, freely make available for export small quantities of widely desired and easily exportable commodities at differentially low ruble prices, which could conveniently be purchased with "convertible" rubles. In these circumstances, the ruble could easily go to a premium in terms of the cruzeiro and, therefore, of the dollar. Such a premium would have little or no economic significance, but it could have considerable propaganda value.