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Currency crises in post-Soviet economies — a never ending story?

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Abstract

Since the collapse of the Soviet Union, its successor states have suffered from cyclical currency crises. The most recent episode of 2014–2016 was caused by a combination of external and domestic factors. The former include tighter US monetary policy, slower global growth, and declining commodity prices, whereas the latter include the former Soviet Union (FSU) economies' extreme macroeconomic fragility (a legacy of past crises), numerous microeconomic rigidities and structural distortions in addition to governmental deficits. In addition, the Russian–Ukraine conflict dealt a heavy blow to both economies and their neighbors. Effective anti-crisis policies must aim at eliminating all deep-rooted causes of repeated financial and macroeconomic turbulence and must involve deep structural and institutional reforms in the entire region.

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1. Introduction

The rapid depreciation of the Russian ruble (RUR) and of the currencies of other countries of the former Soviet Union (FSU) in 2014–2016 revived the question of macroeconomic stability in this region, a question that has arisen several times since the Soviet Union's collapse in 1991. As with previous currency crises, particularly the 1998–1999 and 2008–2009 crises, the most recent episode

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was caused by a combination of global, regional and country-specific factors. While identifying global shocks and related transmission channels seems to be relatively easy in each case, specification of regional and country-specific factors requires greater in-depth diagnoses, which is precisely the purpose of this paper.

Our analysis concentrates on the most recent episode, which cannot be considered as definitely finished as of the date of this paper, i.e., August 2016. We begin by defining various forms of financial crises — including currency crises — and a brief review of three generations of theoretical models that attempt to explain the causes of currency crises (Section 2). In Section 3, to facilitate a better understanding of the deep roots of the latest turmoil, we provide a historical overview of previous currency crises and their causes, beginning with the last years of the Soviet Union. Then, we analyze the dynamics of the 2014–2016 crisis in Russia, Ukraine and in other FSU countries (Section 4), including mechanisms meant to combat regional spillovers and to engage in crisis management. Section 5 discusses the global and regional causes of the recent crisis, including declining oil prices in 2014–2016. In Section 6, we discuss the deeper systemic causes of the fragility of FSU currencies. Finally, Section 7 presents conclusions and policy lessons.

While the paper draws from three previous publications (Dabrowski 2015a, 2015b, 2015c), it offers an updated and more comprehensive analysis of the currency crises in Russia and the FSU and uses a fresh set of statistical data available as of August 2016 that come from the IMF, the World Bank, various national central banks and statistical agencies, and other institutions in charge of cross-country comparative analyses related to the FSU region.

2. Definitions and theoretical models

The meaning of currency crisis is not particularly precise and often requires clarification. For purposes of this paper, currency crisis is defined as a sudden decline in confidence in a given currency, usually leading to a speculative attack against it. Analytically, currency crises can be detected by either substantial depreciation in a given currency, a decline in a country's international reserves, or both (Dabrowski, 2003a, p. 5).

We also must distinguish currency crisis from the broader notion of financial crisis (Table 1), which involves all types of instability related to monetary and financial systems (see IMF, 1998, pp. 74–76). We define *financial crisis* as a sudden decline in confidence in relation to the ability of a country's government/central bank and banking sector with respect to their liabilities (on committed terms).

Other forms of financial crisis are defined as follows. *Banking crisis* refers to actual or potential bank runs or failures that induce commercial banks to suspend the internal convertibility of their liabilities. A *public debt crisis* occurs when

Table 1
Typology of financial crises.

Financial crisis	Banking crisis
	Public debt crisis
	Balance of payments crisis ⇒ Currency crisis

Sources: Antczak (2000); Dabrowski (2003a).