

Soros on Soros

Staying Ahead of the Curve

Interviews with Byron Wien and Krisztina Koenen

George Soros

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The Stateless Statesman

What do you see as the economic future of the Eastern European countries? They have become free and independent at a time when even the strongest Western economies are experiencing major crises, and facing problems that will only be overcome, if at all, over a long time.

At the time of the Revolution, in 1989, the Western democracies were doing very well. Their failure to follow a far-sighted, generous policy toward Eastern Europe cannot be blamed on economic difficulties. It is the other way round. The present-day difficulties of the Western world may be partially attributed to its failure to adjust to the collapse of the Soviet Union.

As to the economic future of the region, one has to draw a sharp line between Central Europe, that is to say Poland, the Czech Republic, and Hungary on the one hand and the former Soviet Union on the other. There are a number of countries that lie between them: Slovakia, Romania, Bulgaria, etc. Central Europe has made good progress toward a market economy. I am basically optimistic that this direction will continue, unless political or military developments intervene. The same can be said about the Baltic States, Estonia, Latvia, and Lithuania, though with less confidence. They have stable currencies and although conditions are very difficult, these countries have survived the worst and are moving in the right direction. Slovenia has also made the grade.

In the former Soviet Union, the situation is very different. The Soviet system has collapsed, but no new system has taken its place. The prevailing trend is still downward, toward disintegration and decay. It is impossible to say how far it may go. There have been precedents: the “time of troubles” at the end of the sixteenth century and the Russian Revolution. Between 1913 and 1917 industrial production fell by 75 percent; between 1917 and 1921 it fell by another 75 percent—that is the kind of decline that is in the cards. I used to speak of a “black hole” that would destroy civilization.

But industrial production has more or less stabilized.

That is true. Many industrial enterprises—those that are still functioning—have learned to fend for themselves. The economy is like an octopus whose head has been cut off. The tentacles have adapted themselves to a more or less independent existence—I say more or less because many tentacles are still attached to the state budget and feed off it.

Something very interesting and unexpected happened in Russia in 1994. The shares of state-owned enterprises were distributed to the public practically free in a mass privatization scheme. This divided the enterprises into two classes: those whose shares had value and those that did not. Roughly speaking, the energy and raw materials producers fell into the first class, the energy users into the second class. The division had been there before, but the voucher privatization scheme made it more obvious. It also engendered a feeding frenzy. Shares representing claims on natural resources could be bought at a tiny fraction of their potential value. Oil in the ground sells for \$2 to \$3 a barrel in the rest of the world; in Russia, it could be bought for 2 to 3 cents. This attracted some enterprising investors from home and abroad and touched off one of the weirdest stock market booms in history. The amounts involved were relatively insignificant—a few hundred million dollars—but the rate of appreciation was phenomenal. Some shares rose tenfold in a matter of a few months—between March and August of 1994. The market was rudimentary: There were no clearing and custodian arrangements and share registries were not properly administered. Banks and brokers suffered from an acute shortage of capital—they gladly paid 10 percent a month or more for dollar deposits.

Is that when you changed your mind and started investing?

Yes, that is when I lifted the ban on investing. I couldn't resist the temptation. Here was an embryonic financial market with tremendous upside potential. Why should we stay away from it? But when I went to Moscow, in the early fall, and took a look at what was going on, I was appalled: it had all the earmarks of a bubble about to burst. I gave the order to sell, but I got the classic answer: to whom?

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At any rate, there was a moment in 1994 when one could see the faint outlines of a new order rising out of the ashes of the old. It resembled the robber capitalism that prevailed in the United States in the nineteenth century, but it was much worse because the legal infrastructure was much more feeble. There is much talk about the Mafia, but the Mafia is nothing else but the privatization of public safety—the most successful privatization effort in Russia.

Has law and order completely broken down?

No, but the public authorities are also working for private profit. What we call Mafia is really an interwoven network of alliances between entrepreneurs and officials. It is the seamy side of free enterprise.

Surely you don't find it attractive?

I find it repulsive, but it may be better than the alternative. People act as robber capitalists because that is the only way they can become capitalists in a lawless society. Many of them are educated, decent people who don't like it any better than I do. Given half a chance, they would become upright citizens. In the United States, the corruption in Chicago and Boston and the New York of Tammany Hall engendered a public outcry for clean government. The same would happen in Russia—because Russians really care about honesty—if only robber capitalism succeeded.

But that is not at all certain because it is being destroyed even before it got started. The enterprises whose shares rose tenfold in the summer of 1994 did not get a red cent out of it—all the profit went to the people who bought the shares and resold them. It is only in the second stage of privatization that the proceeds would accrue to the enterprises, but the bubble has burst and it is doubtful whether there will be a second stage that really amounts to something. Undoubtedly, some energy companies are going to try, because their managements discovered that they can actually raise money by selling shares and are preparing feverishly, but I don't think they will get very far.

Why are you so pessimistic?

Partly because the emerging markets boom—in which Russia was the last and most outlandish entrant—has burst and partly because of political developments inside Russia.

Consider the political implications of a robber-capitalist regime in Russia. The natural resource producers would prosper but the military-industrial complex would decay. The prosperity of the natural resource sector would lead to an import boom because consumers prefer imported products to locally produced goods. The service sector—banking, financial services, distribution, trade—would also develop, but there would be practically no market for producer goods. But that is the sector that constitutes the bulk of the economy.

The old Soviet economy was incredibly distorted: The producer goods industry, including military goods, was called Sector A and it accounted for 75 percent of industrial production; light industry, called Sector B, was only 25 percent. In a market economy, the proportions are reversed. The energy-using industry would be penalized because oil and other raw materials are worth more when they are sold in world markets than when they are transformed into products at home. But the military-industrial complex carries tremendous political clout. Already, the political struggle can be boiled down to a conflict between these two interest groups. The energy-producing sector is represented by the Prime Minister, Viktor Chernomyrdin, the military-industrial complex by Oleg Soskovets, First Deputy Prime Minister. The actual state of play is, of course, much more complicated—the mayors of Moscow and St. Petersburg and the other local potentates are not so easy to fit into the picture—but the main political battle is going to be fought along these lines. It is a battle that the energy users are favored to win. Not only do they carry much greater political weight, they also have a strong political argument: They can appeal to nationalist sentiment. Robber capitalism would lead to the hollowing out of the Russian economy. The bulk of industrial workers would lose their jobs and would have to be redeployed. In any country, there would be a political outcry. Russia is no exception.

No sooner has robber capitalism reared its ugly head than political forces have coalesced against it. Soskovets has been gaining ground against Chernomyrdin since the middle of 1994.

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Even the attack on Chechnya, however badly it was bungled, plays into the hands of the military-industrial complex. The robber-capitalist goose is going to be devoured before it can lay any golden eggs.

Can you explain the invasion of Chechnya?

I have no special insight. Clearly, it was designed to exploit the strong popular prejudice against Chechens, who are associated with the Mafia in the public mind, and to regain some measure of popularity for President Yeltsin. But it was incredibly mismanaged. It started out as a covert intelligence operation, a so-called internal uprising, which misfired and turned into a full-scale military invasion. It will have incalculable consequences.

What do you expect?

Almost anything. The struggle for power has intensified to a point where almost anything can happen. In a country where people are prepared to steal anything, the state itself is up for grabs. Until now, it was not worth grabbing because the economy was unable to support the state mechanism. Those who tried, failed—remember the abortive coup in which incompetent bureaucrats tried to oust Gorbachev. But time has passed, people have recovered their wits, and even the economy has stabilized. It is worth making the effort and the effort is currently underway. A rather sinister group has gathered around President Yeltsin, bent on seizing power. The most visible person among them, and probably their leader, is General Korzhakov, head of the presidential guard and Yeltsin's long-standing drinking partner. The presidential guard is being expanded into a private army and already there have been some ugly incidents. It is rather scary when members of the presidential guard, wearing ski masks, attack the security guards of a banker who controls a television network that is critical of the President; when a key figure in the state-owned television network that has shown a large degree of independence during the siege of Grozny is murdered; when the son of a prominent dissident is killed in a suspicious car accident the same day that the dissident is speaking out about the abuse of state power. There

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seems to be a concerted campaign to silence or intimidate the independent media before the elections.

I don't see why a dictatorship—if that is what is in the making—should be incompatible with robber capitalism. Indeed, that is the essence of fascism.

That is a very penetrating observation. But I don't think you can take the victory of fascism in Russia for granted. The battle has just begun. People are not going to give up their new-found freedom without a fight. The media have shown the invasion of Chechnya in its full horror and people have been shocked, much like Western public opinion was shocked by the gory pictures from Bosnia. Indeed, the effect was much greater because people in Russia were exposed to it for the first time. I don't expect the great masses to be aroused to action—they remain long-suffering and passive—but I do expect the media to fight for its hard-won independence with messianic zeal. No wonder that the recent atrocities were directed at people connected with the media!

Do you really believe they can resist the pressure?

If there is no countervailing pressure, probably not.

Where would the countervailing pressure come from?

From abroad, to start with. People in Russia really care what the world thinks of them. Yeltsin himself cares a great deal. He may be under the control of a small, sinister group around him, but he can't be happy about it. The German Chancellor, Helmut Kohl, called him a number of times about Chechnya and he tried to respond. Unfortunately, his orders were not obeyed. That is how we were treated to the spectacle of Yeltsin announcing the suspension of bombing without any effect. Kohl is demonstrating real understanding and concern with the internal situation in Russia. I wish I could say the same thing for our own administration.

There is a factor at play whose importance is not properly appreciated: the military. The military has stayed out of politics so far, but Chechnya has been a traumatic experience.

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Commanders have refused to obey orders. Large numbers of body bags have been sent home. The army is deeply divided and deeply hurt. When the military becomes politicized, it happens very fast and it profoundly changes the political landscape. That is what happened just before the outbreak of the Spanish Civil War and that is what is happening in Russia today.

So you expect civil war?

I expect the military to play a more active political role than before. And whoever makes a grab for the control of the state is liable to run into resistance. Whether events will deteriorate into full-scale civil war, it is impossible to say. Almost anything may happen, civil war not excluded. One thing is certain: Political instability is not conducive to investment. That is why I give both robber capitalism and fascist dictatorship a relatively low probability, at least in the near term, and increasing instability a much higher probability. We are approaching the conditions I had in mind when I spoke of a black hole.

I am still at a loss as to why you should want to invest in conditions like these.

Conditions in 1994 were very different. It is characteristic of revolutions that conditions turn around completely; that is why they are called revolutions. I anticipated the conditions that prevail today, but the emergence of robber capitalism last year caught me by surprise. It ran counter to the normal evolution of financial markets. Normally the establishment of a legal infrastructure comes first; direct foreign investment next; and the development of foreign portfolio investment last. In this case, the order was reversed: foreign portfolio investment came first and it acted as a catalyst for the emergence of robber capitalism. I could recognize it when I saw it. I was particularly impressed by the way Boris Jordan, working for Credit Suisse First Boston, helped to develop the market. He did not try to hog the market, like some other players, but left room for others and tried to develop the institutional infrastructure. It reminded me of my youth, when I pioneered the opening up of the Swedish market and other markets and I didn't want to be left out. But, for a number of reasons, including my ban on investing where I have

foundations and the role change involved, I was a little slow on the uptake. Instead of first in, first out, we were last in, first out, and instead of a profit, we have a loss.

How do you feel about your foundations in Russia?

Concerned. I committed large amounts of money—the International Science Foundation alone cost me more than \$100 million—and it may have been largely wasted if Russia goes down the drain.

But you tell me you anticipated the current turn of events.

That's right. I did everything I could to prevent the present turn of events and I have no regrets on that score. It was well worth trying, even if it didn't succeed, because so much was at stake. But now that my worst expectations are coming true, I am at a loss as to what to do. I cannot pull up stakes because I would be abandoning those whom I want to support in their hour of need. At the same time, it goes against the grain to throw good money after bad. I am caught in a trap of my own making. I console myself with the thought that in the case of societies, there is life after death. Some of the seeds we sow may survive no matter what happens to Russia in the near term.

Are you trying to extricate yourself?

No; the fight is not yet over.

But you cut your losses on your investments.

That's different. I invest for profit; philanthropy is for a cause, even if it turns out to be a lost cause. I can't quit now. I have a strategy and I shall adjust it as events unfold.

What is your strategy?

The International Science Foundation was meant to be a one-time emergency operation: \$100 million to keep alive, during a period of economic dislocation, a scientific establishment that is

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outstanding by international standards and has been the mainstay of independent thought and action in the former Soviet Union.

The Science Foundation has accomplished its mission. The money that was meant to be spent in two years was committed in 18 months and the program was so highly appreciated that the various governments concerned—Russia, Ukraine, and the Baltic States—offered matching funds in order to get me to continue it. I accepted their offer and committed additional funds for 1995, but I will not extend the program into 1996 unless I also get matching funds from Western sources. I think it is inappropriate that I should be the sole Western source of support for Russian science, especially as European and American governmental programs failed to use the money allocated. The scientists are urging me to lobby for governmental support but I refuse to do so. Let them lobby! We are slowly winding down the operation. The international travel program is already shutting down. The same strategy applies to the science education program that started a year later and, barring outside support, will wind down a year later. But I intend to continue the supply of international scientific journals because the publishers have offered such favorable terms that I consider it matching funds. I shall persevere with the Internet program, which is just beginning to pick up momentum, even if I don't get outside support because I consider it so important for establishing the pre-conditions of open society. I am trying to make the most of the transformation of the humanities program—we are printing millions of textbooks this year—and I shall continue our effort to keep alive the so-called “thick journals,” the cultural journals that have played such an important role in Russian history. I am also ready to embark on new programs for the support of culture, civil society, and the media, but not on the scale people in Russia have come to expect of me. I intend to continue along these lines as long as civil society supports the foundations and the authorities tolerate them. But I can't help feeling despondent about the prospects.

Do you think events could have taken a different course?

I am convinced of it. It was well within the powers of the Western democracies to slow down the

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disintegration of the Soviet Union and lay the foundations of an open society before the closed society collapsed. All it would have taken was some positive reinforcement for Gorbachev's policies of glasnost and perestroika. He was dying for it. He had a naive belief that, once he provided an opening, the free world would rush in to help. But the Western governments lacked the vision and the political will. In the spring of 1989, at an East-West security conference at Potsdam, I proposed a new version of the Marshall Plan, this time to be financed mainly by the Europeans. My proposal was "greeted with amusement," as the *Frankfurter Allgemeine Zeitung* reported. If it had been taken more seriously, history would have taken a different course.

Aren't you overestimating the potential for Western intervention in what were, after all, the internal affairs of the Soviet Union?

Not at all. I speak from personal experience. As early as 1988 I proposed to the Soviet authorities a study group to establish what I called an "open sector" in the Soviet economy. I was not as well known as I am today; I was practically a nobody; nevertheless, I received a positive response. Admittedly, the cooperation of the Soviet authorities was haphazard at best but, when I insisted, Prime Minister Ryzhkov issued an order obliging the relevant officials to attend.

What was the outcome?

Negative. I was thinking of creating a market-oriented sector within the centrally planned economy, a sector not too far removed from the consumer and not too far down the chain of production. Food processing, for instance. I had in mind a kind of embryonic market economy that would grow within the body of a centrally planned economy. But it didn't take too many meetings to discover that the mother's body was too diseased to support a healthy embryo.

Aren't you contradicting yourself? If the centrally planned economy was doomed in 1988, what could Western assistance accomplish?

It could have slowed down the process of disintegration. It could have given people a sense of

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material improvement and built support for economic reform. It wouldn't have taken much. For instance, the introduction of tampons would have generated a great deal of enthusiasm among women who had to rely on the most primitive sanitary devices; or electronic gadgets would have motivated the younger generation. At the time I am speaking about, the Soviet Union still enjoyed a first class credit rating because it had always paid its obligations punctiliously. In those years, the Soviet Union borrowed tens of billions of dollars.

Why didn't it have the desired results?

Because no conditions were attached or, more exactly, the conditions were designed to benefit the lenders, not the recipient. Germany lent tens of billions to gain Gorbachev's consent to the reunification of Germany. But no thought was given to the effect on the Soviet economy. If the lenders had insisted, they could have dictated whatever conditions they wanted. The Soviet authorities were eager to be told what to do. I saw that in connection with the Open Sector Task Force but, of course, I was not in a position to impose conditions because I wasn't lending billions of dollars. But I would have imposed conditions and I would have enforced them. That was a time to be intrusive. It would have been appreciated.

Would it have worked?

Probably not. Nothing worked at the time. There would have been slippage. But there would have been also some positive results and that could have changed the course of history. What Gorbachev lacked was a modicum of success.

Was it possible to keep the Soviet Union together? And would it have been desirable to do so?

I am sure it would have eventually disintegrated, but I am convinced that it would have been better if the process had been slower and more orderly. Look at the dissolution of the British Empire; it took half a century to accomplish and it wasn't without conflict, but the effect was

almost wholly beneficial.

But Great Britain was the motherland of democracy.

That is all the more reason why the Soviet Union needed more time for its dissolution. I do not make myself popular today when I say that it would have been better if the Soviet Union had not collapsed, just as it would have been better if Yugoslavia had not broken up. It would have made possible the transition from a totalitarian system to a free and democratic one. There would have been demands for autonomy, and eventually there would have been an independent Ukraine, for instance, but it would have occurred over a longer period of time. Ukraine would then have been a more stable and viable country when it became independent. To come into the world as a viable organism, a fetus needs nine months. The new countries arising out of the Soviet Union did not have enough time to develop. They are all premature births, and one has to wonder whether they will survive.

I was a great supporter of the so-called Shatalin Plan, or the 500-Day Program as it is also known. I was involved in it from its inception. I met with Nikolai Petrakov, Gorbachev's economic adviser, on the day the task force was formed. I provided a group of eminent international economists to critique the plan, sponsored a group of lawyers to help design the necessary legislation, and brought the authors, under the leadership of Grigory Yavlinsky, to the 1990 Annual Meetings of the IMF and the World Bank in Washington.

The idea behind the Shatalin Plan was to transfer sovereignty from the Soviet Union to the constituent republics but, at the same time, to transfer back certain critical elements of sovereignty from the republics to a newly created entity, the Inter-Republican Council. In theory, it would have replaced the Soviet Union with a new kind of union that would have been more like the European Union. In practice, it would have pitted the new authority, the Inter-Republican Council, against the old, Soviet authorities. Since the old political center was almost universally despised, the new political center would have gained popular support by doing battle with the old one.

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It was a brilliant political conception that was not properly understood. Had it received international support, I am sure Gorbachev would have endorsed it. Even without Western endorsement, it was touch and go. I remember Leonid Abalkin bragging to me how he managed to sway Gorbachev against the plan. He would be the 13th member of a council uniting 12 republics; each member would have a firm territorial base except him; therefore, he would become the least powerful member of the Council. That argument won the day. But a year later, Yeltsin used the Russian state as the power base for toppling Gorbachev and dissolving the Soviet Union. If Gorbachev had accepted the Shatalin Plan, he could have remained in power and the Soviet Union could have been reformed, instead of disintegrating.

You say you were initially involved in the Shatalin Plan. Did you remain involved in the reform process after the dissolution of the Soviet Union?

Not in Russia. I was friendly toward Yegor Gaidar and I would have been ready to help him, but I came to the conclusion that the reform was moving on a false track relatively early on. It happened in April 1992 when I discovered that the enterprises were accumulating receivables at a rate that was roughly half the rate of industrial production. This meant that roughly half the production was exempt from the monetary control that was the cornerstone of Gaidar's policy. Half of industry ignored monetary signals and continued producing according to the old system of "state orders" irrespective of getting paid. This was a shocking discovery. I confronted Gaidar when he came to see me one night in New York, and he admitted it. Then he delivered a rousingly optimistic speech in Washington later that week. I started advocating publicly that Western aid should be tied to the creation of a social safety net. This would have enabled the Russian government to put enterprises that failed to obey monetary signals into bankruptcy. My proposal did not make much headway.

None of the policies you supported seem to have been implemented. Wasn't that frustrating?

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Yes, it was. But the policies I could implement on my own succeeded. I tried to demonstrate my social safety net proposal in a pilot scheme. That was the origin of the International Science Foundation. We distributed \$500 a year to some 30,000 scientists and I had the satisfaction that it worked. Privately I suggested a similar scheme for military officers, but I was not willing to fund it. It might have cost \$500 million, but it would have made a difference.

You are very critical of Western policy. What would you recommend to the IMF today?

I would not like to be in their shoes. But then, I don't like being in my own shoes very much, either.

Can you be more explicit?

I think it is too late to have a real impact on the course of events in Russia. Russians may have had exaggerated expectations of the West, but now they are disappointed and disillusioned. Our influence has been greatly reduced. Even the progressive elements have turned anti-Western. Aleksandr Yakovlev, who had been the architect of glasnost and the former Chairman of Ostankino, the state television, complained to me bitterly about the policies of the United States.

But you are actively engaged in Ukraine.

Yes. That is where it is possible to make a difference and I am doing my utmost to bring it about. And, for the first time, I don't feel frustrated. I have a sense of accomplishment. For the first time since 1989, the Western powers did the right thing: in the communique of the 1994 Naples Summit, they promised \$4 billion in aid if Ukraine embarks on a reform program. This happened to coincide with the election of a new president, Leonid Kuchma.

The previous president, Leonid Kravchuk, was an opportunist who realized that the problems of Ukraine exceeded his capacity to deal with them and he did not even try. All he wanted was to stay on top, bobbing along like a cork in a turbulent sea. He had been the chief ideologist of the Ukrainian communist party and he felt it opportune to change horses from

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communism to nationalism. For a while, it worked; he was elected with a greater majority than practically any other president: more than 60 percent. He sought to maintain his popularity by playing up the conflict over the Black Sea Fleet and other nationalist themes, but he was undercut by the collapse of the economy.

Kuchma is made of a different fiber. The manager of an important enterprise in the military-industrial complex, he is oriented toward problem solving. He realizes that Ukraine cannot survive as an independent country the way things are going and he is determined to do something about it. The Naples Summit offered him a lifeline and he resolved to seize it. He had no deep understanding of the market mechanism, but he understood very clearly what \$4 billion could do for Ukraine because that was the cost of Ukraine's energy imports. On this occasion, the promise of economic aid did what it was supposed to do: It changed the direction of economic policy. The main credit goes to senior United States Treasury officials, who inserted an actual amount into the communique.

Ukraine was, and remains, in a highly precarious state. The economic collapse has been much greater than in Russia, partly because Ukraine is deficient in energy and partly because there has been no serious attempt at macro-economic stabilization or structural reform. In accordance with my boom/bust theory, this actually makes it easier to engineer a change of direction. I was well placed to assist and I rushed to offer my assistance. We put in place a small team of experts, under the direction of Anders Aslund, to help the Ukrainians develop their economic reform program and deal with the international donor community. The cooperation was successful because it was based on mutual trust and an initial agreement with the IMF was put in place in record time. Success is far from assured; the process could be derailed at any point and already we have had to exert ourselves several times to put the train back on the rails, but I have a strong sense that it is moving in the right direction.

Are you confident that the reform program is going to succeed?

Not at all. I can see some glaring deficiencies in it. As it stands at present it suffers from the same

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flaw as the Gaidar program in 1992: the emission of currency is reasonably well controlled but the budget and the behavior of the state-owned enterprises remains out of control. The spending ministries continue to spend and the enterprises continue to operate at a deficit; the liabilities continue to accumulate, and wages, receivables simply remain unpaid. This is unsustainable but it can be fixed. It requires structural reforms and I hope they will not be long in coming. In contrast to the Gaidar times, I can do more than just predict failure.

This must be a novel experience for you.

Yes, and it is very satisfying.

Why do you think it comes so late in the day? You have been trying since 1988.

Because it takes time to catch up with revolutionary change. This applies to the international authorities; it applies to the Ukrainians—for instance, Roman Shpek, one of the first graduates of Hawrylyshyn's business school is a key player on the Ukrainian team—and it applies to me.

But you pride yourself on understanding revolutionary change better than others.

It took time to establish my credentials. I have also learned to be calmer and bide my time. In the early days, I was too eager and jumped on every opportunity. Now, I am ready to abstain or withdraw. I don't need to score.

Are you personally so engaged in any other country?

Macedonia. It is the last surviving multi-ethnic democracy in the Balkans. It can survive as an independent country only if it has a government devoted to the principles of open society—otherwise, the ethnic tensions between its Macedonian and Albanian communities would tear it apart. It is the victim of an illegal and unjustified blockade by Greece, which is a member of the European Union. The Western democracies should have gone to the aid of Macedonia, but they did not. The United States stationed some peacekeeping troops there, but nothing was done to

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provide economic relief. I stepped into the breach. I provided a \$25 million loan that allowed Macedonia to buy oil and I provided a subsidy for an airlift of its export of early vegetables. I continued to agitate for a more constructive policy toward Macedonia but to little effect. As the economy deteriorated, so did ethnic relations.

Tensions reached the breaking point recently. Albanian radicals established a so-called university without government permission. It was a political provocation aimed at creating an illegal parallel structure for ethnic Albanians similar to the structure that Albanians have established in Kosovo. I pleaded with President Gligorov personally not to be provoked, but I failed. He deployed the police and there has been a fatality. Both the Albanian and the ethnic Macedonian populations are becoming radicalized. The ethnic Macedonian inhabitants of the Albanian region are increasingly attracted to the way Milosevic has handled the Albanian problem in Kosovo. The government is failing to provide firm leadership. The situation is liable to deteriorate and I am distressed. Nobody could have done more than I did in the way of early warning and prevention, but it didn't help. I can see the third Balkan War in the making. I am at a loss as to what to do. I intend to go to Macedonia and appeal to their better judgment. But I have some doubt whether they have a better judgment.

You have said that you consider the rise of nationalism the greatest threat to the region.

Yes. Communism represented the idea of a universal closed society. That idea has failed. There was a small window of opportunity for the idea of a universal open society to take hold. But that would have required the open societies of the free world to sponsor that idea. Because open society is a more advanced form of social organization than a closed society, it is impossible to make the transition in one revolutionary leap without a firm helping hand from the outside. The Western democracies lacked the vision and the opportunity was lost. Universal closed society has broken down and no new unifying principle has taken its place. Universal ideas generally are in disrepute. People are preoccupied with their personal survival. They can be aroused to a common cause only by a real or imagined threat to their collective survival. Unfortunately, such threats

are not difficult to generate. Ethnic conflicts can be used to mobilize people behind the leadership and create particular closed societies. Milosevic has shown the way and he has many imitators.

Do you consider the threat of nationalism universal?

There is something self-contradictory in your question because nationalism ought to be, by definition, particular. Yet it has a universal aspect. It is catching. It flourishes in the absence of a universal idea, such as human rights or civilized conduct. The rise of nationalism and ethnic conflicts indicate the lack of international law and order. In that sense, it is universal. Nationalists are kindred souls. Milosevic and Tadjman understand each other; they can make music together.

As far as Russia is concerned» you are quite pessimistic. I am therefore surprised by the optimism you have expressed regarding the countries of Central Europe. Their prospects are surely better than those of the former Soviet Union, but it seems to me by no means certain that they are irreversibly on their way to a market economy and free society.

I am surprised that you are surprised. The communist system is gone and these countries—with the exception of Slovakia—have definitely committed themselves to democracy and market economy. My main concern is whether the European Union will be open enough to accept them.

Aren't you worried that former communists are once again in power both in Poland and in Hungary?

Not particularly. Communism as an ideology is well and truly dead. At the height of the revolution, former communists were repudiated by the electorate. Their return to public life is a welcome broadening of the democratic spectrum. That is not to say that I agree with their policies. On the contrary, I think they are harmful. But, in the case of Poland, the agrarian party is worse than the former communists. In the case of Hungary, I had high hopes when the socialist-liberal coalition was formed, but I have been somewhat disappointed with the prime minister, Gyula Horn.

Why?

Because he hasn't changed. When I got to know him, around 1987, I considered him the most dynamic member of the government; by 1989 he struck me as almost reactionary because conditions had changed but he had not. The overarching problem of Hungary is its accumulated debt. The debt was accumulated during the Kadar era, when Horn's political attitudes were formed. He brings those attitudes to his job now. He would like to maintain economic growth by accumulating more debt. But the music has stopped. After Mexico, Hungary is facing a financial crisis. This is so obvious that I don't see any harm in saying so publicly.¹

You once proposed a solution to the debt problem.

That was during the elections of 1990. I saw an opportunity to draw a line under the debt incurred by the communist government and turn over a new page. At a time of discontinuity, when a legitimate government is replacing an illegitimate one, such a move is possible. But the opportunity was lost and it will not recur.

Would it not be possible to obtain some relief even now?

No. The old debts and the new debts have been intermingled and bank debt has been replaced by market debt. Even to talk about it would make matters worse. At the same time, I don't know how Hungary is going to refinance its debt in view of market conditions.

Doesn't that contradict the optimistic view you expressed earlier?

Not really. I think Hungary has made the grade, both politically and economically. It has a severe debt problem, like many other countries, which has suddenly turned more acute because of the bust in international investing. It will probably force Hungary to take some painful measures that it would have otherwise deferred and, if it does, I hope it will be rescued by Germany because Germany owes Hungary a particular debt. But a financial crisis could destroy the country, so there is reason to be wary.

1 Since that time, there has been a radical change in the policies of the Horn government.

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Poland does not have a serious debt problem because it has defaulted and its debt has been restructured. I consider Poland one of the healthiest countries in Europe today. Its economy is growing but, even more importantly, it has the right spirit. I have the impression that public life is less corrupt and people remain more concerned with the common good than in many of the former communist countries. I am particularly impressed with the intellectual atmosphere surrounding the Stefan Batory Foundation.

That is a strange view. Most people would consider the Czech Republic and Hungary ahead of Poland.

They may be ahead, but Poland is coming up fast. I am interested in the rate and direction of change. My only concern is that Poland may be losing momentum because of political developments. It is unfortunate that the electorate rejected the previous Solidarity-based government just when it got its act together.

Many people would say that the improvement is greatest in the Czech Republic, especially since it got rid of Slovakia.

The Czechs have undoubtedly benefited from the separation from Slovakia, but the Czechs' gain has been Europe's loss. Meciar is trying to align Slovakia with Russia. His ambition is to become the first outpost of a new Russian empire. If he succeeds, it bodes ill for Europe: Slovakia will become a dagger pointed at the heart of Europe. So much for the unabashed pursuit of self-interest.

Is Romania also going to become a trouble spot?

Not necessarily. Romania is a devastated country without the prerequisites for an open society. It has a crypto-communist regime that has unfortunately felt obliged to align itself with some extreme nationalist parties. This carries with it the seeds of trouble, but the trouble may be contained because the regime does not want to be cut off from Europe. The democratic forces are

weak, but fortunately they never got a chance to run the country.

You say fortunately?

Yes. They weren't ready and they would have failed, as the democrats did in Bulgaria. Or the dissident intellectuals in Czechoslovakia, for that matter. They need time to mature, and I see some signs of maturity. They are more willing to cooperate. Not everyone has to be the head of a party. But they don't have much time left. As a new economic and financial structure emerges, elections will no longer be decided by ideas but by funding and the control of the media. The next elections will be crucial. If the democrats fail to make headway, they may be permanently frozen out of power.

What do you think the West should do to help the countries of Central and Eastern Europe?

It varies from country to country and from time to time. Central Europe needs access to markets and membership of the European Union more than anything. Romania needs assistance with the establishment of democracy and independent media, especially television. Generally speaking, the further you go East and South, the greater the need for technical assistance and other forms of aid.

You have been very critical of Western policies. How could the delivery of aid be improved?

The trouble is that technical aid is provided by bureaucracies with all their negative features. Bureaucrats are sometimes very decent, well-intentioned people, but they are confined by rules. We joke inside the foundation that Western aid is the last remnant of the command economy, because it is designed to satisfy the needs of the donors, not the needs of the recipients. The foundations try to reverse the order by seeking to respond to the needs of the country concerned. In Ukraine, our technical experts work for the Ukrainians: they are selected by them and can be fired by them. But as the foundations become increasingly bureaucratized, the joke is

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increasingly on us.

I would sum it up like this: Western assistance has gone through three phases. In the first phase, we should have offered assistance, but we didn't. In the second phase, we promised it, but we didn't deliver. In the third phase, we delivered, but it didn't work. We are now in the third phase.

My foundations have developed a very useful concept for delivering assistance. You have to find a local partner you trust; you have to empower him to carry out his mission, but you had better retain the purse strings.

Do you think you have changed the course of history in Eastern Europe? Would it have taken a different course if you hadn't been there?

Only marginally. Take Hungary, for example. Although the foundation helped to undermine the communist regime—we sponsored writers who then overthrew the communist writers' union; we sponsored youth leaders who then formed the first noncommunist youth league, and so on—the regime would have collapsed without the foundation. After all, it collapsed in other countries where we had no foundation. We can claim a lot more credit for the smoothness of the transition. We did lay the groundwork for an open society. The same applies to other countries. The full impact of our work may be felt only in the future.

Can you envisage developments that would cause you to withdraw from certain countries?

Easily. I am surprised it hasn't happened already. As local conflicts proliferate, our stance in one country is liable to displease another country. Communications and travel may also become more restricted. There is a vicious campaign being waged against my foundation in Yugoslavia even as we speak. But I shall not leave willingly. The more my people come under pressure, the more determined I am to stand by them. I am more likely to be expelled by indifference. That was the case in Prague, where the foundation was neither attacked nor supported—although recently it has shown some signs of revival.

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We may also reach closure because we run out of money, although that is at least eight years away. With the exception of the Central European University, I don't want my foundations to last forever.