



## Russia's Dire Economic Condition

*Anders Åslund, noting recent difficulties in the Russian economy, predicts political and economic troubles for Putin and Russian leaders if the price of oil does not rebound in 2009.*

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Steve Weisman: Welcome to Peterson Perspectives. This is Steve Weisman at the Peterson Institute for International Economics. Today's guest is Anders Åslund, senior fellow at the Institute and author of *Russia's Capitalist Revolution* and the forthcoming book, *How Ukraine Became a Market Economy and Democracy*. Anders, the world has a bad cold and Russia is almost at the door of the hospital, I suppose, in terms of its economy. Give me an update on how serious the economic downturn is affecting Russia.

Anders Åslund: Well, it has just stated industrial production fell by 8.7 percent in November, over November of last year, and clearly this is going much further. And it very much depends on commodity prices because about 85 percent of Russia's exports consist of commodities, most of all, oil and gas. And the reasonable assumption is that Russia's exports next year will fall by 35 percent. And then clearly GDP will be falling also.

Steve Weisman: What about Russian reserves? They have been hit hard by the downturn, have they not?

Anders Åslund: Yes, Russia had the third largest international reserves in early August, \$598 billion. Only China and Japan had more. About now Russia has lost about \$160 billion, a little bit more than one quarter of its reserves.

Steve Weisman: And why have the reserves diminished?

Anders Åslund: Well, you can say that there are three reasons. One, that Russia was kept out of international financial markets, so that Russian companies that had refinancing of loans coming up had to pay back. Much of that has been done by the state. And another reason is that money is leaving the country because people realize that the ruble will have to devalue. And the central bank has been strongly defending the value of the ruble although they have let it go downward in small steps.

Steve Weisman: The ruble has declined in value by how much over the last six months?

Anders Åslund: By 15 percent against the dollar.

And the third reason is that much of the reserves have been in euros and the euro has fallen in relation to the dollar. So the dollar value of the reserves has fallen.

Steve Weisman: Now, of course, when one reads the public comments of Prime Minister Putin and President Medvedev they know who is to blame for the fix that they're in: It's the United States. They have been pretty clear about blaming the United States. Do you think there's any merit to that?

Anders Åslund: Of course, the international financial crisis started in the United States. The United States has had too low a monetary policy for a long time, but so has the rest of the world. So nobody is innocent here where very many people are guilty.

Steve Weisman: And the Russians continue, as you just said, to defend the ruble to some degree. Is that a wise policy on their part?

Anders Åslund: No, it's a very unwise policy because in this situation, everybody realizes that the ruble will fall. So why hold on to it? And the reason why more money has not gone out of the country is that the Russians don't trust the dollar either. So they think that the dollar will go down as well. So what can they do? People are adjusted, frightened, and paralyzed.

Steve Weisman: What should they do?

Anders Åslund: I think that they should buy a basket of the dollar and euro in order to reassure themselves, but certainly not hold onto the ruble because when the commodity prices fall, as they have, then the ruble will have to decline.

Steve Weisman: Is this a point of economic judgment or pride on the part of the Russians?

Anders Åslund: I think the government is entirely afraid that there will be social unrest and the value of the ruble is very important for the popular perception of the situation. If they see the ruble falling sharply, then they think of 1998 when Russia had a serious financial crash. It's a matter of political survival for Prime Minister Putin.

Steve Weisman: What happens to Russian consumers if the ruble is devalued?

Anders Åslund: Well, import prices will be much more expensive, but that will happen in any case as long as the oil prices have fallen as they have now. And it appears to me that Prime Minister Putin is only gambling on one thing: that the oil

prices will be up to at least \$75 within half a year. Otherwise, this strategy would fall into tatters. And he would be likely to fall.

Steve Weisman: That's quite a statement. You don't think that oil prices will rebound to \$75, do you?

Anders Åslund: I don't think so, but of course, nobody knows. I heard one person thinking that it will go up to eight and another that it will stay at \$14, and a third that it will be \$60. So, it's anybody's guess. There are so many factors that influence oil prices.

Steve Weisman: Is it in the interest of the West to have the possibility of political instability in Russia? Or shouldn't we worry that the economy might become so severe that the political situation is unstable?

Anders Åslund: Well, if you have an unstable regime that is authoritarian for no particularly good reasons, you would not necessarily want it to survive longer than necessary. As it reaches Russia, it's normally a democracy. Russia is also highly educated and it's quite an open country. There is no reason apart from the nasty tradition and a sad history for Russia to be authoritarian today.

Steve Weisman: And you mentioned 1998, which of course was a tumultuous and important year for Russia. What is the scenario here? You said that you thought if oil doesn't go back up in price, Putin and his government could fall. How would that take place?

Anders Åslund: The political situation in Russia now looks approximately like the political situation in Poland in the 1970s, when Poland had quite an open battle with the authoritarian regime under Edward Gierek, which survived by pouring money on the population. And it controlled all political organizations, so when there was too much popular dissatisfaction, they started from below. And the communist regime then in Poland was extremely afraid of the workers, not at all of the middle class. The Russian situation is quite similar now. It's a grassroots reaction that the regime is afraid of.

Steve Weisman: Workers, as well as the middle class?

Anders Åslund: Well, protesting masses taking to the streets, that's the concrete danger. And recently we have seen surprisingly substantial protests against high import tariffs for cars and we know that hundreds of thousands of the workers have been laid off. And many more will be laid off. We also know that hundreds of thousands of workers had their salaries cut, often very substantially. And the question is, who will stand up and protest? Often, all kinds of labor laws and regulations are violated. And even Prime Minister Putin yesterday said that this is not acceptable.

Steve Weisman: How acutely aware of this potential of unrest do you think that Mr. Putin is?

Anders Åslund: I think that they are very afraid of this and this is the reason why he doesn't want to devalue. It's also the reason why they don't want to discuss the financial crisis in public, that they have tied them to all kinds to laws. So that now if you do anything that leads to instability in Russia, you can be sentenced for treason.

Steve Weisman: What should be the West's response? Should the West just let Russia stew in its own juices or is this a crisis that can be exploited diplomatically or politically by the West?

Anders Åslund: I can't see that the West can or should exploit this. I think that any attempt to exploit the crisis would be counterproductive. Nor can I see that the West can help Russian in any way. Russia doesn't want any help, and Russia shows a very strong contempt for the West. At present, I think the best thing for the West is to do absolutely nothing. To stand in the situation, to be well informed, but not to be drawn in unnecessarily.

Steve Weisman: Well, of course, doing nothing is what many governments are famous for being able to do best.

Anders Åslund: Indeed.

Steve Weisman: Anders Åslund, thank you very much for sharing your thoughts about Russia at this critical moment at the end of 2008, and we'll talk to you in the new year. But in the meantime, thanks again and happy New Year to you.

Anders Åslund: Thank you very much.

