

The Financial Crisis and the Policy Responses in Russia

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The Russian economy, which had enjoyed a high rate of growth based on the crude oil price surge since 1999, has been plagued by rapid turmoil in financial markets and deterioration of real economy since September 2008 when the global financial crisis surfaced.

The largest cause of the aggravation of the financial crisis in Russia is the large outflow of capital that happened in the private sector mainly during the fourth quarter of 2008, the major system and policy factors of which include the radical liberalization of capital transaction in July 2006 and the exchange rate policy implemented by the Central Bank of Russia since November 2008.

The Russian Government and Central Bank developed large-scale measures to deal with the deepening financial crisis, but the capital provided by the Central Bank to the bank sector was diverted, to a large extent, to capital outflow, and its effects to ease the credit crunch were limited. Moreover, although the Government's measures against the crisis entered into the stage of implementation after a significant revision of the 2009 federal budget, their progress has been delayed. The above inefficiency and delay of policy responses are part of the cause of the deepening financial crisis.

The three points that are considered to be important in predicting the future Russian economy are as follows:

Firstly, the trend of the crude oil price: In recent years, Russia has aimed to free its economy from reliance on crude oil and set the diversification and sophistication of industrial structure through innovation, etc. as a policy target. The above conversion of industrial structure, however, cannot be achieved in a short period of time, and accordingly, the Russian economy's reliance on oil and gas will continue at least on a short-term basis. The crude oil price dropped suddenly toward the end of 2008, but started to rise again. If the tendency continues, it is probable that domestic demand in Russia will gradually recover.

Secondly, the progress and effectiveness of the measures against financial crisis by the Russian Government and Central Bank: The measures against financial crisis based on increased public spending have finally been well under way since this autumn. Moreover, the Central Bank of Russia continues to implement monetary easing, and accordingly, it is likely that the issue of credit crunch, which is one of the causes of the sudden production reduction during the first half of the current fiscal year, will gradually improve.

Thirdly, the outcome of the so-called "non-payment problem" or overdue debts, which became widespread mainly in the corporate sector after the occurrence of the financial crisis: All the overdue debts in the corporate sector owed to corporations, governments, banks, and households have been on the increase since last autumn and there is a possibility that even if the measures against the financial crisis taken by the Government and the Central Bank get fully under way, for the time being, the money will be used to pay back overdue debts (adjustment of balance sheets) and not for production activities.

Thus, it seems that the process of recovery of production will necessarily be slow, even if the crude oil price recovers steadily and the credit crunch gradually subsides. The outlook (basic scenario) prepared by the Economic Development Ministry of Russia says that the Russian economy will return to positive growth in 2010 on a year-on-year basis, albeit only slightly, and full recovery is expected to take place in 2012. As the crude oil price is fluctuating at a level higher than the level forecast in the above outlook prepared by the Ministry, there is a good possibility that the full-scale recovery of the Russian economy will be about a

year earlier than 2012, but basically, the basic trend is likely to be according to the above basic scenario.

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