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Euro Zone Unlikely to Benefit from Kremlin Billions

Russia's economic collapse in 1998 was a central event in the country's post-Soviet history. It derailed many hopes about where Russia was headed, wrecked the Yeltsin presidency and helped create the myth of Western meddling in Russia's internal affairs that helped legitimate the rule of Vladimir Putin. Today the tables are turned. Russian has almost no external debt, falling inflation, a modest rate of economic growth and the world's third largest international reserves. By contrast, the European Union, Russia's largest trading partner, is struggling to stop a debt crisis that so far has cost five state leaders their jobs and threatens to trigger another global recession. "The European monetary union may be deformed or break up," says Russian oligarch Oleg Deripaska, one of Russia's richest men, told Bloomberg last week. Rusal, Deripaska's metals conglomerate, is seeking to diversify from its traditional Western markets and boost sales in China. But the damage is beginning to spread. Russian banks are having more difficulty than usual getting loans from European banks as they try to scale back exposure to Russia. The reason is not that they are concerned about lending to Russia, but the banks' own funding problems.

Like officials elsewhere, Russian leaders were initially slow to appreciate the seriousness of the euro crisis. In early October Prime Minister Putin told French television that he trusted and believed in the euro and was convinced its troubles were only temporary. As the contagion spread, Moscow's assessment changed and it indicated it might be willing to help. At November's G 20 meeting in Cannes, President Medvedev urged European leaders to act forcefully to end the debt crisis and backed the EU-IMF policy of austerity measures and job cuts. Presidential aide Arkady Dvorkovich mentioned \$10 billion as a possible contribution to help bail out the euro zone (an amount far less than that needed to slow the crisis).

Russia also used the euro zone crisis to score political points. Dvorkovich singled out for blame the crisis "incomplete financial consolidation" in Europe and the United States. At Cannes Moscow endorsed a joint position reached by the BRICS group – Brazil, Russia, India, China

and South Africa – that any aid to the euro zone must go via the International Monetary Fund, which would then have to be restructured in order to increase the BRICS formal role.

Political rhetoric aside, there are good reasons for Russia to be wary of getting drawn too far into the euro zone turmoil. Economists have noted that the Russian government has only about \$100 billion left in its special, rainy day fund after spending most of it on recovery measures from the global financial crisis three years ago. (The approximately \$500 billion in international reserves held by the Russian Central bank are mostly invested in low-risk government bonds rather than high-yield debt on the market from struggling countries such as Italy and Greece). Russia is unlikely to continue its current, relatively generous level of social welfare spending after next year's presidential elections, when it may pursue austerity measures of its own. Russia also needs a large financial cushion as a hedge against the possibility that world oil prices, on which its economy heavily depends, will decline.

Nevertheless, as analyst Vladimir Frolov has reminded us, Russia has recently made big strides in economic integration at both global and regional levels. This month it has completed the long process of gaining entry into the World Trade Organization. Also in November the prime ministers of the CIS countries signed an agreement creating a common economic space, while in early October Prime Minister Putin presented his vision of a Eurasian Union that might one day rival the EU. Viktor Khristenko, Russia's Minister of Industry and Trade and the nominee to head the Eurasian Economic Commission of the new union, says that he and his colleagues have studied the troubles of the euro zone and identified the proper ways to coordinate budget, financial and monetary policies. The answer, he says vaguely and probably unrealistically, lies in "localized globalization processes." There cannot be just one center defining the processes and development trends for the entire global economy. Fine words, indeed, but Russia is unlikely to stand by should the new union begin to run into trouble.