

## **A Good Pilot Is Needed for Smooth Flight**

By Konstantin Sonin

Whenever a Russian economist says he teaches "the problems of economic security," other professional economists have treated this in a contemptuous manner. Thirty years ago, this type of job, which requires no real effort, would have been called "the methodology of teaching the fundamentals of Marxism-Leninism." In contrast with Marxism-Leninism, however, economic security is a serious subject that needs to be addressed. I am not talking about simply calculating the share of foreign ownership in Russian mining companies; that is precisely what many economic analysts do in government organizations.

Strong and stable economic institutions give nations the ability to survive periods of turbulence and avoid catastrophic consequences. This is the key to providing economic security to a nation.

In all likelihood, we are now heading toward a period of high global inflation. This is a serious problem for any national leader. Solutions such as indexing pensions to the rate of inflation might make sense for political reasons, but they do not make sense from an economic point of view. The actual outcome will depend on how independent the Central Bank's monetary policies will be -- that is, it will depend on the strength of institutions.

Similarly, real economic security is achieved when the Central Bank is independent enough to strengthen the ruble whenever the situation demands it, even if it means that exporters will suffer additional hardships as a result. It also depends on whether the finance minister feels secure enough to avoid feeding off the national budget and stabilization fund.

It also requires a State Duma that is ready and able to respond quickly if the inability of borrowers to pay back their consumer loans spins out of control. The fact that Russian banks charge high interest rates these days and have just learned the techniques of beating money out of individual defaulters here and there in no way means that they will be able to deal with an nationwide insolvency crisis.

Or take another critically important question -- whether state regulators have a clear picture of what is happening within major banks. For example, do they know who owns a significant share of Gazprombank, which ranks second in assets among all Russian banks? These types of issues may be unimportant during times of economic growth under a popular president with whom the bank's owners have close ties, according to media reports. But the fact that the bank's success is so dependent on the president could prove to be a catalyst for crisis if the president's ratings falter, in which case depositors and insiders could end up stepping over each other in a race to pull their money out of the bank.

In the meantime, economic turbulence is intensifying. It is becoming increasingly likely that the United States will enter a recession soon, and this may be accompanied by relatively high inflation. The problems caused by the subprime mortgage crisis have not only failed to recede, but they are looking more and more serious. European banks are waiting for help from the European Central Bank and will soon turn to their national governments for protection as well. It is unclear just how much the flow of money into new markets -- Russia included -- represents real growth opportunities, or how much of it is simply "flight from the dollar." The Chinese stock market bubble is expected to burst soon with unknown consequences for the global demand for oil.

All of this does not necessarily mean that an economic catastrophe is imminent. Occasional turbulence is a normal economic occurrence. For Russia, the real question is: Amidst all of this turbulence, what is happening in the captain's cabin? As it seems now, the pilot and chief steward eagerly offer each other the pilot's spot. But, so far, the flight is on course.

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