

# THE MOSCOW TIMES

## The Chavez Path Not Taken

By Konstantin Sonin

Tuesday, July 3, 2007. Issue 3690. Page 9.

Venezuelan President Hugo Chavez's just completed three-day visit to Moscow offered a chance to consider the economic pitfalls Russia has avoided and should continue to be aware of in the future. One of the three major factors contributing to growth during President Vladimir Putin's presidency has been a successful economic policy achieved by dint of will and not simply by luck. Things haven't gone as well for Chavez, whose economic policies have created serious problems for Venezuela.

As mentioned, there are three basic factors behind Russia's economic growth. One is high world prices for raw materials -- oil, gas and metals in particular. Second is the fact that the economy's starting point was so low to begin with. Starting from almost zero, the market reforms implemented during the 1990s, willingly or otherwise, the freeing up of the country's manufacturing potential, the formation of a business class and the establishment of a moderately effective system for regulating business activity were all bound to contribute to growth.

The third factor -- for which Putin can claim some credit -- is the conservative fiscal and monetary track the government has steadily followed. This factor is important because, as Chavez's experience points out, it is all too easy to take another path and suffer the consequences as a result.

In 2006, Venezuela's budget deficit reached 2 percent of gross national product, a figure that could double this year. Inflation was 20 percent. These might not seem like especially high figures at first glance and could be considered in line with trends in a number of other countries in previous decades. But the 21st century started off with low interest and inflation rates worldwide, and these economic indicators for Venezuela are South America's highest. Inflation is only half the problem as the wildly popular Chavez also opted to nationalize large chunks of industry -- a far-too-common practice with the just-as-common result of worsening economic conditions. The nationalization was a response to rising prices, which in turn were the result from firms taking advantage of the Venezuelan parliament's limited ability to regulate the economy adequately. The first signs of food shortages appeared early this year, indicated by the widening gap between prices for foodstuffs set by the state and the much higher black market prices for the same items.

Things are only growing worse with time. Chavez has already warned banks that they will be next in line for nationalization -- after energy and telecommunications companies -- unless they can offer low enough interest rates to local businesses. During this period of rapid growth -- it averaged 12 percent over the last three years -- banks earned high profits from rising black market interest rates and by trading on the national currency market, so they are willing to follow the government's recommendations. But banks typically set interest rates in order to hedge their exposure to risk and not based on their own subjective whims. Chavez's aspiration to help the poor by artificially lowering interest rates will only serve to increase that risk.

Cuban President Fidel Castro, a hero for Chavez, was one of the least economically effective leaders of the 20th century. Cuba's per capita GNP after 50 years of Castro's rule is about the same as it was under that nation's previous dictator, Fulgencio Batista. And this while global GNP per capita tripled and the figure for South America doubled. And the speed with which the destruction of Venezuela's democratic institutions has been followed by talk of "sabotage" as a cause for the country's mounting deficit shows that Chavez's regime is hitting a dead end even faster than did Castro's.

Chavez may have had some bad teachers, but that can be good news for Russia. Its leaders are not fools, so they can learn from others' mistakes.

*Konstantin Sonin is a professor at the New Economic School/CEFIR.*