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RUSSIAN ECONOMY IN THE MIDST OF THE WORLD ECONOMIC CRISIS

The last decade of the 20th century and the beginning of the 21st century unfolded under the sign of neoliberal globalization. The new stage of scientific and technological progress has led to a dramatic increase in the economic interdependence of the states of the world due to the rapid development of international trade and sharp increase in the transnational mobility of financial resources and labor. During this period, internationalization processes took place in the context when the market economy became a universal form of organization of economic life, and their most important aspect was consistent removal of barriers that limited the direct interaction between economic agents from different countries in all spheres of activity.

The trend toward an increasingly homogeneous market environment on the planet has manifested in many ways and has apparently determined the qualitative specificity of this stage of internationalization of the world economy. The process of abandonment of administrative and economic (primarily tariff) restrictions that stood in the way of international trade progressed rapidly as full-scale financial liberalization took place. In the monetary sphere, the position of the U.S. dollar has remained unshaken, while liberalization manifested itself in the transition of most countries to the regime of freely formed exchange rates of national currencies. Common standards of macroeconomic policy were established on the spot. Its monetary component in most countries boiled down to the task of minimizing the level of inflation, and financial component – to the rigid framework of the state budget deficit. The market economy globalization also manifested itself in the rapid development of transnational production structures with their emerging branched value chains that linked producers from different countries into a single whole. The regional integration processes that have developed in different parts of the world were seen in this context as a form of enlargement of the world economy structure in the course of its globalization.

All these trends were accompanied by a tangible weakening of the economic positions of nation-states and transfer of their functions to the level of inter- and transnational organizations. More and more often, the idea of creating a single world government in the future appeared in the public and political discourse.

Of course, even in this context, it was evident that the key role in the process of globalization was played by the United States and its allies. However, it was perceived that the interests of the leading states, in fact, coincided with the interests of the global community, since their implementation contributes to the rapid spread of modern production technologies and progressive forms of organization and management. These perceptions were reinforced by the fact that during globalization, transnational companies whose headquarters were mostly located in economically developed countries, moved their production facilities to the developing countries on a massive scale.

Globalization entailed a significant change in the specialization of different groups of states. Economy of the U.S. and many of its allies has become service economy: for the most part, and in the United States nearly entirely, their gross domestic product became generated by services. Of course, the leading place among these services is occupied by the highly intelligent part of the real economy[2] – science and technology, information and communication, educational, medical, transportation, and construction services. But such systemic activities as financial services play a prominent role in the economic structure. In the last decades of the 20th century, the development of securities markets and sophisticated transactions with financial assets based on complex mathematical constructs turned financial intermediation into a very profitable activity. Globally, provision of these services became concentrated in a limited number of financial centers, most of which are either located in the leading countries or are controlled by them.

Lifting of restrictions on transnational transactions did not (and could not) happen according to a procedure pre-agreed by all countries. Therefore, the weakening economic positions of nation-states during the period of neoliberal globalization were not an inescapable trend that equally affected everyone. The most successful developing countries (most notably China), taking advantage of the opportunities of globalization, have carefully tailored their decisions to liberalize economic activity in accordance with national strategic objectives. This means that even during the relatively favorable course of globalization, the potential for interstate contradictions persisted (and partly grew).

It seems that the global financial and economic crisis of 2007–2009 was a turning point. The global catastrophe resulting from radical liberalization of capital markets had severely hit the countries that had previously relied on financial intermediation. And then it turned out that the national interests of the world leaders did not disappear, they just remained in the shadows until they were threatened. As a result of the crisis, the balance of national and state interests shifted, which was due to the rapid rise of China, the change in the overall balance of power on the world economic arena, the increased interest in Russia's position regarding the need to transition to a multipolar world, as well as the appeal of such organizations as BRICS. All this contributed to the return of geopolitics to the forefront of global affairs. During the pandemic, this trend only intensified.

The world economy has entered a zone of institutional crisis. Former leaders of neoliberal globalization switched to restructuring their own economies, a trend that has clearly manifested itself in the return of industries previously

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[2] The real sector of the economy should not be identified with the sphere of material production. This sector includes all activities that are part of technological chains leading ultimately to the satisfaction of people's natural needs.

relocated to developing countries. The standards of rational macroeconomic policy that once seemed immutable became blatantly ignored by the developed states in favor of counteracting the recession due to the pandemic and maintaining social stability within national borders. The arsenal of their actions began to include such "unconventional" measures of limiting the freedom of transnational transactions as the use of sanctions against their geopolitical competitors. All this gives reason to believe that we are witnessing a significant slowdown of globalization at the least[1]; more likely, it is replaced by fragmentation, which will be accompanied by a significant institutional restructuring of economic relations in various macro-regions of the world economy.

Russia, for well-known reasons, finds itself at the center of the geopolitical rifts of the modern world. The unprecedented sanctions imposed on it after the start of the special operation in Ukraine are quite in line with the general logic of the "deglobalization process" – replacement of the competitive relations of classical market economic agents (firms and consumers) by relations of confrontation between nation-states and their coalitions. In this "game situation," in which the largest states are direct or indirect protagonists, Russia must find appropriate responses to the challenges it faces.

Due to the sanctions war, the Russian economy has to deal with three main types of shocks. The existing and potential restrictions on Russian exports are (or may become) a source of "demand-side shocks." Bans on supply of various types of products to Russian firms, as well as naturally occurring or artificially erected logistical barriers that hinder the delivery of imported goods, give rise to the so-called "supply side" shocks. Finally, the reduction of possibilities or even complete blocking of settlements with currencies of unfriendly states falls into the category of "financial shocks." The channels of impact and the consequences of these strikes on the economy are different, which has to be taken into account in elaborating economic policies.

Shocks accompanying a decline in external demand make sale of export-oriented products problematic; they can cause production stoppages and growth of unemployment. Shocks that disrupt the production process can lead to such an extremely unpleasant phenomenon as stagflation – a reduction in output and an increase in inflation at the same time. Restrictions on the use of reserve currencies in international settlements complicate foreign economic relations and thus entail a series of grave problems for an economy that is deeply integrated into the global turnover. Finally, measures beyond civilized relations, such as freezing of sovereign reserves, funds of legal entities and individuals under sanctions, immediately reduce the resources of the Russian economy. All of this together poses the threat of chaos in industrial and financial activity, an uncontrolled decline in production, large-scale unemployment, and erosion of the social and political stability of the Russian society.

The nature of the emerging problems clearly indicates that our economy will go through a period of large-scale restructuring due to the need to modernize its connection with the system of world economic relations. Clearly, such restructuring under time pressure is a daunting task.

The analysis shows that in the current context, availability of basic resources (agricultural land, extractable resources) for production activities and meeting the basic consumer needs is not a burden generating a "narcotic dependence" on income associated with their exploitation (the so-called Dutch disease) but an essential condition for a successful response to the challenges faced by Russia. This national patrimony guarantees us the ability to maintain a decent level of consumption for the population at all times and to prevent an unacceptable decline in productive activity. Now the key task is to determine the optimum mechanism for financing urgent structural changes. The problem is that these changes require significant investment and will take a long time to implement.

An attempt at ensuring structural adjustment based solely on market self-regulation through interaction of private firms would inevitably entail unacceptable levels of unemployment in the short and medium term. Small businesses can play a certain role in alleviating this problem, so efforts to create the most favorable conditions for their activities are perfectly justified. However, this role is inevitably limited. Without active participation of the state, the process of structural readjustment will be invariably long and painful. The state has the toolkit of active industrial policy that helps prepare general design of the necessary structural changes and achieve its implementation. The state can ensure a sufficiently rapid transfer of some of the revenues from the resource sectors of the economy to sectors in need of investment, experiencing a current shortage of demand.

In a sense, this problem is similar to that of the Soviet state during the years of industrialization. Several approaches to its solution are theoretically possible.

The first one consists in direct withdrawal of funds from donor industries through the tough tax pressure. The disadvantages of this modern version of "Prodrazverstka" (a policy and campaign of confiscation of grain and other agricultural products from peasants at nominal fixed prices according to specified quotas by the Bolshevik government during the Russian Civil War) are obvious: it suppresses all stimuli for effective work of the resource sector and arouses socio-political tensions.

The second approach is related to inflationary financing of structural adjustment. The risks associated with it are even higher because the Russian economy is already facing a very acute problem of inflation in the mid-term due to the supply-side shock that has hit it.

Finally, the third approach is to maximize the financial capacity of the state itself. This capacity consist of accumulated funds from the national welfare fund, state-owned factor incomes (profits from state assets, rents for state-owned natural resources), and borrowed funds. Apparently, use of the borrowing instrument will entail that the country will live with a growing public debt for quite a long time. Since today this debt is at a low level, and the attracted loans should be used to create effective production whose income will be the source of this debt's repayment in the future, this development is not especially dangerous.

The structural shock faced by the Russian economy entails special demands to the monetary policy. The first measures taken by the monetary authorities have proven to be effective. The rapid (as early as February 28, 2022) and drastic increase in the key interest rate to 20% made it possible to bring down the agitation on the foreign exchange

[1] This view has become widespread and reflected in the emergence of such term as Slobalization (slower globalization).

market[1], return depositors to banks, and largely suppress the burst of "momentary inflation."[2] Another success is the Central Bank's quick response to the stabilization of commodity and financial asset markets: its key interest rate was lowered first to 17% (from April 11, 2022) and then to 14% (from May 5, 2022). However, the intention to return to four percent annual inflation in 2023 is questionable. Not the very possibility of achieving such a result, but appropriateness of setting such a goal in the present conditions is doubtful.

The supply-side shock and the resulting significant structural changes in the Russian economy are long-term, clearly not within the horizon of 1.5–2 years. A premature attempt to suppress inflation in these conditions is fraught with serious problems in the production sphere – deterioration of the financial situation of enterprises and long-term stagnation of the economy. Therefore, for the foreseeable period, we should not aim to return to the four percent level of annual inflation as soon as possible, but to ensure the most favorable conditions for structural readjustment of the economy.

In terms of investment appeal for economic agents, which is vital in resolving this problem, the level of inflation is of lesser importance than its predictability for economic agents and the real interest rate. At the same time, a low (or even negative) rate alone does not mean favorable conditions for investment: entrepreneurs have to reckon with the fact that in case of a significant reduction in inflation the situation may quickly and drastically change. This consideration is all the more important since in the normal conditions, there is a clear relationship between the level of inflation and its variability.

The standard approach to solving this problem is to steadily reduce inflation while implementing the steps to convince the economic agents that anti-inflationary policies will be firmly in place, despite the current costs on the production side. Supposedly, this is the most reliable way of shaping a favorable investment climate, and it seems that the Central Bank of Russia is pursuing it, albeit not in the toughest version.

Meanwhile, the complex configuration of shocks faced by the Russian economy may result in a situation when the current costs are too high. Therefore, we should seriously consider another option, successfully tried by a number of other countries where the annual rate of inflation exceeded 30–40%. This option suggests introduction of a system of indexation for all fixed-term contracts, with automatic adjustment of obligations of economic agents to the price index that is regularly stabilized by the authorized state body. Certainly, implementation of this idea requires a lot of effort and time: in this case, companies have to move to inflation-adapted system of accounting, and the state has to make changes in tax law. Besides, the indexation cannot be perfect, because it will not occur continuously, but at intervals.[3] But against the background of the long-term structural shock that has hit our economy, these costs may be acceptable given the benefits that a radical reduction in the impact of uncertainty in price dynamics would have on the decisions of economic actors.

Another challenge faced by the monetary authorities is that the unfriendly states have taken restrictive measures against Russian banks and economic agents, making it difficult for them to use reserve currencies in international settlements. But such a possibility has not been completely ruled out. The resulting situation is quite extraordinary. On the one hand, there is still a "bottleneck" enabling payments in reserve currencies by non-sanctioned firms through non-sanctioned Russian banks for certain types of imported goods. On the other hand, one cannot ignore the fact that unfriendly states can narrow down or even shut off payments in reserve currencies at any time.

Russia's response was absolutely adequate. Decisions were made to allow Russian firms to repay foreign debts in rubles if necessary; payments for gas supplied to foreign markets were transferred to rubles. Restrictions on the capital items of the balance of payments, in particular the decision for exporters to sell 80% of export earnings in the foreign exchange market, are also important, albeit forced.

The declining attractiveness of the dollar and euro for Russian economic agents led to an unprecedentedly rapid decline in their exchange rates against the ruble. Moreover, escalation of anti-Russian sanctions in the financial sphere could theoretically lead to complete elimination of the circulation of currencies of unfriendly states in the Russian foreign exchange market. In this case, mutual trade can be carried out either using the ruble (as well as currencies such as the Chinese yuan and Indian rupees), or through the introduction of clearing systems of settlement, or through barter transactions.

In general, the situation with the foreign exchange clearly resembles a game. In an attempt to undermine the Russian economy, Western countries have to consider the danger of a drastic reduction or even termination of supplies of vital goods from Russia, as well as the very real prospect of damaging the reserve status of their currencies. The Russian side avoids complete rejection of the use of currencies of unfriendly states and does not put forward a requirement to switch to rubles exclusively in settlements with them, because it does not want further reduction in mutual trade.[4]

[1] The ruble-dollar exchange rate on February 23, 2022 was 80.42, on March 11 – 120.38, on April 13 – 79.63 rubles/dollar. See: https://www.cbr.ru/currency_base/dynamics.

[2] The rate of monthly inflation (as a percentage of the previous month) in the first quarter of 2022 increased rapidly: January – 0.99, February – 1.17, March – 7.61%; year-on-year: January – 12.5%, February – 15.0%, March – 141.1%, April – 44.0% (see: https://rosstat.gov.ru/storage/mediabank/ind_potreb_cen_03.html). In April, inflation began to decline rapidly. Its average daily level in the first half of the month was already half as much as in March – 0.1 vs. 0.237% (see: https://rosstat.gov.ru/storage/mediabank/60_13-04-2022.htm).

[3] The possibilities and limitations of adapting to inflation by indexing nominal contracts have long been known (see, for example: *Begg D., Fisher S., Dornbusch R.* Economics. 3rd ed. McGraw Hill Book Company, 1991. P. 520–521), but with the establishment of the Washington Consensus ideology, they have been effectively abandoned.

[4] At the same time, it is necessary to take into account the danger of enforcing new decisions for "freezing" the amounts in reserve currencies available with Russian firms and banks. What is concerning in this regard is the significant level of current-account asset recorded in the first quarter of 2022, $58.2 billion; for the entire 2021, the figure was $122 billion (see: https://www.cbr.ru/statistics).