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German-Russian Talks Stir Up Monetarists

by Rainer Apel

Being the biggest single supplier of machinery to Russia, the German economy ranks high on the priority list of Russian diplomats—also because of the fact that, for decades, German banks have been the biggest suppliers of loans to Russia. Some 40% of the foreign debt that Russia owes to the Club of Paris group of lenders, is to Germany alone ($21 billion).

Several high-level diplomatic events during December have underlined the genuine Russian interest in enhanced German investments. On Dec. 1, Russian Prime Minister Mikhail Kasyanov came to Berlin for talks with government officials, industrial leaders, and bankers. The most interesting aspect of this visit was that Kasyanov floated a "debt-for-investment" swap proposal. He said that in order to get some relief on the foreign debt front, Russia was thinking of offering German industrial firms shares in select Russian ones, with the value of the shares balancing up to 3 billion deutschemarks of debt owed to Germany, for a start.

During and after Kasyanov's visit, several proposals were floated in the German and Russian media, for such debt-for-investment swaps. The idea that Russian natural resources companies such as GazProm would offer shares to the Germans, met with instant opposition in Russia, because at the moment, these kinds of companies are flourishing, relatively speaking, because of the increased prices for natural gas and crude oil. These are assets which Russia will not easily give away. But, the exploration and pipeline transfer infrastructure of GazProm and other companies is in urgent need of modernization and overhaul, especially if one keeps in mind the scope of expansion that the European Union-Russian 20-year energy partnership implies. By the year 2010, Russia wants to double its gas and oil deliveries to the EU, which means more pipelines, and more production of gas and oil—and $20 billion of new investments are required, to make that gas and oil available for export to Western Europe.

Because neither Western nor Russian industrial managers are philanthropists, to make investments in Russia attractive requires a political decision, as short-term returns cannot be expected from such longer-term investment projects. Genuine national interests that override considerations from the standpoint of a single company's economic interests, must come into these talks, and this is what Kasyanov introduced in his Berlin talks: He made the German government recognize that it was neither in the German nor the Russian interest to see Russia default on its foreign debt. Any attempt to reinforce debt payments from Russia to the West, based on Russia's increased revenues from gas and oil exports, would be counterproductive at a time when 20% of the Russian state budget is absorbed with such payments while vital investments in Russian industry and infrastructure are being delayed, Kasyanov warned. Therefore, he said, Germany and Russia should work on an arrangement to transform a share of the debt into an initial Russian investment in select sectors of industry, which would be matched by German investments.

Turning Debt into Investment

In the days after Kasynov's visit, this idea was elaborated further, in the context of Germany's role as a big machine-building nation. On Dec. 11, when Russian and German industrial managers met in Frankfurt/Main for a "Day of the Russian Economy" conference, Kasyanov told journalists in Moscow that Russia thought of investing money it would otherwise have paid to service the debt to Germany, in the construction of new, and modernization of existing machinery firms, in which German firms could then acquire shares—a certain percentage of those for free. The Russian government would guarantee the reassignment of funds originally earmarked for debt payments, to investment projects of this type, Kasyanov said. Accompanied by substantial German investments in those machine-building firms, a promising perspective for joint Russo-German cooperation in a vital industrial sector would open up, he said. Russian Economics Minister German Gref discussed that with the German government in Berlin on Dec. 12, and when the new, high-level group of German and Russian government officials met in Moscow on Dec. 18 to further discuss details, the Kasyanov proposal was on the agenda, again, and the machine-building aspect was discussed prominently.

The scope of this new industrial cooperation—DM 3 billion—is a minor portion of the investments that Russia really needs. But, it introduces a form of non-monetarist relations which can be expanded massively. This kind of physical economic cooperation has been bitterly fought by Western banking interests, notably those in the City of London, especially since the fall of the Iron Curtain 11 years ago. Misusing the foreign debt exposure of Moscow to loot the Russian economy, has been the guiding principle of the monetarists, and their great time was the five years under Prime Minister Viktor Chernomyrdin, prior to March 1998. A remark by Russia's President Vladimir Putin during his visit to Canada on Dec. 18, that "international financial circles" are to blame for the Russian financial crisis that broke out in August 1998, indicates that the monetarists have come under high-level attack.

Therefore, the ongoing discussion between the Germans and the Russians has been met with rather aggressive commentaries in the British press, led by the London *Times*. On Dec. 18, it warned that a "new strategic reality" is about to be created on the European continent.

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