

boring countries. Our shares are tradeable only within our country. They all had to be registered immediately. There is no short-selling, if you know what that means.

I share the view, that the international financial system is aging. It needs a major reform, in order to meet the current need for the good of all, and to serve the interests of all. Globalization is a very good word, a very good concept, and we all share it. But, it is good only if all of us benefit from it. We believe in the market economy. Our economy is largely based on the market, but we also have — like you, Russia — in some sectors, the government play a role.

Malaysia has gone through four decades of independence, trying to improve our economic situation, the economic situation for the whole population. Unfortunately, we are still in that process, which requires the government to help the less fortunate sectors of the population, requiring a different kind of medicine, a different kind of strategy, a different kind of policy. And only with that, can we ensure that our people — the poor sectors of the population — will benefit from the richness of our country.

‘The Market’ Is Not Enough

The idea that the market will correct itself, that the market would have the power, the market would have the will, the market would have not only the opportunity but also the possibility to ensure that everybody benefits, is based on a very creaky premise. To assume that the market has a conscience, we cannot accept. The market has no conscience. The market is premised on making profits, and, in fact, it has to make profits at the expense of somebody else. Maybe it’s not intended, but they have no forms of pushing [down] their motivation for making profit. We have seen for ourselves, a couple of months ago, how the market pushed the electricity problem in California. Who can believe, that in America we would have to have emergency rule? But they did, because the market had pushed itself to the very limit, of making profits.

We believe, that the market must be tempered with conscience, and that conscience must come from somewhere other than the market itself.

I think we have heard presentations from the experts. In the policy of the financial system, what is very apparent, is the laws of the jungle. Not all of us, as participants in the process of the market economy and the financial system, share similar possibilities of knowing what is happening. There is a lack of transparency, but certain rules and regulations are known, and certain practices are known to very, very few, indeed. But, we must have extra tentacles, extra ways and efforts — and not all of us have the possibility, to know what is happening in the financial world.

And therefore, what we think is required, is a common effort, a common effort of all, involving various processes, to change the system for the common good. I think, that if there

is a will, there is always a way. Where there’s a will, there’s always a way.

I am very happy to see here today, many Russian experts in the various fields. Today, we have many experts in the field of finance, and the field of economy. Of course, we are privileged to hear experts from the rest of the world. By the end of the day, it is our own experts, who have the role and the responsibility to give their best efforts — the result of their best efforts, their analysis, their forecasts — and, their recommendations for the benefit of each country concerned.

When we say “the best for the country concerned,” I am confident that when all, almost 200 countries in the world, are fighting for their own individual interests, that there will emerge a *common* interest, that will ensure that *all* will benefit. It is in the best interest of everybody, that they have their stake in the system. For so long as the system benefits only a few, the majority will fight. Informed they must be.

What I’m saying is, let’s work together. Let us find a way out together, and let us make sure of that very best principle of a “win-win” situation; so that there is no loser, in the new system.

I thank you for giving me this opportunity to speak.

Sergei Yegorov

Challenges Confronting Russia’s Banking System

Mr. Yegorov is the president of the Association of Russian Banks. The text has been translated from Russian, and sub-heads have been added.

First of all, I should like to say that the Association of Russian Banks considers very timely the idea of the Council of the State Duma to convene these hearings, proposed by the Committee on Economic Policy and Entrepreneurship, on the topic we are now discussing. August 1998 already confirmed for us, what a negative impact financial destabilization can have on the national economy — state finances, corporate finances, and the banks.

Nearly half the banks in the country ceased to exist. The devaluation of the ruble slashed the value of bank capital. Many of them became insolvent, and lost the confidence of their corporate clients and the population. I believe there is no need to recall the consequences of the financial crisis. . . . The main thing, today, is not only to draw lessons from what happened, which of course must be done, but also to under-

stand how and when the destabilization of the world financial system may have a negative impact on economic growth rates in Russia, which have still not solidly taken hold, and on the domestic banking system as it grows stronger.

We have gotten used to thinking that the August 1998 crisis was basically caused by mistakes in economic and financial policy. Without question, there were such mistakes. . . . But, now we should say forthrightly that there was also another cause of that crisis. First of all, it should be noted that the leadership of the government and the Central Bank evidently underestimated not only the role in the crisis, of the instability of the national financial and banking sector, the overvalued ruble, and the current accounts deficit, but also the possibility of this crisis being imported from abroad, under conditions of increased globalization.

The powerful force of the new class of international investors, which has emerged in the global economy, was not duly realized in time. Able to act simultaneously in several emerging markets, if they experienced losses in one market, they would sell assets on another, destabilizing the situation in the country they were ruining. The Ambassador of Malaysia spoke about this very well. . . .

We remember, how the Asian wave of the crisis was accompanied by the plunge of currency exchange rates and stock market indexes, and by the bankruptcy of banks in various countries. In that crisis, the so-called contagion effect was in full operation. It spread from one country to another, even if there were not close economic ties between them. This is a very important point. It cannot be said, I think, that there will be a crisis of the world financial system tomorrow. But, nevertheless, serious preconditions have already been formed for such an eventuality, as the preceding speakers discussed. . . .

We see the task as being to minimize the risks from possible future crises, to limit their depth and range of effect, and to reduce the financial costs of getting out of the crises, in case they affect Russia—reducing the time it takes to overcome them, and to defend the most vulnerable social groups of the population. I think we need to do this immediately in Russia.

Measures for National Self-Defense

But, a crisis can also arise due to mistakes made on the national level, if a timely evaluation of the role of destabilizing factors in the global financial system is not made. In order to avoid this, we believe that it is important to provide a kind of self-defense for the national market, using a macroeconomic policy that makes it possible to prevent the devaluation of the ruble, and thus to avoid the real devaluation of bank and corporate capital.

Secondly, correct decisions have to be made on the convertibility of the ruble. Some of our specialists, when they talk about measures to ensure the development of the Russian economy, are currently proposing to introduce a fixed ex-

change rate, as one preventive measure. . . . This policy would have serious shortcomings, in our view. It would make it impossible for the Central Bank to function as an effective lender of last resort. A floating ruble exchange rate, in contrast, allows the combination of a less strict regime, with more flexibility, thus reducing the risk of an abrupt devaluation of the ruble. This enables the Central Bank to provide liquidity in the event of a crisis. Therefore, as we define measures to ensure the sustained growth of the Russian economy, it seems very important to preserve the floating exchange rate. . . .

We consider it appropriate to have a more balanced approach to the question of relaxing currency controls, as Academician Lvov discussed. There is no question, but that reform is needed in this area, since Russia is becoming ever more noticeably a component of the world economy and of global financial markets.

It seems to us that, attractive as many of the various other arguments may be, there is one indisputable argument, proving the need to prevent a serious collapse of the ruble. That argument is that it is simply impossible to ensure sustained growth, without the replacement and modernization of plant and equipment.

Our domestic machine-building sector has lost much of its capacity during these past years, and is unable to supply other sectors of the economy in the period immediately ahead, including the fuel and energy sector, whose output is the main component of Russian exports, and consequently of the ability to earn convertible currency and use it to purchase modern equipment. This, in turn, means that Russian importers benefit from a less expensive dollar—if, of course, that corresponds to the realities of our domestic economy. A stable ruble is even more important for the majority of Russia's population, with regard to the supply of food, medicines, and so forth on the domestic consumer market.

There are areas of currency regulation, however, which of course do need to be liberalized. In our opinion, the deregulation, for example, of procedures for foreign currency operations by which residents can attract foreign capital, needs to be accelerated. . . . We also consider it important for foreign capital to be able to enter and leave Russia freely, so that we may count on being able to attract it into Russia.

In charting ways to ensure the development of the Russian economy under conditions of destabilization of the world financial system, we cannot limit ourselves to domestic measures. It is important for Russia to take an active part in strengthening the cooperation among the regulatory agencies of countries belonging to the world financial community. This means to introduce international principles of regulatory supervision of the banking system, a process which essentially has already begun.

First among the immediate tasks, we think, is to restore the confidence of investors in countries, which have experienced a crisis. Second, to reduce investors' possible losses,

in the event of new crises. Third, to create a financial system, which would bring into play all the advantages of the global markets and the mobility of capital, while preventing macro-economic and financial unbalances from arising on the national level.

International financial institutions, above all the IMF and the World Bank, need to be reformed. In recent years, we at the Association of Russian Banks have had to have direct, close dealings with them. It should be recognized that the IMF was unprepared to take decisive measures, to prevent the destructive nature of the financial crisis in Russia and other transitional-economy countries, from the standpoint of mitigating its negative impact on the economy; rather, it recommended macroeconomic crisis measures, primarily sharp interest-rate hikes and budget-cutting, while denying the need for urgent measures to stem capital flight from emerging-market countries, or for talks with private creditors and investors on debt restructuring. Its activity was excessively politicized and ideological. The Malaysian Ambassador spoke about this very eloquently. . . .

We can now state that our banking system is emerging from the 1998 crisis, but some questions of principle remain to be solved, not only on the level of the banks, but also on the level of the state. First of all, the question of bank capitalization. If we measure it by international standards, our entire banking system is currently about the size of one major European bank. Of course, this is inadequate for a country like Russia. Moreover, the necessity of enhancing the banking system and bank capital for economic development tells us that the banking system needs to be more powerful.

In this connection, we need to look at sources of capitalization. The banks themselves, within the capabilities of their owners, are more or less actively working to build up their capital, but these capabilities are limited. Moreover, approximately 75% of all bank profits get paid to the federal budget, in the form of various taxes. Therefore, in recent years we have worked for a level of taxation of the banks, which corresponds to world standards. Banks should not pay higher taxes than other economic entities. For the past ten years, our banks have been paying excessively high taxes. . . .

The Role of the State

We believe that strengthening the banking system, means that we have to change the economic environment in which the banks function. I mean the real sector of the economy, above all. It is not prepared to accept credits, which the banking system might extend. Take this figure: 40% of our state-managed industrial firms are loss-making. What reasonable Eastern, Western, or Southern banker would lend money to such companies? In this connection, we share the view that the role of the state in regulating the economy should be increased.

Talking about the economic environment, I have in mind, first and foremost, the need for the state, for the government to create a well-considered state industrial policy. We don't have one. We don't know which sectors are going to develop. Establish this, and it will provide some certainty, including for the banks, even under conditions where not all the financial indicators of industrial firms are, shall we say, ideal; but, a good perspective on the development of a given sector will make it possible for the banks to look at those firms in a different way.

We think that one of the greatest problems in Russia during the past ten years, but especially the last few, is the creation of long-term credit resources. We don't have them yet. In this connection, we are looking at the need to mobilize the monetary savings of the population. International experience shows that any country develops chiefly on the basis of internal resources, and the savings of the population. Our population has big savings, but they take no part in economic turnover. Incentives need to be created, including the strengthening of the banking system, for the population's savings to enter more into circulation.

Once again, here in the halls of the State Duma, I should like to say that we urgently need to pass a law on deposit guarantees. This will make it possible to solve many problems, such as confidence in the banking system, in a completely different way. And, I think that the definition of a firm, state policy on the development of Russia's banking system must play a great role in this. . . .

Finally, I would like to draw your attention to the creation of a normal stock market. At present, you can count on the fingers of one hand, the companies traded on the stock exchanges. And what Academician Lvov said about putting the great wealth of the state on the books, and the state's becoming active in the market, in the stock market, is absolutely correct. Then, we'll get a second wind, and be able to rely not only on Gazprom and another five or so companies, as I said, but we'll have something corresponding to reality, and our stock market will start to function.

I would like to say again, Sergei Yuryevich [Glazyev], that you did the right thing in putting this question on the table for broad discussion. Thank you.

At this stage of the session, the serious and concentrated discussion was interrupted by the clown-like appearance of Vladimir Zhirinovsky. Exploiting his position as Vice-Speaker of the Duma, to get access to the podium, Zhirinovsky intervened with some confused remarks about the world situation and how Russia should strengthen its economy. Then, he abruptly launched into an attack on women, demanding that women should be banned from positions as judges, economists, doctors, or even cooks! Zhirinovsky got what he deserved, however, when the famous economist and former Duma member Tatyana Koryagina took the floor (see page 54).