Sustainability of Growth and Development of Financial System in Russia

Evgeny Gavrilenkov

1 Introduction

According to the State Statistics Committee (Goskomstat), the GDP grew quickly in 2003 (by 7.3 percent), as did industry (by 7.0 percent). This eclipses the much slower rate in 2002 of 4.7 percent for the GDP (which the State Statistics Committee recently raised from 4.3 percent after yet again, revising its historical data), and 3.7 percent for industry. On the basis of these figures, GDP growth in the post-crisis years (1999-2003) comes to 38 percent, or an average of 6.7 percent annually. In the first half of 2004 growth was also high, so that the GDP grew 7.4 percent y-o-y basis. Therefore, Russia continues to demonstrate a healthier macroeconomic performance than many other countries. Equally important is Russia financed this growth mainly from its own sources, that is, without any massive inflow of FDI or external borrowing (albeit, the latter did increase in 2003).

For decades, Russia exported capital. Capital flight was not a phenomenon of the 1990s, it took place in previous decades, too. For differing reasons and channels, from the macroeconomic point of view, continuous support of the communist regimes all over the world can be treated as capital flight legitimized by the government. It also means that once Russia starts attracting more FDI, which will finance particular projects, growth rates may be high even in the case of a lack of domestic financing. With that, the well-known task of doubling the GDP in 10 years, as was suggested by the Russian president in 2003, in principle, looks achievable. Obviously, higher volumes of FDI cannot be considered as the only sufficient condition for sustainable and higher growth rates. Some of the well-known structural impediments should be removed. In particular, one may point out the need for restructuring the financial system, the issue discussed in the paper.

The growth numbers looked impressive not only in 2003, but for early 2004. More important, some structural changes became more visible. The macroeconomic performance in 2002 clearly indicated the country could no longer rely on the advantages of "easy" growth, and a repeat of the same growth pattern which emerged after the 1998 crisis, would be impossible (Gavrilenkov 2003a). In recent years, a rapid rise in incomes shifted consumer demand toward higher-quality goods that could not yet be produced in Russia (Gavrilenkov 2003b). Domestic manufacturers throughout the market therefore, realized to compete with imports, a need to offer better (and possibly more expensive) products, meant they should invest in new productive capacities. Thus, increased investment activity was one of the major growth drivers most recently.

Various factors caused the growth acceleration in 2003: higher oil prices, which caused the money supply to surge, low interest rates, and a rapid increase in domestic demand. The latter was largely driven by greater investment activity, which was needed to resuscitate the exhausted growth mechanism that had emerged from the 1998 crisis, and was based on increased capacity utilization.

Due to the changing growth model, investment activity in 2003 rose not only in the oil and gas sector, as had always been the case, but across the board. Moreover, medium-sized companies oriented toward the domestic consumer market, set