

The Economic Club of New York

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Open Market Committee

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Questioners: Rand V. Araskog,
Chairman, ITT Corporation

Dennis Weatherstone
Chairman, JP Morgan

Introduction

Chairman Donald B. Marron

(No Introduction recorded)

...inside glimpse of Russia. Please welcome Bob Strauss. (Applause)

Robert S. Strauss

U.S. Ambassador to Russia

....responsibilities. I have enjoyed trying to ____ of this country. It leaves me sort of wondering why I am up here, why anyone would want me anywhere. I had trade responsibility and you can understand what has happened to our trade balance. (Laughter) I am the President's Special Representative to the peace negotiations in the Middle East. The situation in the Middle East leaves a bit to be desired. And I went to Russia to bring economic stability to that country. (Laughter) But be that as it may I am here. And I managed to survive. I am delighted to be here. It isn't my first time, as many of you know for this group. I am flattered to be invited and delighted to be here. I am particularly pleased to be on a program with Gerry Corrigan who I have known for some considerable period of time, but we really became good friends during my time in Russia when he contributed so much to help that country try to work its way through some of its problems and it seemed to me that every second or third weekend I would get a call and Corrigan would arrive on Saturday morning having flown all night Friday and he would work Saturday and Sunday seeing everyone from President Yeltsin on down. And back on that

plane Sunday night or Monday and be back in his office either Monday or Tuesday and how he kept it up, I don't know. But it is a great inspiration and I don't know anyone who has contributed anymore.

I am also particularly pleased that Ambassador Designate to Russia, Tom Pickering is in the audience tonight. One of our more distinguished Foreign Service officers. And it is a pleasure to see him in this group.

As far as I am concerned, it is hard for me really to believe that it was only August 1991 that I landed in Moscow myself as the new Ambassador to the then Soviet Union. And as I drove into the city when they met me, our car was held up along the highway while 75 to 100 big Russian tanks lumbered across the road. It was right in the middle of the coup and it seems to me like it was a decade ago. At least a decade ago, but only 20 months ago. Only 20 months, if you stop and think about it separate us from those very grim but yet glorious, I guess is a good word, glorious days of August when those tanks, which they sent out to smash the...oh smash the insurgents, turned, instead of turning against a moxie, turned their guns the other way and their efforts the other way and defended it. It is hard to believe it is just 20 months. And it is in that perspective, I think if you look around today and then you realize that with all of the problems there are, with all of the terrible news we read daily in the newspapers, that the accomplishments of President Yeltsin and of Russia, really are vast and historic. And that is despite the chaos and the confusion, the turbulence and the uncertainty lying ahead. You stop and think, the power of

the Communist Party is substantially destroyed. Market forces weak though they may be, are being introduced, continue to be introduced in the Russian economy. The progress is slow, almost at time not measurable, but it continues, entrepreneurship continues to grow. Even private property has began to get a little niche. And prospects reasonably good for continued improvement there. We are seeing, if you look around you there, a society that is beginning to be based on law with the Chairman of the Constitutional Court handing down decisions that even a strong, a very strong leader like Boris Yeltsin respects and obeys, even when they are against him. Rather than seeking arbitrary and autocratic power and probably of far more importance than any of that, we are seeing the reconciliation; we have seen the reconciliation of Russia with the Western World after decades of isolation and of hostility and Cold War. But those achievements and many more like them are tonight, I guess under the most serious challenge yet in Russia, the reform and the progress of 1991 and 1992 under Yeltsin and earlier than that under Gorbachev are under attack and will be under ceaseless and vicious and unrelenting attack in my judgment in 1993. And the outcome, in my judgment, also is far from certain. It seems to me in that setting that sometimes you think it is almost, well it is futile to talk about, try to separate economic and political questions. There is no point in trying to tell people to take and live in a democratic society and live any way they want, if they have to worry each day whether they are going to be able to live at all. And that is about what the people of Russia are up against.

Simply stated, democratic values and democratic institutions and traditions are too weak to survive in Russia if there is going to be economic desolation. Democracy still has a tremendous

amount to prove to the people of Russia, if it is going to make it. And most Russians understandably remain distrustful and they are alienated from the political process, and from government at all levels, and they wonder, what in the hell is in it for me. How did I end up in this shape? Particularly the older members of that society. And it is understandable. It is obvious, it is two and two just makes four. And I say to you that the people in Russia in my judgment again, are going to need to see reasonably soon some sort of positive confirmation that reform and democracy can mean something to them individually. Can bring something into their lives they didn't have before. Today, they have only seen suffering. They have seen pain, and they see insecurity and particularly those people 45, 50 years and older have democracy, leaves a lot to be desired in terms of their daily life.

The problems that the government and the people inherited from the old Soviet Union are too staggering almost to think about. The population has actually decreased in the last year; people are dying faster than they are being born. And disease, diphtheria, scarlet fever, things we don't even think about here are beginning to assume epidemic like proportions and the health of the children in that country is shocking. And the Asian Mafia grows bolder each day and permeates the society more. In the industrial sector I saw that *The Economist* magazine recently estimated that in many industries the add-on really when they take raw materials, reduces value. They take good raw material and the manufacturing process is so poor that value is reduced, make scrap out of raw materials in many industries. The most frightening aspect of it all is, of course, is that hyperinflation is just; it is on the brink, if not there, it is around the corner. And in a

hyperinflated economy, as, Gerry Corrigan knows far better than I do is one that is almost impossible for any sensible programs to take hold or progress to be made.

And after that set of dire predictions and statements, let me turn just a second to the positive side and say that Russia does have vast human resources with a well educated work force that can work and work well if given any decent motivation. In scientific and in technological talent alone, I think Russia is the most under-utilized economy in the world. And it is certainly one of the world's greatest reservoirs of natural resources. In food production, with all I have talked about on the negative side, food production is up a bit. In privatization, while slow, is going forward and continues to inch forward. Just this morning I spoke with my former deputy in Moscow and he was telling me of a new \$15 or \$20 million just a pityingly sum of money that was necessary, that he had his hands on, been able to get, and to keep the privatization program going forward. \$15 or \$20 million pityingly dollars, to keep a privatization program going. But he has it, and that is going forward.

So I would say to you, that while on a macro basis everything seems to be negative. And daily you read in the newspaper of what is wrong here and what is wrong there, and how a collapse is taking place somewhere else. But I will tell you that on a macro basis there are many positive things taking place. Many new enterprises, mostly small. You see a little something here and a little something there. The young people, the young people who have seen the west, and they understand the opportunities and they understand democracy and what it offers and what market

society offers. And it is now a society of, and by, and for those young people. And they know it. And they are not going to see democracy turn back in my judgement if they have any chance. They have a passion, a real passion, a Russian passion for individual fulfillment and I think they are going to stay steady on that course.

Centralized decision making with respect to whether it be output or distribution or anything else, is beginning to be a thing of the past. And while it is creating a good deal of initial chaos right now, that too will get better and it has again, removed the shackles on individual initiative. Regions and localities are operating more on their own. They are in business for themselves. Moscow begins to be irrelevant in many areas to these people. And while many of the results so far are still pretty bleak or meager, there are positive things taking place, and strangely with all of the hyperinflation and everything else, but there is a sense of discipline, a realization that money, there is some discipline to money and its use, and to interest rates, and to profits and losses, and more and more people are beginning to understand that. And recognition is going around the country that closings and bankruptcies and unemployment are inevitable. And that government just can't keep them alive, businesses alive, just to prevent unemployment.

So as privatization moves forward and more and more Russians become owners, it will become more and more difficult to turn back the clock in my judgment. But unhappily, unless inflation that I have talked about is brought under control, these things are not going to be able to continue. Well let me get on with it.

Boris Yeltsin remains an amazingly strong leader. He is...I am highly prejudiced in his behalf, and I am not a very good one to talk about him, but I see him and I have seen him under attack, from almost all sides, but his popularity with all of his problems, while it is not 60% as it was, or 65%, it still remains pretty close to 40% range. And I don't think it would happen in this country, if a leader of ours did to his people, and forced on his people, what Boris Yeltsin has had to force on the Russian people. In my judgment, he is going to survive. He is going to survive because he is anti-communist. Not fail to survive because of communism. And he is going to continue to survive because he is courageous and because he is standing for the right things, and because he literally dwarfs those who would compete with him. Literally dwarfs them. Dwarfs his detractors and the comparison is obvious to the people. This week he is busy meeting with his government. The people in his government. He is meeting with people coming in from the regions, and he is going out to them, as he moves towards the referendum, the April Referendum that can be the turning point in whether he makes it or not. And he just simply has to come to grips with that constitution and with the political process over there, because Russia desperately needs in my judgement a rebirth of political institutions and that is what he hopes to accomplish.

The Constitution is a relic of I guess the Brezhnev era. And nobody took it very seriously, I don't think. All decisions were made by a few central people. And the people in that Congress were elected in 1978 and it is not three co-equal branches. This Parliament has the power, it has the power. When it is put in place, no one cared what the power they gave it, because it didn't amount to anything. They won't ask him. But Yeltsin knows that the Constitution is hopeless. He

wants a new one for a non-Communist and a non-Soviet Russia. One tailored for Russia, the Russian Federation, for Russia today, and hopefully he will get it.

So, I would say, that as we talk here tonight, there is a high stake game going on over there. He also is going to try to force a vote on a new Constitution. They are going to try to force a vote for the situation where Yeltsin has to submit himself to another vote of the people. And while all of this is going on, we in the west have been, we have been in general, I would say, preoccupied, whether on elections, and whether on problems, and whether on affairs, and we tend to forget as we tend to them that our self interest is very, very much at stake. That our own self interest is very, very much at stake in what takes place in Russia and the other Republics and we could have, and we should have, in my judgment made a much greater contribution to positive change in Russia last year. The Russians should have done more for themselves. They can do more for themselves and we should have done more to help them. And I am not talking just about money.

But in speaking of money, I have mentioned to Gerry Corrigan earlier that I am not sure that this is absolutely accurate. It may be an over-simplistic statement, but when you stop and think about help, if you converted, the Russian GNP today, on currency conversion using 600 rubles to the dollar, you would have a Russian GNP of no more than \$100 to \$125 billion. Now that is a pygmy of a pygmy of a GNP. Technically that won't hold up. And Mr. Corrigan can tell you why. But it holds up in my mind. And I will tell you why I use it, because, if you look at it in those terms, as \$100 billion GNP, then you can realize that if we, in terms of debt restructure, for

one thing, if we pull just, force them to pull \$2 or \$3 billion out in the next couple of years for debt payment, debt service, you can see the negative impact it would have on that size economy.

By the same token, if we put in a few billion dollars wisely, wisely, it can have a tremendous positive impact, because of the size of that economy over there. So I say, we are going to have to make up our mind in this country whether Russia is really important. Important to our own self-interest, and if the answer is yes, as I think it will be, and should be, then we are going to have to do more. We are going to have to do a lot more. We are going to have to decide where Russia fits in the competition for our attention. And I think this, that the choice I will tell you is not between a benign, weak, Russia on the one hand, non-Democratic Russia and a strong Democratic Russia on the other hand, that is not the choice. The choice is between two strong Russias. One a strong non-democratic Russia, ruled by some demagogue who steps in to avoid....that the west lets get created. And you have a strong Russia like that, or on the other hand, the choice is of a strong democratic Russia that will rule the civilized world and community of nations. And in my personal view, that if we tell the story properly to the American public, and you give them a choice, the American people will choose the right course, they always do. Thank you very much. (Applause)

Chairman Donald B. Marron: Bob, thank you very much. Those are very inspiring comments. Our next speaker is Gerald Corrigan. As President of the New York Federal Reserve and Vice Chairman of the Federal Reserve System's Open Market Committee, Gerry occupies one of the

most influential posts in the U.S. financial system. He is an economist and has long been recognized as the Fed's number one trouble shooter. We saw him operate back when the markets went into the 1987 tailspin; Gerry was the Fed's point man in dealing effectively with that crisis. All of us thank you very much for that Gerry. He has acquired enormous respect and influence in the world financial markets. He is the Chairman of the Basel Committee on banking supervision. That has become the key mechanism for devising international banking standards and negotiating inter-country regulation. He has traveled to Russia numerous times last year to help coordinate the Russian/American Banker's Forum. An organization that he was influential in establishing. And where he is currently co-chairman. And this organization, and Gerry personally has been giving Russia crucial help in the development of its banking, and financial system infrastructures, two things that are needed for Bob Strauss' vision to come true. Gerry is also confident of Russian President Boris Yeltsin, a tremendous American, let me welcome, Gerry Corrigan. (Applause)

E. Gerald Corrigan

President, New York Federal Reserve

Vice Chairman, Federal Reserve System's Open Market Committee

Thank you Don very much. And good evening ladies and gentlemen. I have this question for you, Mr. Strauss, why is it that you get introduced as the honorable and I don't. Something gets lost in the translation there I suspect. But it is a great pleasure to be here this evening, ladies and

gentlemen. I think you will hear a little bit of the same of what Bob said earlier with perhaps a slightly different emphasis but I can't help but let this occasion rise without getting into a little of the real spirit of Russia. I was sitting here, minding my own business and out of the clear blue Bishop Victor walks up to me. Now the Bishop and my good colleague, had a surreptitious meeting in Russia a year or so ago if I remember correctly. And there is always a great danger, and I am sure this is true in the Russian Orthodox Church, as it is in other churches about telling stories out of school or out of confession, about your dealings with the hierarchy of any church, but perhaps especially the Russian Orthodox Church. But when Bishop Victor and I had our first meeting, at this marvelous establishment in the suburbs of Moscow where they manufacture these incredibly beautiful icons and you can't imagine how beautiful these things are. In the middle of our visit I had the feeling that Bishop Victor had something on his mind. And indeed he called me off to the side and I could see in his eyes that he wanted to say something to me and I couldn't imagine what a Bishop would want to say to me. But I said to the Bishop, can I help you. And he looked at me, in this very serious and penetrating way just as he is looking at me now, and he said, yes, Mr. Corrigan I need your help. And I said, well how can I help you. And he said to me, I need you to tell me how to establish my own bank in Russia. (Laughter) And I think in its own way, that tells a very, very important story that is relevant to what I have to say in a broader context tonight.

But let me begin by saying if I may that seeking to condense into a brief address the complexity and the dynamics of one of the most historic events of the 20th century and beyond is of course

impossible. What I will try to do, therefore, is to share with you a number of broad-brushed insights and impressions that I have accumulated in the roughly 20 months since President Yeltsin first visited the Federal Reserve Bank of New York in June of 1991. And I will also share with you some thoughts as to what I believe must be done to further solidify the prospects for reform in Russia over the period ahead.

My starting point is to stress as forcefully as I can how complex this situation really is. And how misleading it can be to judge it by using conventional western standards. In the economic sphere for example, there is virtually no room for the transplanting to Russia of ideas, concepts and experiences, with economic reform efforts in other countries, except at the very highest level of generality. In human terms, we are all mindful, if not awed, by the legendary patience of the Russian people. But few of us can begin to grasp the daily hardships that are faced, not by a small minority of the population, but by a sizeable fraction of the citizenry. We also tend to forget that the economic and political doctrines and values which we hold so dearly are doctrines and values which have been forged over centuries. In contrast our friends in Russia have embarked on a course of immediate and simultaneous economic and political reform that considering its starting point is unprecedented in the recorded history of mankind.

Now the obstacles to be overcome in Russia are almost incomprehensible. For one thing, there are no obvious points of national reference in either political or economic terms. Nor, is there any institutional memory that can be brought to bear in charting the future. There are complex

economic and financial interdependencies within and among the Republics. Interdependencies I might add, that in many ways are quite artificial and can be traced in part to the demonist genius of Stalin's efforts to achieve political control through elements of forced economic interdependencies. There are vast monopolies, quasi monopolies, and bureaucracies. Typically, and I want to stress this, having no ideological content whatsoever, but, each of with, with a large vested interest in the past.

Finally, there are very complex issues growing out of the ethnic, religious, and cultural differences within a heterogenous population spread out over a truly massive land area. We tend to forget for example, that Russia spans 11 time zones. Now our ability to put the Russian situation in perspective is also hampered by a number of popular myths about Russia and Russians. For example, it is sometimes suggested that Russians are not entrepreneurial. That view in my judgment is simply bunk. In many ways, I would submit to you that the Russians wrote the book and that is how they survived 75 years of tyranny and repression.

As another example, it is sometimes suggested that the Russian people don't relate to the west or even worse, don't trust the west, especially the United States. Based on my experience, and for most Russians that too is bunk. Indeed, from what I have seen, the Russian people have an almost idealized admiration for the United States which I sense grows in part out of their recognition that we as a large country have managed to blend ethnic, cultural and religious differences into a source of national strength and pride.

With that perspective in mind, let me now turn to the economic reform process, the process that began in earnest only a little more than a year ago. Now we know and the Russians know that economic adjustment and reform must start with the standard general menu of monetary and fiscal discipline; price liberalization and liberalization of trade and currency systems. We also know, and again, the Russians know, that even the best of macroeconomic policies are necessary but not sufficient conditions for success. That is, sufficiency comes only when macro-policies are effectively blended with appropriate micro or structural policies. Particularly in certain strategic industries or sectors of the economy.

Now in the Russian case, the gap between necessity and sufficiency is very wide indeed. For example, the continued presence of monopolies and poor distribution systems makes the supply side effects of price liberalization slow and uncertain at best. Similarly, the initial and inevitable instability associated with the reform process tend to generate a flourishing underground economy. A phenomena of course we have seen in many countries. While that underground economy helps to provide more goods, more jobs, and more competition, it also cuts significantly into tax collections. Thereby, aggravating the budgetary deficit. It also produces at least in the short term, visible and potentially very troublesome differences in relative incomes and standards of living.

Now despite these and many other obstacles, I believe it is fair to say that the initial phase of the economic reform process went better than most expected. Unfortunately, it is also fair to say that

beginning in the summer of 1992 conditions began to slip and more recently that slippage has taken on dangerous proportions as inflation has escalated sharply, approaching or reaching the proportions of a classical and highly destructive hyperinflation. This associated breakdown in financial discipline is being aggravated by a renewed buildup in inter-enterprise, and inter-republic debt and payment backlogs, which are both a cause and an effect of the inflation problem.

While the dynamics of the inflation process in Russia are very complex, it is hard to escape the fact that the severity of the current problem is not fundamentally rooted in the monetary sphere. This is particularly the case, since at least till now; budgetary deficits must be financed by printing money. It is also very hard to escape the fact that checking and ultimately reversing the current inflationary problem will be extraordinarily difficult in political terms, especially with the April referendum waiting in the wings.

Now while it would be wrong, ladies and gentlemen, and as Bob has said, to understate the current problems in Russia, it would be even more erroneous to conclude that the situation is void of continuing in important signs of progress. Let me also cite a number of those distinctly positive signs, briefly.

First and foremost, there is an ample supply of progressive and energetic leaders in the Russian government who are strongly committed to the reform process; and who have a clear sense of the

programs and policies that are necessary for success. Indeed, I would go one step further and say that there are also many, many industrial leaders who may differ with the government on matters of priority and timing, but who nevertheless are committed to the goals of both economic and political reform. And I say that notwithstanding occasional press reports in the west, to the effect that these differences about tactics and timing are deeply rooted in the ideology of the past. They are not.

Second, as Bob has said, at the microeconomic level, I strongly suspect that there is much, much more occurring in the Russian economy than is widely recognized and certainly much more than is captured in the official statistics.

Third, the Russian privatization program has had a greater measure of success in a shorter period of time than I frankly would have thought possible.

Fourth, important initial steps have been made in the codification of laws and regulations in a wide range of commercial and financial endeavors.

Fifth, slowly but surely, and with a measure of success, foreign investors are establishing operations in Russia often on a joint venture basis.

Sixth, and of special importance, this winter, unlike last winter, will pass without fear of food

shortages with all of the human and political problems associated with such fears. Much less, such a reality.

Now looked at in this light, the obvious question before us is whether the evident problems can be contained and controlled as further progress is made in strengthening and broadening the areas in which true progress is being achieved. In seeking to shed some light on that question, let me begin with a central observation that may strike all of you as a clear case of a fool rushing in where a brave man dare not go.

Namely, I believe the chances are good, very good, that the process of political and economic reform has passed the point of no return. In saying that, let me hasten to add that the process will not be a straight line. Mistakes and misjudgments will occur. Personalities will change. But let me especially and forcefully suggest that the risks of reversal, however great or small they may be, carry with them such dire consequences for the world. (Audio ends and begins again, no overlap)...whatsoever but to shape our attitudes and our policies with a view towards suppressing those risks to the point where they are negligible or nonexistent. A condition which is certainly not the case today.

There are many elements needed to ensure success. One, that strikes me as particularly important is the continued courage and leadership of President Yeltsin. Now perhaps we have all come to expect too much of political leaders, perhaps the world has become so complex, that, that lofty

vision of a man for all seasons is now nothing but a dream. But, I will say to you if there is a man for all seasons in the contemporary Russian setting, that man is Boris Yeltsin.

Now looking to the future, it is clear that the period immediately ahead is of vital importance. The Russians for their part must redouble their efforts in an extremely difficult economic and political setting. Since I see nothing to be gained, and indeed much to be lost, in engaging in a lengthy public discourse into what I as an outsider thinks the details of Russian policy should be, I have no intention of broaching that subject in specifics tonight. I will, however, make the general observation that quickly achieving a measure of monetary and financial discipline strikes me as a must. I will also make the general observation that aggressive efforts in key sectors such as banking, agriculture, energy, and defense conversion must command a high priority.

And finally, the underpinnings of a healthy economy including such items as the tax collection system, the collection of relevant, reliable, economic statistics, and the workings of the payment system, must be made to work better as soon as possible.

Now closer to home, attitudes and policies in the west and in the United States in particular are also crucial. Before turning briefly to those subjects a more general observation should be made, however, namely, when Russian leaders, but especially when western leaders, stress the virtues of a market-economy and even the virtues of democracy, many Russian citizens do not have a clear vision of what those terms of art really mean. Absent that vision, confidence about the

future, is of course elusive. And for many Russian citizens, grasping that vision of the future is understandably clouded by the fact that they are in fact worse off today than they were a year or two or perhaps ten or more years ago.

That vision is also clouded by the very obvious disparities in the well-being of the relative few who are doing very well indeed and the many who are not. For example, while I neither speak or understand Russian, I have the deep suspicion that the words merchant and speculator are often used interchangeably and that the connotation of both is not particularly becoming.

Now against that background I believe there are several key points of reference that should help guide western attitudes and policy formulation toward Russia and the other Republics of the Commonwealth of independent states. Those points of reference include the following:

First, we should and I will say we must, embrace the philosophy that we want to help them do what they think is right for their country, rather than force feeding detailed approaches and techniques that may have been successful here, or in other settings but simply aren't relevant in Russia.

Second, while we admire the patience of the Russians, we too must be patient and recognize that they are seeking to achieve in a very short time what it took us centuries to achieve. I might also add that even after centuries it is quite evident that we don't exactly have it perfected.

Third, we must not judge either failures or successes by western standards or at least by western standards alone.

Fourth, we need to more fully recognize that thinking small may be much more relevant than thinking big. To put it different, unless there is true progress at the micro level of the economy, even the most brilliantly conceived and executed macro policies will bear only limited fruit. In this regard, the underpinnings of the economic and financial system of which I spoke earlier, or the plumbing as I like to call it, warrant special attention.

And fifth, and finally, while a vision of the future is clearly needed, that vision will come only slowly and it will come only if there are some quick victories and visible success stories here and now.

This of course is neither the time nor the place to attempt to spell out in detail what these principles might imply in terms of concrete policy initiatives. I will say, however, that it is my fervent hope that the Clinton administration working with its partners in the G7 governments will move swiftly and decisively to sharpen policies and programs aimed at facilitating the economic and political reform process in Russia and elsewhere in the CIS. And in this connection I do believe that a great deal can be done even with budget constraints and pressing agendas of domestic needs.

I will also say in the category of quick victories that it is unambiguously in the interests of both sides to complete a debt restructuring agreement quickly that explicatively recognizes that multi-year debt service relief but not, not debt forgiveness, is needed and is in the interest of the debtor and the creditors alike.

And finally, based on my admittedly imperfect impressions I believe that a great deal of effort is needed on both sides in better shaping and coordinating technical assistance programs from the west. And based on my own experience with the work of the Russian/American Bankers Forum, I believe that such programs across the board will have a greater potential for success to the extent that they enlist on a large scale volunteers from the private sector who know how to get things done. It is one thing to write and to talk about what needs to be done. But it is quite another thing to help get it done in the trenches and that is the only place where it will get done.

Therefore, it is my conviction that hands-on private sector practitioners can play a vital and unique role in assisting the process of economic reform in Russia. And I intend to continue to do all I can to facilitate that effort.

Now in closing, ladies and gentlemen, let me offer one last thought. I said before that I believe the chances for ultimate success in this venture for mankind, that is what it is, a venture for mankind, I believe the chances for success are good, very good. But to emphasize they are far from certain. I also said that many Russians do not clearly comprehend or have a vision of a

market-economy or a democracy, but the Russian people do understand, embrace, and cherish, a vision of freedom. Every one of us has a very large stake in seeing to it that each of us does all we can to ensure that that vision of freedom becomes a lasting reality for ultimately their freedom is our freedom. Thank you very much. (Applause)

QUESTION AND ANSWER SESSION

CHAIRMAN, DONALD B. MARRON: Gerry thank you very much for those incisive comments. As is our custom, we will now turn the program to questions. We have two questioners this evening, Rand Araskog, the Chairman of ITT and Dennis Weatherstone, the Chairman of JP Morgan. Also as is our custom, we are going to do it in alphabetical order. Rand, you want to take the first question and then on to Dennis.

RAND ARASKOG: Well I will start it off with Ambassador Strauss. Don you have already described him as a consummate Washington insider, I think he has also become a consummate Muscovite insider. So I would like to be a little provocative and ask if he would comment since he has been involved in both, on the performance of the transition and the first few weeks of presidency of Mr. Yeltsin and Mr. Gorbachev and Mr. Bush and Mr. Clinton. (Laughter)

(INAUDIBLE COMMENT)

AMBASSADOR ROBERT S. STRAUSS: I am glad the damn microphone wasn't on; I need a second to think. (Laughter) I think that is an impossible task. There is no basis for that kind of comparison. I will say this, with respect to transitions in general, I think that to have a good term in office and a good term in government, you need a good transition. And I think that with respect to President Clinton, although he has had a wobbly ten days or so, I think he had a good transition. And I think he will have a good term in office. I am more familiar with his economic team, but as most of you are here, since we are before the Economic Club of New York, I would say to you, that in my judgment this is the strongest economic team I have seen in any administration since I have been watching Washington and that goes back a long time, I will leave it there. With respect to President Yeltsin I had amazing experiences, some of my good Russian friends, Anatoly Dobrynin here, Ambassador Vorontsov and others know, as I said, I landed in Russia and I found myself with a front row seat on the greatest revolution in the history of mankind, and after six months or so I found myself moved from the front seat to behind the curtain. And it is the darndest experience in the world. And I have been amazed as I have watched the Yeltsin government take shape. The quality of the people that he put in there when he was picking from a group of people who had had exceedingly limited experience in many of the subjects that they were dealing with. So I would say they are both positive.

DENNIS WEATHERSTONE: Rand had a four people question; I have a four part question for Gerry Corrigan. And I will remind him if necessary what they are. With Russia, and the other Republics, basically starting from scratch in building a financial system infrastructure what

advice would you offer Gerry on the role and structure of central banks? What are the key building blocks to a discipline growth supporting financial system? Do any of the developed or developing countries strike you as a good working model? And is there room for derivative instruments in this world? (Laughter)

GERALD CORRIGAN: Well I will tell you Dennis, that last one is a God damned gimme pot if ever I saw one. (Laughter) I think it is probably fair to say that of all the things they need over there right now, derivative instruments are not high on my list. (Laughter) But, the first three parts of your question, I think are really very important. The first part, if I understood you, relates to the role and functioning of the central bank. And of course in the context of the CIS this is an incredibly difficult question in its own right, because it inevitably brings into play this whole related matter of will there be a ruble zone or will there be 10 or 12 or 15 separate currencies, and all the rest of it. I could go on much more than anybody wants to listen to on that subject. I will simply make two or three quick points. First of all, I think that no matter what is arrived at kind of in the political arena, the central banks or bank, within the CIS are going to have to work closely together and cooperate. My own preference and I can explain it if anybody wants to take the time to listen is that I think it would be a mistake in the short run to go the separate currency route. All you have to do is look at this little microcosmic example we have right now of the Czechs and Slovaks and see what that entails. And you know, again a separate currency of course, currencies, presupposes by definition that some will be weak and some will be strong. Now you tell me, what political leader in what newly emerging sovereign state is

going to be happy with the weak currency. And you tell me what is that political leader going to do when faced with that weak currency. Well, it is obvious, the first thing he or she is going to do is say, well we are going to have to put in some capital controls and Dennis you know and I know that is not going to work. And the next thing they are going to say is well, we are going to have to get protectionists, we are going to have to keep those goods out, and you know what that is going to do, especially in the context of that contrived economic interdependency I spoke of before; and of course the third thing is nationalism runs amuck. So I am, I think at this point nearly a minority of one. But I got to tell you that strikes me as a very, very slippery slope indeed. But, however that all sorts itself out, first and foremost the central banks are going to have to cooperate and indeed, there are some parallels as you know that can be drawn from the United States in the teens and the twenties about how that can work, even in the context in which there may be different interest rates in different parts of the country. The second thing that goes without saying is that the central bank or banks are going to have to have a legitimate element of political independence. Now again, as I said in my prepared remarks that we can't try and force feed a cookbook of western definitions of what that means. That is not going to work. But you cannot have...I have a rather vested interest in this of course, you cannot have a central bank that is under the thumb of a Parliament or a President or anybody else. So those are the two most important things to me, is cooperation and independence. Now within that framework, you know my trilogy in terms of the functions, and we can get to that later. Your second question about building blocks for the financial system, again, this is where my point about the trenches really matters. You know I feel very strongly that the basic elements of the infrastructure here are kind

of the blood and guts stuff. A payment system that works. An emerging government securities market, an emerging system of genuine deposit taking and services for individuals and small businesses and that is where you have to work. All this fancy stuff, including derivatives, I mean, forget it. I mean if you don't get that stuff working right down in the trenches, forget it. And that is what we have been trying to do. And we have been doing it with a measure of success. You know last May 25th, a number of my colleagues sitting right here, and I started a project over there and everybody thought we were nuts, so did I. But I would never tell them that. To try and get a small semblance of a government securities market working, that was on May 25th starting from zero. There is a fighting chance that by the end of this month, from that starting point, we with our Russian colleagues will see the first true western style auction of ruble denominated treasury bills in book entry form, by the end of this month. Now, you know, the importance of that, you know, not just in terms of a wild eyed dream, but also in terms of taking the burden off the central bank and having to finance the budget deficit is incalculable. You know in terms of developing capital markets. Everybody wants a stock market. Well you know that is fine, but you have to get some stuff working. So yes, there are those building blocks and they start way down in the trenches and that is where all of the people who we have enlisted from the Bank of New York, from the Morgan Guarantee, and from other institutions throughout this room have really paid off. The private sector practitioners. The ladies and the gentlemen who know how to get stuff done. That is what we need. As far as the third part of your question on models. There is no model. (Applause)

RAND ARASKOG: Gerry, Dennis and I didn't coordinate this at all. We are going to shift back and forth I think between the speakers, so I am going to ask you another question and it has to do with the market economy and if you can call it the euphoria that existed at the very beginning of the Yeltsin administration. Your first visits there and your recent visits there, and could you give us a snapshot if you will of your first impressions and your now impressions as to whether the euphoria has really developed into real progress or whether that euphoria was not well founded?

E. GERALD CORRIGAN: Well first of all, Rand, speaking for myself, I never had a sense of euphoria. The most powerful instinct I had when I first started to try and be a little bit helpful there, I got to tell you was fear. Outright fear. You know I have done a lot of stuff as you know. In terms of degree of difficulty and all the rest of it, this whole thing is off the charts. So I am a little hard pressed to associate myself with euphoria. I think the best way to try and put it to you is in two or three quick points. First of all, I have had the good fortune there to meet a lot of people, big people, small people, in between people, industrial people, military people, and I have to say that the most lasting impression I have is that sense of reaching that desire for something that is better. And as I said in my prepared remarks, the inherent difficulty of trying to figure out what that is, but I see absolutely no diminution whatsoever in that reaching. And that makes me feel good, it really does. On a more pragmatic level I am impressed with a couple of things. I just mentioned to Dennis, I could cite other examples, but if you really thought in my heart of hearts, and as I said I would have never said this to my distinguished colleagues, that we could have pulled off some of the stuff that we have, you know, I would have said no. But God

dammit we did. And the reason why we did it was because once those seeds were planted, the Russians themselves were the ones that made them grow. It wasn't us, it was them. And third, as I said, at the micro, micro sector level of the economy and Bob said this too, there is a lot of stuff going on, there really is. And my overriding concern other than this political stuff that I am not smart enough to understand, is this breakdown in what I call financial discipline. And we have to get at that. They have to get at it too. They are the only ones that can do it. But the problems, as I said, are incredible, but there is a lot of good stuff going on, and I am impressed to this day about, that drive, that searching, that reaching, and as long as we can keep that flame, and it is not a spark it is a flame, as long as we can keep that flame alive, we can make it work. That is the best I can do.

DENNIS WEATHERSTONE: Mr. Ambassador, Russia has demonstrated world class skills in defense and aerospace technologies, are there ways for that expertise to be harnessed for peaceful economic development purposes? What types of controls if any, are needed to ensure that it isn't sold to the highest bidder who might use it for military purposes?

AMBASSADOR ROBERT STRAUSS: Well I don't think we can...I don't think there is any question that defense conversion that we talk about so glibly in this country, and I thought was going to be more reasonably doable, that was a pipe dream. Defense conversion is far tougher than I ever thought it could be. It can be done but it isn't easy and it is going to take a long time and it is going to take a lot of money. In terms of what the Russians may do with that defense,

with those defense institutions, institutions who build weapons of mass destruction if you will, some of them are either going to continue to operate and continue in the weapons business just as we are in this country, and I might say that I don't think the west has shown, if we wanted to, tell our Russian friends they ought to ship less, and do less, we haven't given them a very good example in this country. We tell them, don't do as we do, do as we say. And very frankly, you talk about the patience of the Russians, I suspect they are appreciative for what we have done, but God almighty if we had done one-tenth as much as we have talked, they would be in pretty good shape today. Most of what we have done is preached. We have delivered little and preached a lot. And that area is one of those areas now. To elaborate on that just a little bit, in terms of the weapons of mass destruction that are over there, which is of interest to this audience I think, we have done a very good job in working with our Russian friends in the other Republics, getting our hands on the strategic weapons. Really, I would say it is a first rate job and we are on schedule or ahead of schedule in that, on tactical weapons. But when you get to strategic, we are having as you know a far more difficult time, and it is going to take a long time. It is going to take a lot of persuasion and if everything went perfectly, I don't know what it would cost, but I used to try to get a fix on it, and you are talking about a \$10 to \$12, \$15 billion project over 10, 12, 14, 15 years. If we all cooperated and it all worked well, and that isn't taking place right now. With respect to the scientific community over there itself, that rather elite, I guess that is the proper word for it, a good word for it, elite educational system has produced marvelous human resources over there to work in this whole area, far ahead of what you find in the west. You go to Germany, you go to France, England, and you come to this country, that educational system has

produced in the scientific and technological area, people far more, a far greater inventory of good minds and well trained minds than we have in this country, fortunately. So there is a lot work with if we ever get it harnessed. There was one more point I wanted to make, it had to do with, well I think he covered it well enough.

CHAIRMAN DONALD MARRON: We have time for one more question from each of the questioners to finish before 10. Rand.

RAND ARASKOG: Bob, this really could go to either of you but I will put it to you. There is, as you well know, Americans can visit the Soviet Union, former Soviet Union, the Russian Republic, Moscow, and live there on dollars, without ever having to worry much about the ruble. There is of course reported information on a tremendous outflow of dollars from the Russian Republic to safe haven banks in Canada and Switzerland and elsewhere in the world. And the obvious concern about this is the lack of confidence of people in the Russian Republic in their system, and the transport of those dollars out, rather than reinvestment there. Would you comment on this, on what you think should be done and can be done?

AMBASSADOR ROBERT STRAUSS: To begin with I don't think there is any question that there is a substantial flow of money to safe havens. That is true of many countries in the world. So it certainly should be true of a country with a lack of stability and a lack of rules and a lack of law enforcement that you see as the Russian Federation puts his act together. But I think it is

grossly exaggerated. I think my personal view is based on my personal experiences. I had any number of American businessmen tell me the same story. And the first couple of times I assumed it was like the flight of money from South America to Florida or the flight of money from New York to Switzerland or wherever. But when businessmen tell me that...the first businessman told me, he said, you know the damndest thing happened; I owe the XYZ Enterprise over here, \$25 million. As a matter of fact he said \$24 million point some dollars, I still remember the figure and they won't let me pay them. And I said, well where do they want the money shipped, to Switzerland or where thinking that it was going to a safe haven? And the man's answer was, the fella's answer was, no, Bob, it is for something entirely different. The reason they don't want that money to come back here is that they are afraid that it would be devoured up into the system. And I am sure there are tax aspects to it. But he said, what has happened is that we receive communication from them, and they say, we need \$2 billion worth of this for inventory and we need \$4 million worth of that kind of equipment, and we need \$2 million worth of food for our enterprise, for our people, and what they are really doing is running a barter bank. And that money is being used to benefit people in Russia, and particularly to benefit that specific enterprise, but the money isn't over there being hidden from the authorities for the normal purpose that we see money hidden, it is really kept away so that they are able to purchase goods and merchandise in the west, using dollars, and getting shipped back over and it keeps the enterprise running. So I don't think it is a major problem. It as serious a problem as it is in all countries.

DENNIS WEATHERSTONE: This is a capital question as well, for Gerry Corrigan. We talk about a global capital shortage. I don't know whether you believe that or not. But in view of what happened in Latin America, do you think there are any lessons from the Latin American experience that are applicable for the authorities in Russia, a U.S. government policy, participation of banking institutions in the development process of Russia and the other Republics?

GERALD CORRIGAN: Again Dennis as I said in my prepared remarks I don't think there is much room for transplants except at a very general level. But at that general level I think there are some very, very concrete examples that can be drawn from our experience, for example, in Latin America. For example, as you know very well, the first premise, the first principle that we all embraced in the Latin American experience was case by case. And if ever there was an environment in which case by case should fit, it is here. So that is clear. Second, again, as I touched on very briefly in my remarks, that we have to have a sensible approach and Bob touched on this too, to this whole question of debt restructuring. And you know, right now, I have to say that I am less than comfortable if I can put it that way, with what is I think on the table in that area because for all intents and purposes that kind of looks like, smells like, walks like, talks like a single year in 1993 restructuring. And I don't think that is good enough. I just don't think it is good enough. And that, as you know very well, is not what we did in Latin America. So that is another example. I think that again, at a very general level you know the Latinos that succeeded and most of them now are doing reasonably well, did ultimately succeed

in part because they got that blend of broad macro and micro policies right. Now, you know the numbers as well as I do, many of those countries in the early 80's had budget deficits that were 12, 15, 16, 18% of GDP and you might reflect upon this ladies and gentlemen, many of them have smaller budgetary deficits relative to GDP, right now today, even does the United States of America. Think about that. But also, privatization, debt equity swaps, debt for debt swaps. So again, as long as you don't get seduced into thinking that you can force feed the details and you look at some of these broad principles that worked elsewhere, and above all, keep in mind that case by case, yes, I think there are things that are relevant, but, and I really want to emphasize this, again, you know for better or for worse I think have seen, I don't know if I can say I have seen it all, but I have see most of it, and this situation really is much more complex; even without the political dimension than anything that we have ever tried to deal with in Latin America. And that I think is where the west broadly defined has to get its act together and recognize what it is we are dealing with. It is not Mexico, it is not Chili, it is not Bolivia... it is none of those things. So yes, there is some room. But you can't transplant in that literal sense. Thank you. (Applause)

CHAIRMAN DONALD B. MARRON: Thank you Rand Araskog and Dennis Weatherstone for those questions. Ladies and gentlemen, this is the end of our program. Thank you to Bob Strauss and Gerry Corrigan for a very stimulating evening. Thank you very much.