

## **Erkki Liikanen: Issues related to the Russian, Chinese and other emerging market economies**

Opening remarks by Mr Erkki Liikanen, Governor of the Bank of Finland, at the BOFIT (Bank of Finland Institute for Economies in Transition) Anniversary Conference, Helsinki, 22 November 2016.

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Your Excellencies, ladies and gentlemen

It is my pleasure to welcome you all to the 25th Anniversary Conference of the Bank of Finland Institute for Economies in Transition, or as it is more commonly known, BOFIT.

This Conference brings together central banking and academic research communities to discuss issues related to the Russian, Chinese and other emerging market economies.

Where were we 25 years ago when this all started? The world, and especially Europe, was experiencing a massive political and economic upheaval as the Soviet Union broke up and many countries in the socialist bloc were embarking upon a journey towards liberal market economies.

Finland was greatly affected by all these events. Finland's own economic and financial crisis was deepened by the collapse in demand from the Soviet Union – and later from Russia.

As this collapse coincided with the end of our bilateral trading arrangements, some could have linked the two events. But in reality the Soviet Union and later Russia had very limited purchasing power in 1991 and 1992. No trading agreement between our countries could have maintained the trade on the earlier levels.

On this particular issue – Finnish-Soviet trade – a book will be published next year, written by Professor Pekka Sutela, a former head of BOFIT and Ms Inkeri Hirvensalo. Both writers are here with us today.

The changes brought by the end of this special trading arrangement had a big impact also on the Bank of Finland. An entire department had handled payments related to Finnish-Soviet trade.

But already in the 1980s there were economists at the Bank who were following the Soviet economy and trying to analyse the reforms or changes introduced in many areas. Economists involved in this work formed the basis of BOFIT.

When bilateral trade was ending, the Bank's board decided to maintain its analytical activities. A new unit was tasked to follow and analyse the formerly socialist countries in Central and Eastern Europe. Russia was the largest and economically most important for Finland. But during that period there was also a great need for information and analysis on e.g. the Baltic States. The Bank of Finland responded to this demand.

Over the years the geographical focus of BOFIT has changed, and – for example – analysis of the Baltic States was discontinued after they joined the EU.

On the other hand, BOFIT already recruited its first China economist in the late 1990s. It was clear then that China was becoming a very important player in the global economy, and so also for Finland.

Analysis and research on the Russian economy has continued uninterrupted for more than 25 years at the Bank of Finland.

BOFIT has always been ready to publish its reports and analyses, and this has helped build its

reputation both within Finland and abroad.

At the same time, analysis of these emerging market economies is also one of the areas of specialization that the Bank of Finland offers other members of the European System of Central Banks. I am happy to see representatives from many other members of the ESCB here today.

As to the Russian economy today, it has gone through a period of major difficulties. Last year, GDP declined by almost four per cent, and this year it continues to decline, by almost one per cent. Forecasts for recovery are relatively subdued. Russian GDP is not expected to reach the level of 2014 until 2019. While the macroeconomic situation has been difficult, Russia has been able to push through reforms. The decision to float the rouble and to move towards fully fledged inflation targeting has been instrumental in helping the Russian economy adjust to the period of lower oil prices.

In addition, the Bank of Russia is tackling consolidation of the Russian banking sector with renewed vigour. The number of banks has been reduced by more than one third during the last two years. This consolidation will make the banking sector more stable.

Despite these policy reforms, the Russian economy still faces significant challenges. Structural reforms are needed in many areas to raise economic potential. To enhance productivity, greater competition is needed, both at home and from abroad. Productivity improvements are vital, as the working-age population is declining.

In China, GDP growth has been very rapid for the past three decades. It is now decelerating towards six per cent. This was to be expected after such vigorous growth. In China, too, the working-age population is declining.

Despite this deceleration in growth, the Chinese experience shows that it is possible to lift literally hundreds of millions of people from poverty through market-oriented reforms.

But, in China, too, a lot can still be done to further raise productivity. For example, further reform of many large state-owned companies would free up resources for the rapidly growing private enterprises. And given China's sheer size and its growing links to the rest of the world, any challenge to China's financial stability is an important issue outside China as well.

In our programme, we will discuss many issues related to emerging market economies. I am very glad to note that we will enjoy keynote presentations from two very well-known economists in the field. In order of appearance on the programme, we have **Professor Gérard Roland** from the University of California, Berkeley, and **Professor Justin Yifu Lin** from Peking University. They have both made tremendous contributions to our understanding of the complex links between various institutions and economic growth.

Economic transition – still under way in many parts of the world – provides us with many fundamental insights into economic theory and policy.

A big question today – among others – is what kind of institutions and policies offer the best chance for inclusive economic growth.

Our keynote speakers will address these questions. They represent top quality academic research, and some also have a wealth of experience in policy institutions.

The interaction between theory and practice is also the cornerstone of the research papers presented in the session devoted to banking and financial systems in emerging market economies.

It is always interesting to note the many similarities countries share, e.g. in their banking systems, but more careful analysis always brings out many differences, too. Both similarities

and differences are an important area of analysis before any policy recommendation.

At the Conference we also have a high-level panel devoted to more practical issues of central banking. We will be able to hear how different central banks are coping with the current global economic situation, where capital flows are large and often volatile.

This brings its own challenges even to large emerging market economies. Large capital flows can hamper the functioning of monetary policy, and financial stability may also sometimes be at risk, especially if external indebtedness is high.

Again, I welcome you all to the 25 Anniversary Conference of BOFIT. I hope that today's programme will be intellectually inspiring and stimulating for us all.

Once more, a warm welcome!