FINANCIAL INSTITUTIONS AND RULES FOR DEVELOPING COUNTRIES

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"Do what I tell you, not what I do" well known phrase could be very well applied to central bankers from advanced countries lecturing their less developed brethren; in fact one should turnit around, i.e. let's do what they are doing – "extraordinary measures" – and what they used to do – strong arm intervention in foreign exchange and financial markets - not what we are told to do.

1. Each country and most emphatically EMEs have to device its financial system according to its own circumstances and traditions. A single model to be applied to each and every country in the world might be of the interest for internationally active banks to generate a "level-playing-field" for them. Whatever has been developed in this direction and the teachings that may be derived from its application are not to be rejectedout-of-hand but only if adequate for each country's needs. For instance, rather late, after more than a quarter century of campaigning for financial de-regulation, even in AEs – in spite of opposition from the sector – it is somehow accepted that it was a mistake and that it was the breeding ground for massive crises more serious and persistent than the ones experienced in other contexts; something that quite a few EMEs learned the hard way decades ago only to see ourselves criticized from centers of learning and IFIs for being too interventionist.

2. The structure of the financial sector in EMEs has to be designed taking into account the role of external financial flows. Instability might have been at some points a consequence of wrong public sector policies but in the eras of financial globalization the main source of instability has been located in the instability of international finance.
   A permanent structure for monetary and financial stability cannot but include institutions and rules for management of external financial inflows and outflows, so-called capital controls. And central banks cannot be designed without having them playing an active role in this area. In fact, without integral rules for managing foreign financial flows there will be no monetary policy but the one run by those external movements, let alone financial stability as an outcome of the impact on the financial sector of external instability.
   In that sense, EMEs have had to device something that some of these countries had beenimplementingin the last more than 30 years of crises;so more than being attentive to what is debated in the AEs we have to learn from each other. But confronted with criticism from academics and institutions it should be recollected that for a prolonged period an only up to some 30-40 years ago, AEs also had capital controls, either permanent or transitory.

3. Stability, however, does not generate full employment and growth automatically; that is a leftover of a doctrine that a private initiative economy left to itself,withina

stable structure set up by the authorities in the fiscal, monetary and financial sphere, will achieve a stable equilibrium associated with full employment and growth, even with an acceptable income distribution. But that doctrine has been repeatedly found false.

And for us, EMEs the main concern should be how to achieve growth as stable and equitable as possible. Therefore, our financial sector has to be structured so as to not only put it at the service of the "real economy", if such a thing exists separate from finance, but definitely to promote development, a restructuring of our productive activities and the way in which wealth is distributed in a more equitable way.

4. The experience of our central banks in the last quarter of a century have beenone of pressure to transform them into "narrow central banks" with a single mandate about preserving monetary stability and perform the role of ensuring fiscal discipline by denying financing totheir governments. Commercial banks, at the same time, out of their own choice but also under the strictures of regulations pushed from international institutions have shown little propensity to make credit available for productive investment.

   Attempts, actively promoted from the IFIs to make us adopt an Anglo-Saxon like market-based rather the traditional bank based financial system so that those markets would provide long-term finance has been mainly a failure. And, when concentrated around our pension systems have not shown to fully provide what a pension system is supposed to provide. In both cases, that of the CBs and that of the pension system there has been a distorted use of institutions, i.e., why should central banks become the guarantors of fiscal discipline and why should the pension system revolve around developing a domestic capital market in both cases disregarding their specific roles?

   Commercial banks devote themselves to personal loans, at most, mortgages for housing, arguing that they cannot take upon their shoulders the necessary maturity transformations to be able to finance productive investment. And CBs applying Basel-like oriented regulations have mostly consecrated such a business strategy even if in many cases leading to serious processes of over-indebtedness by the household sector far from good for financial stability let alone for growth.

5. National Development Banks used to play - and still do in some countries – a crucial role in financing productive investment using various sources of funding. As John Williamson in a talk delivered some years ago, in which a blanket defence of "Washington Consensus" policies was essayed, explicitly acknowledged that the weak contribution of the banking sector had not sufficiently been taken into account and that countries should not hold any guilty feelings at rebuilding their State Development Banks, mostly closed down in the last couple of decades.

6. Both our own experience plus that of many central banks in the AEs shows that only a few decades ago there is also a role for central banks in promoting long-

term lending for productive purposes. Even right now under the paralysis of credit in the countries undergoing the North-Atlantic financial crisis, for instance, the Bank of England has introduced the “Funding for Lending” scheme. But in decades previous to the rule of neoliberal thinking central banks like those of England and France, did play an important role in directing credit to priority sectors in coordination with the rest of State agencies. And in most developing countries in the second postwar period CBs did play a role in funding national development banks or through the habitual commercial banks provide support for creditdirected to export promotion and investment finance.

7. In the last few years in Argentina, we have developed some instruments to enter into this field. First, through rediscounting loans – against good collateral - for productive investment at low interest rates and medium term maturities in the manufacturing sector. And, second, by directing the major commercial banks – under legislated new authority to direct credit granted by a new charter to the central bank– to extend medium term credit for productive purposes up to a percentage of their private sector deposits at reduced interest rates, with 50 per cent having to go to SMEs.