Financial Markets and Geopolitics

Recently, the US and the EU have imposed economic sanctions against some powerful Russian individuals, and against Bank Rossia, in retaliation for developments in Ukraine: earlier this week, Russia was suspended from the Group of Eight developed economies, and more sanctions are threatened. With war amongst nuclear powers unthinkable, economic sanctions in effect mean conduct of war by other, if less lethal, means. (In any case, after its disasters in Iraq and Afghanistan, Washington has little appetite for another military adventure.) The Russian stock market prices have crashed, and a large outflow of foreign money is expected. Meantime, Russian entities have withdrawn an estimated 100 billion dollars plus from US banks. Perhaps few now recall that the birth of the now huge market in offshore dollars (and other currencies) was the fear of the Soviet Union in the 1950s that its banks' dollar accounts in New York may be frozen as part of the Cold War, crippling its ability to pay for imports and receive export proceeds. (The offshore market was called the Eurodollar market, until the birth of the euro.) Iran is undergoing that experience for some years now, though there has been some temporary relief as negotiations about its nuclear program have made some progress.

To go back to recent events in Ukraine, this is the second time that Crimea is at the centre of Great Power rivalry. (The first time was more than 150 years back, with a military confrontation between Russia and the other major European powers. Incidentally, Florence Nightingale formed the first military nursing organization during the Crimean war, which later gave birth to the International Red Cross.) Great powers have always been very conscious of the need to preserve their spheres of influence: the US proclaimed the Monroe Doctrine almost 200 years back declaring that it would not tolerate the presence of any European military power in Central and Latin America. The last major manifestation of the doctrine was 50 years back when the USSR tried to install missiles in Cuba. At that time, the world had come within handshaking distance of a major nuclear war.

Russia has always believed that the “near abroad” (countries in East and Central Europe) are part of its sphere of influence. The background to the on-going confrontation was that the Ukrainian President refused to sign a treaty with the European Union after the Russians offered a $15 bn loan: Russia was worried that the treaty would be only a step towards joining the EU and NATO, as other countries on its border have done. In what can be termed as a coup, the President was thrown out and power assumed by his opponents. Ukraine is in a financial crisis and owes Russia $16 bn for gas supplies.

After the coup, Russia encouraged a referendum in Crimea, a Russian majority province of Ukraine for the last 50 years. (Before that, for a long time, it was part of the Soviet Union and earlier the Russian Empire.) The referendum voted with a 97% majority to secede from Ukraine and Crimea has now become part of Russia. Hence the sanctions: EU and US consider the referendum as being illegal. However, as *The Guardian,* the well-known UK newspaper, commented a couple of weeks back, the US has *a "record of flagrantly breaching international law over Iraq, Afghanistan, drones, extraordinary rendition and torture"* and is being hypocritical in denouncing Russia.

In the current dispute, China has, broadly speaking, remained on the sidelines: it abstained from a Security Council resolution on Ukraine, which Russia vetoed. China's reticence is understandable: it has a few trillion dollars of assets in the US!

Post-sanctions, Russia has taken steps to strengthen economic ties with China and Japan. Their needs are complementary. Both China and Japan need to import energy and other natural resources on a very large scale, which Russia can provide – and the former have the finance and technology to exploit them, which Russia needs. Western Europe also has a large trade with Russia, including imports of oil and gas. The "City" too makes a lot of money in offering financial and legal services to Russia and its oligarchs: no wonder the EU has been noticeably less enthusiastic about the sanctions than the US!

……………………………………………..

In the context of the controversy about the CBI enquiry against Mr. Bhave, I remember one personal experience from about 5 years back. One morning I got a call in my office that the SEBI Chairman wanted to speak to me. I had never met him or known him until then and was surprised to get the call. At the material time, the losses on derivatives suffered by many Indian companies were in the news (I recall that Mint was the first to break the story, and follow it up). Mr. Bhave had heard that I had analysed a number of such cases and requested me to make a presentation to SEBI about the issue in general and whether, in terms of the regulations for listed companies, SEBI needs to do anything. I duly made the presentation: as for regulations, I said that clause 49 of the listing agreement requires companies to have a risk management policy but few companies seemed to be following the spirit of the regulation.

Few top regulators or civil servants display such openness of mind, and willingness to listen and learn from outsiders.

A.V.Rajwade

Email: avrajwade@gmail.com