

## **The drivers of institutional change in a post-socialist economy: The case of deposit insurance introduction in Russia**

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### ***Abstract***

This paper studies the dynamics of the social institution of state paternalism as embodied in the deposit insurance. It focuses on the circumstances surrounding the adoption of explicit deposit insurance. Deposit insurance is an institution originating from the United States that subsequently became widespread worldwide. In the early-1990s, a group of proponents initiated parliamentary discussions that culminated with the enactment of Deposit Insurance Law in December 2003. Thus, the institution was imported into Russia.

The case of deposit insurance introduction in Russia may suggest that subjective factors affected institutional change in transition economies, and that the choice of imported institutions was rather random. The circumstances under which explicit deposit insurance emerged in Russia might explain its subsequent malfunctioning and social costs. Material and institutional pre-conditions were missing at the time the topic of deposit guaranteeing came up in the parliament. The key actors (large banks controlling most household deposits and their depositors) did not demand hard a formal scheme of deposit protection. The advantage of an explicit protection scheme over the existing implicit one was unclear because of the prevalence of state-owned banks. I suggest that the introduction of deposit insurance was driven by a combination of factors such as: genuine good intentions of its proponents; demonstration effect of western experiences; the desire to disrupt the monopoly of Sberbank and boost the competitiveness of privately-owned commercial banks, probably stemming from ideological bias in favor of private ownership; and, last but not least, search for a new field of activity for deposit insurance initiators themselves. Despite the random selection, the institution of deposit guaranteeing fit well in the Russian setup because it was consistent with the long tradition of state paternalism.

The motivation for this paper came from two different streams of literature:

— on institutional change and transfer of institutions between countries (North, 1990; Rodrik, 2000; Polterovich, 2001; Berkowitz et al., 2003; Oleinik, 2005; Kirdina, 2004; Kleiner, 2005; Kuzminov, Radayev et al., 2005; Nureev, 2009; Polishchuk, 2008, 2013; Nureev, Latov, 2017);

— on deposit insurance and its effects, which entails theoretical works (Diamond, Dybvig, 1983; Keely, 1990) and empirical studies (Martinez-Pería, Schmukler, 2001; Demirgüç-Kunt, Kane, 2002; Demirgüç-Kunt, Detragiache, 2002; Demirgüç-Kunt, Huizinga, 2004; Demirgüç-Kunt, Karacaovali, Laeven, 2005; Cull, Sorge, Senbet, 2005; Anginer, Demirgüç-Kunt, Zhu, 2014), including papers on Russia (Kuzina, 2005; Cámara, Montes-Negret, 2006; Peresetsky, 2007;

Ungan et al., 2008; Krotov, 2009; Karas et al., 2010; Chernykh, Cole, 2011; Chernykh, Sokolov, 2012; Pyle et al., 2012; Karas et al., 2013; Ibragimova, 2015).

Along with academic motivation, there is also an empirical one stemming from the dramatic developments in the Russian banking industry. Deposit guarantee eroded market discipline, increased the fragility of privately owned deposit takers, enabled criminal business models by individual banks, and caused a huge waste of public funds.

Existing literature accepts the existence of deposit insurance as a fait accompli, without questioning the reason for its existence nor opportunity cost. I find little research into institutional aspects and the political economy of deposit insurance in Russia, so my paper aims to fill that void. I rely on statistical data from the Central Bank of Russia and the Deposit Insurance Agency (ASV) for market shares of different banks in household deposits market and for the outcomes of the deposit insurance system functioning in 2003-2017.

I show that the adoption of deposit insurance results from a random choice. For the first time in the literature, to my knowledge, I identify the main interest groups and the main stakeholders of the process. I look separately at explicit and implicit motives that could have driven the initiators of deposit insurance, before describing the position of other stakeholders like depositors of state-owned banks, depositors of private banks, bank owners and managers, bureaucrats and public politicians, and external parties. I conclude that this particular episode of institutional change was supply-driven and influenced by subjective factors.

Another novelty of this paper is the application of the concept of misuse of institutions (Polishchuk, 2008). I argue that deposit insurance was misused in Russia. While the classical model views deposit insurance as a means of preventing depositor runs on fundamentally sound and solvent banks, in Russia its proponents intended to use deposit insurance to enhance artificially the competitiveness of private banks and reshape banking market structure in their favor. Deposit insurance in fact was employed to prevent depositor runs on fundamentally weak banks otherwise incapable of competing against state-owned ones. Another example of misuse was the intention to apply deposit insurance as a tool for banking sector purge.

I believe that this paper adds to the literature on transfer of institutions and deposit insurance alike.

**Key words:** Russia; deposit insurance; banks; misuse of institutions; assessment of regulatory impact; state-controlled banks

**Conference Topic: SOCIOLOGY.** I believe that this paper belongs to the Sociology section of the conference whose scope includes the dynamics of social institutions. This paper looks at the dynamics of the institution of state paternalism and, more specifically, its manifestation in deposit insurance.