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TRANSFORMATIONAL PROCESSES IN GLOBAL BANKING SECTOR

The last several years have been critical in the process of transformation of the financial markets around the globe. The recent crisis has shed the light onto the flaws of the financial systems exacerbated by government profligacy and fundamental changes in human/consumer psychology. In order to mitigate the consequences of the current crisis as well as prevent similar from happening in the future financial regulators have to undertake a large number of measures. This in turn brings up the question of financial system transformation and transformation in banking specifically.

One of the factors that affected the urge of financial regulators to make adjustments to their policies was the weakness of local labor and consumer markets. With the weak consumer spending countries are tempted to indulge into aggressive protectionism and trade expansion. Shifting trade balance in the direction of surplus has become one of the main goals of national governments. In this context national banks have to succumb to the will of political powers and support trade protectionism by the means of monetary intervention. Term "currency wars" has become very common during the last months. Governments of Switzerland, Japan and Brazil are among the main culprits of currency war development. Interestingly, the direction of monetary intervention in Brazil and Japan are quite polar: with Japan fighting for the Yen devaluation, while Brazil tries to prevent a capital run caused by a rapid influx of "hot money" in previous year.

It is important to note the growing pressure for currency rate revaluation within European Union. Despite the fact that all countries within the Union enjoy stable Euro rate, some countries, like Germany, benefit more from the common currency and weaker Euro than others (e.g. Greece and Ireland). The pressures between countries grow as the trade balance between the countries of the union become more and more disproportionate. The talks about creating separate central bank like institution to control the currency rate in the interest of all the member countries have been frequent in recent months. On the other hand many economists claim that it would be in the interest of the EU in general if the countries were able to have their own currencies and employ monetary policy compliant with the fundamental economic situation.

In terms of European crisis it is important to note growing role of banking system in financing government debt. Commercial banks have played an important role in bond auctions held by Spain, Greece and Portugal. It is not a secret that most of these banks had to accept a 50% cut in their holdings of Greek debt in order to ease the pressure on this South European country. The connection between private banking sector and the state has become very noticeable and strong in a somewhat risky way. Last year economists paid special attention to the transfer of risks and debt burden from the Irish and Spanish banks to the government balance sheet. By bailing out commercial banks governments of these countries took over a large share of debt burden accumulated over years and almost overnight became the subject of sovereign fiscal risk discussions. If 20 years ago investors could easily shift their capital from private (stocks or c-bonds) sector to sovereign (treasuries, state bonds) sector, now the line between the two is very vague and the risks are interchangeable. Experience of both Greece and Ireland/Spain shows that banks can easily be forced into accepting the sovereign risks, while the “too big to fail” dogma will force governments to finance commercial sector.

In the context of what has been said above European authorities are developing a plan of implementation of an independent financial facility, that would play a role of financier of last resort and would fill in the gap of function not performed by the European Central Bank.

Another peculiarity of the current crisis is the shift of targeting policies. In previous years most of banks would engage into rather straight-forward inflation targeting. In a lot of cases this would solve the rest of the fundamental economic problems. However it is important to note that in previous years global economy was characterized with much higher growth rates. Nowadays, however, economic growth is just not there and the talks about the global economic slowdown are much more frequent than the opposing opinions. Both Fed and ECB have abandoned inflationary targeting in their long term strategy and have pointed out that their main goal is wellbeing of labor market. As a result currency regulation has become a secondary goal and comes across as an important issue only through the prism of international trade and possible protectionism favoring national manufacturers. For such countries as United States and Great Britain, which are more service oriented, currency regulation has much weaker impact than for the export -dependent countries as Germany and China. So instead of maintaining reasonable interest rate many countries chose to keep it at record low (in some cases real interest rate can be negative) and provide as much liquidity on the market as is takes to propel consumption and, hopefully, further hiring.

Elaborating on the changes to central bank monetary policies around the world implies mentioning the changes in the transfer of liquidity from the central banks to real economy. As taught in most economic courses, reduction of reserve rates as well as lower discount/repo rates for commercial banks almost always lead to a massive inflow of liquidity to the market; the kind of liquidity which both financial markets and main street manufacturers can take advantage of.

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