**Chapter 11**

**Review Questions**

1. **Why is it vital for business to have confidence in the international payments system?**

Students could start off by identifying the characteristics of a good payments system for business: ready availability; affordable; fast; secure; free from fraud; stable.

They could be encouraged here to consider why a stable and reliable international system of money transfer is essential for business: to pay for exports and imports of goods and services; to finance foreign investment; to remit profits; the fact that good payments systems allow firms to concentrate on what they do best: produce goods and services and to plan ahead. Significant instability or a major breakdown in international payments systems could shake confidence and, by deterring firms from involvement in international trade and investment, could threaten revenues, profits, and even survival for some businesses.

2. **Explain the increasing internationalization of the banking system. What factors have made it easier for banks to internationalize their operations?**

- Students could start off by explaining what is meant by the 'internationalization' of the banking system: the moves to enter markets abroad. Students could illustrate with evidence and examples on internationalization, for example, the moves by some banks into China and E. Europe.
- Then reasons for internationalization could be addressed, for example: the desire for growth in the face of slow growing domestic markets in rich countries; fast growing markets in S. E. Asia, E. Europe, Latin America; avoiding what the banks regard as overly tight financial regulation.

- Facilitating factors: students could discuss the international trend towards deregulation of financial markets at least up to the financial crisis; the advances in, and international diffusion of, information and communication technologies; in the EU the establishment of the single currency Eurozone; the attempts to complete the single market in the EU e.g. moves towards centralization of bank supervision in the Eurozone and the consequent reduced ability of countries to protect their domestic banks against foreign predators (see http://www.reuters.tv/v/5do/2018/01/03/predictions-watchdogs-will-drive-eu-s-2018-bank-mergers)
- Students could identify barriers such as the increased regulation following the financial crisis and the continuing resistance by countries to foreign banks acquiring domestic rivals.

See: http://bruegel.org/2018/06/european-bank-mergers-domestic-or-cross-border/
http://www.reuters.tv/v/5do/2018/01/03/predictions-watchdogs-will-drive-eu-s-2018-bank-mergers
https://www.bloomberg.com/news/articles/2018-03-27/why-large-european-bank-mergers-still-face-hurdles-quicktake
https://www.hellenicshippingnews.com/new-eu-bank-capital-rules-favourable-for-cross-border-mergers/

**3. Analyse the need for effective regulation of the financial system. Explain why bankers resist the tightening of regulation.**

Students could, especially in the light of the financial crisis, point to the need for national/international regulation ideally to ensure:

- the financial system as a whole is stable and resilient to future financial crises;
- individual banks have sufficient liquidity, are effectively managing risk and are not so large as to pose a threat to the financial system if they go bust;
- payment systems are effective and efficient;
- savings are efficiently channelled to productive investment;
- confidence among savers that their savings are safe;
- removal of the risks taken by banks to public finances;
- to prevent financial fraud.

They could also contend that: an effectively regulated financial system helps a country's economic performance; and that history shows that the financial sector soon forgets the lessons of previous financial crises.

Several proposals for banking regulation can be found in the BIS Working Paper 412 at: http://www.bis.org/publ/work412.pdf.

For more detail on the UK recommendations on dealing with the banks see the speech by Sir John Vickers at http://web.archive.org/web/20110914044642/http:/s3-eu-west-1.amazonaws.com/htcdn/Interim+Report+publication+JV+opening+remarks+-+check+against+delivery.pdf: The full Vickers report is available online to download as a PDF.

For an historical overview up to the Basel Accords see:

https://www.bankofengland.co.uk/-/media/boe/files/paper/2013/constraining-discretion-in-bank-regulation.pdf?la=en&hash=46E1F9BF24E99D85DBC28746A190ABBC5DA785E2
For a history and critique of regulation see Barry Eichengreen's article at http://www.prospectmagazine.co.uk/features/time-to-get-serious-about-bank-reform

One would expect students to focus their discussion on the bankers' view that regulation can restrict their freedom to make decisions, as they see it, in the best interests of their business and can have adverse effects on costs, competitiveness, revenues, profits, and innovation. They also argue that regulatory costs will fall on their customers. And, of course, bankers' bonuses could be affected adversely by tighter regulation.

See:

https://gulfnews.com/business/sectors/banking/banks-resist-as-g20-feels-pressure-to-boost-bank-regulation-1.1036775

https://dealbook.nytimes.com/2013/05/23/banks-lobbyists-help-in-drafting-financial-bills/

https://www.telegraph.co.uk/finance/newsbysector/banksandfinance/10141142/Mervyn-King-Banks-lobbying-at-highest-level-against-regulators-demands.html

The Financial Times reported on 6 June 2015 that UK banks had cranked up their attacks on regulation: Banks increase attacks against wave of regulation.