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Transmission mechanisms of international competitiveness and expansion of transnational banks in countries with emerging markets

Annotation
This paper is dedicated to investigation of theoretical and practical aspects of impact transnational banks have on competitive environment of emerging financial markets. It develops systematisation of structural changes in international banking activity in the context of global financial instability, and identifies basic tendencies in globalisation and transnationalism of banking activity. Mechanisms of support of international competitiveness of a national economy in the context of interaction with transnational banking capital are researched. The paper also identifies negative effects of processes of entry of transnational banking capital on the national economy.

Keywords
transnational banks, financial system, competitive environment, mechanism of bank regulation, policy of promotion of direct investments, entry of foreign banking capital, countries with emerging markets, transnational banking capital, transnationalism of banking activity, emerging financial markets

1 Problem statement

The present stage of development of the global economy is characterised by profound transformations in international financial relations in the aftermath of the latest wave of economic globalisation at the turn of the 21st century, which was noted for buoyancy of capital flow between industrial countries and countries with emerging markets. On one side, capital flows significant by their volume were associated with high rates of growth, while on the other side, during the same period countries with emerging markets incurred great macroeconomic and social losses, experienced recurring decline of growth rates resulting from financial crises that took place in 1998 – 1999, 2001 – 2002, and 2007 – 2008 of both local and global nature.

At the present stage, formation of mechanisms of monetary support of international competitive opportunities of states becomes one of the key tasks of emerging market economies. A strategy of fully established and consistent interaction with international capital markets has become the cornerstone of foreign policy in the context of insufficiency of financial resources, while unfolding of crisis phenomena at the beginning of the 21st century brought into focus scientific agenda of competitiveness of national economies which typically reduces in the context of financial instability. Intensity of such reduction, on one hand, depends on the level of development of economic opportunities, and the degree of openness of the national economic system, while on the other hand it depends on efficiency of state monetary and financial policy capable of providing an adequate response to external threats and dangers while minimising negative effects of international capital flows on the economic sector.

2 Analysis of recent researches and publications

Research of the impact of expansion of transnational banking capital on economic growth of receiving countries is reflected in scientific works of scholars such as J. Bhagwati, F. Cardim de Carvalho, E. Craft, G. Edison, B. Eichengreen, A. Filipenko, N. Hood, T. Kalach, M. Klein, M. Obstfeld, T. de Swaan, G. Olivei, J. Taggart and others. However, the aspects of impact transnational banks have on competitive environment of emerging financial markets remain insufficiently investigated. All this requires implementation of efficient system of interaction with transnational banking capital.

3 Research results

The contemporary economic theory includes contradictory views on the impact of expansion of transnational banking capital on economic growth of receiving countries. According to some theories, inflow of capital of transnational banking groups facilitates the process of distribution of

risks and, therefore, contributes to specialisation of production, allocation of capital, and economic growth [15]. Moreover, in the conventional neoclassic model of growth deepening interaction of the monetary system with transnational banking capital facilitates flowing of cash to countries with capital deficit. Furthermore, the aforesaid interaction may improve functioning of internal financial systems through intensification of competition and import of financial services that will eventually have positive impact on growth [13].

Investigating the problematic of steadiness of competitive positions of national economies, A. Filipenko emphasises the issue of availability of a developed financial market infrastructure in a country, as well as that of capital production factors and novel intangible resources providing opportunities to achieve steady economic growth in the context of post-industrial economic development [7].

Western academic community also has contradictory views on the impact of international financial interaction on economic growth, and in particular, with regard to the degree to which economy does not limit transborder transactions. Furthermore, such researchers as M. Obstfeld [14] and G. Edison [5] substantiate the thesis stating that entry of international banking groups and financial liberalisation facilitate the process of distribution of risks and, therefore, contribute to specialisation of production, allocation of capital, and economic growth. Moreover, in the conventional neoclassic model of growth international financial liberalisation facilitates flowing of cash to countries with capital deficit. Interaction with transnational banking capital may also improve functioning of internal financial systems through intensification of competition and import of financial services that will eventually have positive impact on growth.

On the other side, if there are any deviations, international financial integration may actually slow down the process of growth. According to B. Eichengreen, expansion of transnational capital is especially threatening in countries with emerging financial markets, with weak institutions, an unstable monetary system and legislative framework which may actually result in capital outflow from countries with deficit to countries with excess of capital having better institutions [6].

However, optimisation of monetary support of international competitiveness as a factor of encouragement of economic growth remains the key theoretical issue. T. de Swaan [16], M. Klein, and G. Olivei [12] suggest that the very intensification of competition may increase efficiency of an internal financial system through introduction of international standards, as well as due to potential threat of "struggle for quality" on the side of foreign intermediaries. Branches and outlets of foreign banks may expand the absolute size of a national banking system and occupy those market niches that have already been ignored, as well as to introduce financial innovations which immediately expand the scope of financial services. Such advantages as increased efficiency and expanded size of a financial market may increase the volume of savings available by increasing internal savings and as a result of funds raised. Increase in the volume of savings, in turn, may provide an opportunity for intermediaries to use the advantage of economies of scale.

Substantiating paradigmatic fundamental principles of economic development, followers of the left radical scientific school, and J. Bhagwati in particular, emphasises non-equivalence of advantages of high international mobility of capital gained in the process and competitive positions of receiving countries. Asymmetric information, herd behaviour, financial bubbles, and other issues are just a few of reasons of abnormalities in international financial markets. Opening of borders for capital flows just aggravates the risk of loss of international competitiveness for receiving countries, while advantages of capital mobility are not big enough to justify its potential threats [1].

An argument of different comparative efficiency of international banking groups in markets of developed countries and those of a lower degree of economic maturity is one of the dominant theses in studies of interaction of transnational banking capital and competitive opportunities of receiving countries. Such scholars as S. Claessens, A. Demirguc-Kunt, and H. Huizinga support this argument, emphasising in their studies that in markets of less developed countries foreign banks are more efficient that local ones due to a high level of stability of their parent capital, access to external funding sources, stronger commitment to innovations, and high quality of banking supervision in the country of their origin. However, in markets of developed countries local banks are more efficient that foreign ones, as the latter incur significant expenses related to monitoring of their business abroad, as well as collection and interpretation of information about the local market [2].

Furthermore, in the opinion of some specialists, and of F. Cardim de Carvalho, E. Craft, and T. Kalach, transnational banks typically are not prevailing in promotion of new products in markets of receiving countries. Thus, in most countries of Central and Eastern Europe international financial organisations were pioneers in lending to small business, while local banks were the first to introduce consumer credit and credit cards. In Latin America and in Brazil in particular, quite a few of technical innovations in the banking sphere (wide-spread automation, on-line services etc.) were first

introduced by national rather than foreign banks.

The current period of development of branch networks of corporate business transnationalism that started at the beginning of the 21st century is characterised by emergence of fundamentally novel models of managing international companies and banking groups that move their subsidiaries and their divisions to various countries pursuant to the logic of efficiency maximisation. This process became technically possible as a result of revolutionary changes in transport and information and communication technologies. Development of world transport infrastructure resulted in drastic decrease of the cost of redeployment of qualified labour while essentially reducing the need of production facilities for transnational companies in relatively isolated countries and regions. The scientific and technological revolution in the field of information and communication technologies has drastically reduced expenses on collection and transmission of information, thus, simplifying monitoring and enabling much greater centralisation of managerial, monitoring and financial functions in countries of location of transnational banks than it was possible in the 20th century.

Western European investigators emphasise the opposite side that has developed into a concept of the so-called "branch capitalism" which considers migration of decision-making centres beyond the borders of the countries of strategic decision-making. Furthermore, in their studies Scottish authors J. Taggart and N. Hood note that in the context of globalisation strategic decisions are made in centres that are geographically isolated from effects of implementation of such decisions [17].

Moreover, J. Taggart and N. Hood stress some negative effects emerging in the context of the unfolding tendency of "branch capitalism", such as 1) reduction of the volume and intensity of economic relations of branches with local suppliers of products and service providers due to benefits of internal corporate agreements, i.e. supply of goods and services from countries of origin of transnational companies or from other branches; 2) migration of managerial functions abroad and, as a result, simplification of functions performed by a branch, and loss of experienced personnel possessing insight and skills that cease to be used in the production process in this country; 3) reduction or dead stop in research and development being carried out at branches, and their concentration in a centre broad which reduce scientific and research opportunities of the country.

Transnational companies and international banking groups seek to reduce costs on external expansion that results in further specialisation in which economic activity of national enterprises turned into units of transnational companies increasingly results in sets of partial or intermediate products, and separate operations being intermediate elements of provision of completed services [10].

Thus, world experience of interaction of development of local financial markets and expansion of transnational banking capital shows that the role of branches and subsidiaries in national economies may differ a lot depending on functions performed by these branches. Regardless of the fact that in many aspects sets of these functions depend on objective factors, vectors of transformation of branches and subsidiaries at the local market and the role they play in the value creation chain become controllable as a result of taking a set of institutional and economic actions. Formation of regional and divisional centres of transnational banks at local markets and winning of a regional or a global position both are cumulative processes: effective performance of these functions result in increase of investment inflow to this branch and enhancement of its managerial functions [8]. However, along with positive and negative effects of economic interaction with international banking capital, contemporary investigators identify some contradictory channels of influence such interaction has on competitive opportunities of emerging market economies. Furthermore, Ukrainian researches V. A. Vergun, A. I. Kredisov, and O. I. Stupnitsky emphasise lack of evidences to the contribution of international financial groups to specialisation of production being a factor of increase in productivity and growth. Without a mechanism of risk management the structure of a highly diversified production will be characterised by fluctuation of production volume and, thus, by irregular consumption. A prospect of a possible intensification of fluctuations may interfere with specialisation employed by countries which facilitates growth; more intense fluctuations typically involve decrease in aggregate volume of savings, as well as reduction in investment volumes [19].

Ongoing investigations have not identified any steady specialisation of transnational banks in financing of specific industries or spheres of foreign economic activity of receiving countries. In developed economies foreign banks had to compensate costs on expansion to external markets mostly at the expense of specific knowledge and relations with the country of origin. Accordingly, companies dealing with this country or related to it in some way become their first customers. In countries with emerging markets transnational banks, on one side, have advantages of external funding that cover costs on their expansion and, thus, have an opportunity to select their customers; on the other side, they face some challenges in estimation of credit solvency of local companies. As a result, when entering a new

market, foreign banks, in the first instance, target enterprises with risks that are the easiest to assess, i.e. with export-oriented companies or enterprises with foreign investments. Depending on the structure of national export, this means tendency to deal with the basic materials sector (Kazakhstan), enterprises in the engineering industry (countries of Central and Eastern Europe), the textile industry (Turkey), labour-intense manufacturing (China) etc. [3, 9]. In spite of the fact that some scholars accuse foreign banks of credit blockade, in scientific literature there are no accounts of cases of a purposeful credit blockade of solvent local manufacturers by foreign banks, for instance, in order to remove them from the market clearing up the way for their foreign competitors. However, it is evident that there are industries, including export ones, which have no prospect of an adequate financing on the side of foreign capital. The military-industrial complex, nuclear power industry and some other specific industries are the best examples of such a situation.

While in theory there are no essential evidences of any clear link between financial integration and economic growth, it can be stated that countries with emerging markets hardly have any other choice but to strengthen their financial relations in order to eventually widen their opportunities of growth in the long term. The problem lies in the way of managing short-term risks related to financial globalisation which in the short term may have just a few advantages of growth and result in greater fluctuations in production and consumption if no appropriate pre-conditions have been created.

In order to ensure protection of national interests in the context of intensification of global competition, it is required to integrationally transform the national monetary system directed at development of a branching network of purpose-specific financial institutions, appropriate infrastructural support for efficient functioning of all financial market sectors, and development of an up-to-date regulatory system. This process should start with transformation of organisational structures of monetary support of countries of new market economy with international banking capital as a factor of competitiveness of the national economy, and minimisation of costs of investors and other market participants which are related to practice and standards of financial regulation influencing cost effectiveness of specific contracts and estimation of the investment climate. Improvement of stability and functionality of financial institutes and development of financial infrastructure form the basis of strengthening of competitive positions of national economies in the context of interaction with transnational banking capital (Figure 1).

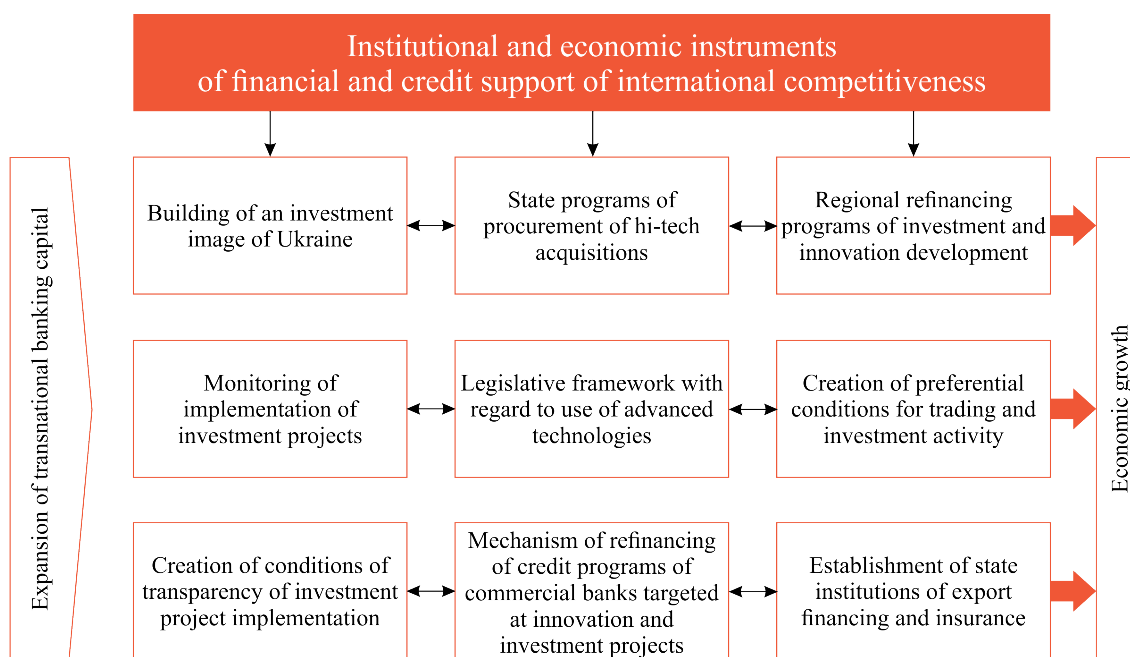

Figure 1 Mechanisms of support of international competitiveness of a national economy in the context of interaction with transnational banking capital. Source: [2, p. 56]

Economies that have been integrated to the global financial environment attract disproportionately high share of direct foreign investments that in future may result in inflow of technologies and create a channel of transfer of managerial knowledge. Increase of the share of foreign capital in commercial banks give rise to direct macrofinancial positive effects, and in particular facilitates access to international financial markets, contributes to improvement of the

structure of banking management and supervision, promotes deployment of a great amount of novel financial instruments and banking technologies; involvement of foreign banks result in intensification of competition which, in turn, may improve both quality of internal financial services and efficiency of resource allocation and overall competitive positions of a national economy in the world.

The category of the transmission mechanism was first identified in monetary policy analysis carried out by Keynes who introduced the term "transmission mechanism of monetary policy" meaning a system of variables mediating influence of money supply on economic activity [11]. The category of the transmission mechanisms of monetary support of international competitiveness applies to the complete process mediating influence of state macrofinancial policy on macroeconomic changes, such as economic activity and pricing. Policy of supporting financial stability is dictated by monitoring and estimation of key indicators of financial stability, such as macroeconomic conditions, financial markets, institutions and infrastructure in order to timely identify potential risks; estimation of the state of financial stability on the basis of such monitoring; taking preventive actions and measures on efficient solution of crisis situations. At the same time, the following key instruments of regulation of crisis phenomena which can be used by states are identified: mechanisms of employment of the private sector, maintaining an appropriate level of liquidity using schemes of the ultimate creditor, state intervention to activity of financial institutions through guaranteeing deposits of individual depositors and recapitalisation of assets of financial institutions that have been affected.

4 Conclusions

An efficient system of interaction with transnational banking capital should include a rather wide range of organisational and legal instruments and economic levers, as negative effects of expansion of transnational banks are usually preceded by various economic and even political issues. A national mechanism of counteraction to negative effects of expansion of transnational banks shall identify situations in which actual or foreseeable risks are beyond the limit values, develop measures to be taken on removing the country from the risk zone, to expertly assess regulatory and legal acts that have been passed and state decisions made on financial and economic matters while being guided by national interests.

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