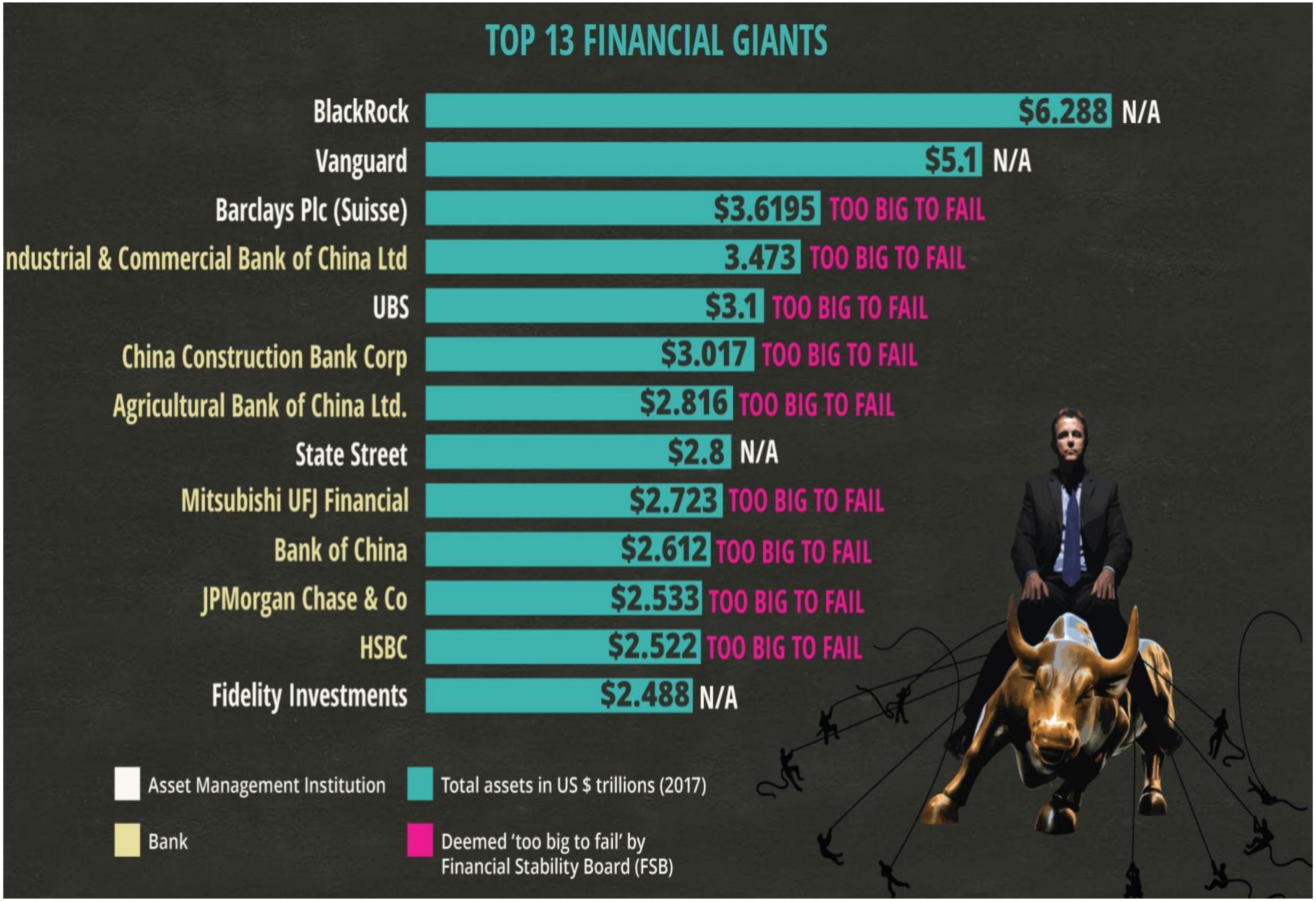
Governance of the financial sector and financialisation in de context of Africa

Myriam Vander Stichele

Centre for Research on Mulitnational Corporations

SOMO

Where is the biggest money?



INTRO

- global governance & how Africa fits (not) in it
- governance of global financial system excluding the international and regional development banks
- governance of financialisation instruments

Underlying principles of the governance of the financial system

- No internationally binding agreement vs. trade and investment treaties sanctionable
- are international fora for political decisions and fora for official standard setting
- all finance issues out of the UN
- financial sector is highly involved at all levels of governance : pushing hard to have least regulations
- financial sector self-governs
- No obligations for the financial sector or even central banks to finance socially and environmentally sustainable activities

Africa not part of multilateral decision-making fora

BIS – Bank of

- serves central bankers and their cooperation, and acts as a bank for central banks
- has 60 members of which only the Central bank of Algeria and the South African Reserve Bank is part

- The Committee on the Global Financial System is a central bank forum for the monitoring and examination of broad issues relating to financial markets and systems

G20

- G20 Ministers of Finance and Governors of central banks/finance track and working/study groups
- Only S Africa is member, sometimes a least developed country (African or other) guest
- Now not agreeing on reforms but monitoring & discussing
- Important agreements in 2009-2011 to reform the financial system on banks (Basel III), OTC derivatives trading, securitisation, etc.
- Dispatches work to other agencies (FSB, BCBS, IOSCO. OECD, IMF, WTO, etc. , hardly UN)
- rubber stamps standards at the G20 MinFin meetings or G20 Summit
- Influenced by **B20** and to a lesser extend: L20, T20, C20, Y20, W20

Priorities for Japan G20 Finance Track in 2019

I. Global Economy - Risks and Challenges

(A) Surveillance on global economic risks

(B) Global imbalances

(C) Aging and its policy implications

II. Actions toward Robust Growth

(D) Quality infrastructure investment

(E) Resilience against natural disasters

(F) Strengthening health financing for move towards UHC in developing countries

(G) Debt sustainability and transparency of LICs

III. Response to Structural Changes caused by Innovation and Globalization

(H) International taxation

(I) Addressing financial market fragmentation

(J) Financial innovation - opportunities and challenges

Financial Stability Board (FSB)

- coordinates at the international level the work of national financial authorities and international standard-setting bodies
- Membership : mostly G20+; African: only South Africa
- **Policy development and coordination:**
  - building resilient financial institutions (Basel III, Compensation practices)
  - addressing SIFIs
  - effective resolution regimes and policies
  - more effective supervision
  - making derivatives markets safer
  - resilient non-bank financial intermediation:
- No relationship with NGOs / FSB Watch

“resilient non-bank financial intermediation” = shadow banking

- **annual monitoring** exercise to assess global trends and financial stability risks in non-bank financial intermediation
- **oversight and regulation** need to be strengthened to mitigate the potential systemic risks associated with non-bank financial intermediation, namely:
  - mitigating spill-over risks between the banking system and the system of non-bank financial intermediation;
  - reducing the susceptibility of money market funds to “runs”;
  - improving transparency and aligning incentives associated with securitisation;
  - dampening procyclicality and other financial stability risks associated with securities financing transactions such as repos and securities lending; and
  - assessing and mitigating systemic risks posed by other non-bank financial entities and activities.

FSB Implementation monitoring and effects of reforms

- progress reports to the G20
- monitoring of priority areas
- monitoring of other areas
- monitoring by jurisdiction
- peer reviews
- effects of reforms
- initiative on cooperation and information exchange

NB: developed industry led voluntary climate-related financial risk disclosures

International standard setting bodies

Basel Committee on Banking Supervision

- **Core Principles for Effective Banking Supervision** and bank reform standards (“Basel II”, Basel III”)
- Members from 28 countries of which only South African Reserve Bank;
- Basel Consultative Group includes Central Bank of Tunisia, Central Bank of West African States,

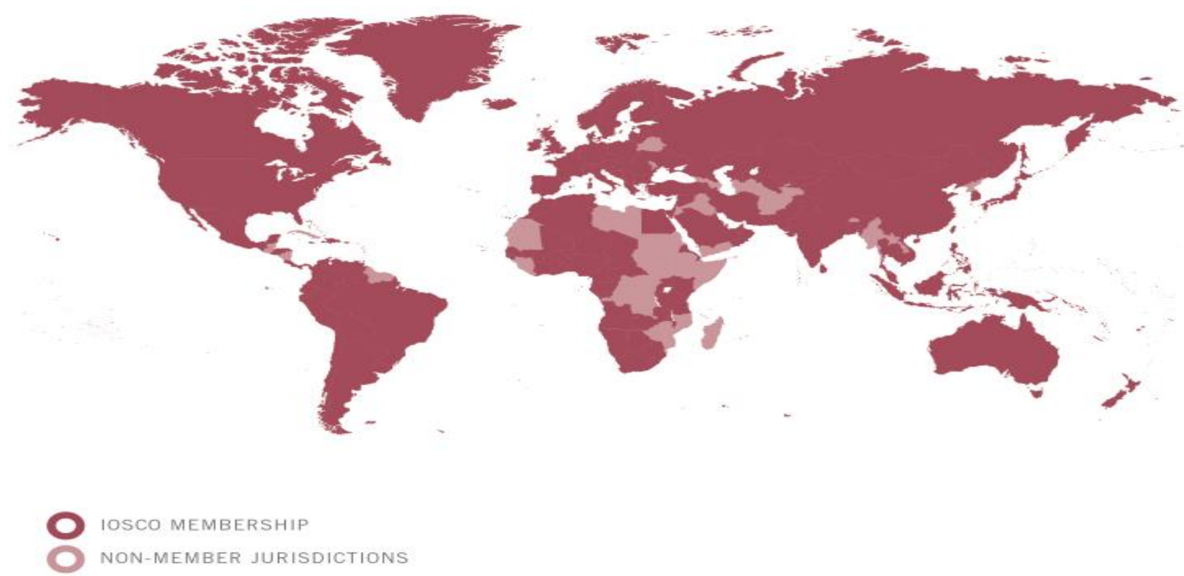
International Association of Insurance Supervisors (IAIS)

- **Insurance Core Principles (ICP)** provide a globally accepted framework for Standards, Guidance and Assessment Methodology
- members: Conférence Interafricaine des Marchés d'Assurances (CIMA), Botswana, Burundi, Cape Verde, Congo (Democratic Republic of the) , Egypt, Ghana (National Insurance Commission Ghana), Guinea, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Nigeria, Rwanda, South Africa, Swaziland, Tanzania, Tunisia, Uganda, Zambia

International Organization of Securities Commissions (IOSCO)

- **Objectives and Principles Securities Regulation**
- All financial market (infrastructure) sectors
- Members

IOSCO Membership Map



Note: The following two organizations are ordinary members:

1. The **West African Monetary Union (WAMU)**, which comprises Benin, Burkina Faso, Ivory Coast, Guinea-Bissau, Mali, Niger, Senegal, and Togo.
2. The **Commission de Surveillance du Marché Financier de l'Afrique Centrale (COSUMAF)**, which comprises Cameroon, Central African Republic, Congo, Gabon, Equatorial Guinea, and Chad.

UN

- UNCTAD: has become an organisation for ‘consensus building’ and monitoring, and monitors and promotes FDI & BITs vs. in first stages was were commodity agreements and global new economic cooperation regimes were negotiated (e.g. ‘New Economic Order).
- UN General Assembly ‘Stiglitz report”: ignored by N
- UN Finance for Development: somewhat influencial in validating financialisation through blended finance (AAAA)

African cooperation mechanisms

- SADCC cooperation mechanism of central banks
- West African Monetary Union
- Commission de Surveillance du Marche Financier de l’Afrique Centrale
- Central Bank of West African States
- Conférence Interafricaine des Marchés d'Assurances (CIMA)
- ...

Legally binding agreements

Foreign banks and others of the foreign financial services industry (stock exchanges, derivatives trading, investment funds, trust funds & tax advisors, hedge funds and private equity)

Protection of foreign banks and financial industry (FSI)

- **WTO/GATS and trade agreements (include investment)**: open up FSI for establishment and operation, with rules in favour of FSI → allows concentration of foreign FSI
- **investment protection agreements (BITs, RIAs):** protect FSI and sanctionable under investor to state dispute settlement (ISDS)
- **no or little capital controls allowed** by trade & investment agreements, scrutiny by the IMF and IMF institutional view; EU constitution; OECD code on liberalisation of capital flows
- Foreign banks and FSI are **often listed** = shareholders influence govern and push for high profitability

= Profit oriented instead of development oriented finance

Important players in African financialisation

Bonds and debt

- -government bonds can be defined as ‘investments’ in investment protection agreements and corporate bonds normally are covered by BITs: investors in bonds are protected by BITs rules (e.g. fair treatment by host country). = corporate bond defaults aresubject to ISDS based.
- EDCs bonds contracts are often judged under laws of New York or UK incl. collective action clauses.
- Public debt is renegotiated in ‘Paris club’ of donors
- Private debt resolutions are discussed at the ‘London club’ of private creditors.

Cf E.U IPAs have annex on public debt (def. of “restructured negotiation” vs. vulture funds) when to be judged by ISDS.

NB Ghana-Netherlands BIT definition of investment: (“ ii)rights derived from shares, bonds and other kinds of interests in companies and joint ventures; iii) title to money and other assets and to any performance having an economic value;)

Global investment banks

- issue African bonds (syndicates) with private placement: are regulated and supervised by home countries
- Regulated at national/EU level based on Basel III and FSB GSIBs standards.
- Most investment banks are listed = shareholder value pressure for high yields

Trading of African bonds

- Trading of African bonds on investment bank platforms
- On other non open market trading on electronic platforms (e.g. data base platform such as Refinitiv (ex Thomson Reuters) as secondary markets where price discovery happens:
- Trading platfoms regulated and supervised by the home country and IOSCO standards.
- Johannesburg's stock exchange (JSE) on which South African government bonds are traded, including electronic **trading** platform result of "a collaboration between the JSE, National Treasury, the Central Securities Depository, known as Strate, the Financial Sector Conduct Authority and banking institutions servicing primary dealers"

Investment funds, asset managers and related services

- incorporate sovereign and corporate bonds in investment funds (many different ones in one fund (mutual funds, ETFs):): also for Africa?

- have affiliates in different countries where they are regulated.

- Selling of investment funds is regulated by national/EU regulation regarding composition (in EU: UCITS) , governance and selling (in EU: MiFID II/MiFIR), but NOT how big the asset managers can be, non-standardised funds, earnings of managers, etc.

How investment funds are sold to individual customers

→W individual investors profit from S companies

→without assessment of social & environmental impact

Source: [https://www.ing.nl/particulier/beleggen/beginnen-met-beleggen/index.html (6](https://www.ing.nl/particulier/beleggen/beginnen-met-beleggen/index.html) December 2018)

Hedge funds and private equity

- Not regulated in the US vs. light EU regulation (AIFMD) of the managers and marketing in EU markets while being based in tax havens.
- FSB monitoring
- Based in tax havens

Credit rating agencies

- regulated by national/EU jurisdictions;

- G20 pledge to reduce reliance on credit ratings (2014) is proving hard to implement

Commodity derivatives trading

- on exchange and off exchange (OTC) with hedging and speculative trading defines prices: in developed countries;
- Regulated by national/EU authorities in N and S: position limits too weak, more reporting, CCPs
- Exchanges are listed = shareholder pressure
- Exchanges self-govern integrity of price setting, warehousing

Sustainable finance

- central banks: Network on Greening the financial sector; IFC Sustainable Banking Network
- inititatives, policies and regulations in South (China !) and North (e.g. EU: taxonomy)
- Banking sector: ESG risks vs ESG impact & remediation (OECD discussions based on Guidelines)
- Investment sector: transparency (and obligations) to do ESG risk assessment (e.g. EU)
- Cf. UN Guidelines on Business and Human Rights
- Cf. UN Binding Treaty on Business and Human Rights

This was a selective overview

Thank you

ANNEXES

Financial services in trade agreements with developing countries

Developing countries had little say in the WTO negotiations on (financial) services : US and UK/EU Financial industry demands to make more profits abroad

→ WTO & FTA rules are restricting regulations' and guaranteeing open markets

→ no guarantee of sufficient supervision & regulation

→ foreign financial sector can take over 100% → prohibition to restrict capital flows

"*The econometric evidence suggests that more liberal commitments [in financial services] may be associated with greater vulnerability to currency and banking cris*es." N. Valckx, **WTO Financial Services Liberalization: Measurement, Choice and Impact on Financial Stability, De Nederlandsche Bank,** *Research Memorandum WO no 705, October 2002*

GATS Article XII: Restrictions to safeguard the balance of payments

- In the event of serious balance-of-payments and external financial difficulties or threat thereof, a Member may adopt or maintain restrictions on liberalised trade in services, including on related payments or transfers
- Many conditions apply, incl.:
  - Not discriminatory
  - Consistent with IMF Articles of Agreement
  - Avoid unnecessary damage
  - Be temporary
- Consultations to take place at WTO, based on findings by the IMF on balance of payments etc.

GATS Article XI: Payments and Transfers

- Member shall not apply restrictions on international transfers and payments for current transactions relating to its specific commitments (e.g. in financial services)

- Exchange actions are allowed when in conformity with the Articles of Agreement, but still consistent with its specific commitments, except under Article XII or at the request of the IMF

Problems of EU capital movement regime

- No restrictions on outflows cf. QE
- Freedom of investors to decide on inflows and outflows
- No distinction between capital flows for FDI and trade, and speculative
- No coordination with central banks and financial market authorities of EMEs and other developing countries
- Inflows into EMEs are not always related to national macro-economic policies and status: capital controls cannot be last resort.

Dynamics of Western financial services industry (FSI) in developing countries

= presence of different financial actors & products/services:

- more integration in global financial markets
- M&A and ‘unfair’ competition that side-lines the (development of) domestic & local FSI
- market expansion strategies = risky lending and activities, targeting rich & ignoring the poor & rural areas
- profit goes abroad and domestic wealth is invested abroad
- more vulnerable to non-domestic volatility and crises

= Profit oriented instead of development oriented finance

In the eye of the storm: how?

- QE: to support the W financial sector

→ loans and investment to the S where profits are higher due to lack of capital controls

- presence of W financial sector e.g. TBTF banks, etc.

→ allows W investors to invest in (very short term) developing country stock exchanges, government & corporate bonds, derivatives markets

- Investment funds with bonds and shares on S corporations (+ derivatives to hedge currency risk etc.) cf. financing of S palm oil conglomerates

→ W individual investors profit from S companies

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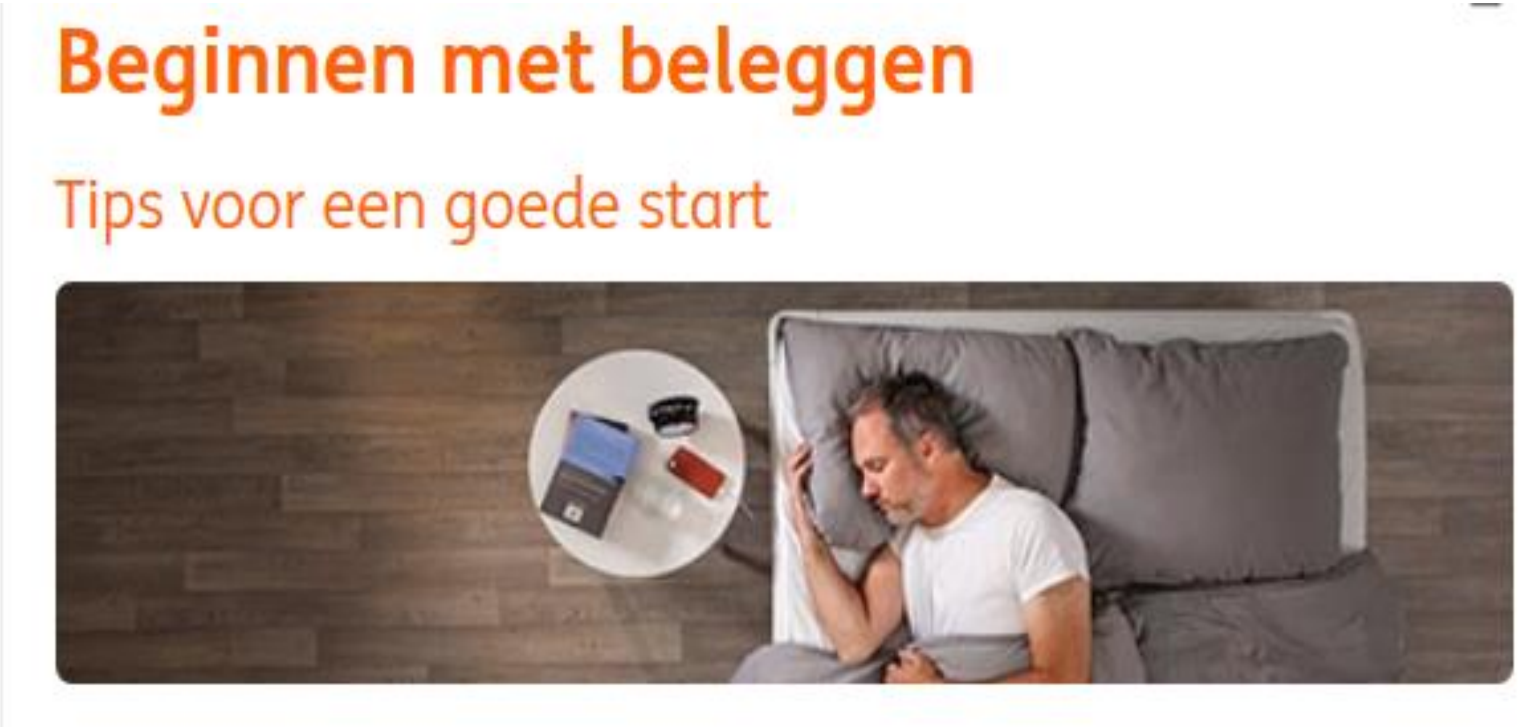
Storm for whom?

→ W individual investors profit from S companies
→ without assessment of social & environmental impact



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Lack of financial reforms

- W reforms with no say by developing countries

→ still TBTF banks, no obligation to finance /invest with sustainability and development impact, too many speculators with weak regulations, too short term investments, weak limits on speculating with derivatives on (food) commodity prices

- W : reforms not in VN (Stiglitz report, 2009)

→ non-binding reforms in G20, Financial Stability Board (FSB), OECD, IMF (FSAP) where majority of developing countries are excluded, B20

Change at international level?

- G20, FSB, Finance for Development, COP, etc.:

→ increase citizens voices (NB: C20 vs B20)

→ join global/S-N platform on financial system to raise S perspective

→ Promote: capital controls, further regulation = damage control

→ argue that finance should serve only people and planet

Looking forward to the debate!

Contact: mvanderstichele@somo.nl

ANNEXES

EU FTAs exceptions on capital free movement

- Only in “exceptional” circumstances, when payments and capital movements (threaten to) cause “serious difficulties” for exchange rate and monetary policy
- EU- South Korea, Art. 8.4:

  can measures be taken to limit capital movements that are ‘strictly necessary’ and for not more than six months: with very detailed description of conditions.
- EU - Colombia and Peru FTA, Art. 170: without being protectionist:
  - Colombia can adopt safeguard measures regarding capital movements for not more than one year (and unilateral extension possible)
  - Peru or the EU state can adopt safeguard measures regarding capital movements for not more than one year (extension only after coordination etc.).

GATS Art. XVI/FTA articles: Market access

- When liberalisation commitments are made, WTO Members shall not maintain or adopt:
  - 2.(b): limitations on the total value of service transactions or assets in the form of numerical quotas or the requirement of an economic needs test;
  - 2. (f) limitations on the participation of foreign capital in terms of maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment.

- Exceptions possible: in the liberalisation commitment schedules of GATS
- EU demands in GATS/FTA negotiations: eliminate (half of) Chile's inv. tax, Thai coming onshore prohibition

GATS Art. XVI :
Market Access in services, footnote 8

- If a WTO Member undertakes a market-access commitment in freedom of cross-border trade in services (mode 1) and if the cross-border movement of capital is an essential part of the service itself, that Member is thereby committed to allow such movement of capital.

- If a Member undertakes a market-access commitment in liberalising investment in foreign services (mode 3), it is thereby committed to allow related transfers of capital *into* its territory.

EU exports Lisbon treaty/TFEU

- Art. 63: no restriction on movement of capital between EU countries and with third countries
- Art. Art. 65(1b): Exception: Member States have the right…to take measures which are justified on grounds of “public policy or public security."
- Art. 66: Where, in exceptional circumstances, movements of capital to or from third countries cause, or threaten to cause, serious difficulties for the operation of economic and monetary union, the Council, on a proposal from the Commission and after consulting the European Central Bank, may take safeguard measures with regard to third countries for a period not exceeding six months if such measures are strictly necessary.

cf. Cyprus

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