Global Financial System
Yesterday, today and tomorrow

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Outline

- A panoramic view of the global financial system with emphasis on the emerging markets – the permanence of change!
- What tomorrow looks like.
- Questions & Reflections.
GFS - A complex, interconnected system involving billions of people across 195 nations of the world

Learning objectives

- Understanding the **financial ecosystem as an integral part of the global economy** (Desai, 2019) - Treasurers, strategists, financial managers of firms, government and investors as key operators within a large and complex financial system.

- Evolution and emerging dynamics of global FMIs which has high impact on the availability of **financial options and outcomes of investment decision-making processes**.

- Implications for the **emerging markets** – impact of the pandemic, technology changes, globalism vs. nationalism in combat.
Some key words…

- **Global financial system (GFS)**
- Financial markets, money markets, capital markets, FX, insurance industry,
- Financial institutions, global institutions, globalisation, globalism, international trade, gold standard, IMF, WTO, WB/IFC, New Development Bank, Islamic Development Bank, Asian Development Bank, Asian Infrastructure Investment Bank
- Investment banking, private equity, PPP, Privatisation, REITS, Pension Funds
- Derivatives, securitization, cryptocurrencies (Bitcoin)
- Bonds, equities, hybrids, share valuation
- Sovereign debts, Sovereign debts, QE
- Market regulation, financial inclusion, Anti-money laundering
“Health is Wealth” – in the past, now, & for the post-COVID-19 pandemic economy

• Sustainable GFS is really about Life and Livelihood - sustaining People, Planet, and Profit (PPP) with the right balance to meet the needs of future generations.
Basic financial system...

Financial system

Central Banking / Monetary Policy

Capital Market Authority

Financial Institutions

Financial Markets
Investment banking system / SBUs

- Debt Capital Market
- Equities Capital Market
- Structured Trade Finance
Investment banking system / 2

Investment Banking

- Asset Management
- Stock Broking
- Private Equity
- Alternative Financing
Financial Market....

- Physical vs. financial markets
- Money market vs. Capital market
- Short-term vs. long-term
- Debt / Equity / Derivatives
- Primary market vs. Secondary market

- Public vs. Private
- Retail vs. Institutional markets
- Spot vs. futures markets
- UBs / CBs / IBs / MFBs / MBs / Discount houses / other specialized financial institutions, customers, investors & market regulators
- Domestic markets vs. International markets
Financial Market / 2.... A key tool for economic development

1. Savings mobilization –
2. Investment
3. National Growth
4. Entrepreneurship growth
5. Industrial development

❖ Wealth-creation
❖ Capital formation
❖ Sale mechanism
❖ Productive usage of funds

❖ The raising of capital (capital markets)
❖ The transfer of liquidity (money markets)
❖ The transfer of risks (insurance and derivative markets)
❖ Price discovery
❖ Global transactions with integration of financial markets
❖ Facilitating international trade (currency markets)
❖ Information
Financial market / 3 - a marketplace of ideas
(Desai, 2019)

- **Public market** – stock exchanges
  - **Bond market** + securitization
  - **Stock market** – common stocks, preferred stock; companies, CEOs, CFOs, **ideas**, Investment relations officers, returns
- **Other markets** – derivatives, futures exchange, foreign exchange, real estate
- **OTC** – forwards, options, spot market, swaps
- **Trading participants** – regulators, clearing house, others; e.g. pension funds, mutual funds, hedge funds, endowment funds, sovereign wealth funds, households/savers, capital, **ideas**
  - **Analysts** – (Buy-side – institutional investors)/ (Sell-side – investment banks, broker-dealers), salespeople, Bankers – stockholdings, compensation, financing, M&A/advisory services, rankings, **ideas**
  - **Media** – reputation, efficient market hypothesis, **ideas**
Global stock markets – the “giants”…
Size is in the eye of the beholder!

<table>
<thead>
<tr>
<th>Company</th>
<th>Description</th>
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<tbody>
<tr>
<td>Walmart</td>
<td>11,000+ stores in 27 countries</td>
</tr>
<tr>
<td>ICBC</td>
<td>150 million customers; $4 trillion in assets</td>
</tr>
<tr>
<td>Facebook</td>
<td>2.5 billion users</td>
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A dynamic (going up and down or stagnating) market indicator reflecting the performance of 30 large, US-listed companies (blue-chip firms)

- The Black Tuesday, July 8, 1932 – crashed to 41.22 eroding 33 years of gains in just 3 years
- Black Monday, October 19, 1987
- Attained the record 30,000 points on 24 November 2020, on the back of various good health (multiple coronavirus vaccine prospects) and political news (Joe Biden Presidential transition approval), etc.

Other indexes: S&P 500
- Nasdaq Composite
- Russell 2000 (RUT)
- NYSE

The “monopolists” – The Big 3 $15 tn Fund Industry – BlackRock (BLK), Vanguard *State Street (STT)
Some countries (e.g. Norway, Hong Kong, Germany, Russia) have one consolidated agency that regulates all financial institutions.

Others, e.g. the US have separate agencies for different types of institutions such as banks, insurance companies and brokers.

- US Federal Reserve
- **Central Bank of Oman (CBO)**
- Bank of Japan
- Peoples Bank of China
- Bank of England
- Swiss National Bank
- Deutsche Bundesbank
- Central Bank of Brazil
- Bank of Canada
- Reserve Bank of Australia
- **Reserve Bank of India (RBI)**
- Bank of France – Banque de France
- South Africa reserve Bank, etc.
Oman’s advantageous geographical location great for global trade [https://www.nationsonline.org/oneworld/map/oman-map.htm]
Strategic objectives

- The Central Bank of Oman (CBO) adopting a sound licensing policy - setting proactive prudential regulations and supervision, set proactively, as means to maintain monetary and financial stability.
- Sustainable development - contributing to the growth and enhancement of the Sultanate’s image and reputation – Oman Vision 2040...
- Evidence-based establishment of linkages and evolve a suitable model for the behavior of the financial system – via the study of macroeconomic and sectoral dynamics in conjunction with financial soundness indicators and external developments.

Structure

- Conventional + Islamic banks
- Finance and leasing companies,
- Money exchange establishments,
- Investment/ brokerage companies,
- Insurance companies
- Pension funds.

Entities, coming under the jurisdiction of the CBO, are banks, finance and leasing companies and money exchange companies licensed by it.

- Seven local commercial banks, 2 specialized banks 6 finance and leasing companies, 16 money exchange establishments
- Nine foreign banks (with 470 local branches and five overseas branches and representative offices)
The Financial System...e.g. the Omani context/2

- Capital Market Authority (CMA) since 1998/99
- CMA regulates & supervises the capital market + the insurance sectors in the Sultanate
- Focused on diversification of products & maximise investors confidence & building the right environment for capital investment.

- Muscat Securities Market
- Muscat Clearing & Depository Company (MCDC)
- Companies operating in the field of securities
- Public-listed companies
- Insurance companies
- Brokers & agents
- Audit firms accredited by the CMA
The Financial System...e.g. the Nigerian context

- Financial Policy & Regulation - MPC
- Banking Supervision

- Other Financial Institutions Supervision Department
- Consumer Protection Department
The Financial System...e.g. the Nigerian context/2

Note “Financial Institutions” under the MLA, 2011 (Section 24)

- Banks, body association or group of persons, whether corporate or incorporate which carries on the business of:
  - Investment and securities
  - Discount house
  - Insurance institutions
  - Debt factoring and conversion firms.

- Bureau de change
- Finance company
- Money brokerage firms involved in factoring, project financing, equipment leasing, debt administration, fund management, private ledger service, investment management, LPO financing, export finance, project consultancy, financial consultancy, pension funds management
Money Laundering (Prohibition) Act, (MLA) 2011 – Salient Aspects

- Makes comprehensive provisions to prohibit the financing of terrorism, the laundering of the proceeds of a crime, or an illegal act.
- Limitation to make or accept cash payment – N5 million for individual; N10 million for a body corporate (Section 1); $10,000 funds, negotiable instruments, or securities.
- Duty to report contraventions to CBN and SEC within 7 days from the date of the transaction.
- KYC - Proper identification of customers
- Special surveillance on certain transactions
- Prohibition of numbered or anonymous accounts (section 11)
- Preservation of records for at least 5 years after closure of the account (Section 7)

Designated Non-FIs

- Dealers in Jewelry, Cars and luxury goods
- Chartered Accountants, Audit Firms and Tax Consultants
- Clearing and Settlement Companies
- Legal Practitioners
- Hotels, Casinos
- Supermarkets
Share valuation

- Professionally handled by the Issuing House in consultation with associated professionals.
- Overpricing is as bad as underpricing
- **Two major criteria**: NAV and Sustainable / maintainable annual profit basis
4.7 Trn Euros Global insurance industry…
(McKinsey & Company)

- **Life Insurance**
- **Health Insurance**
- **P&C Insurance**

Emerging markets contributed 43% of the growth between 2010 and 2017.

- **Europe** – Axa, Prudential etc.
- **South Africa** – Sanlam, Old Mutual, Liberty & MMI
- **Ghana** – Enterprise, Express Life Insurance
- **Rwanda** – Soras Group
- **Kenya** – Shield Insurance
- **Reinsurers** – Africa Re, Continental Reinsurance, etc.
Other key aspects ....

- Microfinance models
- The two main mechanisms for the delivery of financial services to such clients:
  - relationship-based banking for individual entrepreneurs and small businesses; and
  - Group-based models

- FX market
- International Monetary Transfer Service Operators . e.g. WU, M/Gram.
- Mortgages
- REITs / PPP / Privatization schemes
- Financial inclusion, crowd funding
- Pension funds, Mutual Funds
- Sovereign debts/QE
- Green Banking
- Pension funds
Financial Services

- Financial Inclusion Perspective (Global Index, 2014)

- Savings
- Credit
- Payments
- Risk Management
Islamic finance industry – a fast-growing $2 tn global industry

- Has increased net profit of 20%
- Average ROA of 1.9%
- Margins generally wider than the conventional banking & finance; leveraging technology to achieve good cost-to-income ratio.

Selected top players – the likes of Kuwait Finance House, Samba Financial group; Abu Dhabi Islamic Bank in Egypt; Maybank Islamic Berhad (Malaysia & Singapore); Jaiz Bank (Nigeria); Bank Nizwa (Oman); Amana Bank (Sri Lanka); HBZ Bank (South Africa); Emirates Islamic Bank (UAE)
Global Islamic Financial system...

- Islamic banks make a profit through equity participation - requires a borrower to give the bank *a share in their profits rather paying interest.*

**Omani context** - authorized Islamic Banking in 2012, when the CBO started licensing Islamic Banking Entities

- Two full-fledged/ local Islamic Banks
- Six Islamic Banking Windows of six local commercial banks – in all having 70 dedicated Islamic Banking - individual branches.

**Key drivers**

- *Increasing awareness and demand for Shari’a-compliant products*, not only from financiers in the Middle East and other Islamic countries, but also by investors worldwide.
- *Easier access* to Islamic Banking services – e.g. allowing a dual banking system, under which Islamic Banking co-exists with conventional banking globally, particularly in the GCC, South-East and South Asia (which is home to over 50% of the total Islamic Banking industry)
- *Offering a wide range of financial products*, notably, personal banking, insurance and capital market investments.
Global Islamic Financial system...more drivers/2

- **Global mobility/international talent** - Increasing demand from many Muslim communities (including Muslim immigrants to western countries);

- **Oil wealth** in GCC countries

- **Non-Muslim investors** seeking 'ethical' investments and banking practices – finding Shari'a-compliant financial services attractive

- **CSR opportunities**
  - Shareholders
  - Depositors
  - Zakat (the needy)
  - Microfinance products
Islamic banking as ethical business...

- Avoids all the prohibited activities such as
  - **Riba** (usury-interest),
  - **Gharar** (uncertainty),
  - Financing of **haram** (forbidden) trades & businesses like alcoholic beverages, pornography, gambling, etc.

Basic principles

- Absence of interest-based (**Riba**) transactions
- Avoidance of economic activities involving oppression (**Dhulm**) and speculation (**Gharar**)
- Avoidance of speculative activities (**Qimar**)
- Discouraging production of goods and services which contradict the injunctions of Islam (**Haram**)
Global Institutions....

*UFPCFC
*The IMF
*The World Bank / IFC
* The WTO
“Institutions”… beyond the rules of the game

Market Regulation

Preventive

Protective

Supportive
Financial system regulation ...

How much is much!?

- Public interest
- The importance of financial intermediation
- Protecting consumers and depositors
- Enhancing efficiency of the financial system

- Keeping with the pace of financial innovation
- Guiding against micro- and macro-systemic risk and contagion
- Mitigating externalities from financial system failure
- Financial Institutions’ access to the public safety net – ‘too many’ or ‘too big’ to fail.
Market Regulation
...Perspectives from the USA

- Dodd-Frank Wall Street reform
- Consumer Protection Act passed in 2010

- Bank of America reportedly asked to pay a record $16.65bn fine to settle allegations that it knowingly sold toxic mortgages to investors [www.time.com – Aug. 21, 2014]

- US sub-prime mortgage crisis in 2007
“No organization is more crucial to the stability of the global economy than the International Monetary Fund.”

- Janet Yellen (The US Former Federal Reserve Board Chair)
- (Time, May 2/ May 9, 2016, p. 66)
The IFC (2020) – creating markets, supporting growth & driving sustainability across the globe...

<table>
<thead>
<tr>
<th>Country</th>
<th>Initiative</th>
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<tbody>
<tr>
<td>Afghanistan</td>
<td>Energy Security</td>
</tr>
<tr>
<td>India</td>
<td>E-access to healthcare during the pandemic</td>
</tr>
<tr>
<td>Indonesia</td>
<td>First ever gender bond</td>
</tr>
<tr>
<td>Brazil</td>
<td>A woman entrepreneur’s recipe for launching a market for allergen-free foods</td>
</tr>
<tr>
<td>Solomon Islands</td>
<td>Going green in the blue Pacific Ocean</td>
</tr>
<tr>
<td>Mali</td>
<td>Production of local quicklime</td>
</tr>
<tr>
<td>West Bank &amp; Gaza</td>
<td>$32 m project boosting learning through solar power – 500 schools</td>
</tr>
<tr>
<td>Kenya</td>
<td>Supporting small businesses to withstand Covid-19</td>
</tr>
<tr>
<td>Serbia, Columbia, El Salvador</td>
<td>Cleaning up of Europe’s largest landfills, empowering future finance leaders, &amp; lowering cost of electricity for business growth</td>
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Paris Club & London Club

- **Paris Club** – 19-member industrialised countries including the US, UK, Germany, France, Canada, Australia, etc.
  - Guarantees export activities of their nationals via their official export credit agencies.
  - Default by recipient nation’s government to pay the FX equivalent of the domestic currency becomes government debt owed to creditor nations.

- **London Club** – mostly a private sector-based creditors institution – commercial banks mostly in industrialised countries.
  - Mainly uninsured and unguaranteed debts extended by their commercial banks to nationals of debtor nations.
Uniform Framework for Preventing & Combating Fraud & Corruption (UFPCFC)

- February 18, 2006 – Establishment of Joint International Financial Institutions (IFIs) **Anti-Corruption Task Force**
- **Founding members** – AfDB Group, ADB, European Bank for Reconstruction & Development, EIB Group, IMF, Inter-American Development Bank Group, & The World Bank Group
- **Aim**: Consistent & harmonized approach to combating corruption in the activities & operations of member institutions

**Aspects:**

i. Definitions of fraudulent & corrupt practices
ii. Principles & guidelines for investigations

iii. **Exchange of information**
iv. Integrity due diligence policy
v. Mutual recognition of enforcement actions
vi. Support for anti-corruption efforts of member countries
The US & Asia in top share of the world’s $280 trillion total wealth (2017 Credit Suisse Report)

- US: 38%
- Asia: 50%
- Rest of the
“Today”
Approx. 35% decline in oil prices has impacted on the oil-dependent economies

Will innovative **aviation finance** be able to rescue a sector that the pandemic has brought to its knees?

- $510 billion in lost sales
- Will lose $157 billion in profit
- Cuts tens of thousands of jobs
- Passenger volume fell by a whopping 60% to 1.8 billion from 4.5 bn pre-pandemic
- Sector will see some rebound in 2021? (see opposite graph)
Sources of uncertainty…

(IMF, 2020)

- Climate change
- Technology and automation of jobs, FinTech and rise of digital currencies
- Lower returns on savings
- Rising inequality & debt

- Global regulatory responses/concerns - $12 tn fiscal actions; $7.5 tn monetary actions, financial sector surveillance, risks and vulnerabilities, enhancing lending toolkits for inclusiveness
Unemployment rate % impact of Coronavirus 2019-20: Why is the situation somewhat different in India? (The Economist, Nov. 2019 & 2020 issues)
“Tomorrow”
Jeff Bezos could be world's first trillionaire by 2026. Mukesh Ambani, Jack Ma to follow?

Photo credits: Wikipedia & Gulf News
“America is Back” – President elect Joe Biden of the US

• Greater ‘openness’ and transparency
• Climate Change - protecting the “Earth” - Norway’s International Climate & Forest Initiative (NICFI) Forestry Investing (Doyle, 2020)
• Return to “normality”? A couple of economies are projected to rebound in 2021 – e.g. Oman, Kenya.
• Revamping the Dodd-Frank – 2010 wall Street reform law
• Dealing with US-China trade wars
• Russia-Saudi Arabia Oil price war
• REITs $3.5 trillion global market in 35 countries + all G7 countries - but watch interest rate.
  ❑ Pre-mature Covid-19 aid withdrawal – the G20’s Debt Service Suspension Initiative
  ❑ Fear of no-deal Brexit
  ❑ Solvency & debt sustainability (in the wake of explosion in public debt)
Tomorrow's products, people & authority!
(Harari, 2017; Brad Smith – President of Microsoft, 2019, Watson, 2012; Piketty, 2014)

- **Sweeping digital transformation**
  
  “Don’t ask what computers can do, ask what they should do.”

  - Brad Smith

- **US-China relations** – A bipolar tech world, the geopolitics of technology

- **Technology and public safety**: “I’d rather be a loser than a liar”

- **Cybersecurity** – the global wake-up call.

- **Ubiquitous surveillance**

- **Digital democracy (open data revolution) – Economic inequality**

- **Next generation transport**

- **Resource depletion – beyond fossil fuels – precision agriculture**

- **Internet of things – AI – brain-machine interfaces - transhumanism**

- **Medical data mining, remote monitoring – user-generated medicine**

- **Dematerialisation – What & where is work? “Working at home of home at work?”**

- **Solar energy – alien intelligence – Moon mining**

- **Future shock** (Kaplan et al, 2020)
**Bye-bye to...??**

- TVWs – Textiles, Vehicles & weapons
- Industrial Revolution working class
- “Democracy” and “the free market” as the likes of Google and Facebook “know us better than we know ourselves”

**Welcome to...??**

- BBMs - Bodies, Brains & Minds
- “…the next big revolution will create the useless class” (emphasis is mine)
- “The way humans have treated animals is a good indicator for how upgraded humans will treat us”
- Shifted authority “from individual humans networked algorithms”.
- The “marriage” of humans with machines
Isn’t it worth restating? “Health is Wealth” – now, & for the post-COVID-19 pandemic economy

• Sustainable GFS is really about Life and Livelihood - sustaining People, Planet, and Profit (PPP) with the right balance to meet the needs of future generations.
“Never let the future disturb you. You will meet it, if you have to, with same weapons of reason which today arm you against the present.”

- Marcus Aurelius (AD121-180)

“Recommendations of the style “Do not do” are more robust empirically.”

“…success consists mainly in avoiding losses, not trying to derive profits”

“Do not confuse absence of volatility with absence of risk.”

- Nassim Nicholas Taleb
Thank you
Q & R
Questions & Reflections…

- Corporate governance & banking reforms: Are bankers paid too much? Risk vs. return / sector’s real contribution to the People, Planet vs. Profit?
  - How could banks reform themselves? Building business vs. purely chasing returns?
  - Women-dominated boards vs. men-dominated boards?
  - How could other stakeholders reform the banks?

- Why is a Tesla “booming” with 500,000 deliveries while a struggling Toyota is selling 9.4 million vehicles?

- What could “America is back” mean to the GFS?

- How to sustainably finance Oman’s Vision 2040? (Non-oil expected to grow to more than 90% of the GDP)

- What are the key drivers of Islamic finance’s growth?

- What could be the way forward for Financial Research & Innovation? – e.g. applications of ML, AI & Big Data Analytics (e.g. the Saudi’s $20 bn AI investment plan by 2030 is worthy of emulation)
References & Further Readings

References & Further Readings / 2


References & Further Readings

- [https://en.m.wikipedia.org/wiki/Closing_milestones_of_the_Dow_Jones_Industrial_Average](https://en.m.wikipedia.org/wiki/Closing_milestones_of_the_Dow_Jones_Industrial_Average)
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