

Letters on financial services liberalisation to the Financial Times

(published and unpublished, in chronological order)

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19 October 2008

Sir,

The calls from Britain's prime Minister Mr Brown that a 'Bretton Woods II' conference should also finalise the Doha Round of trade negotiations at the WTO (FT 16 October, "Leaders back call for 'Bretton Woods II' summit), is worrying for many reasons. First, all political will needs to focus on reorganising international financial regulation and supervision that confines the financial industry. So far, a major political problem has been industrialized countries' unwillingness to accept international surveillance, and to implement existing international standards or even EU directives. Secondly, the Doha Round is to include important further liberalisation of financial services in the GATS negotiations. However, the financial crisis is due to international liberalisation of financial services before proper regulation and liberalisation was in place, resulting for instance in banks that are too big to fail, and problems like Icesave of the collapsed Landsbanki. There should be a tested system of proper international regulation and supervision before any new financial services liberalisation takes places. Thirdly, an international financial reorganisation also needs to include much more mechanisms to finance sustainable development world wide and investments that prevent climate change - a new and urgent task.

One should not forget that the Havana Charter of 1948 designed a more comprehensive international architecture of trade and included competition policy, employment objectives and fair labour standards, economic development support and prevention of 'pronounced' fluctuations of commodity price – all of which were rejected by the US. The current trade architecture also needs reform since free trade among unequals has become unfair and unsustainable. A Doha round deal based on the current negotiation proposals on the table in Geneva will not do that job, and should not be rushed.

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18 August 2008

Reform needed before more liberalisation in the financial sector

Sir,

The correspondence between Sir Stephen Wright and John Cooke (22 July), Kavaljit Singh (July 29, 6 August) and Roger Brown (5 August) misses an important point, which is also lacking in the current discussions about the reform of the financial system after the sub-prime crisis emerged. The WTO negotiations to open up markets in financial services are mostly about deregulation, which are incorporated in the rules of the WTO services agreement (GATS) and the negotiation 'requests' for liberalisation. For instance, during the GATS negotiations the EU has requested, based on demands from the financial industry, to eliminate many national prudential regulations some of which are now proposed in the financial reforms (e.g. regarding adequate capital reserves).

In a statement of 14 August 2008 (1), the International Chamber of Commerce (ICC) states that the still ongoing WTO negotiations should not be concluded without liberalisation of financial services and that the current crisis in the financial sector should not stand in the way to do so. Although the ICC recognizes the need for better (self)regulation and more phased liberalisation in developing countries, it only calls for technical assistance from donor countries. However, the lack of coordination at international level between liberalisation on the one hand and reforms/regulation at the other, is a key problem in the financial sector that needs to be tackled before the WTO can push forward with liberalisation of financial services. At a time that it is recognized that self-regulation of the financial markets and the financial services industry has not been working, it would be inappropriate for the WTO to allow the financial industry to spread their risky products and risky behaviour without new regulation to be in place.

In addition, the current reform proposals on the financial system need further discussion. For instance, they do not take into account the need for better access by the poor, farmers (to fight the food crisis) and SMEs. This lack of access is recognized amongst others in studies by the World Bank, IMF and the UN who see the need to find solutions beyond micro-finance. The sub-prime crisis shows that even if the banks serve the poor, in casu poor American households, they do not always do so responsibly. Also, regulatory reforms should promote lending and investment practices that promote environmentally friendly production, trade and consumption in order to match the challenge from climate change.

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Note to the editor:

(1) Financial services liberalization must be part of any Doha Development Round deal - Statement by the Chair of the Commission on Financial Services and Insurance, <http://www.iccwbo.org/uploadedFiles/ICC/policy/financial_services/pages/196%20Doha%20Round%20Deal%20Statement%20by%20the%20Chair%20of%20the%20FSI%20Commission.pdf>

NOT PUBLISHED
10 August 2008

More reform needed before more liberalisation in the financial sector

Sir,

The correspondence between Sir Stephen Wright and John Cooke (22 July), Kavaljit Singh (July 29, 6 August) and Roger Brown (5 August) misses an important point, which is also lacking in the current discussions about the reform of the financial system after the subprime crisis emerged. The WTO negotiations to open up markets in financial services are mostly about deregulation, which are incorporated in the rules of the WTO services agreement (GATS) and the negotiation requests for liberalisation. For instance, GATS Art. XVI note 8 demands that countries that allow the establishment of a (financial) service sector can no longer limit capital inflows related to that (financial) service. An insight in the EU requests, which are clearly based on demands from the financial industry (1), during the GATS negotiations shows that the EU wants many national prudential regulations to be eliminated (e.g. eliminate regulations that limit the operations of hedge funds), some of which are now proposed in the financial reforms (e.g. to hold better capital reserves). The sub-prime crisis made many recognize that the self-healing power of the financial markets -in which the financial services industry plays an important role- is not working and that

new financial regulations need to be in place. As long as such reforms are not in place, it would be inappropriate to allow the financial industry to spread their risky products and risky behaviour, which were very much encouraged by international competition that is promoted by WTO/GATS liberalisation.

The current proposals to reform the financial system do not take into account the need for better access by the poor, farmers (to fight the food crisis) and SMEs. The lack of access is more and more recognized amongst others in studies by the World Bank, IMF and UNCTAD. The UN Department of Economic and Social Affairs and the UN Capital Fund even have a special programme on inclusive Finance (2) to find solutions beyond micro-finance and to improve access by the poor to regular banking. The subprime crisis shows that even if the banks serve the poor, in casu poor American households, they do not always do so responsibly. In addition, the discussions and instruments to improve lending and investment that promote environmentally friendly production, trade and consumption, are still far from sufficient to match the challenge from climate change and environmental degradation.

So, even the current reform proposals on the financial system need further discussion. The lack of coordination at international level between liberalisation on the one hand and reforms/regulation at the other, is a key problem in the financial sector that needs to be tackled before the WTO can push forward with liberalisation of financial services.(3)

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10 August 2008

Note to the editor:

(1) Some EU requests (negotiation documents) mention "EU industry raises this issue"

(2) see for instance: <http://www.unctf.org/english/microfinance/pubs/bluebook/>

(3) See article by M. Vander Stichele on these issues "Ignoring the Crises? How Further GATS Liberalisation Impacts the Financial and Food Crises", in South Bulletin: Reflections and Foresights (Issue 16, 01 June 2008), p. 7

(http://www.southcentre.org/index.php?option=com_content&task=view&id=637&Itemid=105)

**PUBLISHED : From letters page of FT.
22 July 2008**

Give priority to financial services

From Sir Stephen Wright and Mr John Cooke.

Sir, Ministers from some 40 countries are meeting in Geneva to decide the fate of the Doha round of multilateral trade talks. It is vital that they achieve a breakthrough, and lay the foundation for a lasting agreement.

The Doha round offers a unique opportunity to address the barriers to global trade that continue to hold back the world economy. This would bring benefits to developed and developing countries alike, and would offer some palliative to the bleak prospects facing the global economy.

The focus of the negotiations so far has been on agriculture and the tariff barriers to trade in manufactured goods. These are undoubtedly important, and need to be addressed. But the services sector, which has received far less attention, comprises more than 70 per cent of gross

domestic product in most Organisation for Economic Co-operation and Development countries, and a rapidly rising share of economic activity in emerging markets. It is essential, for all countries, that the Doha round enables a substantial liberalisation of trade in services, including financial services.

The development gains would be considerable. Businesses at every level in emerging markets need easier access to capital in order to enable the sustainable rates of growth and wealth creation that will address poverty over the long term. They also need modern tools to manage risk and plan for the future. Their governments need help to secure the investment in infrastructure that will be the key to the development of their economies.

What is good for development is also good for the UK economy. The financial services sector accounts for more than 10 per cent of UK GDP, generating substantial revenue and employment. Greater opportunities for UK financial services suppliers to access markets overseas will translate into real gains for the UK economy. Furthermore, Britain's continued pre-eminence as the international financial marketplace of choice is a key asset for the whole European Union. Research indicates that access to the UK financial services hub creates €33bn a year of value for our European partners.

For all of these reasons we urge Peter Mandelson, as the EU's negotiator in Geneva, to give high priority to securing a real breakthrough on trade in services. There are still far too many barriers to investment, restrictions on market access, and regulatory burdens in too many of our trading partners. All too often these restrictions do more to shelter domestic incumbents than to benefit local people. The prize from dismantling them is great, if ministers will grasp it.

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29 July 2008

Entry of big foreign banks has not widened access to include India's poor

From Mr Kavaljit Singh.

Sir, Stephen Wright and John Cooke (Letters, July 22) strongly advocate the liberalisation of trade in financial services under the Doha round. However, developmental gains from such liberalisation are highly debatable. In the case of India, the entry of foreign banks has not widened the access of banking services in the country.

Of a total 602 districts in India, nearly two-thirds (391) have inadequate banking cover. Banks are reluctant to open branches in "under-banked" regions because of concerns over meeting profitability criteria. According to the Reserve Bank of India, of 933 bank branches opened during between June 2005 and July 2006, just two were opened in under-banked areas. Recent studies have pointed out that 72 per cent of Indian farmers have no access to the formal banking system. One of the important factors behind rising farmer suicides in the countryside is lack of access to cheap credit from banks and institutional sources. The traditional moneylender faces no competition in rural banking markets.

On the other hand, there has been a sharp rise in foreign and domestic big banks lending to risky and speculative businesses such as commercial real estate, derivatives trading and commodities.

In terms of providing banking services and products, foreign banks typically have a bias towards wealthy customers.

The question must be asked: Are big foreign banks going to serve the 500m Indian citizens with no access to banking services? Also, do big foreign banks have the requisite expertise to provide banking services to poor farmers, landless labourers and the urban poor?

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5 August 2008

Further liberalisation can widen Indian bank system

From Mr Roger Brown.

Sir, Kavaljit Singh (Letters, July 29) is right to lament the scarcity of banking services to the rural poor in India, but is mistaken in suggesting that liberalisation of financial services cannot be part of the solution. What Mr Singh did not take into account in criticising Sir Stephen Wright and John Cooke (Letters, July 22) is that any foreign banks seeking to cater for the rural poor in India are severely restricted in the number of new branches and teller machines they can open.

On average, only about 15 new branches a year are authorised for all foreign banks for all India. This means foreign banks have been effectively prevented from opening up networks in rural areas to serve small and medium-sized businesses and the unbanked.

A number of British and other foreign banks are already heavily committed to microfinance and other poverty alleviation schemes in India. But they could do a great deal more if Mr Singh and others who favour the development of rural banking pressed for further liberalisation so foreign banks could expand their operations in the regions of India now so little served by existing banking services.

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Indian banks denied market reciprocity

From Mr Kavaljit Singh.

Sir, Roger Brown (Letters, August 5) calls for further liberalisation of financial services to widen access to the Indian banking system. Contrary to popular perception, India has gone beyond existing international commitments to give greater market access to foreign banks. The number of branches permitted each year to foreign banks has been higher than the World Trade Organisation commitments of 12 branches a year.

During July 2006-June 2007, India allowed seven foreign banks to open 20 new branches and an additional seven foreign banks to set up representative offices. One of the key policy issues

determining market access is reciprocity. How much market access are Indian banks getting in return? During 2003-07, India allowed US-based banks to open 19 branches (excluding the off-site teller machines). But, in the same period, the US did not allow a single Indian bank to open a branch or subsidiary or representative office in its territory despite many requests by Indian banks.

Further, there are no restrictions in India on the establishment of non-banking financial subsidiaries by foreign banks. Citigroup and StanChart have successfully used their finance companies to reach out to more parts of the country. Since foreign banks in India are predominantly located in metropolitan and urban areas, they could very well serve poor and low-income people residing in their neighbourhoods. There is no regulatory ban on foreign banks to serve the urban poor. Rather, India's approximately 190m urban poor provide a huge untapped market that could be reached by foreign banks. The potential market size cannot be overlooked given the saturation of retail banking markets in several developed countries. Therefore, it is not the regulatory constraints or the lack of market that is hindering the delivery of banking services by foreign banks but primarily their business model and bias against the poor people in general.

The spread of microfinance institutions (MFIs) in India is welcome but they cannot be a substitute for the formal banking system. With just 15m clients, MFIs have reached only a fraction of the "unbanked" population in India. The penetration of MFIs is highly skewed towards a few southern states. There are several recent instances of aggressive lending by MFIs with negative outcomes.

In 2005, many poor borrowers (mostly women) landed themselves in debt in Andhra Pradesh. For these borrowers, MFIs were no better than traditional moneylenders as they charged exorbitant rates of interest (100 per cent and above). Some MFIs are also believed to have used coercive methods of loan recovery.

So lending by MFIs could also be counter-productive if not properly regulated.

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