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# **BANKING INDUSTRY IN THE GLOBAL MARKET: FOREGROUNDS OF AN EVERLASTING EVOLUTION**

## **Abstract**

*The present financial crisis, starting in the year 2000 with the dot.com bubble break out, lately evolved into something very peculiar and different from any previous historical cyclical turmoil, as considered in our political economy models: Classical, Austrians, Keynesians Monetarist and post Keynesians. Such approaches cannot be seen as appropriate to explain an epochal change in the world economy but simple temporary economic disorders. The new age of turbulence, as Greenspan used to say Greenspan (2007), seems to require a central authority as a regulator of most financial flows and markets and a framework of new rules related to new financial products, new trading rules of markets and financial institutions, mostly banks and trading platforms to pursue the long hoped goal for economic growth in general stability background.*

*Recently, the overlapping prevailing global market has shadowed most local markets and productions, as some low cost Asian Countries industrial production hubs have globally crowded out most western industrial areas.*

## **Key words**

banks, financial, crisis, markets, asymmetries, regulation, Asia.

## **JEL classification Code**

G210

## **1. INTRODUCTION**

Assuming a common general suggestive definition, the present financial and banking market crisis may look like the final effect of an unjustified global deregulation of financial markets, as originated in the USA through the *Depository Institution Deregulation and Monetary Control Act* passed in 1980, the *Garn-St. Germaine Depository Institution Act*, deregulating the *Savings and Loan* industry in 1982, the *Gramm - Leach - Bliley Act 1999*, known also as *Commodity Futures Modernization Act*, a general unleashed control over banks and a widely spread abuse of management compensation through generous stock options programs and common leveraged buy out and take over and by some management recurring misbehaviours.

On the other side, the market collapses in the years 2000, 2007 and 2008 and the last derivative toxic financial bubbles bursts and connected stigma might be seen as the outcome of all worsening economic scenarios or the unexpected final effect of very deep rooted series of mistakes, like a *tsunami* in an inexperienced phase of unrelenting global bubbles.

These events suggested large efforts towards:

1. the reshaping of regulatory agencies, the elimination of the national thrift charters and the promotion of new oversight councils and boards to evaluate systemic and local financial risks;
2. comprehensive regulation of financial markets, including increased transparency of derivatives trading (bringing them onto exchanges) and related banking activity;
3. consumer protection instruments reforms, including a new consumer protection agency and monitoring uniform standards for "plain vanilla" products, as well as strengthened investor protection acts;
4. tools for assessing financial crises, including a "resolution regime" complementing the existing Federal Deposit Insurance Corporation (FDIC) authority to allow for orderly winding down of bankrupt firms, and including a proposal that the Federal Reserve (the "Fed") might receive authorization from the Treasury for extensions of credit in "unusual or exigent circumstances";
5. various measures addressed to implement increasing international standards and cooperation, included in this

section were proposals related to improved accounting and tightened regulation of credit rating agencies.

The pending inflationary risk, linked to the world new financial and monetary quantitative basis expansion, following the 1971 disclaimer of the gold standard, has not actually been offset and sterilized by the productivity and technological innovations, as commonly asserted during the nineties. Most of the times, prices have been under control by the inflow of low cost Eastern labour, competitive growing of quality technological standards and consequent swelling productions, pouring over western markets at low prices. These events have greatly increased trade, monetary transactions and linked contract settlements as well as all capital flows through a new network of large size banking institutions linked to the huge involved risks. Local side banks and banks out of the new Eastern business have developed residual financial side activity, as developed in recent years after a set of deregulatory instruments. Large availability of funds, easy credit, quantitative easing, have set the base of a huge worldwide indebtedness of both public administration and out crowded traditional western industrial facilities setting lower rating for both Countries and banks.

Within these angles a proper financial market adjustment and banks resizing must consider a preliminary necessary fine tuning of worldwide monetary policies, labour costs and standards and a reconsideration of the welfare State frameworks and structures as stratified during the cold war. A strict set of rules related to market instruments and trading specifications alone, without considering the financial intermediaries might not be sufficient. Outside the free market price fixing mechanism there is only room for market abuse and manipulation. The present crisis is so far likely linked to some obsolete asymmetries between the welfare state framework and the modern free world markets, with some unsolved related monetary issues.

President Obama later added the *Volcker Rule* to this proposal in January 2010, the rule, which prohibits depository banks from proprietary trading (similar to the prohibition of combined

investment and commercial banking in the 1930 Glass ó Steagall Act) which was passed only in the Senate bill, and through the conference committee which enacted it in a weakened form that allowed banks to invest up to 3% of their Tier 1 capital in private equity and hedge funds, as well as trade for hedging purposes. My deep belief is that what happened at the end of the last century causing the three bubbles bursts is not strictly related to some specific deregulation or financial institution or authority misconducts or criminal offense, neither to dangerous financial innovation, on the contrary, what happened began in the year 1987 with the Greenspan large credit easing to stop the Dow Jones fall and became a monetary expansion phase which culminated with the technology, denominated *NASDAQ*, index rising from under 1,000 to 5,000 between 1995 and 2000. It was an unavoidable course linked to at least thirty years of monetary instability, contradictory remedies and rising uncontrolled public spending, in a new world of monetary euphoria, growth and prosperity, without any care about the potential consequences of a swelling Keynesian monetary *deficit spending*.

## **2. Economic integrations, competition and cooperation**

### *Present Financial Crisis, origins effects in a local versus global Framework*

As traces of first banking activities are present in the Hammurabi's code, all through any ancient society, even within the French revolution period, and the COMECON clearing agreements, history has shown with strong evidence the ascent of money and banking institutions which seem not to have any alternative in any modern social system based on the external exchange productions, except for the primordial nomadic populations.

Goal of this paper is to verify, even in present days, how the banking and the financial systems may evolve toward new patterns and guidelines, but the economic models cannot disregard the banking industry and its significance, even if deeply changing its profiles and structures and operational procedures.

In the 2008 fall the *Development Committee* of the World Bank meeting, chaired by the Italian Central Bank President Draghi, lately named *Financial Stability Board*, trying to work out some measures aimed to save the collapsing Western Economy, adopted the mission statement:

*“We are concerned by the impact of the turmoil in world financial markets and the continued high prices of fuel and food. We welcomed member countries’ commitment to take comprehensive and cooperative measures to restore financial stability and the orderly functioning of credit markets.”*

The literature emphasis has been focusing on banks, as deemed in their behavior the only determinants forces of present dangers and turmoil, not considering enough the underlying real economy issues, linked to the huge shift of the world financial order from the English speaking world communities to the Asian reemerging Countries, as changed after the monetary disorders following the demission of the gold exchange standard, announced by President Nixon on the 15<sup>th</sup> August 1971, Ferguson (2008).

The lasting turmoil in most world financial markets, called also euphemistically *banking or financial crisis*, has gradually been revealing itself as something definitely new and very different from any previous historical recession or depression as known and as described and studied in our classic and modern economy models: classics, neoclassic, Keynesians<sup>1</sup> and post Keynesians ones Hyman Minsky P, (1964), and, according to this analysis, this may not be just a financial or banking crisis in its real nature, or a global monetary crisis at all, which are simple collateral fallout effects, but the issue here is which are the remedies to such a deep

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<sup>1</sup> HAYMAN MINSKY P., MARCUS WALLENBERG, (1986), PAPERS ON INTERNATIONAL FINANCE, *The Global consequences of financial deregulation*.

discrepancy of work costs and the widening of the global occupation market on a world wide basis and its effects.

The present Western crisis stems out of a worldwide historical scenario and may be connected, in its mostly relevant fundamentals to some unsolved monetary issues as described by Robert Mundel in his delivery speech at his Stockholm Nobel price assignment Mundell, (1999) and to some recent social radical changes, starting with the reforms adopted during the seventies and, first of all, and as a generating determinant factor, first and only issue to be considered from the collapse of the Berlin wall in 1990, when the cold war ended and the global market was subsequently reactivated within a new competition scenario, with new free areas and values.

To better understand the recent events, we must reconsider the 1921 Genoa economic conference, addressed to the restoration of a *gold standard*, plan firmly supported by Ralph Hawtrey but strongly opposed by the young John Maynard Keynes, basically unsuccessful, which failure, according to Mundell, led to the second world war as a main underlying factor towards autarchy, custom barriers and spread worldwide nationalism Keynes, (1920).

The 20th Century's unsolved financial unrest starts with the FED foundation in 1913, enacted to save some major bankers, strong supporters of this project, hoping for a lender of last resort in the aftermath of the 1907 banking crash, and deepens during the first world war huge monetary base financing and during the second world war, two global wars in one single Century, according to Mundell, somehow both strictly related to those unsolved monetary instabilities.

The nineteenth century had shown a long lasting efficient international monetary system, as a result of the Vienna 1815 Congress and the aftermath of the British Empire with the sovereign gold pound prevailing after the Napoleonic wars, when a new world order was globally defined Kissinger (1994).

Such system was primarily based on the *gold standard*, operating under the Hume self adjusting price assumptions, which was unfortunately dissolved in the first World War monetary chaos, and its successive failed restoration attempts which, in the last century twenties and thirties years, might have triggered the great depression, most general national autarchies, the collapse of the world trade and, likely as foreseen in *The economic consequence of the peace*, the second World War Keynes (1920).

The new settlement arrangements and the *summary agreements adopted in July 22, 1944*<sup>21</sup>, at *Bretton Woods*, as defined by the Secretary Mr. Harry Dexter White, definitely disclaimed by Nixon in 1971, relied in a new version of the gold standard, linked to the dollar policies of the Federal Reserve, alongside the simple self-governing discipline of gold itself. When the link to gold was ultimately severed in the seventies, the Federal Reserve System faced the greatest inflation ever in the United States, which spilled out over the rest of the world as unseen since the days of the Secession War, as shown by (Milton Friedman and Anna Schwarz, 1963) in their *Monetary history of United State*. Even so, as the last century was closing, an angle reconsidering its monetary history created an entirely new framework of unresolved issues and questions about some of the advantages of the payment and monetary system with which the century had previously begun.

Last century can be divided into three different phases:

- the first phase, 1900 - 1933, is the story of the international gold standard demise, its breakdown during the war, its failed restoration strives in the 1920's and its termination in the early 1930's;
- the second epoch, 1934 - 1971, starts in the mist of the great depression from the devaluation of the dollar and the establishment of the new \$35 gold price parity in the year 1933, which stops as the United States took the dollar off gold external convertibility for central banks, with the Nixon's announcement in 1971: *"I have directed Secretary Connally to suspend temporarily the convertibility of the*

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<sup>2</sup> <http://www.ibiblio.org/pha/policy/1944/440722a.html>

*American dollar except in amounts and conditions determined to be in the interest of monetary stability and in the best interests of the United States*;

- the third remaining part of the century, 1972 - 1999, is characterized by the consequent unavoidable arrival of the flexible exchange rates system, the subsequent outbreak of massive inflation and stagnation during the 1970's, the huge interest rates volatility, the hedging derivative innovation and the new supply - side economics in the 1980's. Finally, the return to some monetary stability, mostly based on the oil standard and the EMS plan. Since its conception in 1978, the European Monetary System (EMS) as outlined by the Luxembourg Prime Minister Pierre Werner was designed as a framework for monetary policy coordination to overcome the long lasting unsettled turmoil among European and World currencies.

Disillusioned by the uncertain attempts to restore a global monetary reform, likely due to cold war arguments, through the Gold Commission appointed by President Carter and chaired by Donald Reagan in 1982, which minutes were not published, and by the devastating floating exchange rate system, the EMS founding fathers wanted to restore a system of fixed - but - adjustable exchange rates within most of the European Community, which finally brought to the issuance of the Euro at the end of the 1990's.

At Bretton Woods in New Hampshire, the gold reserve problem was eluded by the establishment of the new platform leading to the *gold-exchange standard*, supported by Harry Dexter White, from the U.S. Treasury Department, a necessary compromise between gold supporters and gold contrarians based on the circulation coverage by both gold and dollars. The IMF and the linked gold parities system lived up to its dismissal in August 1971. In that year the *gold standard* was unquestionably and unconditionally definitely abandoned and we entered the present cycle of ever growing financial and monetary turbulences, likely primary precondition to an *oil standard* and to the more or less efficient fine tuning of most of the monetary policies implemented by the issuing Central Banks.

### **3. The present crisis, specific causes and determinants.**

The principal factors affecting the present financial crisis, the banking industry and the financial markets, start in the unpredicted 1987 October exceptional and sudden stock market crash, which leads to the Greenspan appointment at the FED, after an interest rates tightening along Paul Volker era. Greenspan has supported and justified, after expressing some younger point of view stressing the opposite, the loose monetary policy, in a new age dominated by the three following new major features:

- the second unavoidable world wide trade liberalization, which led to the *second globalization*, as collateral effect of the cold war conclusion in 1990 and the fall of the Berlin wall;
- the existing asymmetries in local social, work, taxing and regulatory frameworks and fundamentally asymmetric welfare standards, accounting rules, financial reporting and auditing practices, which eventually promoted the Asian large and sudden industrialization;
- the mass progressive reallocation of most industrial finishing productions on a world wide basis from regional local markets to the Eastern and far Eastern regions, pursuing the final target of a larger critical industrial size through mass production, lowering costs in the global world competition, unquestionably prevailing over a single or minor areas trading approach, NAFTA, EU, ASEAN, EFTA, EU-CARICOM, CIFTA, ALADI and more similar trade agreements.

Just to stress some of these special determinant factors, promoting on a global basis unprecedented fair competition, we outline some Western countries unparalleled costs stemming from tight regulation about:

- labor protection stringent procedures, permanent growing compulsory training, updating requirements and new fiscal reporting duties;

- privacy strict protective widespread rules;
- financial transactions monitoring and reporting costly procedures;
- filings against illegal recycling activities;
- financial auditing and complex filing requirements;
- labor and enrolling preferred compulsory paths;
- unions strict political and social monitoring attitudes;
- labor permanent challenging negotiations;
- unavoidable dismissal rules and labor severance penalties.

Furthermore, the overlapping synergetic global logistic facilities became overcrowded while at same time they were downsizing any local market and production in a new dual market system. The rapidly industrializing hosting Asian countries were globally outperforming all the elsewhere local active producers and had as well self enlarged and rapidly grown on a planetary scope.

The out breaking US trade deficit, alone, jumped from \$65 billion in 1993 to a more than \$700 billion annual average from year 2005 to 2010, about 5 percent of GDP.

Today imports from the *Middle Kingdom*, or *Chinese Empire*, and the petroleum deficit, account for nearly the entire U.S. trade deficit. Chinese and Middle East exporters use their dollar proceeds from growing large trade surpluses to mainly buy U.S. treasuries, real estate and industrial property worldwide. This global trend has been keeping long-term interest rates low, permitting Americans, as largely happened, to borrow *recklessly and sub primarily* on homes and commercial buildings and find support to public deficit spending. The Asian funds inflows and loose monetary policies have been inflating property values, stock prices and related derivatives in an enlarging swelling row of bubbles, meaning inflationary potentials not compensated by any Central bank action, but misrepresented as technology and productivity major factors offsetting inflation instead of effect of low Asian labor costs.

At any meeting, held every month by the US Senate Committee on Banking<sup>3</sup>, Mr. Greenspan, when chairing the Fed, was assuring that *innovation and productivity* were providing price stability, while offsetting risk of inflationary consequences. Actually, the process was an enlarging crowding out of western more expensive industrial productions by less expensive Chinese and far Eastern reallocated industrial numeric controlled productions, restocking all over the world retail and wholesalers shelves at lower prices.

#### 4. The underlying outsourcing volumes analysis.

The volume evidence of what said is easily supported and verified recalling the dynamic quantity of TEU (twenty equivalent unit) traffic trough same Asiatic harbors origins and its booming trend after the 9/11 attack. These data are yearly published by the *London Container Industry Review*, and assessed in millions of teu per year as handled by single Asian harbors considered with each one showing a turnover of more than two million teu per year:

TABLE 1 - OVERALL TEU TRAFFIC: FIRST 20 PORTS

YEAR 2002

Geographic Area	Volume	Total (% of Total)
É Asia	84.951.148	65,89%
É North Europe	22.448.422	17,41%
É Nord America	14.381.242	11,15%
É Middle East	4.194.264	3,25%
É Mediterranean	2.954.571	2,29%
É Total	128.929.647	100,00%

<sup>3</sup> <<http://banking.senate.gov/public/index.cfm?FuseAction=Home.Home>>

TABLE 2 - OVERALL TEU TRAFFIC: FIRST 20 PORTS  
YEAR 20011

Geographic Area	Volume	Total (% of Total)
É Asia	214.130.458	79,10%
É North Europe	29.586.043	10,93%
É Nord America	14.001.610	5,17%
É Middle East	13.000.000	4,80%
É Mediterranean	-	- %
É Total	270.718.111	100,00%

Source < [www.ci-online.co.uk](http://www.ci-online.co.uk) >

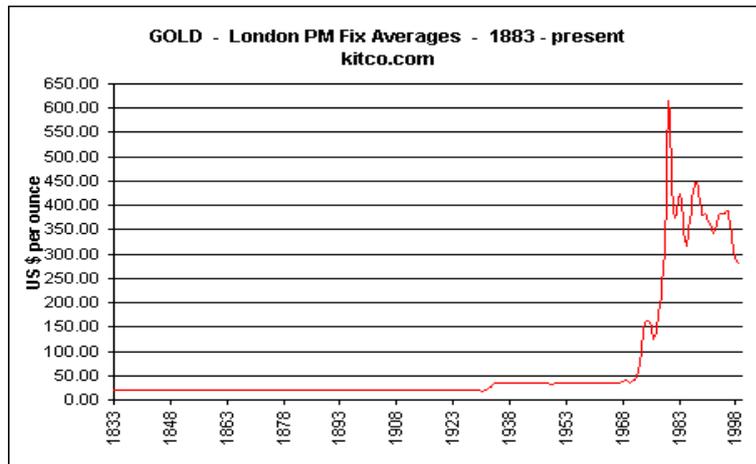
The Chinese trade balance financial surplus have systematically supported both American deficits, the external and the internal one, trough the systematic purchase of public debt treasuries and bonds while reallocating most of the excessive Chinese liquidity with North American banks, without an acceptable risk caring liquid reserves diversification.

American banks found, therefore, new ways and instruments to lend ever growing deposits against relatively small amounts of paid in capital, which should eventually provide their cushion against bad loans during forthcoming recessions. They wrote *credit default swaps* - insurance policies that were generally backed by few if any assets. Financial investments houses and banks placed swaps in a grand *Ponzi*<sup>4</sup> scheme that shall take a decade to completely unwind, just because producers were not investing and industrial output was progressively deteriorating

<sup>4</sup> The scheme has been named after Charles Ponzi, who duped thousands of New England residents into investing in a postage stamp speculation scheme back in the 1920s.

and credit demand have been insufficient to match growing banks' fiduciary deposits.

At the beginning there was just the monetary crisis and bubbles, which started with the definitive repudiation of gold, which had always been an independent objective ceiling to money creation, as proclaimed in the year 1971 by President Nixon during the Vietnamese war. The circumstance was immediately followed by an impressive rising effect on gold prices, previously steady for almost forty years since 1933. The unresolved monetary issues led to a huge inflationary bubble up to Paul Volker, previously Secretary of the Treasury (1969-1974), nomination to chair the FED and trying to reduce the developing inflationary trends.



Source < [www.kitco.com](http://www.kitco.com) >

FIGURE 1. PRICE OF GOLD AS DAILY TRADED IN LONDON

From such an interruption of a long lasting unquestionable fixed price and prevailing foreign exchange stability, an interest rates symmetric trend was immediately discovered and driven out by market forces and policies intervention under same grounds.

In this period the derivative industry was founded and new products appear over the market as both hedging instruments and speculative vehicles, up to their final eruption in the last huge 2008 bubble.

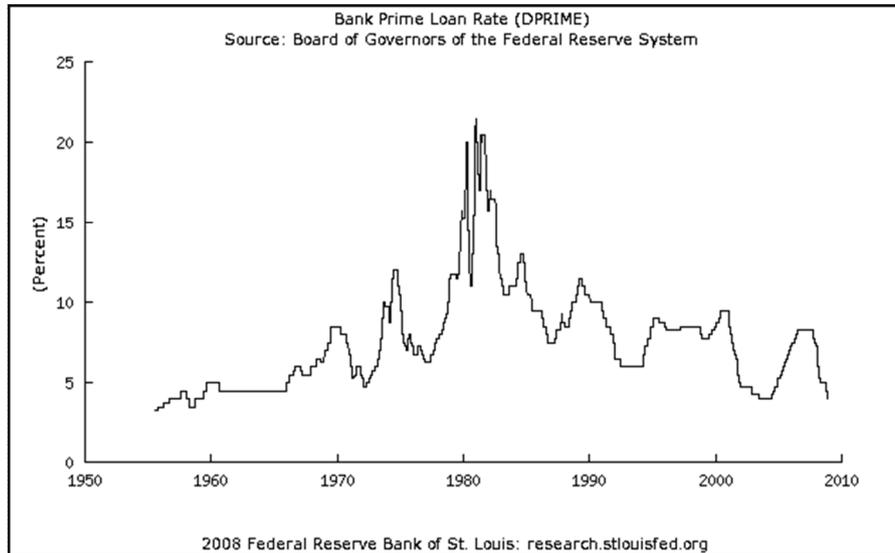


FIGURE 2. PRIME RATE LOAN RATE

The historical inflationary dynamic, experienced since 1913 ó 1919 First World War monetary consequences, were prevailing closely reflecting both the deflationary and the inflationary policies, alternatively implemented during different monetary policy phases. The unsuccessful return to gold and the implementation of legal tender alternating periods in Europe during the thirties, finally terminated with the multilateral clearing system, mostly settled trough the new IBS Basel bank.

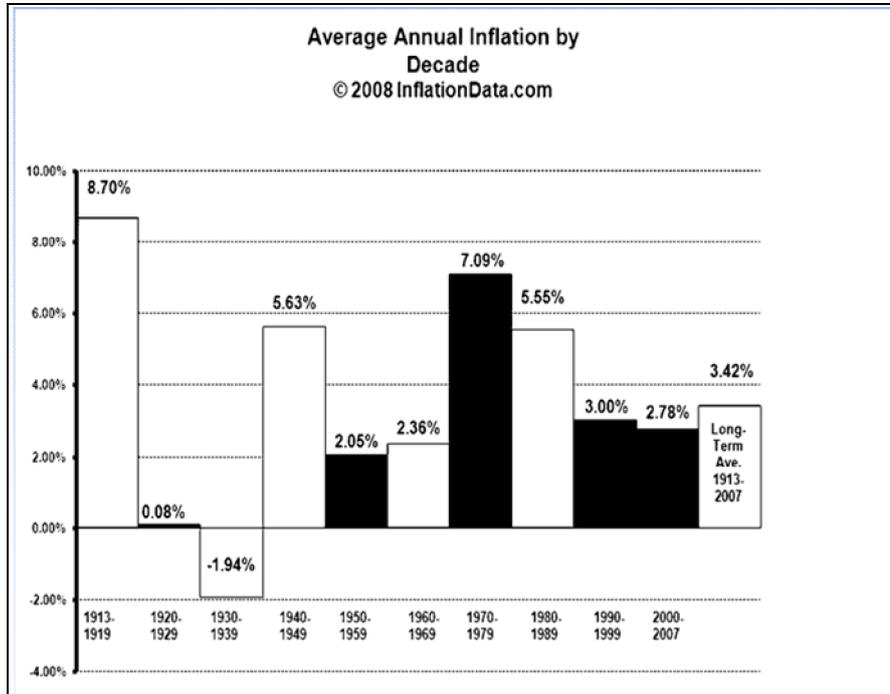


FIGURE 3. AVERAGE ANNUALE INFLATION BY DECADE

Source <<http://inflationdata.com/Inflation/Inflation/DecadeInflation.asp>>

Autarchy and the dismissal of the first globalization, through custom barriers, protectionism and nationalistic attitudes, with devastating military effects, trade obstructions have been definitely rejected after the 20<sup>th</sup> Century tragic events. In our current present scenarios, such events neither are evoked nor considered repeatable. A soft exit to the present monetary stalemate may be reconsidered through a set of guidelines targeting realistic available resources, global social welfare average standards, within a global enforcement of legal and institutional competitive market rules.

### 5. Some unresolved monetary issues.

The economic case against possible trade protectionism is that it distorts incentives: each country produces necessarily goods in which it has a comparative disadvantage, and consumes too little of imported goods, under normal conditions thatø the end of the general prosperity.

From an economic point of view, the final collapse of the monetary *Gold Standard* induced some consequent monetary market abuse in the late eighties, clearly perceived in the year 1987, with the second stock exchange collapse in the 20th century. The October crash was faced by the Fed trough a progressive lessening of the previous tight monetary policy, in connection with some tax, social welfare and reporting worsening conditions which started to promote a slow but progressive migration of most Western productions towards the East Asian tigers countries, pursuing cheap manufacturing and labour costs. During this period, most of the international banks started to revise their growing projects and a new era was shifting banks form international to global, with new larger operational critical volumes and operational patterns. Since then, the connected price stability, notwithstanding the general monetary base increasing volumes, was seen as productivity expansion and technology progresses, both offsetting major monetary supply inflationary risks.

The unreliable efforts to exploit new form of money standards and payment systems: from *bancor* at Bretton Woods, to the *special drawing rights* in the seventies, to the Ecu or *European currency unit* in the eighties and lately trough the EMS to the *Euro*, while challenging Asian low wage countries competition was growing in the last Centuryø decades, have produced a real global imbalance in a world split between a progressively more industrialized expanding half hemisphere and a consuming but not competitive half, leading to the present economic crisis, to growing oil prices and to a set of general monetary imbalances.

The Americans made a historical plan for monetary reforms, including a world currency called the unitas already at Bretton Woods in 1944. President Franklin D. Roosevelt told U.S. Treasury Secretary Henry Morgenthau, Jr. to study instruments

for an international currency to be implemented after World War II. Harry Dexter White from the U.S. Treasury finally formulated his planned return to gold.

In practice, up until the final collapse of the Bretton Woods system in 1971, gold itself newly performed this monetary stabilization role, when the U.S. dollar was valued and multilaterally traded among central bankers at pre war 35 dollars an ounce and all the other currencies were collateralized to either the U.S. dollar or directly to gold with an official intrinsic parity registered with the IMF.

The 1987 stock market collapse came surprisingly and unexpected for most of the specialist observers while a monetary reaction was unavoidably due to the prevailing loose monetary policies, on the contrary of what happened in 1929, when the planned return to gold was already in full gear.



FIGURE 4. STOCK MARKET INDEX YEAR 1987

The consequences are now well known and may be seen in the following charts: which represent the shifts in monetary policies from loose and tight money, blowing bubbles which afterwards disintegrated down and collapses around most of the markets from year 1999 do year 2008 and likely will further continue to explode.

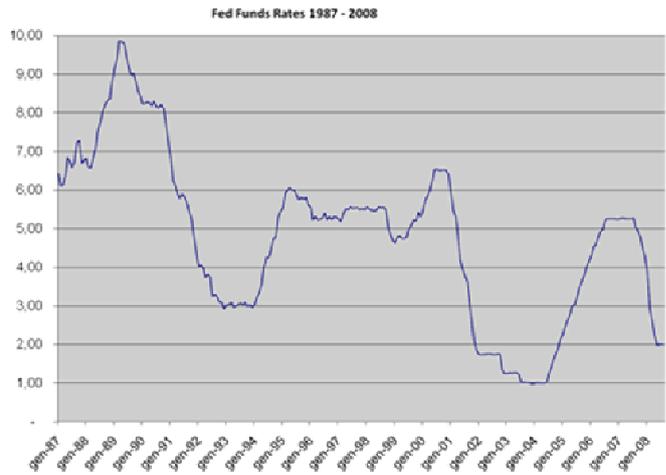


FIGURE 5. FED FUNDS RATES 1987 2008

The Fed funds slope reflects both the tightening monetary policy and the monetary cycles acting as monetary factors originating bubbles and their subsequent blast in the market. This development was not foreseen under the prediction of Greenspan's *soft landing*, assumed as a return to the true market price discovery function, after the monetary supply extravaganza would have been removed.

Actually, the Dow Jones reached unprecedented and unthinkable levels and the inflation started to develop in the year 2004 in an imperfect market.



FIGURE 6. Down Jones index 1960 - 2008

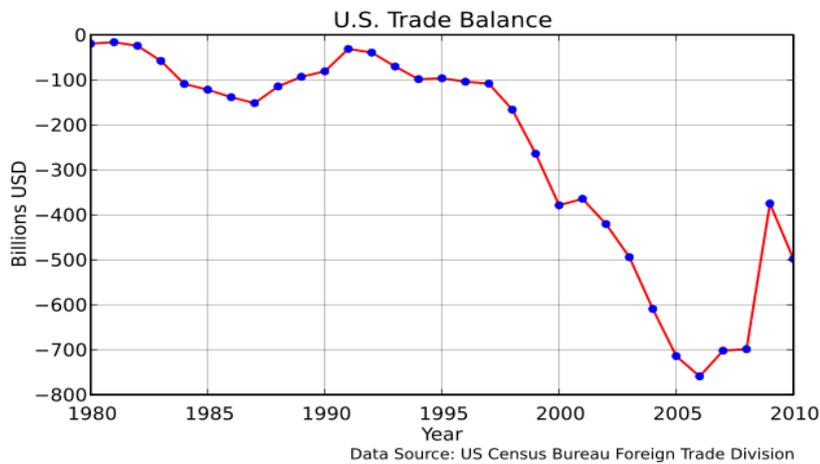


FIGURE 7. US TRADE BALANCE 1980 - 2010

Source <[www.mwhhodgehome.att.net/reserves.htm](http://www.mwhhodgehome.att.net/reserves.htm)>

These figures reflect the huge growing of both internal and external US debts and the monetary effects on stock market, which are a clear and real sign of what was producing the loose monetary policy enforced in the system. Since then, the resulting effects appeared to look like:

- an unprecedented huge trade deficit with global exchange disruptions and world-wide financial turmoil: banking upsizing and refinancing by States and international financial institutions;
- a huge internal and external deficit, with unparalleled outstanding US liabilities to most of foreign Central Banks, especially the Bank of China, which is heading to over three trillion dollars;
- an energy dependency due to the self adjusting oil prices which reflect the gold price movements, almost pegged, while setting itself in a range of 5% to 10% of gold's price movements;
- a huge chance for global and international banks to enlarge their size, operational range and trading activities through new global trading platforms, apart from usual trading facilities on the world scenario with new technologies, instruments and connections.

The idea to promote the Euro as a reserve currency and to strengthen the European economic presence in such a World scenario has faded as the Asian economies have been undertaking a cost competition that has been crowding out most of the western industrial productions, while hoarding huge amount of US currency supporting the internal and external US deficit at same moment.

The world financial activities and monetary base expansion has not been developing into an inflationary arena because of the productivity and technological asserted innovations but, on the contrary, mostly because of Eastern low labour costs, growing improving quality standards, large scale productions and their distribution all over the global markets.

## **6. Conclusions - The exit strategy and its alternative choices, a new evolving approach.**

Within these angles, only complex continental agreements seem to be an exit strategy to face a challenging economic struggle in an open and integrated trade space, with appropriate new never seen before bank sizes, which require critical large fiduciary masses, asset diversification capable of huge synergies and, finally, levelling off the asymmetries in the global technological platforms.

As the flowing liquidity supplied by the Far Eastern growing economies on one side supported the internal US and on a growing scale some European deficit, the stemming credit potential due to such huge resources, after the repudiation of the *Glass and Steagall Act* and the adoption of the *Gramm - Leach - Bliley Act* in the year 1999, named *Commodity Futures Modernization Act*, backed by the Treasury Secretary Lawrence H. Summers, led on the other side, to the

- the technology companies bubble and their year 2000 collapse;
- the ENRON and WORLDCOM entering global banking activities on an intercontinental basis;
- aggressive subprime lending in the mortgage markets;
- the transfer of financial risks from global banks to third no banking parties, trough the sale of unprecedented quantities of CDS and all sort of derivatives which have swollen to uncontrolled OTC instruments;
- the emerging global banking structures, too big to fail, and a general attitude to take over most of bad banking liabilities trough tax payers funding;

Such new legislative instruments, were promoted by the Clinton banking industry deregulation, and caused the exceptional bubble eruption under the dot.com label first and the widespread subprime lending and derivative global shifting of related risks within the banking industries there-after. Banks were progressively free to expand in the financial instruments market,

while losing confidence in progressive lacking new industrial reliable financing opportunities.

Indeed, the upsurge of new financial derivatives and finally the general slowing down in the industrial activities in the Western hemisphere, led the everlasting banking industry to the *sub prime* new swelling activity, and to the final fatal collapse of all the financial markets, when the Fed tried, unsuccessfully, to frame the inflationary symptoms in the year 2004 by raising the Fed interest rates.

The Fed choice led to the collapse of some major financial institutions in the year 2007. Afterwards, followed the fatal demise of both the *Federal National Mortgage Association* Fanni Mae, and the *Federal Home Loan Mortgage Corp* (FHLMC) Freddy Mac and spread troubles in most of the investment Banks since the year 2008.

Henry Paulson Jr. Treasury Secretary tried all the ways to find a solution on the multiple sides of banking institutional crisis, the toxic bonds issue, the bad banks segregation and the TARP (Troubled Assets Recovery Plan) programs, but there was not a single common agreement about what to do and when do it.

The World financial and political community has been organizing meeting at top level but every single session has been promoting a different explanation and a different strategy of very new and assorted problems, as emerging out of the such new situation..

Finally, Treasury Secretary Henry M. Paulson Jr. has adopted the solution of *the Troubled Assets Relief Program*, the TARP starting with a first \$700 billion bailout. The frequent changes of direction have not only been embarrassing, they also upset the very markets this program was designed to ease and actually has instated the quantitative easing programs, that are waging over new potential bubbles.

The fact is that among so many choices, the Administration had not yet decided how to solve the unsolvable problem of an almost declared banking system failure, which was already history and

probably couldn't be solved. Either you declare inconsistent the assets inscribed in the financials of a bank, or the equity inconsistent, or finally you declare that the banks don't exist any more since they are bankrupt showing negative equity.

The TARP program acquired strength under President Obama and Secretary Geithner with two further large quantitative easing, bringing the monetary base to unprecedented levels in a race against roaring deficits linked to the incoming economic recession.

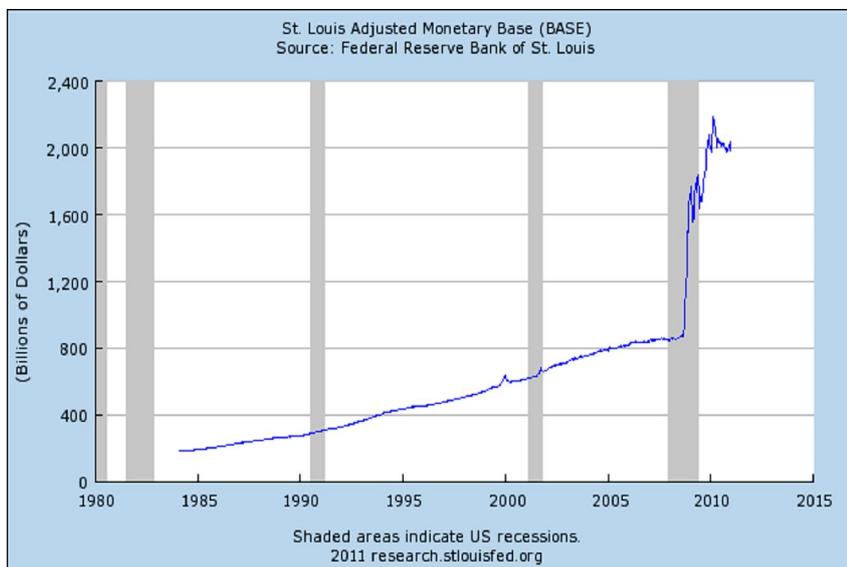


FIGURE 8. MONETARY BASE INCREASE 1980 - 2012

So, the music is now strong with the financial and banking industry but what really matters is the crisis with bank borrowers, either private mortgage borrowers, which are unemployed or firms that are unable to service their scheduled loan plans as the relocated producers are fighting toughly back from the far East on rebates and gadgets which are crowding out firms like General Motors, Ford, Chevrolet. These are not global market producers like Lexus or Tata, or have not relocated Eastward on proper time.

The Japanese liquidity trap has already shown the ineffective role of loose credit policy and inefficiency of all set of monetary

remedies: it has been already a decade since the Japan trade marks have disappeared from western shelves with the Bank of Japan keeping interest rates on loans close to zero and the continental Europe has been facing a definitive debacle in its automotive, electronic and durables productions on similar grounds.

This real problem has turned now in a global unemployment risk and in an unique purchasing power in the hands of few oriental Central Banks to be likely spent in overtaking Western industrial complexes. China, Singapore, Korea, Japan and Taiwan, which have the largest vault of assets in the world history, are facing a dilemma in avoiding a general monetary collapse, which could lead to a disruptive inflationary wave, but meanwhile have become large buyers in the major stock exchanges trough most western large banks shifting money from one angle of the planet to the other in real time.

All has been stemming from a progressive two layers coexisting economy systems: a local split set of national and regional markets and a contextual huge global market, confronting each other. The final success lies in the volume synergy linked to the global market potentials and to a more flexible social infrastructure, which better face to a new age, where the global versus local markets economy has no solution in reinstalling trade barriers.

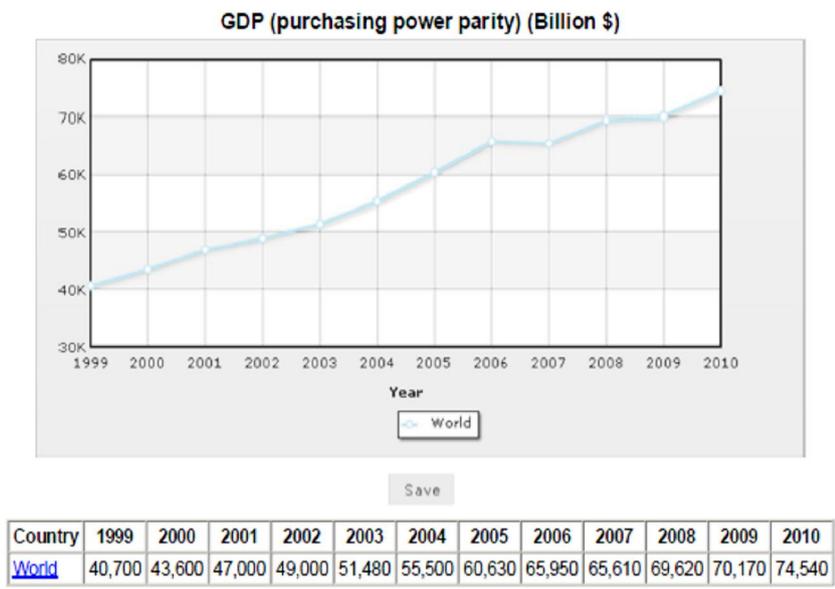
Joseph E. Stiglitz stressed out, a consequence of the recent crisis that might stem from the following principles arising from the last decade events Stiglitz (2010):

- markets are not self-regulating;
- market information is too huge to be handled;
- there is not enough tight policies to fight inflation;
- financial innovation has not been always successful.

His remarks may not be correct as most of the present financial disorder stems out of the market asymmetries which have been favouring the huge reallocation of world production Eastward and actually along some simple Smith's free market rules. Since the welfare State has been held up during the cold war as a remedy to

avoid global dissemination of totalitarian regimes, reforms have developed social and political costs in Western world, affecting industrial and services production; the collapse of the Berlin wall has freed the basic of market competition all over the Eastern hemisphere, causing the greatest depression ever in the western area. At same time, starting from year 2000, the world total GDP has grown mostly in Asia bringing the total from 32 towards 90 tr.

Such an immense success of the Far Eastern new economies is the final proof that State intervention, mainly supported by legal tender monetary expansion (*fiat money and quantitative easing*) has showed once more not to be efficient. From an exchange rate point of view, the Chinese currency exchange rate value seems definitely irrelevant. From a competition point of view, as long as labour costs are freely adjustable to any price movement, not being fixed or under labour unions monitoring, cost production factors are easily adjustable to any exchange rate fluctuations in Asian markets. The elasticity in labour costs is potentially offsetting any foreign exchange variation at least in short terms..



**FIGURE 9. WORLD GDP FIGURES**

Source <<http://www.indexmundi.com/g/g.aspx?v=65&c=xx&l=en>>

As can be easily seen, the world GDP has, actually, more than doubled from 32 trillion US\$ at the beginning of the millenium to over 70 trillions today, in only eight years, since the year 2000 to year 2008, it has grown dramatically and more than ever in history before. From 32 to 74,54 trillion at the end of 2010, this period reflects one of the greatest world economic successful growth, if reconsidered from a quantitative global production point of view and is mostly linked to the facilities supplied by the successful global banking industry within the modern technology, allowing the electronic shifting at light speed of bills of lading, purchase orders and any sort of documentation in digitally, registered, stamped and signed species form a continent to the other.

As a consequence of the previous considerations and data, shown in all collected figures, the structure of the real economy is therefore not reflecting issues linked to the financial turmoil over the trading markets, speculation not covered by hedging risk offsetting contracts, has produced losses as well as the sale or the purchase of coverage derivatives. From an economic point of view, the irrational uncovered risks taking on by savers and public entities, has reflected the final conclusion that risk is not avoidable, just transferrable, therefore only arbitragers and inside traders have not lost their capital.

I would stress that any form of regulation may not prevent losses, but may become a misleading approach if addressed to solve the underlying global monetary adjustments not yet sufficiently studied and understood, reforms pending unsolved since the 15<sup>th</sup> of August 1971.

From a geographical angle, the GDP has as well dramatically changed in its distribution trough countries, the following pictures, as reflected in the last edition of the *Economist* shows the likely source of next 10 tr. of new world GDP, the location reflects the actual growth, not properly definable a depression or even a recession on a world basis outlook.

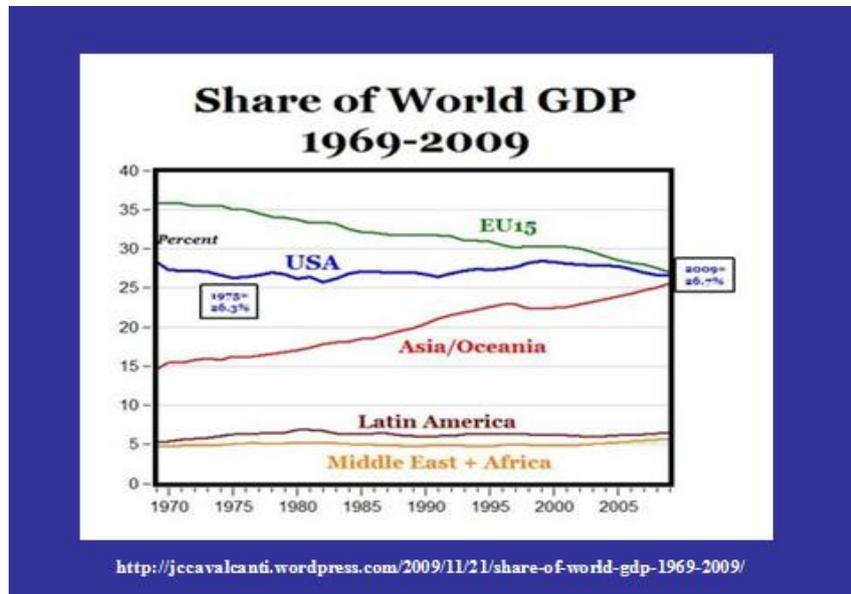


FIGURE 10. SHARE OF WORLD GDP BY WORLD BANK

From a global share point of view, while still a stable amount of the increasing GDP, is reported for North America, a growing share lies in Asia-Oceania, where it has been gaining space, the loosing area appears to be Europe. This gross deflated product figures reflect the global banks relocating strategies and merging operations from a national and international to a global point of view.

Putting emphasis over market patterns, short positions limits, derivative trading and risk assuming constraints, without a clear consideration of what happens in the real world economy, seems not be meeting much chances of success or, as it has already happened, avoid future losses and disruptions. Whenever the fundamentals of the economy reflect a gap between the real economy, or market forces and the financial connected transactions and banking activities, there will always be no coherent behaviour or what Keynes used to call euphoric exuberance, due to the immaterial side of human brain.

Most of the losses on financial markets and stock exchanges actually are developing in Western institutional markets and are

likely due to the underlying real economy imbalances, both public and private.

This present evolution requires a review of some previous economic obsolete models:

- old industrial production technology;
- market restricted fragmentations and stems likely from a
- huge monetary crisis, as a consequence of the end of the cold war;
- the refusal of the gold standards guidelines discipline, as restored at Bretton Woods in 1944, but *temporary* repudiated in 1971 by President Nixon and
- the end of some affluent society patterns, collapsing within the welfare state sovereign colossal debts.

Such models must be reconsidered and set up in a global banking monitoring compatible new global angle. All the modern welfare political costs and inefficiencies are surfacing as a freer competition arises from the new Eastern, radically different, social relations.

Only a slow adjustment to the new global open markets behaviour and to the related unquestionable new standards prevailing in the world wide competition, under new critical corporations and new global banking functions as trading and market platforms, after a deep monetary reconsideration, restoring a vehicle able to stimulate savings and stable values, will bring new chances of economic stability and capital formation to the now recessing Western world areas, while new ones are dramatically remerging and taking over the old world.

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## **BANKARSKA INDUSTRIJA NA GLOBALNOM TRFIŠTU: OSNOVNE KARAKTERISTIKE STALNE EVOLUCIJE**

Sažetak

Trenutna financijska kriza koja je započela 2000. godine s pucanjem dot.com balona, kasnije je evoluirala u nešto vrlo specifično i različito od bilo kojeg prethodnog povijesnog ciklusa zbog previranja, onako kako se obično navodi u našim političko-ekonomskim modelima: klasičnim, austrijskim, Keynesovim monetarnim i post-Keynesovim. Takvi pristupi ipak nisu prikladni za objašnjavanje epohalne promjene u svjetskoj ekonomiji već samo privremenih ekonomskih previranja. Nova era turbulencija, kako je govorio Greenspan (GREENSPAN, 2007), zahtijeva centralni autoritet koji bi bio regulator većine financijskih tokova i tržišta kao i okvir za nove zakone vezane za nove financijske proizvode, nova pravila tržišta i financijskih institucija, uglavnom banaka i platformi za trgovanje kako bi se radilo na dugoročnom cilju ekonomskog rasta u situaciji opće stabilnosti.

U posljednje vrijeme, preklapanje prevladavajućeg globalnog tržišta je zasjenilo većinu lokalnih tržišta i proizvodnji, nakon što su neki jeftini industrijski proizvodi azijskih zemalja globalno preplavili većinu zapadnih industrijskih područja.

Neizbježan inflatorni rizik povezan s novom svjetskom financijskom i monetarnom kvantitativnom ekspanzijom, nakon odricanja od zlatnog standarda 1971., nije zapravo neutraliziran i steriliziran od strane produktivnosti i tehnoloških inovacija kako se općenito tvrdilo u devedesetima. Cijene su uglavnom bile pod kontrolom radi pritoka jeftine radne snage s Istoka, konkurentnog rasta tehnoloških standarda kvalitete i posljedici nog

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bujanja proizvodnje koja se prelila na zapadna tržišta uz niske cijene. Ti su događaji uvelike povećali trgovinu, novane transakcije i vezane nagodbe po ugovorima kao i sve tokove kapitala putem nove mreže velikih bankarskih institucija povezanih s ogromnim uključivim rizicima. Lokalne banke i banke izvan novih istočnih poslova razvile su rezidualne financijske pratnje i aktivnosti koje su se razvile posljednjih godina nakon niza deregulatornih instrumenata. Velika raspoloživost fondova, lako kreditiranje, kvantitativno ublažavanje, postavili su temelje ogromnoj svjetskoj prezafulnosti kako javne administracije tako i tradicionalnih zapadnjačkih industrijskih postrojenja donose i niži rejting kako zemljama tako i bankama.

U tim okvirima, prava prilagodba financijskog tržišta i smanjivanje banaka moraju razmotriti potrebno preliminarno finougovanje svjetskih monetarnih politika, cijena i standarda rada te revidiranje okvira i struktura socijalne drflave onakvih kakvi su se stratificirali tokom hladnoga rata. Strogi skup pravila povezanih isključivo s tržišnim instrumentima i trgovinskim specifikacijama, bez uzimanja u obzir financijskih posrednika, mogao bi se pokazati nedovoljnim. Izvan mehanizma određivanja cijena na slobodnom tržištu ima mjesta samo za zloupotrebu tržišta i manipulaciju. Trenutna se kriza do sada može povezati s nekim zastarjelim asimetrijama između socijalne drflave i modernih slobodnih svjetskih tržišta, uz nekolicinu neriješenih povezanih monetarnih pitanja.

**Ključne riječi:** banke, financijska kriza, tržišta, asimetrije, regulacija, Azija