

Dependent financialization in CEE countries

Daniela Gabor
UWE Bristol

My arguments

- Dependent financialization: new forms of organization and new activities in financial markets through which foreign financial actors generate financial profits.
- Transnational banks at the core of market-based modes of profit generation characterized by interconnectedness, state agency and fragility.
- Taxonomy of fragile/financialized connections to theorize dep. financ. and to consider possible policy responses

Background

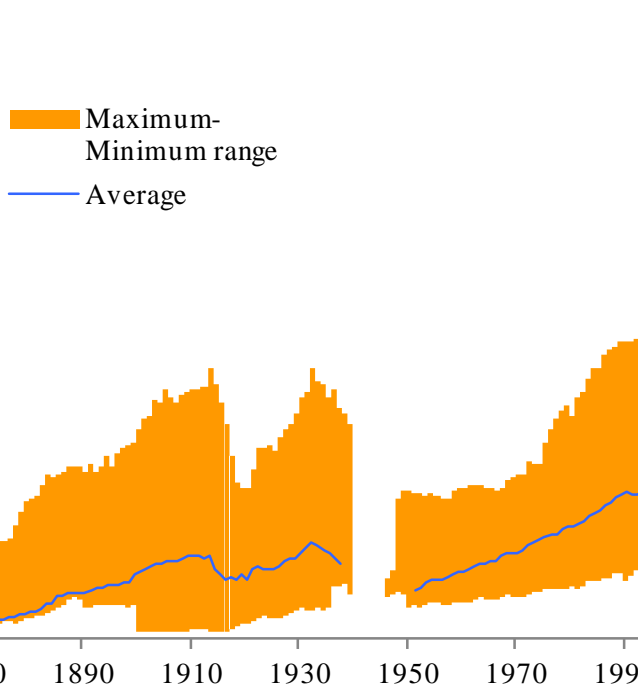
- Two waves of politically-driven KA liberalization post 1990, fast (Czech Republic and Baltic States by 1996) and gradual liberalizers (Hu, Ro, Bg, Sk by 2006).
- Similar sequencing: first FDI, last 'hot' interest-sensitive flows (non-resident access to money markets instruments)
- KA liberalization with FDI targeting bank privatizations

Foreign bank assets/total banking assets (2012)

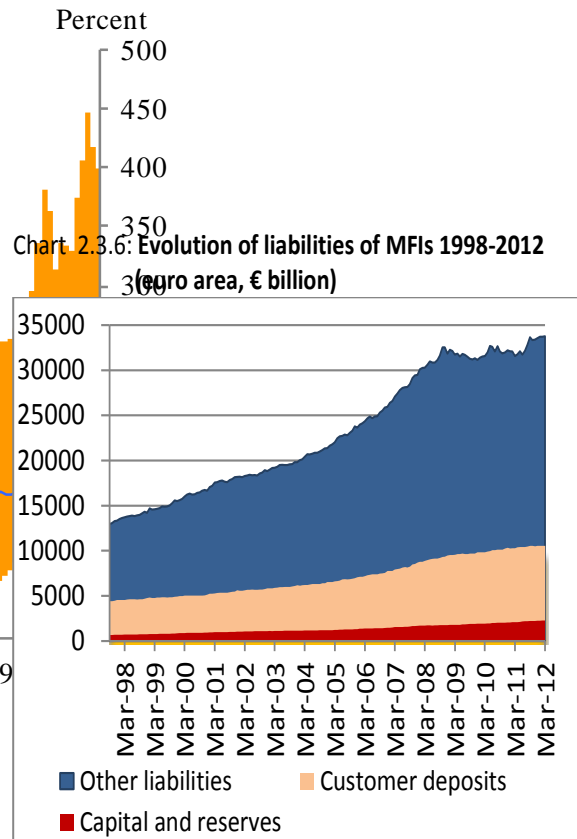
	Bulgaria	Cz. Rep	Hungary	Poland	Romania	Lithuania	Estonia	Slovenia
2004	72	84	65	72	78	91	90	20
2009	79	80	64	68	92	91	91	21

While European banks grew rapidly

Bank assets/GDP in selected countries

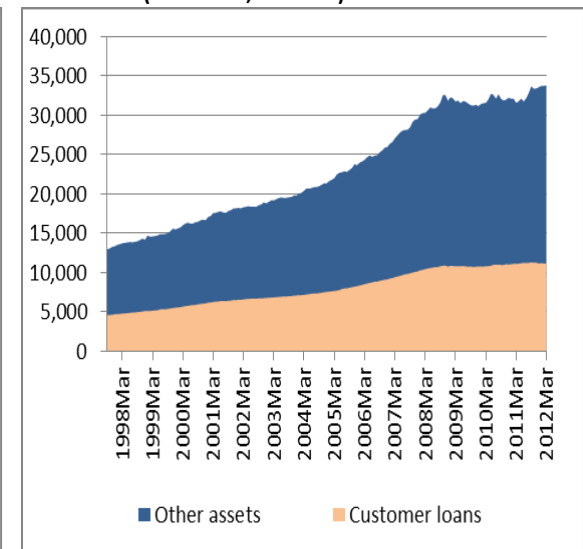


Source: Jorda, Schularick and Taylor (2011)



Notes: Customer deposits are deposits of non-monetary financial institutions excluding general government.
 Source: ECB data.

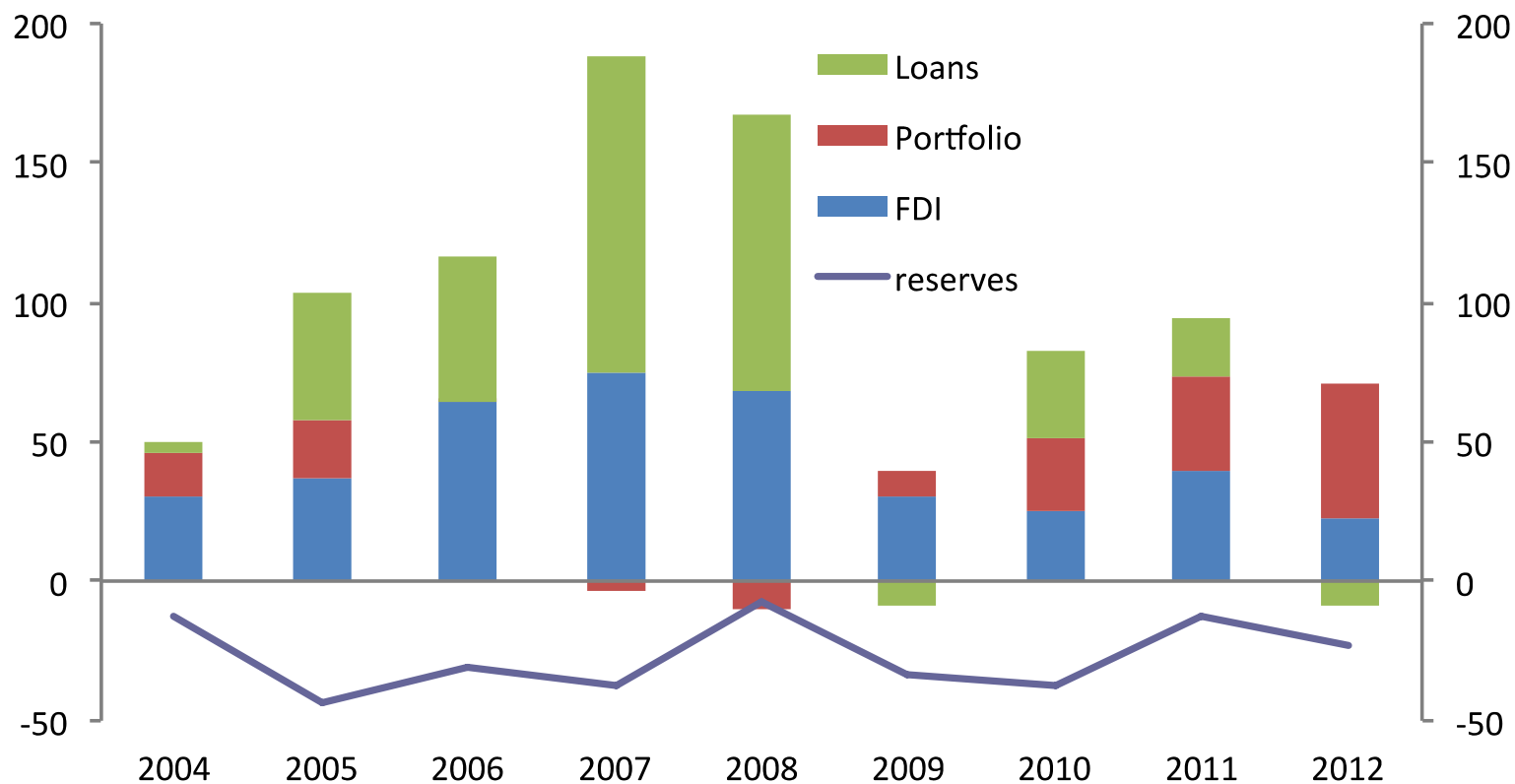
Chart 2.3.7: Evolution of assets of MFIs 1998-2012 (euro area, € billion)



Notes: Customer loans are loans to non-monetary financial institutions excluding general government.
 Source: ECB data.

CEE absorbed some of that balance sheet growth

Figure 1 Net financial flows (USD bn), Eastern Europe



Source: IMF World Economic Outlook

Financialization – early contributions

- As regime of accumulation (Krippner 2005), changing every-day life(Langley) of households (Lapavistas), as shareholder pressures (CRESC Manchester)
- *States*: financialization of monetary policy (D'Arista 2005; Vernengo, 2008); central bank (Gabor, 2010; 2012).
- *Markets*: currency, commodities, interbank etc.

Financialization as interconnectedness

- Critical interconnectedness literature (Haldane 2009, IMF 2010, 2012; Blundell-Wignall et al 2010, 2012, Bruno and Shin 2012; Yellen 2013):
 - global banks as key nodes in global financial architectures, super-spreaders of systemic risk
 - intra-financial system creation, trading and management of risk (market-based banking)
 - cross-border, cross-currency funding of high-yielding assets (carry-trades)
 - political influence, regulatory capture or benign neglect
- States as promoters, rather than (only) victims of financialization (different benefits depending on IPE)

Theoretical framework

- Typology of financialized/fragile connections
 - Interbank connections: with the domestic banking system
 - Protective connections: with the central bank
 - Shadow connections: with non-resident investors

Interbank complementarities

- Transnational banks use internal capital markets or lend to non-affiliated domestic banks (Cettorelli and Goldberg 2011)
- Allocation of liquidity dependent on relative profitability
- Internal capital markets as conduit of risks between host and home locations (de Haas and van Lelyveld 2011, Allen et al 2012)

Figure 1 Cross-border loans from BIS banks, as % of GDP

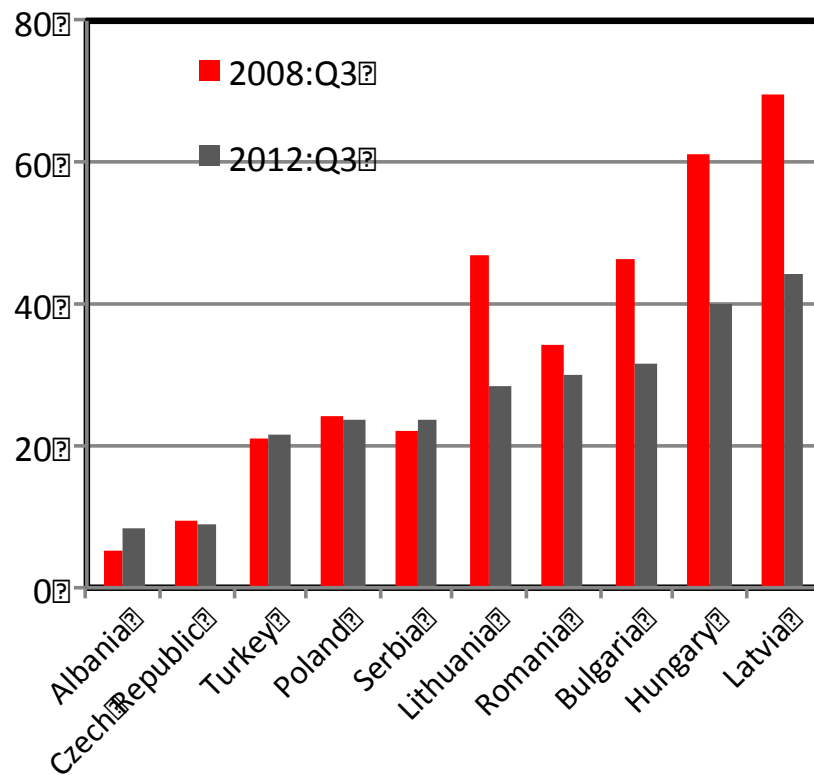
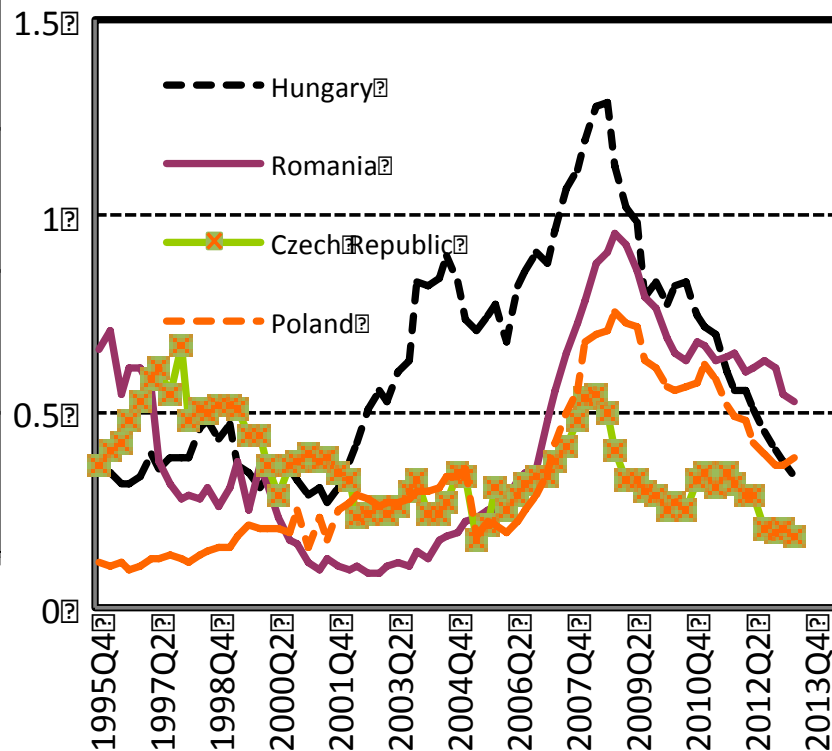


Figure 2 Interbank cross-border loans/central bank reserves



Vienna Initiative(s)

- 2008-09: CEE initiatives to segment internal capital markets (Poland, Croatia, Latvia, Romania); 2011 Austria
- VI: yes to local banking model, but not through regulatory means 'free movement of bank liquidity and capital in accordance with the Treaty for EU members' (EBCI 2012)
- Instead, accelerate financial development (mkt driven) to improve availability of domestic savings

Banks as actors in IMF conditionality

‘We are aware that it is in our collective interest and in the interest of Hungary for all of us to reconfirm, in a coordinated way, our commitment to maintain our overall exposure to Hungary. Mechanisms to specify this effort will be developed in due course, taking into account availability of *adequate lending opportunities or alternative investment instruments* in Hungary’

(European Banking Group 2009).

Protective connections

- Banks' market activities + cb currency manipulation
- Resident banks endogenous create liquidity by intermediating K flows a la Rey's (2013) dilemma: autonomous mon pol vs. free K flows
- Financialization of interbank money markets – structural excess of liq across CEE (Balogh 2009)
- Sterilization games – the Czech Republic (1994-1995, Christiansen 2004), then across Eastern Europe (Gabor 2010, 2012)

Sterilization games

Figure 1 Poland, domestic bank assets (PLN mil)

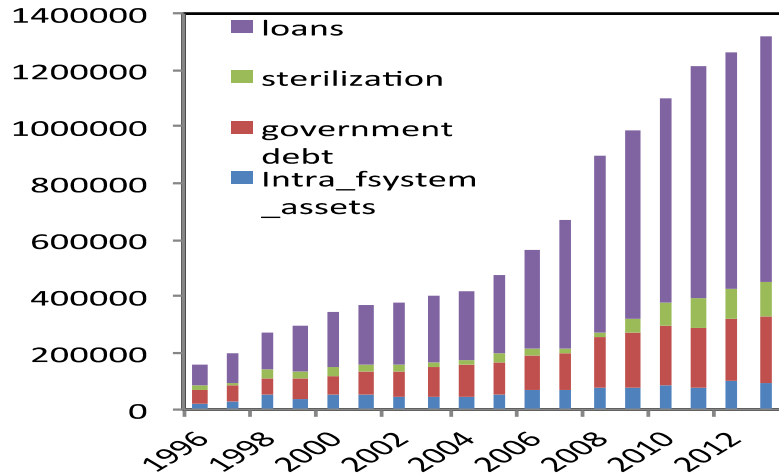


Figure 2 Hungary, domestic bank assets (HUF bn)

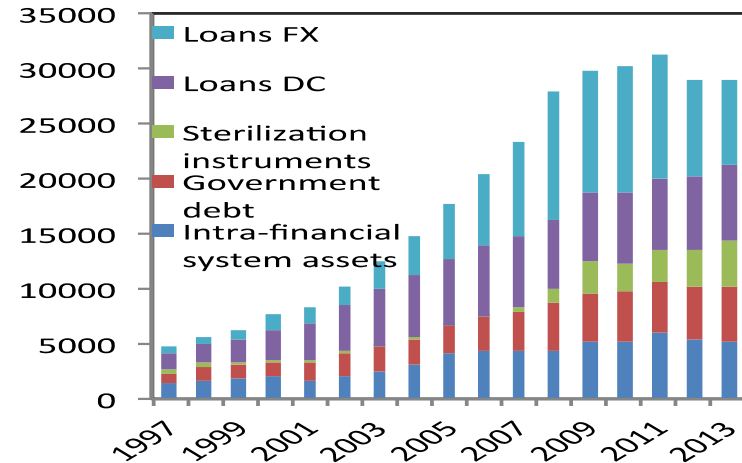


Figure 3 Romania, domestic bank assets (RON bn)

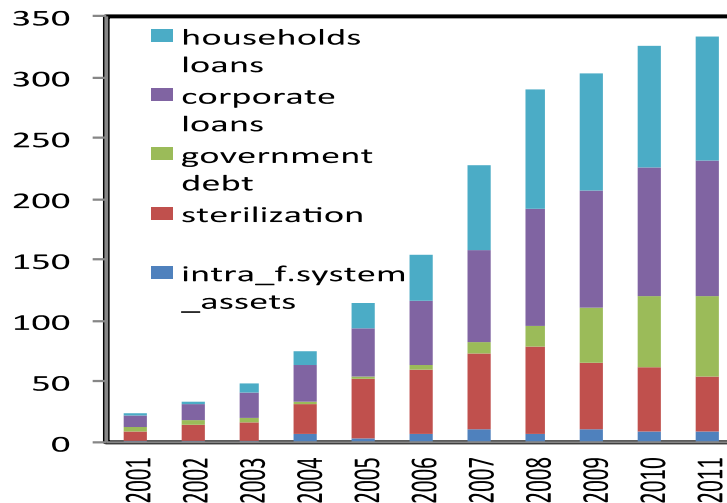
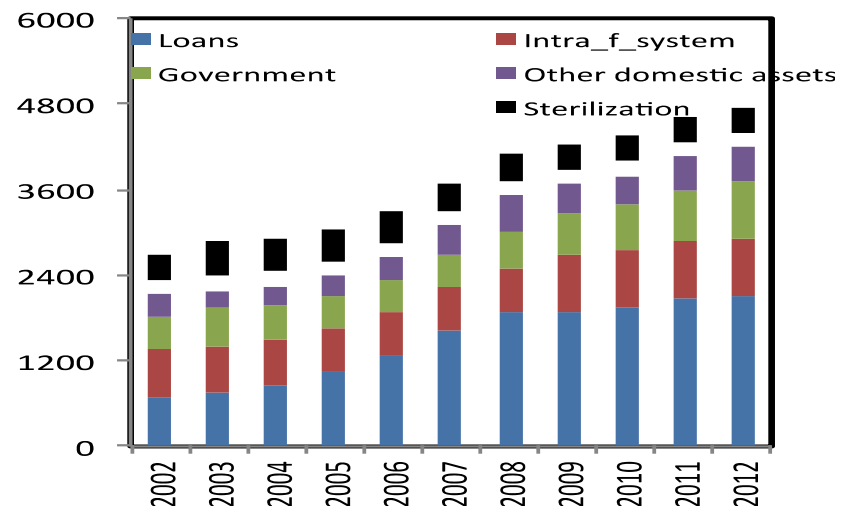


Figure 4 Czech Rep., domestic bank assets (CZK bn)



Shadow connections

- Domestic banks' provision of local currency to non-residents for narrow or broad carry trades
- Enabled by protective complementarities, exposes countries to global financial cycles (Rey 2013), sudden stops (Curcuru et al 2010).
- Informal capital controls (Romania, Latvia; see Buiter and Sibert 2008, Gabor 2012).

Non-resident exposure to CEE

Figure 1: Non-resident holdings of debt securities (USD bn, 2001-2012)

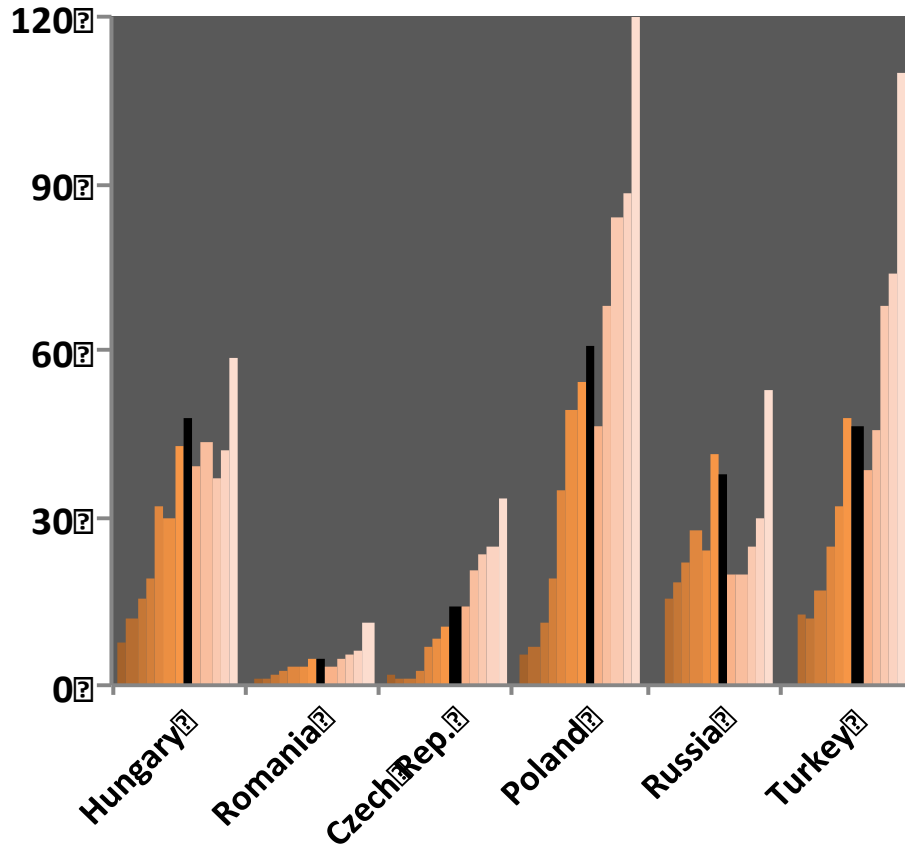
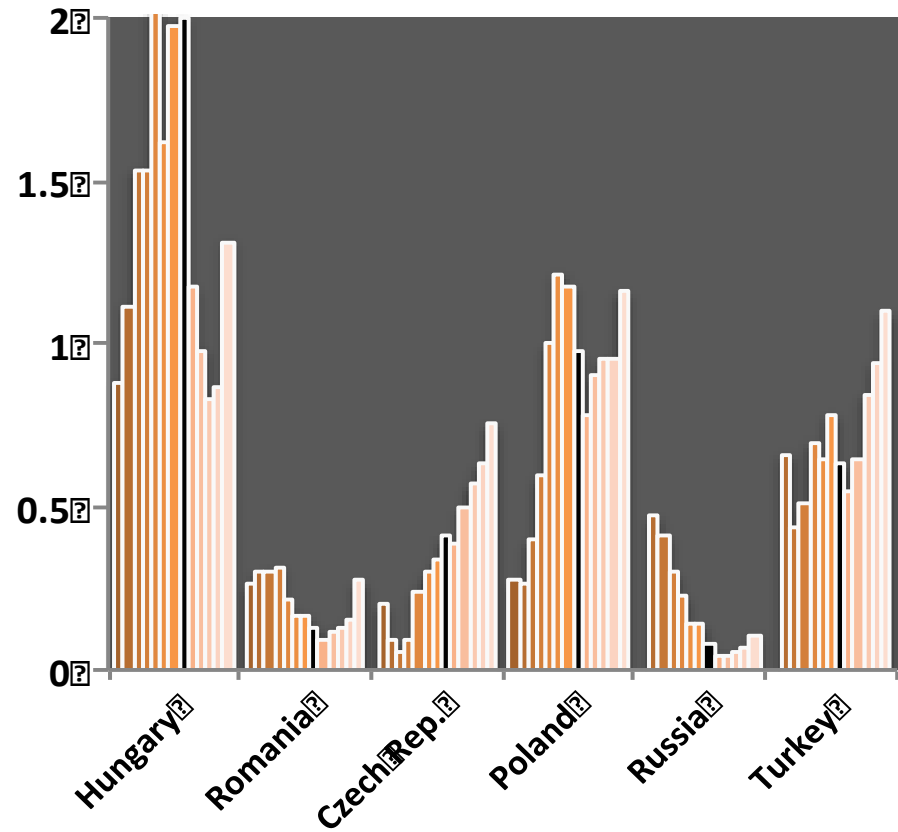
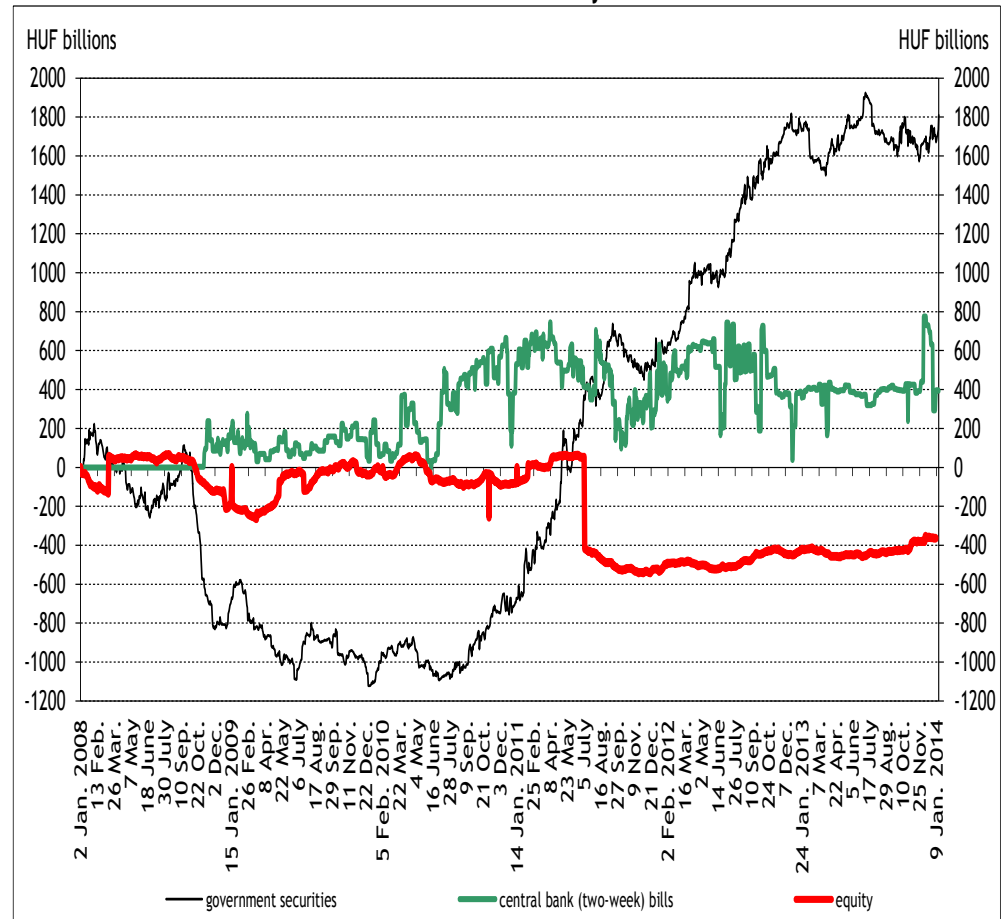
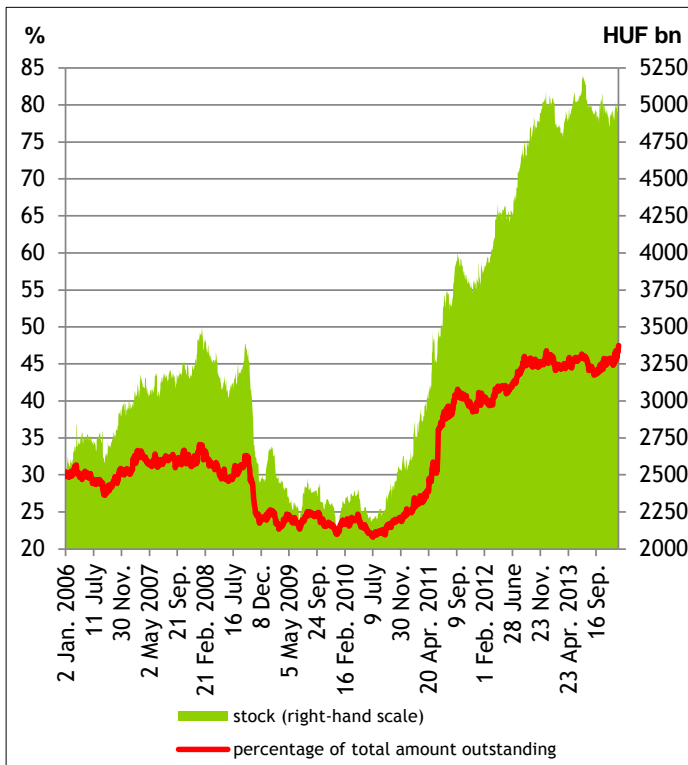


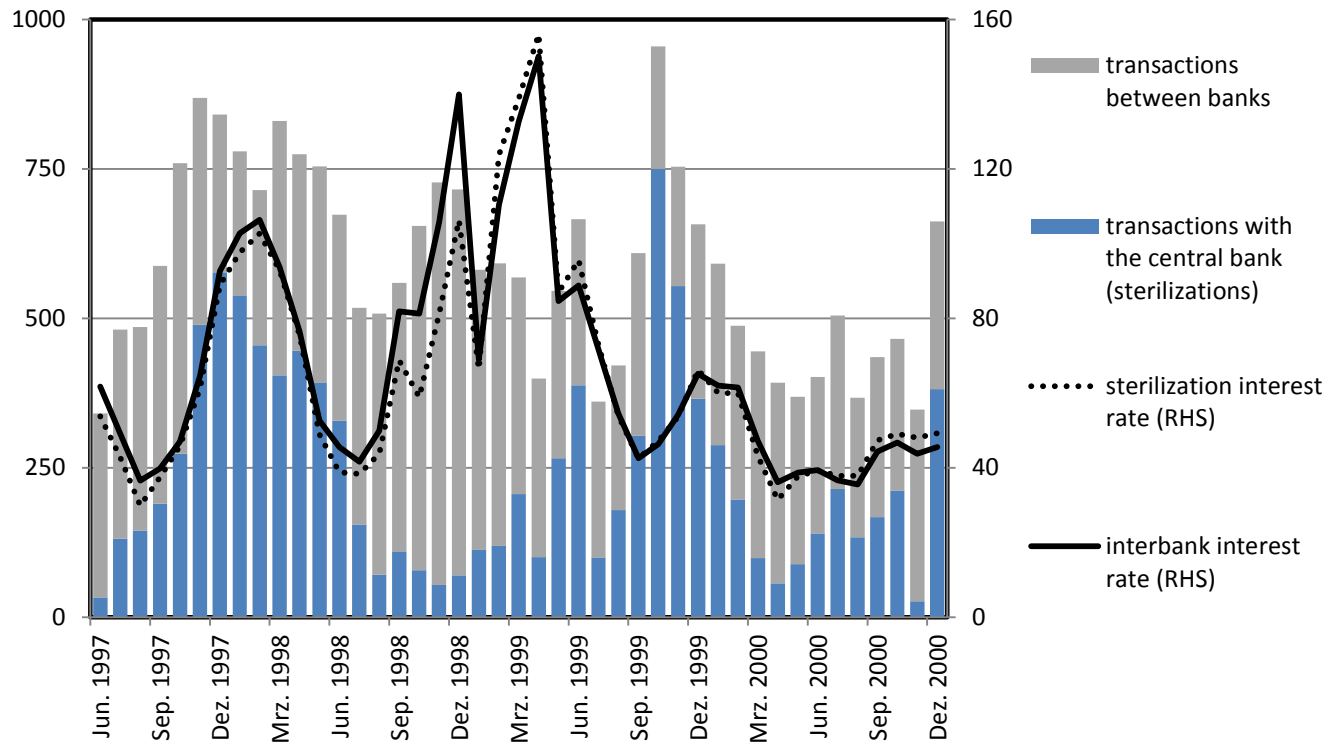
Figure 2: Non-resident holdings of debt securities/foreign reserves (2001-2012)



Non-resident holding of LC assets, Hungary



Costs of reacting to sudden stops



‘restrictions on nonresident access to funding in local currency can at times make currency speculation more difficult’ (IMF, 2013: 18). The challenge is to ensure that non-speculative domestic demand for liquidity is satisfied at normal market rates (IMF 1997).

Dependent financialization

- Transformative: financialization of interbank money market, currency markets, government bond markets
- How to reverse it?
 - Local banking model
 - Low interest rate environment
 - Questioning the paradigm: the more liquidity the better
 - Financial repression: development banks, state ownership of banks, captive funding for government debt