

Term paper on international financial markets

[Business](#), [Marketing](#)



Abstract

In the past, the international financial markets have had diverse ways and means of achieving their financial satisfaction and objectives based on different operation platforms. For this reason, there arose challenges with integration of different financial systems without a common platform. This led to most countries modifying their models of international finance for them to remain competitive in the market as well as possibilities of investing in new markets and having investors from anywhere in the world invest in their financial system. For example, Japan's - GAAP financial system has in the recent past been harmonized with that of the U. S. - GAAP. Bennett identifies four structural trends that can be used to define financial markets. This includes, but not limited to, globalization coupled with cross-border integration, technologies and the financial market and very large financial institutions that play a key role in the financial market.

Introduction

The international financial market has had many definitions as far as their achievements and models of operations are concerned. For example, in Samitas (2005), it can be noted that some large international financial markets have created subsidiaries dubbed secondary markets whereby small and medium size enterprises can purchase and sell stocks in an environment that is competitive at their level of operation. With respect to this, the secondary markets offer capital for entrepreneurial development as well as capital for investment plan unlike in the primary market where the rates and costs are very high (Samitas, 2005). It has also been argued that the stock

market has the capability of speeding up the economy of a country if well balanced and control measures are put in place to absorb market shocks (Samitas, 2005). The main reason for this course is the fact that secondary markets increase liquidity and thus risk diversification mechanisms in place and thus increased investment (Samitas, 2005).

Gulen (2006) on the other hand posits that bank insolvency that have the capability of affecting the financial market ought to be an issue of public concern (p. 66). For this reason, bank failures and finding solution to this aspect of financial institution includes cooperation from international markets as well as other investors (Gulen, 2006, p. 68). Additionally, when considering a mature financial system, the following criteria is used as proposed by McKinsey & Company (2006, p. 25; Aliogo, 2011, p. 3) for the function that the institutions play. To start with, such a financial institution tries to mobilize savings such that there is transfer of consumption to the future by both companies and households (McKinsey & Company, 2006, p. 25; Aliogo, 2011, p. 3). Secondly, the monies that are so saved are then allocated to capital users as loans that are used to finance their operations leading to future interest earnings for both the secondary market and the savers (McKinsey & Company, 2006, p. 25; Aliogo, 2011, p. 3).

Thirdly, since it is expected that the stock market should be transparent in its operation, there are provisions of price signals as well as information regarding capital users (McKinsey & Company, 2006, p. 25; Aliogo, 2011, p. 3). Fourthly, there is trading of risks through disaggregation of risks by provision of oversight from investors that might threaten to withdraw funding which can consequently affect borrowers to some extent as well as

some intermediaries (McKinsey & Company, 2006, p. 25; Aliogo, 2011, p. 3). Since it is a financial system, it is expected that the institution should have an upbeat payment system (Aliogo, 2011, p. 3). Lastly, for efficient company operations, there is provision of incentives (McKinsey & Company, 2006, p. 25; Aliogo, 2011, p. 3).

International Financial Markets Operating Together

There are a myriad of published literature that indicate clear cooperation between various international financial markets. For example, in Samitas (2005), it is noted that most of the international financial markets have in the recent past adopted a clear and cutting edge approach to financial systems such that there has been an increased integration of technologies into their operations such that various players in the market, regardless of their geographical location difference, can access vital information in real-time concerning the stock markets and other issues. Samitas (2005) adds to this notion saying that the geographical barrier no longer makes sense due to investment by these financial institutions in technologies that enable fast access to information anywhere anytime.

Samitas (2005) continue to note that common international financial markets have adopted a common approach towards market liberalization and deregulation which is an indication of cooperation. A good example can be found in countries like Greece, France, United Kingdom and Germany whereby there are these countries operating on the European stock market do so under one representative stock index (Samitas, 2005). Although speculative, there is a higher possibility of the current European financial downturn can be attributed, at least to some extent, to common trading

among other factors.

Another evidence of cooperation in international financial market is the fact that regional markets have been providing opportunities for financial institutions as well as commercial banks of member countries room for expansion beyond the restriction of their jurisdiction (Gulen, 2006, p. 71).

Looking at the United States' market trend, it is interesting to note that there has been a noted integration of cross-border international market in its financial market that can be attributed to increased globalization (Bennett, 2011). This means that despite investors and other corporations not falling under the U. S. jurisdiction, yet there is acceptance to carryout financial investments and transaction in the region that is made possible by formulation of relevant regulations (Bennett, 2011). In an effort to increase its overall return on sale, the U. S. market has made it possible for large institutions and corporations like investment & commercial banks to be integrated through investment in technologies that make this a possibility (Bennett, 2011).

It has been noted that in recent years, there has been introduction of technologies that give the U. S. financial market cutting edge advantage by provision of very rapid trading strategies and thus aid investors in proper decision making (Bennett, 2011). This means that, unlike in the past where there was passive investment and follow-up on the market trend, investors have the tool they need to stay in touch with the current market trend and proactively make decisions on where they would like to invest in next.

There is also evidence of the U. S. financial market having inclinations towards very large financial institutions that are perceived as being too large

to fail and who's physical, political and technological level seems savvy with multinational regulations where central banks are given the mandate to make supervision of such institutions (Bennett, 2011). A good evidence of these trends is noted in the works of Johnston and Nedelescu (2006) where it is noted that after the September 11, 2001 attack on the World Trade Center, and due to resource diversification, maintenance of good liquidity as well as financial institutions that were sound, there was ease in as far as absorbing that shock was concerned (Johnston & Nedelescu, 2006).

Johnston and Nedelescu (2006) continue to note that after the September 11 as well as the attack on Madrid; there was an effect on the global scale. The attack on September 11 made a large dent on the financial markets human capital since, of the deceased 74 % were human capital for U. S. financial market in addition to over \$ 27. 2 billion in loss mainly from private sector loss accounting for about \$ 14 billion, \$ 1. 5 billion loss to local government enterprises and state government, US federal government loss accounting for about \$ 0. 7 billion as well as \$ 11 billion for cleanup and rescue operations (Bruck and Wickstrom, 2004; Johnston & Nedelescu, 2006). The loss accounted for $\frac{1}{4}$ % of the annual GDP in United States and it was aimed at undermining the United States as well as the international financial market's stability (Johnston & Nedelescu, 2006).

As evidence of cooperation in the international financial market, there was a recorded decline in Standard & Poor's 500 index between the 17th and 21st September of 11. 6 % while the NASDAQ index recorded a decline of 16. 1 % within the same time following the attack on World Trade Center (International Monetary Fund, 2001; Johnston & Nedelescu, 2006) and

(Becker et al., 1990; Rafiq, Vaziri & Alyusef, 2008, p. 143). The ripple effect following the attack was evident in international financial markets where there was recorded sharp decline (Johnston & Nedelescu, 2006). For example, it is noted that the Dow Jones Euro STOXX index fell down by a whopping 17.3 % for the consecutive ten days following the attack of September 11 (International Monetary Fund, 2001; Johnston & Nedelescu, 2006).

In general, international financial markets share some common qualities that include increasing efficiency, increasing liquidity such that those seeking lending have an easy time accessing the finance as well as an improvement in transparency in their operation while maintaining integrity in all sections (Samitas, 2005). Additionally, international financial markets are in the process of continuously seeking ways and means of operation with increased cost efficiency and thus integration of new and emerging technologies in the running of the businesses (Samitas, 2005). International financial markets give an opportunity to stakeholders to access other markets that have similar operations and divergence in ordinary market to maximize on profitability (Samitas, 2005). Due to the difference in the market place for international financial markets, there is encouragement for more innovations and use of technologies for effectiveness in operations and thus makes financial and other corporate institutions become effective and profitable (Samitas, 2005).

Difference in International Financial Markets

However, despite the notable and the well acclaimed integration and cooperation between different international financial markets, there are also

disparities that have emerged in international financial market arena mainly due to the fact that some of these international financial markets are centralized to certain regional frameworks. A good example can be sourced from the Middle East and Asian countries that over a long period have had a regional market in the name of international financial market (Duangploy & Gray, 2005, p. 225 +). During the mid to late 1996 to 1998, the Middle East experienced a great recession after the famous economic boom in the region following successful oil and natural gas exploration (Duangploy & Gray, 2005, p. 225 +). The near-collapse of the financial market of that region led to the development of stiffer and more sustainable regulation famous as the Basel II and later Basel III accords (Duangploy & Gray, 2005, p. 225 +). As it seems, although the level of liquidity in region was upbeat, there were some crucial international financial market information and regulations that were overlooked that led culminated in this recession (Duangploy & Gray, 2005, p. 225 +).

On the other hand, Christiano and Eichenbaum (1995; Laing, 2011, p. 37), Crane (2007; Laing, 2011, p. 38) do show a comparative study of a similar nature. In their works, it is noted that the U. S. mortgages and subprime mortgages financing in late 1990s through to 2005 saw a record increase and overpricing of the housing boom with more middle-class being offered subsidized mortgage financing such that the initial repayment values appeared small and relatively manageable that later shifted to high repayment figures that these people could not afford and most of them resulted in selling their houses to repay these loans (Laing, 2011, p. 37). Conversely, the financial market offered these financing with open arms and

capitalized on it until 2009 when the issue led to mass demonstrations and public outcry of foul play by financial institutions (Laing, 2011, p. 37). As a result of this there have been numerous campaigns like the Occupy Wall Street campaigns that have been fueled by these occurrences.

Comparing these two scenarios, it is clear that international financial markets played a role in the recession by offering more liquidity that could not be serviced. For U. S. there was a recession in the stock market while in Middle East there was a recession in the banking sector with some banks having to file for bankruptcy protection and others closing their doors altogether due to the depth of these effects (Laing, 2011, p. 37). U. S. housing recession was mainly attributed to the subprime mortgages that in return affected the global financial market as reported by Crane (2007; Laing, 2011, p. 38).

Valli (1995) notes that the U. S. capital market tends to share more of their risks with investors and other agents and thus in the event of a recession, the U. S. capital market takes only a small portion of the shock and transfers the rest to the investors and other agents (p. 83). Comparing the U. S. subprime mortgage housing recession and the effects this had on Australia financial market and the housing sector, it is evident that there was no effect on the Australian market especially in housing categories AAA and AA, an indication of the disparity in their financial market approach and housing financing (Laing, 2011, p. 37 +). As early as 1981, Dufey and Giddy (1981) found that different international financial markets use different market instruments, which to some extent are to blame for some forms of recession (p. 33). For example, it was noted that over time, different international

financial markets offered different monetary exchange for different currencies and that while some institutions focused on saving, others focused on investing across the board for equitable distribution of risks (Dufey & Giddy, 1981, p. 33).

As far as regulation of multinational enterprises in different international financial markets are concerned, there lacked a common regulatory environment and thus different competitive conditions coupled with differences in exchange rate by sudden and/ or unexplained changes that add to organization risks in these financial markets (Dufey & Giddy, 1981, p. 36).

A study by Rafiq, Vaziri and Alyusef (2008) also showed that the U. S. capital market did have a substantial effect on the Japanese market when comparing between Standard & Poor's 500 index and Nikkei index while the Japan's capital market did not have as much changes as would be thought on the U. S. market. Seemingly similar results are obtained from the works of Duangploy and Gray (2005) when considering U. S. – GAAP (generally acceptable accounting principles) and that of Japanese – GAAP (p. 225 +). Although there were many similarities in operation and after harmonization of the Japanese – GAAP to international standards, there is still evidence of disparity in as far as financial ratios preparations is concerned with the U. S. – GAAP offering a relatively optimistic model to profitability (Duangploy & Gray, 2005, p. 225). On the other hand, the model offered higher debt risks as well as decrease in sales generation efficiency (Duangploy & Gray, 2005, p. 225).

Conclusion

In conclusion, it is evident that Bennett identifies four structural trends that can be used to define financial markets. This includes, but not limited to, globalization coupled with cross-border integration, technologies and the financial market and very large financial institutions that play a key role in the financial market. There are a myriad of published literature that indicate clear cooperation between various international financial markets. Samitas continue to note that common international financial markets have adopted a common approach towards market liberalization and deregulation which is an indication of cooperation. Looking at the United States' market trend, it is interesting to note that there has been a noted integration of cross-border international market in its financial market that can be attributed to increased globalization. International financial markets give an opportunity to stakeholders to access other markets that have similar operations and divergence in ordinary market to maximize on profitability. However, despite the notable and the well acclaimed integration and cooperation between different international financial markets, there are also disparities that have emerged in international financial market arena mainly due to the fact that some of these international financial markets are centralized to certain regional frameworks. When all is said and done, one thing that remains clear is the indispensable part that the international financial markets play in economic growth of local and multinationals despite the difference in working environment.

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