Mohamed Khaider University, Biskra

Faculty of Economics, Commerce and Management Sciences

Commerce Department

Module: International Finance

Branch: International Trade
Level: Third year Bachelor

Lecture 03: International Financial System

Learning Outcomes

When you have completed your Study of this Lecture and its readings, you will be able to:

- Defining the concept of the international financial system.
- Analyzing financial globalization and identifying the key factors driving it.
- Highlighting the significance of global financial centers.

1-Definition of International Financial System:

The global financial system encompasses financial markets and institutions that function within the legal and tax framework of international commerce.

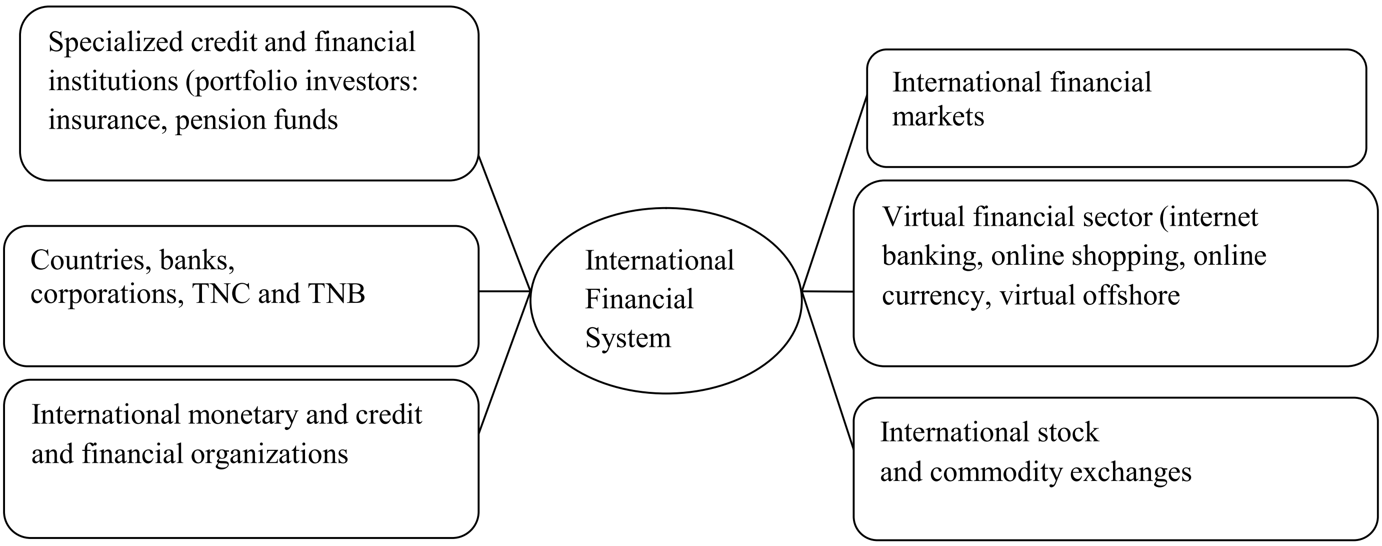

Fig. 1 The main components of world's financial system

- **National Participants**: These consist of corporations, banks, specialized credit and financial institutions (such as insurance and pension companies), stock and commodity exchanges, and government entities.

- **International Participants**: This category includes multinational corporations, international banks, transnational banks (TNBs), specialized financial institutions, major stock and commodity exchanges, and international monetary and financial organizations.

- **Role of Commercial Banks**: Commercial banks play a central role in the global financial market due to their extensive financial activities. Their liabilities primarily consist of deposits with varying maturities, while their assets include loans to corporations and governments, deposits in other banks, and bonds.
- **Corporations and Capital Attraction**: Corporations, particularly transnational corporations (TNCs), seek foreign capital to finance their investments through equity sales, loans, and the issuance of debt securities in international capital markets. Bonds issued by corporations in a currency different from that of the financial center where they are sold are known as euro bonds.
- **Non-Bank Financial Institutions**: These institutions engage in diversifying their portfolios of foreign assets through various investment strategies.
- **Central Banks and Government Borrowing**: Central banks participate in global financial markets through currency interventions. Governments secure funding from international sources by issuing bonds and borrowing from foreign commercial banks. In developing countries, both government bodies and state-owned enterprises rely on loans from international commercial banks.

2-Financial Globalization and the global financial system
The current global financial system operates and develops in conditions of financial globalization.
A-Definition of Financial Globalization
It is an objective process of the integration of a large part of capital of different countries, strengthening of their interdependence.
B-Main Features
The availability of huge financial resources of TNCs and TNBs.
High intensity of cross-border financial transactions of the global financial system's members.
The emergence of new mechanisms and instruments of international financial transactions and the formation of the world financial market.
The international market and off-market redistribution of financial resources is carried out through the world financial market.
C-The driving forces of financial globalization
International financial integration
International financial institutions
Financial innovations.

- International Financial Integration

The goal of international financial integration is to eliminate barriers to the movement of financial capital. It involves unifying financial services, banking operations, and payment systems, liberalizing customs procedures, and coordinating activities through international financial and credit institutions. Additionally, it aims to establish a global monetary system with a standardized world currency.

The European Union has made significant progress in financial integration through its single financial area concept, which includes:

- Full liberalization of capital flows and payment transactions.
- Open market access for banking, insurance, and financial services among partner countries.
- Harmonization of banking, tax, and investment regulations.
- Strengthened supervision of national credit and financial institutions to protect investors.
- Enhanced transparency and public access to financial regulations.

- International Financial Institutions

The international financial system consists of major global organizations such as the International Monetary Fund (IMF) and the World Bank Group (including the International Bank for Reconstruction and Development, International Finance Corporation, and International Development Association), as well as regional financial institutions. These organizations form an extensive network of currency, credit, and financial institutions.

Their primary objectives are:

- Stabilizing the global economy and financial systems.
- Regulating international currency, credit, and financial markets.
- Developing and coordinating international monetary and financial policies.
- Providing loans and financial assistance.
- Establishing principles for the global monetary system and resolving international financial challenges.

Their financial resources contribute significantly to official international aid flows.

- Financial Innovations

Financial innovation refers to the development of new financial instruments such as Eurodollar certificates of deposit, foreign exchange swaps, zero-coupon eurobonds, syndicated eurocurrency loans, and euro notes as well as the implementation of new financial technologies.

Technological advancements enhance the speed, efficiency, and volume of international financial transactions, improving overall financial market operations.

3-Global financial Centers :
These centers are: New York, London, Zurich, Luxembourg, Frankfurt am Main, Singapore, Hong Kong, Bahamas, Panama, Bahrain and others. International banks, consortiums of banks, the stock exchanges, which engaged in international foreign exchange, credit, transactions with securities and gold are concentrated in these centers.
The national currency, credit and equity markets, that are closely interconnected with the similar global markets, take part in the operations of the world financial market The global financial centers were formed on the base of the huge domestic markets. They conduct international operations.
Global financial centers (GFC) occur in the countries where there are:

- sustainable monetary and economic position;
- the developed credit system and well organized exchange;
- moderate taxation;
- preferential currency legislation, that allows access of foreign borrowers and securities to exchange quotation;
- comfortable geographical location:
- relative stability of the political regime;
- standardization and high degree of information technologies of paperless operations are on the base of the use of the newest computers.

Reference

Y.Kozak and others. Essentials of International Finance: Questions & Answers. Tbilisi Publishing House „ Universal“ 2017