A new RESOURCE *for* STRATEGISTS

The state's growing post-crisis role in banking and finance highlights the need for more reliable comparative data across diverse global markets. Bangor Business School's Professor JONATHAN WILLIAMS welcomes a World Bank initiative covering 203 countries.

In banking and other financial markets, strategists and policymakers devote a considerable amount of time to collecting, collating, organising, analysing and interpreting data. Data analysis can reveal if a policy initiative, say to raise the level of competition between banks by deregulating interest rates, realises the intended outcome; or analysis can identify and verify which markets offer the greatest potential for financial investors.

Despite the importance of good quality analytical acumen, the sources of relevant information tend to be disparate. This creates inconsistencies and makes it more difficult to compare apples with apples. Although economists working at the World Bank amongst other agencies did prepare and make available often very detailed databases of information, until recently no formal attempt tried to collate the different datasets.

Each of us should be interested in financial system development and the relative performance of financial firms. Financial institutions and financial markets (both bank and non-bank) exert a powerful effect on economic growth, the alleviation of poverty, and economic stability. Financial intermediaries like banks resolve information problems and identify the most promising firms to invest in. Similarly, banks and markets mobilise savings and channel those resources to end-users like firms.

The monitoring of firms and other borrowers by financial intermediaries offers scrutiny of managerial performance and assists in improving corporate governance as well as limiting the potential for agency conflicts, which should positively affect the efficiency of firms. A competent financial system offers opportunities to diversify risk and provide investment in high-risk, high-expected returns projects that may not receive financing otherwise. Ultimately, an efficient financial system lowers transaction costs, which benefits trade, innovation and growth. However, from time to time, markets can fail with devastating impact. Poorly functioning financial systems retard the economic growth process and destabilise economies often harming most the poorest in society.

A vital feature of the policies governments the world over chose to enact in response to the banking and economic crises of 2008-09 is a greater role for the state. The obvious and (with the benefit of hindsight) the most controversial employment of state resources relates to the recapitalisation of banks suffering extreme duress as the credit crunch bit hard with key markets like the interbank turning into channels of contagion.

Some countries like the UK chose to nationalise a handful of banks to facilitate the recapitalisation process. Across the advanced group of industrialised nations, quantitative easing let the money supply increase to keep markets liquid and to avoid a credit crunch. In other countries, particularly in the emerging markets, governments opted to use state-owned banks or development banks as a channel of funding not only to assist private-owned banks in distress but also to financially aid private-owned corporations typically via equity purchases.

In response to developments in public policy that emphasise a leading role for the state, the World Bank published its inaugural Global Financial Development Report *Rethinking the Role of the State in Finance* in 2013, followed by a second Global Financial Development Report on *Financial Inclusion* in 2014. An extensive exercise of collating different databases has culminated in the release of the Global Financial Development Database (GFDD) by the World Bank, which offers statistical support for its new series.

> *"Aside from its unambiguous benefits to researchers and policymakers, the World Bank's new database could become an important resource for bankers and other financial industry participants."*

The organisation of the GFDD follows a 4x2 framework which reveals the areas of financial activity and markets that the World Bank regards as most important. The two markets are the banking sector and the non-bank financial sector, which includes stock and bond market activity. The crisis did demonstrate the increasing importance of the shadow-banking sector, which researchers struggled to sufficiently quantify and assess.

The GFDD uses four broad financial system measures – depth, access, efficiency and stability – and offers several indicators of each measure for bank and non-bank sectors:

- **Depth indicators** measure the size of the bank and non-bank sectors. Plentiful evidence reports the causal effect of financial deepening on economic growth.
- **Access measures** identify the proportion of the population with a bank account and government bond yields amongst other indicators.
- **Efficiency measures** include indicators such as net interest margins and the ratio of overhead costs-to-assets, whilst the ratio of stockmarket turnover-to-stock market capitalisation performs the same function for markets.
- **Stability** of the bank and non-bank sector, lastly, is indicated by the Z score and PE ratio.

The GFDD covers 203 countries with some data available from 1960 to 2011. Whilst the new database majorly improves on what was formerly available, the extent of the coverage varies across countries and measures.

Aside from unambiguous benefits to researchers and policymakers, the GFDD could become an important resource for bankers and other financial industry participants. At national level, a banker could observe trends, say, in market concentration, and use the sector-level information on items including interest spreads, profitability, cost efficiency and stability to gauge the performance of their own institution. An investment manager could identify the volatility of national stock and/or bond markets as part of defining an asset allocation strategy.

An international banker could use the GFDD to identify possible countries and/or regions for the bank to expand. How deep is the target banking market, the stock market? Does the level of financial inclusion suggest there is room to grow the business? How efficient, competitive and stable are the banking and non-banking sectors in these countries? Should the bank specialise or offer a universal package of products and services?

Downloads: The latest (April 2013) version of the Global Financial Development Database is available for download from the World Bank website. Links to earlier versions are also available as are links to relevant working papers and the Global Financial Development Reports.

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