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Dynamics of global financial governance: Constraints, opportunities, and capacities in Asia

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Abstract

Policy design, or the deliberate governmental effort to attain desired policy objectives, is an integral part of micro and macro-level fiscal and financial regulation. This paper seeks to address the role of regime coherence and policy capacity in contributing to effective financial policy design. Drawing on the cases of the Global Financial Crisis and Asian Financial Crisis and focusing on Asian states, we assess regime capacity at both international and domestic levels. We argue that it is the integration of analytical, operational and political capacities that have contributed to the overall ability of a government regime to address and respond to crises.
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1. Introduction

Policy design, or the deliberate governmental effort to attain desired policy objectives, is an integral part of micro and macro-level fiscal and financial regulation whose salience has increased in recent decades, reflecting growing recognition of its role in driving economic growth (Beck, Levine, & Loayza, 2000; King & Levine, 1993; Levine, 1997). As a result, governments around the world have devoted considerable efforts to maintaining and promoting the 'finance-growth nexus' deemed crucial for continued economic and financial sector growth (Woo, 2015, 2016). In the context of Western developed economies at least, such efforts have largely focused on the development and implementation of financial regulatory and supervisory infrastructure, notably in the form of codes of conduct, disclosure laws, regulatory bans and rules of conduct (Capie, 2007; Murinde & Mlambo, 2011; Vittas, 1993), intended to enhance transparency and discourage risky behavior, including fraud and malfeasance.

However, neither policy designers nor policy analysts have been able to adequately address the conditions that trigger crises or the capacities required to prevent or ameliorate crises, as their continued frequency and pervasiveness

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appear to demonstrate. This is due at least in part to the fact that the nature and form of financial regulatory policies promulgated has often been motivated and determined by extant political interests and contestations as well as the influence of political and technocratic elites (Carney, 2001, 2010; Hamilton-Hart, 2002; Lall, 2012; Rajan & Zingales, 2001). However, the exact impact and influence of such activities varies and is little understood.

We seek to address this gap by relating the design of domestic financial policies to the coherence of the relevant internal and international policy regimes. By coherence, we refer to the extent to which the various components of a regime (policy processes, objectives, actors, institutions, etc.) are arrayed and directed towards some collectively defined purpose (Howlett & Rayner, 2006, pp. 168–169). We argue, following Wu, Ramesh, and Howlett (2015), that three types of capacities enhance regime coherence – analytical, operational and political – and that each of these is an important determinant of successful or unsuccessful financial policy design.

That is, a deficiency in any of the components of capacity may pose dire implications for policy and governance as this could lead to a lack of coherence in policy outputs and processes. More importantly, deficiencies in the capacity of either domestic or international regimes or both can result in undesirable policy outcomes. In sectors such as finance and banking, these deficiencies often manifest in crises, which occur when a regime is not capable of dealing with exogenous and/or endogenous shocks. However, and as we further argue in this paper, there are also positive aspects of such crises, as when they provide 'windows of opportunities' for policy designers to assess existing deficiencies in regime capacity, stimulate reconfigurations of regime dynamics, and embark on capacity-building efforts which can promote greater integration and regime coherence.

In order to explicate our argument, we draw on the cases of the 1997 Asian Financial Crisis (AFC) and the 2008 Global Financial Crisis (GFC). We focus especially on the impacts of these two crises on the banking and finance sector in Asia. However, unlike most comparative case studies, the two crises are studied as chronologically linked cases. Taking such a chronological approach allows us to assess changes and adaptations to regime coherence and capacities over time. It further allows us to establish a 'checklist' of regime capacity, which, along with our conceptualization of regime coherence, offers a useful analytical tool for assessing regime capacity and identifying any shortcomings or deficiencies in capacities which states and regimes may have. This provides a more systematic way of understanding the ways in which regime capacity and coherence can facilitate the design of effective financial sector policies which has implications for other sectors.

2. Multi-level governance and international regimes

In an interdependent and globalized world, public policies are increasingly characterized by transnational origins and consequences. This is particularly true for banking and finance, which in most countries has become increasingly globalized (Eichengreen, 2008). This globalization of finance and banking has brought new challenges for national policymakers as they now need to cooperate and coordinate policies not only at the domestic level, but also at the international level, with the consequence being a weakening of these policymakers' autonomy, in addition to the growing difficulty of governing national regimes across this increasingly complex policy landscape.

Finance and banking policies increasingly require cross-border regulatory cooperation and coordination to be effective (Rodrik, 2012; Schoenmaker, 2011). This internationalization of regulation poses major challenges for national regulators, with states struggling to define the boundaries of monetary sovereignty in the globalized world economy (Lastra, 2006; Zimmermann, 2013).[1] The emergence of networks of policymakers in the form of "transgovernmental coalitions" (Keohane & Nye, 1974), or "transnational executive networks" (Slaughter, 2005), the rise of private sector and non-governmental organizations (NGOs) (Büthe & Mattli, 2013; Keck & Sikkink, 1998; Rosenau & Czempiel, 1992; Strange, 1996; Tsingou, 2015), and a greater role attributed to intergovernmental, regional, or international organizations are all recent developments and have raised questions over the extent, or indeed possibility, of the capacity of national authorities to effectively regulate finance and banking on their own.

[1] Monetary sovereignty is defined as "the power to issue and regulate money" (Lastra, 2006, p. 16). The state has power to issue notes and coins, can regulate money, control supply of money and interest rates, control exchange rate, and impose exchange and capital controls (Lastra, 2006, pp. 22–23).

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