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Financial Market Deregulation Special Issue Introduction

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Financial markets are essential for economic growth and development, because they provide the crucial function of financial intermediation from savers to borrowers and allow for the spreading of risks among individuals with varying levels of risk exposure preference (Schumpeter 1911 and Saint-Paul 1992).[3] Supporting this link between financial markets and economic growth, King and Levine (1993) provide cross-country evidence suggesting that high levels of financial development are positively associated with faster rates of economic growth, physical capital accumulation and economic efficiency improvements, after controlling for country specific characteristics. They also find that financial development is a predictor of long-run (10-30 years) economic growth. But beyond this macro-level perspective, access to financial markets is essential for economic development because access to the formal economy often hinges on whether or not an individual is banked, i.e., employers can direct deposit wages into their

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[3] The direction of causation in the relationship between financial markets and economic development runs both ways. While growth requires well developed capital markets, well developed capital markets are also a product of economic growth. Greenwood and Jovanovic (1990) suggest financial intermediation and economic growth are inextricably linked.

The Impact of the Community Reinvestment Act on Neighborhood Gentrification

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Abstract

This paper examines whether the Community Reinvestment Act (CRA) is fulfilling its statutory goal of promoting lending to low- and moderate-income (LMI) communities. We use Home Mortgage Disclosure Act (HMDA) data for the District of Columbia to analyze patterns of bank lending across census tracts. We find that most CRA lending goes to non-LMI borrowers in LMI census tracts, consistent with the hypothesis that banks are "skimming off the top": lending to less risky borrowers while fulfilling the letter (though not necessarily the spirit) of the CRA. We further explore the question of whether the CRA might be speeding up community gentrification by facilitating lending to higher-income residents moving into historically low-income neighborhoods. In the context of supply-side constraints on housebuilding, this could speed up demographic and socioeconomic changes in CRA census tracts, undermining the financial inclusion objective of the CRA.

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Financial Regulation and Income Inequality

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Abstract

Several studies find that the liberalization of financial markets is associated with lower inequality, possibly due to greater access to credit for those at the lower end of the income distribution. Others, such as de Haan and Sturm (2017), find that liberalizing financial markets increases income inequality. One explanation for the divergent results is that liberalization is a product of the political process. If incumbents in the financial industry hold political power, they may counter efforts to deregulate by lobbying for re-regulation to protect their interests. Using an alternative measure of liberalization in a large panel of countries, we confirm the positive association between inequality and liberalization found by de Haan and Strum (2017). However, our results indicate that the positive association between inequality and liberalization decreases in magnitude and significance once a measure of banking supervision regulation is included in the analysis. Moreover, we find that banking supervision regulation is positively associated with income inequality. Based on this evidence, we conclude that one plausible explanation for the positive association between in income inequality and financial market liberalization is that the process of deregulation is often captured by incumbents.

Shadow Banking Activities of Non-Financial State-Owned Enterprises and Financial Regulation in China*

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Abstract

After the global financial crisis in 2008, a new form of shadow banking emerges rapidly in China. Non-financial state-owned enterprises (SOEs) re-lend the low cost funds they obtain from

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Learning from The Financial Crisis: What Can Basel II Teach Us About How Basel III Will Fare?

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Abstract

The global economy is more connected than ever before, through both trade and investment. Financial regulations in one country impact other countries much more, as crises that begin localized can have significant global impacts. As a result, there is wide support for international financial regulation and banking supervision standards to harmonize standards and prevent one country's poorly designed regulatory regime from negatively impacting other countries. However, international financial regulations suffer from shortcomings themselves. This paper will attempt to address the potential problems of the newest international banking regulatory framework, using a historical narrative to understand the shortcomings of the Basel II regulations in the financial crisis in the United State, and public choice theory to understand the mechanisms and incentives that helped shaped those provisions of the regulation. Understanding the incentive structure that helped cause the failures of Basel II can help us understand the potential for future problems with Basel III.