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Conference Report on the 46. Radein Research Seminar "A New Global Financial Architecture in the Aftermath of the Crisis: A European View"

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Since 1967, the purpose of the *Forschungsseminar Radein e.V.* (*Research Seminar Radein*) is to promote scientific research in the field of economic and social orders. The objectives, as stated in the by-laws, are achieved by organizing meetings (particularly the annual Radein Seminars) and by publishing the findings if they are relevant. The subjects of the *Research Seminar Radein* are wide-ranging and always topical. As a result the seminar succeeded in integrating different specialist fields and ways of thinking within the sphere of theories of economic order and comparative systems.

In February 2011, the *Research Seminar Radein* engaged the members of this year's committee to organize a conference to the topic "reorganization of the financial markets as a result of the global financial crisis" for the annual meeting of the *Research Seminar* in February 2013. The objective of the conference was to bring together international researchers, academics and central bankers interested and involved in the field of international financial architecture. The organizers called for papers on a wide range of topics, including the future of international capital markets, international regulation of financial markets, the new role for monetary and fiscal policy, financial development and economic performance and the European retail market for financial services.

At that time, it was really difficult to predict the further development of the financial crisis and especially the growing intensity of the European sovereign debt problems with milestones like the haircut on Greek sovereign debt in March 2012, the tremendous Long-term Refinancing Operations (LTROs) conducted by the European Central Bank in December 2011 and March 2012 with net injections of more than 800 bn. EUR or the readiness of the ECB for the unlimited purchase of government bonds under certain conditions in September 2012 ("Outright Monetary Transactions", OMTs). So, of course, our expectations with regard to the topics and main policy conclusions of the contributed papers were completely different from today.

From February 11 to 16, 2013, the *Research Seminar Radein* hosted the 5-day conference entitled, "A new global financial architecture in the aftermath of the crisis: A European view" the first time in collaboration with *Kredit und Kapital* in Radein/South Tyrol (Italy). After the end of the call for papers in summer 2012 and the following standard refereeing process at *Kredit und Kapital*, the organizing committee invited the authors of five accepted papers to present and discuss their results at the main conference. Furthermore other authors were directly asked to present their papers in Radein. Provided that, a publication in *Kredit und Kapital* was envisaged, these papers were reviewed by the organizing committee and then peer reviewed by referees in order to improve and get ready for publication.

Finally, ten papers were chosen for the main conference and were complemented by two keynote speeches given by Hans-Peter Burghof (University of Hohenheim) and Thomas Mayer (Center for Financial Studies, Goethe University Frankfurt/M., and Deutsche Bank, Frankfurt/M.). Furthermore, five of the nine lectures in the free part of the conference, a slot traditionally reserved for PhD students, were strongly related to the topics of the main conference. As a result, many of the originally envisaged topics in the preparation of the conference could actually be discussed in Radein.

After a short introduction to the current situation on the financial markets by the member of the organizing committee Franz Seitz (University of Applied Sciences, Amberg-Weiden), Hans-Peter Burghof gave a detailed summary of the developments since the beginning of the financial crisis and a further outlook especially from a business management view. Furthermore, he elaborated on the sense and the perspectives of a European banking union.

In their empirical paper "The U.S. current account and real effective dollar exchange rates" Joscha Beckmann and his co-authors Ansgar Belke and Robert Czudaj (all University of Duisburg-Essen) dealt with the global imbalances issue from a financial markets perspective and analyzed the long-run determinants of the U.S. current account employing an innovative variant of the econometric regime switching approach. Applying multivariate cointegration techniques, they pay particular attention to the evolvement of the coefficients over time based on an estimation of a time varying coefficient approach and Kalman filtering. The underlying coefficients turn out to be subject to substantial instabilities. Another result is that the link between the current account and the exchange rate does not seem to be in line with theory at least over the last decade. This is true for both short-run dynamics and long-run relationships.

In their contribution "Rethinking remuneration laws for the financial sector" Jonathan Ben Shlomo (co-author Tristan Nguyen, University of Lahr) described in which way inappropriate remuneration structures can contribute to excessive risk taking, that such remuneration structures persist in the aftermath of the crisis as part of the finance industry's remuneration culture and that efficient regulation should ensure remuneration policies and structures to be aligned with an effective risk management. The financial authorities should therefore closely observe the market development in this perspective and take countermeasures if necessary. Furthermore, it is important to eliminate the existing regulation gaps.

Elias Bengtsson (Sveriges Riksbank, Stockholm) explained the process according to which the Basel Committee on Banking Supervision (BCBS) developed the so-called Basel 3 accord in his paper "The political economy of banking regulation – Does the Basel 3 accord imply a change?". He also assessed whether changes in BCBS's governance and standard setting process may have caused the impact of Basel 3 to differ from the Committee's preceding accords Basel 1 and Basel 2. His findings indicate that the changes in the governance structure and influence of private players seem to have led the BCBS to develop an accord that is relatively less beneficial for the traditional BCBS member countries and large international banks. This suggests that the gain in power of the emerging markets and publicly accountable authorities has occurred in the political economy of banking regulation and the international financial architecture.

Ulrich van Suntum (University of Münster) developed a new macroeconomic model of an open economy in his paper "Long-term effects of fiscal and monetary policy in a stock-flow-consistent macro-framework". The core of the model is the financial sector with both a capital and a money market and correspondingly differing interest rates. He argued that some fundamental issues of fiscal and monetary policy could be discussed within this stock-flow-consistent framework. Concerning monetary policy, different regimes were assessed, including monetary abstinence, quantitative easing, and monetizing public debt. Furthermore, typical Keynesian policy measures such as rising wages, expansionary monetary policy, and public deficit spending were also analyzed. The main focus was on long-term effects of these measures, with the dynamics being only briefly sketched.

Giovanni Calice (University of Southampton) presented a paper entitled “An empirical analysis of the dynamic relationship between European sovereign CDS and government bonds“. He empirically explored the dynamic price discovery behavior of the CDS and the bond market for a group of European countries during the sovereign debt crisis in the Euro zone. Using a VECM framework, he was able to show that the sovereign CDS and bond markets are cointegrated and that there is considerable heterogeneity across European issuers in credit default swaps (CDS) markets in their contribution to price discovery. In particular, his evidence suggested price leadership of the Portugal sovereign CDS market whilst for Italy and Belgium the sovereign bond market appears to dominate. For countries such as Austria, Denmark, Finland and Spain, both markets contribute to the price discovery process of sovereign credit risk. Regarding the most vulnerable sovereigns in the euro area, such as Greece and Ireland, it is not obvious which market lead the other.

In his paper “Designing a stable and sustainable European financial architecture – Implications of a model that recognizes bank credit creation” Richard A. Werner (University of Southampton and Centre for Banking, Finance and Sustainable Development) explained the new consensus among economists that it is necessary to include a banking sector in macroeconomic models, and include systemic, macroeconomic feedbacks in the finance and banking theory. In the analysis he employs a model that fulfills the requirements by distinguishing between different types of bank credit – credit boosting GDP and credit boosting asset prices which in turn causes banking crises. The implications of this model are explored for the design of a financial architecture that is more stable and likely to deliver sustainable growth. This also includes concrete proposals on how to resolve the European sovereign debt crisis and deliver stable growth in the Euro zone, while avoiding the corner solutions of euro exit or fiscal union.

In his paper “Crises and exchange rate regimes: The time to break down the bipolar view?” Moussé N. Sow (University of Auvergne, Clermont-Ferrand) revisited the link between crises and exchange rate regimes (ERRs). First, he asked for the legitimacy of the bipolar view that the corner solutions – to peg or to float – are immune to crisis and the moral hazard hypothesis that an exchange rate peg is conducive to financial crisis due to the implicit insurance. Second, he tested empirically the fiscal theory of currency crisis (FTC) which states that pegged regimes are not sustainable under fiscal imbalances. Third, he offered some empirical evidence regarding the vulnerability of the alternative regimes to debt crises. His main findings strongly reject the systematic claim that intermediate regimes are more vulnerable to crises compared to the hard peg and the fully floating regimes. In addition, his results do not support the moral hazard hypothesis, while the FTC is empirically validated. Besides, he finds support that pegged regimes are more prone to debt crisis than intermediate regimes, while floating regimes appear less vulnerable compared to soft pegs. As a consequence, he clearly breaks down the traditional bipolar view. The results are robust to regime classification, the econometric approach and the country's level of development.

Thorsten Polleit (Degussa Goldhandel, Frankfurt/M., and Frankfurt School of Finance & Management) then talked about "The financial and economic crisis and the aberrance of economics". From his point of view, the knowledge of the Austrian school of economics – founded in 1871 with the publication of Carl Menger's "Principles of Economics" – is well-suited to explain financial crisis and undesirable developments in the last decades. In this context, he argued that "positivism-empiricism-falsificationism" has become the 'state-of-the-art' methodology of economics. He claimed that this approach (1) suffers from (logical) deficiencies when applied to the science of human action and (2) has helped legitimizing, and putting into practice, policies that have actually contributed greatly to bringing about the latest financial and economic crisis. He outlines the 'Austrian', or to be more precise: the 'Misesian' method (*praxeology*), as the proper methodology in the field of social science. What is more, he applied his approach to the arguably uncontrolled expansion of fiat money by the central banks.

In his paper "Cross-border retail banking: Exploring the unknown financial globalization in times of financial crises" Harald Sander (University of Applied Sciences Cologne, co-author Stefanie Kleimeier, University of Maastricht) elaborated upon the transmission channels between the local markets in stress situations especially in the Euro zone. Employing a unique data set of European cross-border financial instruments, the study uses various specifications of gravity models. He started from the observation that the surge in cross-border banking prior to the

2007/08 global financial crisis took place not only in the interbank market but also in the retail market, e.g. between banks and their private customers abroad. Cross-border retail activities of banks now account for a substantial share of total international activities. In order to understand the role of cross-border retail banking for globalization and stability, he assessed this less known part of financial globalization by reviewing the development and structure of cross-border banking. For this purpose, he identified the factors that drive retail customers across borders and gauged the impact of financial crises on global retail banking.

The next contribution was entitled "Do we need a separate banking system? An assessment". Motivated by the current discussion on different separate banking systems, Michael Schröder (Centre for European Economic Research (ZEW), Mannheim, and Frankfurt School of Finance & Management, Frankfurt/M., co-author Gunnar Lang, ZEW Mannheim) provided an overview of the different systems, questioned them and outlined their effect on systemic stability and the German banking sector. The results showed that the various separate banking systems only play a minor role in reducing and limiting systemic risk. A separate banking system could, however, facilitate banking supervision by reducing the banking system's complexity. Furthermore, credible threats to not support investment banks with federal resources in times of crisis could lead to a more adequate incentive structure of suppliers of equity and outside capital. More efficient measures to further reduce systemic risk in the financial sector should, however, use different levers, such as additional minimum regulatory capital requirements.

In the written version of his keynote speech "Does the euro need a state?" Thomas Mayer explained at first the different money systems and orders according to Walter Eucken: commodity money, debt money and credit money and the implications for the European Monetary Union (EMU). In his analysis he concludes that the majority of EMU members see the euro as debt money and the ECB as part of an "economic government", only a minority of the members sees the euro as "commodity money". In his paper he explained the usefulness of soft and hard parallel currencies and the opportunities of a three-tier EMU divided in a Latin (core-) group, in a northern group and in a southern group of member states.

The discussion in the "core part" of the conference went along with the following topics presented and discussed in the "free forum" of the conference: (i) "Is there a speculative bubble in the price of gold?" (by Patrick

Stephan: co-authors Jedrzej P. Bialkowski, Martin T. Bohl and Tomasz P. Wisniewski), (ii) "Contagion during the sovereign debt crisis" (by Andreas Kokot: co-authored by Heinz-Dieter Smeets), (iii) "Transaction costs in the interbank market and bank lending in the Euro area" (by Achim Hauck: co-authored by Monika Bucher and Ulrike Neyer), (iv) "An ethics of financial markets based on John Locke's theory of appropriation (authored and presented by Felix Heider) and (v) "Exchange rate nonlinearities in EMU exports to the US" (authored and presented by Florian Verheyen).

On behalf of the organizing committee of the *Research Seminar Radein* and *Kredit und Kapital*, we wish to thank the authors and referees of the papers for working with us on a tight schedule and the conference participants for stimulating comments that led to papers even more significant for academics and practitioners alike.

This issue (Heft 2) and the following issue (Heft 3) of *Kredit und Kapital* contain nine papers of the main conference and in addition the keynote speech of Thomas Mayer. This selection will be augmented by an externally contributed paper by Roland Vaubel (University of Mannheim) on "Why the current plans for European Banking Supervision are not well founded".

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