Open access • Journal Article • DOI:10.1504/IJRAM.2016.074433

Theory and Regulation of Liquidity Risk Management in Banking. — Source link

Enzo Scannella

Institutions: University of Palermo

Published on: 01 Feb 2016 - International Journal of Risk Assessment and Management (Inderscience Enterprises)

Topics: Liquidity crisis, Liquidity risk, Funding liquidity, Accounting liquidity and Market liquidity

Editorial

Enzo Scannella

Department of Economics, Business and Statistics,
University of Palermo,
Viale delle Scienze, Building n. 13,
90128, Palermo, Italy
Email: enzo.scannella@unipa.it

I am deeply honoured to be the guest editor of this special issue 'Finance in the time of crisis: new perspectives on sustainability'. The papers collected in this special issue have mostly been selected among the papers presented at the Business Systems Laboratory's 2nd International Symposium on 'System thinking for a sustainable economy: advancements in economic and managerial theory and practice', which was organised on 23–24 January 2014 in Rome, Italy.

The aims of the symposium were to bring together researchers and practitioners who conduct research on business and management to discuss the most recent advances in economic and managerial theory and practice, and to address the global sustainability challenges by a multidisciplinary systemic perspective. The symposium was organised along nine core subjects: advancements in systems thinking; viable firm; sustainable development; sustainable marketing; education for sustainability; business models for sustainability; corporate social responsibility; economic development; and sustainable finance. Most of the papers in this special issue are extended papers presented at the 'Business models for sustainability' session and at the 'Finance in time of crisis' workshop.

Thinking about finance today entails responding adequately to the question: what is the proper function of finance? The financial crisis that erupted in the middle of 2007 has caused several structural changes in the global financial system. It started in the USA, but rapidly expanded globally owing to the growing globalisation of economies, and the interconnectedness of national financial systems, financial institutions, and corporations. The financial crisis revealed fundamental weaknesses of the financial systems and vulnerability of business models and financial practices adopted by financial institutions, regulators, and corporations.

The effect of the financial crisis was felt far beyond the financial sector. It is systemic in nature. Financial turmoil is transmitted throughout the entire economy. In several countries, corporations, banks, and households have reported substantial deterioration in economic and financial conditions, liquidity problems, and heavy losses. Savings decisions, investment and financing decisions, and risk management decisions have been negatively affected by the increased market volatility, uncertainty, and financial instability.

What is today in a state of crisis is the nature, and meaning, of 'finance'. Is finance – which consists of a set of instruments, markets, and financial institutions that people and firms make use to allocate scarce resources over time – still a tool at the service of the economy? There is a general lack of confidence towards the original meaning of finance and the proper function of the financial system. The purpose of finance – which is connected with the transfer of economic resources through time, across borders, and among industries; managing of risk; dealing with incentive problems; pooling of resources – is put under severe pressure by the financial crisis.

The severity of the financial crisis has raised many theoretical and empirical questions on the objectives and meaning of finance nowadays. Confidence in the finance sector fell globally, suggesting doubts over financial innovation, and the sustainability of financial practices and business models.

We are in search of a new way to do finance, through a set of economic operations regarding the exchange of assets, liabilities, and risk, in accordance with the original meaning and purpose of finance. That involves also a deep analysis of the dominant ideological context that has set the background of the financial crisis: globalisation of finance; market-centric view of the financial institutions management; predominant role of financial markets; efficient markets hypothesis; short-termism paradigm; information asymmetries, adverse selection, moral hazard, excessive risk-taking, and distorted incentives in the financial intermediation chains; financial deregulation and liberalisation; financial innovation.

The purpose of this special issue is to offer different perspectives on finance sustainability and to develop analytical frameworks for the analysis of the drivers of sustainability at a firm and industry level. Financial mechanisms, instruments, markets, risk management techniques, and business models are identified and their interactions are examined and discussed in the following papers.

The first paper, by Enzo Scannella, is titled ‘Theory and regulation of liquidity risk management in banking’. The financial crisis has emphasised the importance of liquidity risk to the functioning of banking and financial system. The paper presents a theoretical and regulatory investigation of two types of liquidity risk in banking: funding liquidity risk and market liquidity risk. The paper analyses the different approaches to measure the impact of funding and market liquidity risk in the economics and management of banks. The paper provides also an analysis of the organisational implications of the asset and liability management perspective of liquidity risk.

The second paper, by Valerio Pesic, Fabrizio Santoboni, and Paolo Zenobi, is titled ‘The availability of consumer credit during financial crises’. The paper aims to provide an outline of the main factors that characterise the demand and offer side of the consumer credit market in Italy. In particular, the authors evaluate some management policies and commercial practices adopted by the leading Italian consumer credit firms in the aftermath of the recent financial crisis. The paper documents that the financial crisis strongly reduced the capability of consumers to achieve any financing for their consumption purposes.

The third paper, by Igor Perko and Franjo Mlinaric, is titled ‘Decreasing information asymmetry by sharing business data: a case of business non-payers sharing agency’. The paper focuses on sharing business partners’ defaults data. The authors propose a data-sharing mechanism whereby non-payment pattern data is shared to gain mutual advances. The authors demonstrate that the combined information from multiple data-reporting sources reduces information asymmetry and generates value added for the receivers; an efficient early warning system does not require complete information in order to optimise business decisions, and the default information sharing can cause negative feedback by the reported parties.

Rosa Lombardi, Raffaele Trequattrini and Giuseppe Russo write the next paper, 'Innovative start-ups and equity crowdfunding'. The paper is based on the following research question: what are the strengths and weaknesses of equity crowdfunding on the development of innovative start-ups? The paper analyses the development process of innovative start-ups, through the method of existing funds on a national level, with special attention to the new financial regulation of equity crowdfunding in Italy. The authors aim to interpret the effects of equity crowdfunding on the development mechanism of innovative start-ups, in comparison with other financing mechanisms.

The next paper, written by Sabrina Leo, is titled 'Capital requirements and credit policies in Italy: what effects do they have?'. The paper provides some evidence of the 'EBA effect' on credit supply of Italian banks in the period 2007 to 2012. The lending policies put in place by Italian banks have been strongly affected by Basel 2. The author confirms that the 'EBA effect' is not important in the Italian bank credit market. The author also suggests that domestic banks have to rethink their business models in order to ensure a sustainable level of profitability in the long term.

The next paper, by Marta Borda and Patrycja Kowalczyk-Rólczyńska, is titled 'Impact of demographic factors on household financial decisions – evidence from Poland'. The authors analyse the demographic changes observed in Poland in comparison with other European countries, and examine the types of household financial decision sensitive to demographic risk, with particular emphasis on borrowing decisions and decisions on private healthcare financing. Taking into account the current financial situation of households in Poland, as well as their future financial needs and possibilities, the paper focuses on details of the potential effects of demographic trends on the borrowing decisions and the decisions concerning additional private healthcare financing.

The final paper, by Anna Jedrzychowska and Ewa Poprawska, is titled 'Is the minimum amount of coverage from motor third party liability insurance enough to cover personal injuries?' The paper studies a particular market segment of the insurance industry: the compulsory motor third party liability insurance. The paper presents a detailed description of selected methods used in the calculation of annuities. It also investigates whether the legislature specified minimum amount of cover is sufficient to cover claims for personal injury annuity as annuities are paid for many years.

I would like to thank the authors of the papers, and all the participants at the Business Systems Laboratory's 2nd International Symposium, for their comments and suggestions, and the reviewers of the papers for their helpful support.

Finally, I hope this special issue provides readers with the insight that I gained in editing it.