WEEK 1: INTRODUCTION TO INTERNATIONAL BANKING

LEARNING OBJECTIVES:

1. **Defining and contrasting international and multinational banking**
2. **Explain why domestic banks expand aboard**
3. **Identify the various organisational forms MNBs might take overseas as well as the advantages and disadvantages of each**

WHAT IS INTERNATIONAL BANKING

- International banking is the business undertaken by banks **across national borders** and/or activities that involve **different currencies**
- Lewis and Davis (1987) classify international banking into **traditional international banking** and **Eurocurrency banking**
  - **Traditional international banking** involves transactions with non-residents in domestic currency that facilitates trade finance and other international transactions
  - **Eurocurrency banking** involves wholesale foreign exchange transactions (loans and deposits) with both residents and non-residents
  - **Both** entail financing trade, transacting foreign exchange business and making wholesale short-term Eurocurrency loans and deposits
- Traditionally international banking and eurocurrency banking does not necessarily require banks to have a physical presence in a foreign country
- **Multinational banking (MNB),** however, requires some element of **ownership & control** of banking operations outside home market through foreign direct investments (FDIs).

WHY DO DOMESTIC BANKS GO ABROAD?

- **OPPORTUNITIES FOR GROWTH AND PROFIT:**
  - Domestic banks may seek to increase their growth and/or profits overseas
  - These potential MNBs may face a mature or intensely competitive domestic banking and financial services sector – so, **larger foreign markets with high growth rates have more appeal**
  - Domestic banks also seek **local business in overseas markets** – this was an important driver for many countries (like Australia and New Zealand) to expand into Asia in the 1980s
  - The foreign market competitiveness hypothesis argues that **potential MNBs are more likely to expand into less competitive foreign banking sectors**

- **LEVERAGING OF STRENGTHS:**
  - A bank may have **superior** management skills, knowledge and experience or developed leading-edge business processes, practices or information technology
    - It may therefore seek to **capitalize upon these capabilities overseas**
    - The resulting **economies of scale** should help reduce their overall transaction costs
  - Domestic products and services, systems and management could be effectively duplicated F

        - These may have been acquired from years of competing in a sophisticated domestic financial sector, previous multinational banking or past operations in a similar foreign market
        - Researchers have found positive relationship between the level of domestic market sophistication and the MNB's presence in foreign markets
    - A MNB **size**, however, is not its sole cost of capital advantages
        - Other sources include home-country national saving behaviour, macroeconomic policy, industrial organization, financial policy and taxes