

Who rules the

MONEY MARKETS?

Howard Davies explains why financial regulation is a hot topic at LSE – and the subject of his new book.

When I left the Financial Services Authority to come to LSE, almost five years ago now, I thought I would escape the world of financial regulation. Being a financial regulator is like lying on a bed of nails, as the current incumbents at the FSA and the Bank of England have discovered in the Northern Rock affair, and it's a great relief when you get off.

But, slightly to my surprise, there are a lot of people in the School interested in financial markets and the way they are overseen – both researchers in the Financial Markets Group and the Centre for the Analysis of Risk and Regulation, and students taking a variety of master's programmes. Finance and accounting people are interested, as one might expect, but lots of lawyers too. Regulators have become quite big employers. So I have been drafted in to give seminars and teach on a variety of master's programmes.

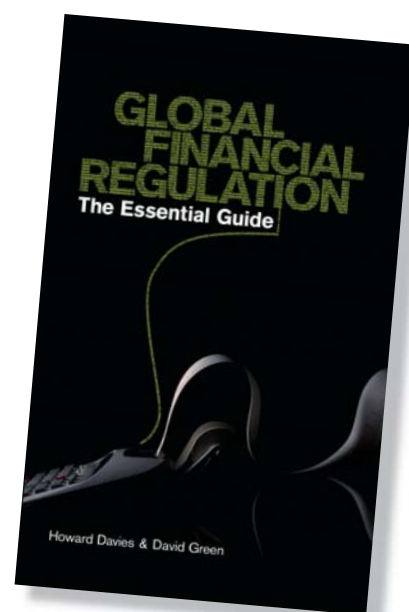
I enjoyed the teaching, and particularly the global nature of the classes. Because I represented the FSA in the main international financial groupings I know quite a lot about the ways in which different countries supervise their institutions – indeed it is true to say that if I were forced to appear on

Mastermind it would be my specialist subject! How sad is that, as my sons would say.

And in preparing for those classes I have discovered that there is no single text to which you can point people if they want a description of how the global system is supposed to work, of what the Basel Committee actually does, for example, how its output relates to the work of the International Monetary Fund and the World Bank. So last year, with the help of a former colleague from the FSA, David Green, I set about filling the gap and a book called *Global Financial Regulation: the essential guide* appears this spring, published by Polity Press/Blackwell Publishers.

I doubt if you will find it on the shelves of an airport bookstore – but please snap it up if you do. However, it does look as though public interest in the subject has escalated helpfully (for us) in the last few months. There is a growing perception that the international regulatory system has not kept pace with the widespread interconnectedness of different financial markets. Indeed at the World Economic Forum in Davos this year Gordon Brown, in his plenary address to the conference, said: 'we need a global regulatory system to match global capital markets'.

This is right, as a matter of principle. But achieving such a happy outcome is not straightforward. Up to now, individual countries have been very resistant to the idea of handing over control or even influence over their domestic financial markets to any supranational bodies, even those on which they are strongly represented. So the current system is a patchwork of largely informal standard setting bodies, and their standards are implemented by individual countries on a 'best endeavours' basis. In some places they are observed more in the breach than the letter.



There are also a growing number of important financial institutions, notably hedge funds, private equity funds and sovereign wealth funds, which exist largely outside the regulatory net. There may be some logic in that – they are largely investors rather than intermediaries after all – but from a financial stability point of view the world's financial authorities need better knowledge than they now have about their activities; they are simply too large to ignore. And there are important questions to be addressed about the role of the ratings agencies, who have not covered themselves with glory.

It seems fairly clear that one consequence of the financial crisis of the last year will be an overhaul of some of these bodies. The heads of government of the G8 have begun to take an active interest in the subject. That is not before time, and indeed we recommend such an overhaul in our book. The downside for me is that I will need to start working on a second edition rather sooner than I had expected. ■



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