KNOWLEDGE ORGANISER LIBF Unit 3 Topic 6 – The Impact of Global Events & Ethics

What is globalisation? **KNOWLEDGE ORGANISER LIBF Unit 3** This international integration of business, industry and society through developments in technology, communication and migration is what we mean when we speak of 'globalisation'.

Globalisation

What happens in one country is now more likely than ever to affect what happens in other countries. Some of the factors fuelling this globalisation are as follows:

◆ Travel between different countries is now easier, and it is both quick and relatively cheap to move around the world.
◆ Communication is faster now than it has ever been, and information communication technology (ICT) has made contact between people and between financial markets almost instantaneous.
◆ Businesses frequently trade across borders because of the ease with which goods can be transported and with which people can get in touch with each other,
◆ People from one country often migrate to live in another and, because people take a part of their culture with them when they move, many individual countries now have much more diverse local cultures than they used to, influencing demand for various goods and services, eg food and fashion.

◆ Many businesses – particularly financial services providers – have expanded their activities to span national borders. They conduct business in more than one country and often have offices in many different places.
There is no agreed standard definition of the term, but it is commonly described as:
◆ the trend towards a single global economy and society; or
◆ a process of increasing international networking, which means that communities and economies that used to be isolated are increasingly linked and affected by what is happening elsewhere in the world.

International Monetary Fund (IMF)

The International Monetary Fund (IMF) is an international body comprising 189 countries that aims to promote international co-operation on exchange rates and other economic matters. It describes its aim as: . . . to help member governments take advantage of the opportunities – and manage the challenges – posed by globalisation and economic development more generally.

Criticising Globalisation

one of the features of globalisation is the existence of increasingly large organisations that span several countries. They usually set up similar operations in each country by importing their own brand values and sticking to them consistently. Some people think that this is a positive trend – especially if it leads to an improvement in the standard and range of products, and to consistency in services. Others see globalisation as a bad thing, because they feel that it undermines the local culture in those countries and they do not like the depersonalisation that they believe results from it. They feel that they are getting a 'one size fits all' solution that may not take into account the way in which people like to do things in their own country.

Positive Impacts of Globalisation

Abbey, which was purchased in 2004 by the Santander Group, a Spanish bank. While there were job losses at the time of the takeover, Santander was not so badly hit during the financial crisis as other financial services providers and so Abbey (now rebranded Santander) was better protected than many other lenders in the UK.

Ill-Advised Acquisition

An example of an ill-advised acquisition is the takeover of the Dutch bank ABN Amro by a consortium in which Royal Bank of Scotland (RBS) was one of the main participants. ABN turned out to be less valuable than RBS had thought, and so RBS was forced to declare huge losses in 2009 and to accept government funding to keep it afloat

The Effects of Globalisation

◆ Increasing globalisation means that UK providers face competition from overseas providers, which may set up operations in the UK or simply offer their products via the internet, as a comparatively low-cost way of finding and serving customers. Local providers will need to decide how to respond to these pressures. The increased competition between providers should mean that consumers enjoy better services and lower prices than would otherwise have been the case.
◆ At the same time, it also means that UK providers may decide to expand overseas. They must decide how much of their resources to commit to the UK market in light of the opportunities elsewhere in the world – which, conversely, may mean that UK customers see a reduction in the standard of products and customer service. The losses suffered during the financial crisis, however, have forced some banks to pull out of foreign markets: in January 2009, for example, RBS sold its equity stake in Bank of China.
◆ UK providers also need to understand the cultural, regulatory and other constraints that may affect how successful they will be overseas.

Outsourcing

This is the process of one provider paying another to carry out certain functions that it previously performed itself. The benefits of outsourcing to the provider are that it can focus on the 'core' functions of the business. It may also bring cost savings because the company offering the outsourced service may be able to achieve 'economies of scale' through its focus on only a single process.

Offshoring

The practice of moving some of a company's operational functions to overseas locations. Companies can cut their overall operational costs by relocating operations to countries such as India, Indonesia, South Africa and the Philippines, where there is a labour force with the necessary skills, but the country's lower cost of living means that wage costs are much lower.

The Global Economy

The word 'economy' refers to all of the economic activity that takes place between the people living in a particular region or country. This activity consists of producing and consuming all of the goods and services that people need and want. The UK economy is a part of the global economy, ie the global economy is the aggregate (or total) of all activity in the national or regional economies of which it is composed. Financial providers are affected by what goes on in their local economy, eg what can happen when local interest rates change or when the job market suffers a setback. But each is also affected by what is going on in the global economy.

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Exchange Rates

We can illustrate both of these factors by considering the impact of changes in the European Union's economy on the exchange rate between the euro against the pound sterling. Exchange rates also affect, and are affected by, what happens in the world's financial markets. The Bank of England's Monetary Policy Committee (MPC) is responsible for setting Bank rate in the UK, which is used to influence the demand for and supply of the pound sterling – the goal being a stable rate of inflation.

International Trade Organisations

The authorities in a country often have to take steps and adopt new policies to try to improve the local economy. There are a number of international bodies that try to persuade governments to co-ordinate their countries' economic policies in an attempt to stop one from damaging another and to get the best outcome for the world as a whole – although, in practice, individual countries often take different views and it can be difficult to reach consensus. The economic recession that followed the 2007–08 global financial crisis meant that a lot of people lost their jobs, or had to take a pay cut, or switched to part-time jobs. The way in which each country tried to deal with this caused some controversy.

Protectionism

Policies designed to protect a country's own economy and labour force are known as 'protectionism'; they might involve a government giving money to one of its industries to preserve jobs, or imposing import taxes on the goods and services that it purchases from abroad in order to make its own products seem more competitive.

World Trade Organisations

The World Trade Organization (WTO) has over 160 member countries, and promotes co-operation and trade between those members. It is the only international organisation dealing with the global rules of trade between nations. Its main function is to ensure that trade flows as smoothly, predictably and freely as possible.
There are, in addition, a range of regional economic unions around the world, including (among others):

◆ the European Union (EU), which has 28 member states at the time of writing (early 2019, before the planned Brexit);
◆ the Association of South Eastern Asian Nations (ASEAN), which has ten members; and
◆ the Caribbean Community (Caricom), which has 15 full members and five associate members.

Measuring the Performance of the Economy

We can measure the performance of an economy in a number of ways. One common measure is gross domestic product (GDP) – ie a country's economic activity in terms of its total output of goods and services, usually measured at their market prices. Generally, rising GDP growth is seen as a good thing, because it reflects a higher standard of living of the people with higher employment and production. Most governments want to achieve GDP growth each year to show that the economy is performing better. A common way of expressing the standard of living of the people of a country is to find the GDP per capita (meaning per head) – ie total GDP divided by total number of people. This is an average, however, and can hide inequalities in the distribution of income.

The Effect of Changes in the Global Economy

Our focus now is on how these economic factors influence personal finance – ie how they alter the circumstances of individuals and of the markets that offer them financial products. What is the likely effect on providers and consumers of financial products of changes in the overall world economy during this period of falling world growth?

Saving & Borrowing

A fall in growth is likely to be accompanied by falling share prices and a lack of investor appetite for shares. Providers of savings and investment products need to offer products that give the opportunity for growth in falling markets; this will normally involve persuading savers to make riskier investments, rather than to use a bank savings account

Investing

Investment companies may find it difficult to identify good investment opportunities. If the world economy is performing badly, they may struggle to find any particular country in which the economy and markets are doing well. Some businesses are better suited to surviving a recession than others. In times like these, it is those stockbrokers and investment fund managers who are particularly good at 'stock picking' who are successful. In other words, those who can identify the companies in which it is still worth investing (even when the market as a whole is falling and investors are losing money) will be those who are able to maintain – and even increase – the value of their investment portfolios.

Employment & Earnings

Falling growth and recession generally means falling employment levels – ie rising unemployment. Those who manage to keep their jobs may also see the real value of their wages and salaries fall, either because their hours are reduced or because any growth in earnings is outstripped by a higher rate of price inflation (reducing the value of earnings in real terms).

Emerging Markets

At the same time as the economic downturn has gripped the United States, Europe and other developed, industrialised countries, the world's emerging markets have been experiencing a high level of economic growth – which has caused problems for the established economies.

The European Economy

UK financial services consumers and providers are very much affected by what happens in the wider European economy, because of the amount of trade that the UK does with European countries and especially with those in the European Union. The economies of European countries did not escape the impact of the financial crisis, with the countries in the euro area (or 'eurozone') – ie those countries that have adopted the euro as their currency – particularly hard hit. The impact of the financial crisis has seen the euro put under pressure as some of its members – particularly Greece, Ireland, Portugal, Spain and Italy – struggle to pay their government debts. . The richer members of the euro area have, in effect, been forced to bail out (ie to lend money to) those that are struggling, to prevent the euro itself from collapsing.

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The UK Economy

Within the UK, the government department responsible for setting economic and financial policy is HM Treasury. he Bank of England is the UK's central bank. Its Monetary Policy Committee (MPC) meets regularly to decide on whether or not to change the level of interest rates. It publishes the minutes of these meetings and these include a discussion about the current economic situation.

Financial Crises & Recession

We have already discussed at length the 2007–08 financial crisis and the problems to which it led. Some financial institutions failed, while others were 'bailed out' to prevent them from failing, damaging confidence in banks and other financial institutions. The global economy was plunged into a recession from which many countries are still recovering. The globalised nature of the financial markets, and of the trade in goods and services, means that the countries of the world are so closely linked that problems in one part of the world quickly spread to others. The rapid spread of defaults in the US sub-prime mortgage markets illustrates this very clearly.

War

When a country itself is at war, there can be a range of immediate and long-term effects on the financial markets, and consequently on financial providers and personal finances. Finding the money to pay for a war generally means that taxes must rise or that the government must borrow more. Each of these options has wide-ranging economic and financial effects.

Weather Patterns, Climate Change & Natural Disasters

Weather can have a considerable effect on financial markets, and therefore also on financial product providers and consumers. It is accepted that world temperatures are rising and many people now agree that this is the result of human carbon emissions (although there remains a group of people who believe that the phenomenon is caused by natural factors). Global warming is having significant and increasing effects on many industries – particularly on agriculture – and these effects often feed through into higher prices for consumers.

Company Collapses & Financial Scandals

In recent years, the world of big business has been plagued by a series of business collapses brought about by false, or 'creative', accounting or poor operational controls. Sometimes, a single individual has falsified or hidden records, so that senior management does not know how bad the business's finances are until it is too late; in other cases, companies deliberately adopted unethical – and sometimes illegal – business practices as part of their overall business strategies.

Directors

Directors have a duty of care to the shareholders in the company on the board of which they sit. If they do a particularly bad job, either through deliberate dishonesty or through negligence, the shareholders can sue them for 'breach of fiduciary duty'. Increasingly, in recent years, directors have also taken on a wider duty of care for the interests of all stakeholders in the company.

Auditors

Auditors also have a duty to check the accuracy of published accounts, for the protection of shareholders and other stakeholders. In some cases, auditors have been sued for failing to identify problems with accounts that they should have found and these auditors have had to pay compensation to people who have lost money as a result. Auditors can be sued because people trust the accuracy of the accounts that have been audited.

Political Changes

A change in political leadership can affect financial services providers and consumers.

◆ Some governments work to protect the consumers of financial services as much as they can. They are highly critical of certain aspects of the financial services industry (often because of the kind of issues discussed above), and see reassuring the public that the industry will be tightly controlled and regulated as more important – and perhaps as a better vote winner at election time – than being seen to help big business.

◆ Other governments are more 'business-friendly' and may relax regulation and reduce the taxes that financial services businesses have to pay to make it easier and cheaper for financial product providers to make their products and services available to consumers. Consumers, in turn, should then benefit from cheaper products and services.

◆ Some governments have specifically encouraged financial activity in the general population. There are many reasons why a government might do this, including encouraging people to set up their own pensions to reduce the pressure on state pension funding

EU Expansion

Many of the issues that we have discussed in this section are unplanned changes, but we should bear in mind that some changes are carefully planned. One such example is the expansion of the European Union. Beginning in 1958 as the European Economic Community (EEC) comprising just six member states, it has grown over the years to the extent that the admission of Croatia in July 2013 brought EU membership to 28 states. Other countries still hoping to join the European Union include five official 'candidate' countries (the former Yugoslav Republic of Macedonia, Montenegro, Iceland, Turkey and Serbia) and three further potential candidates (Albania, Bosnia and Herzegovina, and Kosovo).

◆ New countries joining the European Union become part of a group that is trying to establish a single market for financial products and services across all member countries.

◆ As the new EU members begin to adopt, and adapt to, EU rules and regulations, investors in the UK will gain enough confidence to start investing in these new markets and buying shares in new companies.

◆ In addition, people who live in the new EU member countries will find it easier to move to other EU countries and get work there. This might lead to effects on the employment figures in various countries, with many side effects, including that:

− financial providers in the UK may be able to recruit employees who have recently moved to the UK

− providers may find it worthwhile to develop products to suit these new immigrant people.

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Social Change

Many changes to society as a whole can affect product providers and consumers, and it is beyond the scope of this text to cover them all. We shall therefore touch on only a few examples of social change here.

Changing Attitudes Towards Money & Financial Provision

Society's attitudes towards money and financial provision are changing. People are becoming more aware of the importance of finding the best products and services. The impact of highly publicised problems, such as the mis-selling of payment protection insurance (PPI) – see Topic 3 – and the belief that the banks were largely to blame for the financial crisis mean that many consumers no longer trust financial providers the way that they used to

Increasing Ethnic & Cultural Diversity

Most countries are becoming more ethnically and culturally diverse. Many providers themselves are multinational organisations; even on a local basis, they employ people of different nationalities and from different cultures. In addition, big organisations tend to move their senior employees around the world, so you might find a New Yorker heading up a UK bank.

Increasing Complexity

Complexity is increasing in almost every area of life, not least of which is financial services. At one time, each financial product fulfilled one need; now, it is possible to buy products that fulfil many. Offset mortgages, for example, combine the benefits of a savings account or current account with the loan needed to finance house purchase.

Changing Demographics

The UK, along with many other countries, has an ageing population, which is creating opportunities for many product providers. Saga, for example, is a group that provides financial products (and a range of other products and services) to the over-50s. But, at the same time, this ageing population is placing an ever-increasing burden on the working population, which has to pay the taxes that will finance the rising costs of pensions, medical services and residential care.

Various organisations specialise in meeting the needs of other special interest groups. An example is NFU Mutual, which was founded in 1910 to provide insurance for farmers. In 1998, it began insuring individuals and businesses outside the farming sector. We can see this type of specialist approach as an effort on the part of the provider to choose a customer base and to get to know its needs in greater depth.

Changing Attitudes to Debt

Attitudes to issues such as debt changed dramatically and are changing again. At one time, people who could not afford to buy what they wanted simply did not buy until they had saved enough to do so. In recent decades, many people were much more relaxed about debt and used credit to finance the purchase of what they wanted when they wanted it. Now, following the financial crisis, and resulting credit crunch and economic recession, people are drawing back: they are trying to pay off their debts and are not running up more. This will probably change again in the future, but it is likely that a more cautious attitude will prevail for some years.

Ethical Considerations

When we speak of ethical considerations, we are concerned with the way in which people within a particular culture believe that things should be done. Unfair pay and conditions are examples of unethical business behaviour regarding workers' rights or, more generally, human rights. This is only one aspect of business ethics, however. Other examples of ethical business behaviour include:

Environmental Ethics

Ensuring that business activities do not cause pollution, or produce greenhouse gases that contribute to global warming, or damage the local or global environment in some other way.

Product Sustainability

Designing products and services that meet consumers' long-term needs and do not unnecessarily use up non-renewable energy, raw materials and other resources (this category includes the 'Fair Trade' movement regarding producers in developing countries).

Political Ethics

Not supporting or doing business with undemocratic political regimes that have a poor record on human rights, not supporting the armaments industry or producers of alcohol and tobacco products, and not resorting to bribery and corruption to maximise sales

Animal Welfare

Not being involved in animal testing or factory farming.

Ethical Investment Decisions

People who want to invest their money in ethical projects and companies are not always concerned about all of these different types of ethical behaviour. Some may be concerned only that the organisations in which they invest will carry out activities that are considered to be 'good' or 'green', such as activities that support the environment. Others may be more concerned about human rights or animal welfare violations. What they have in common, however, is that they do not want to invest their money in a company, sector or industry if they do not agree with its activities.

Corporate Social Responsibility

Corporate social responsibility (CSR) is a form of self-regulation now practised by many large companies. It is a way in which a company can demonstrate that there is a social conscience behind its business model, setting for itself standards that it believes are ethical and complying with the way in which society expects it to behave. A company with an active CSR policy is showing that it is trying to take responsibility for its actions and to have a positive impact on the environment, its consumers, employees, communities and all other stakeholders.

Ethical Operations

The phrase ethical operations refers to how providers, carry out their everyday activities. One example of ethical operations in the financial sector is the paperless bank account, aiming to save trees. Holders of current accounts have, over the years, become used to receiving bank statements through the post.