
Foreword

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The World Economic Forum's Financial Services team is pleased to release *The Financial Development Report 2012*, the fifth edition since its inaugural publication in 2008. This *Report* represents a key ongoing initiative undertaken as part of the Forum's Industry Partnership Programme, which provides a platform for CEOs and senior executives to collaborate with their peers and an extended community of senior leaders from the public sector, academics, and experts from civil society to tackle key issues of concern to the global community.

The effects of the financial crisis continue to be felt in both advanced and emerging economies around the world. Europe remains plagued by debt overhang, high unemployment, political divisiveness, and a general lack of competitiveness. The United States faces political gridlock in a time of fiscal uncertainty and increasing public debt. Traditional emerging market powers, such as China and Brazil, are experiencing an economic slowdown, which may have significant ramifications for global trade. Generally speaking, although policymakers have sought reform through structural adjustment, global output is expected to slow over the near term. It is clear that economic growth continues to be a vital issue for the global community. We believe that *The Financial Development Report* provides a better understanding of how both emerging and advanced economies can identify and rectify areas of weakness in their financial systems, ultimately leading to sustainable economic growth.

Stalled recovery: In search of growth

Although arguably improving, the global economy has yet to fully stabilize. This instability applies not only to developed economies but also to emerging ones, which are experiencing the knock-on effect of advanced economy woes. Recovery efforts are still needed to address both lingering legacy issues, such as rising debt levels, and post-crisis issues, such as increasing unemployment, with the ultimate goal of creating long-term, sustainable growth. Given the crucial role that the financial system plays in any economy, recovery efforts will depend on a well-functioning system of saving and allocating capital, among other factors. Although a number of reforms that address some of the underlying issues within the system have been well received, there are still many issues that remain to be addressed, including effective supervisory frameworks, cross-border bank resolution in times of failure, and the role of the shadow banking system.

Perhaps one of the most important issues is waning trust in the overall system, a by-product of which has been the withholding of capital and a reduction in much-needed investment in medium- to long-term growth. The lack of trust can also be seen in volatility in various markets, particularly equity markets, across the world. In order to restore confidence in the system, actors and participants will need to take concerted action to align activities with the core economic and social objectives of the financial system.

The variables in this *Report* help provide guidance for measuring the effects of programs and reforms across three broad categories: (1) factors, policies, and institutions; (2) financial intermediation; and (3) financial access. The *Report* uses a comprehensive framework that includes 121 variables that measure the stability and efficacy of the banking system, financial markets, and many other related factors. We believe this *Report* will be highly informative and useful as a vehicle for future dialogue and debate.

The Financial Development Report 2012

In this context, we offer this year's *Report* as a way to identify the factors that play a crucial role in achieving much-needed economic growth and in enabling stakeholders to collectively prioritize, implement, and assess any necessary reforms. Part 1 of the *Report* summarizes this year's Index results and related findings in three chapters. Chapter 1.1 outlines the methodology for the Index, the academic theory and assumptions supporting it, and some of the key findings from the Index results. Chapter 1.2 provides insight into the debate about regulating the traditional, as well as shadow banking systems in light of the financial crisis of 2007-2009. Finally, Chapter 1.3 discusses the rise of emerging market banks, their importance as foreign investors, and how the global financial crisis has allowed these banks to increase their footprint at the regional level.

We also encourage readers to delve into the details of Part 2: Country/Economy Profiles and Part 3: Data Tables of the *Report*. The richness and breadth of the data paint a balanced picture of the challenges and opportunities faced by different countries.

By design, this *Report* must rely on data that are available for all the economies it covers, to proxy for key elements of financial development. This year, as every year, it is with a

degree of humility that we put forth our findings, given some of the inherent limitations and occasional inconsistencies of these data, the rapidly changing environment, and the unique circumstances of some of the economies covered.

Yet, through its attempt to establish a comprehensive framework and a means for benchmarking, we feel the *Report* provides a useful common vantage point from which to unify priorities and develop a course of action.

We welcome your feedback and suggestions for how we may develop and utilize this *Report* to promote the potential of financial systems as enablers of growth and individual prosperity.

On behalf of the World Economic Forum, we wish to particularly thank the members of the Expert Committee, the Academic Advisors, and the project team, Isabella Reuttner and Todd Glass, for their boundless support.