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THE FINANCIAL SECTOR AND ECONOMIC DEVELOPMENT: BANKING ON THE ROLE OF HUMAN CAPITAL

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Evidence suggests that human capital development contributes to the stability of banks. Unfortunately, developing countries, both pre- and post-liberalization, often suffer from an inadequate supply of capable professionals. This situation threatens the potentially positive relationship between financial liberalization and economic growth. It is therefore urgent that developing states develop policies aimed at addressing the supply and demand-side requirements of the financial sector. Such policies must target the development of professionals with both appropriate academic backgrounds in business and the requisite on-the-job skills. Public-private solutions are advocated as the most efficient and effective approach to the development of comprehensive policies in this regard.

INTRODUCTION

The financial sector and its role in the process of economic development has attracted notable attention since the early 1990s. In particular, the crucial need for a stable banking system was highlighted in the wake of the Asian financial crisis of the late 1990s. The rapid influx of short-term, speculative capital flows to Asian economies was a major contributing factor to the crisis. States with stronger domestic financial sectors and particularly

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robust banks, however, better absorbed the ripple effects of the external shock. Increasing the openness of financial markets via liberalization may not be positively related to economic growth unless banks are stable and sophisticated enough to absorb international investment, competition, and negative shocks. This article examines whether strengthening human capital in banks can bolster the integrity and stability of domestic banks and thereby improve their ability to respond to the complexity and volatility of international financial markets.

This article does not argue against liberalization; rather, it employs a methodology that analyzes the empirical, theoretical, and industry conditions in order to investigate the importance of human capital formation and related policies to the development of stable and sophisticated domestic commercial banks and long-run economic growth. The article argues that human capital is crucial to bank stability, a factor that has been overlooked in the financial liberalization literature. Although there is a positive relationship between human capital formation and financial sector development, many developing states lack graduates and professionals with the academic and on-the-job training necessary to operate efficient banks. This article first provides an in-depth examination of the potential role of the state and the industry in policy design. Two policy approaches are then developed, both of which articulate how well-designed public-private partnerships can be used to develop the human capital requirements necessary to increase overall domestic financial system stability and economic growth.

Economic Theory and the Financial Sector

To understand why financial sector development, under certain conditions, may be positively related to economic growth, it is necessary to understand the critical function the sector provides to the economy. The financial sector is unique because of the risk and uncertainty faced by both savers and investors (Stiglitz 1998). Savers are often unable to select the investment project that best matches their personal risk appetite and without pooling their money, savers cannot take advantage of increasing returns to scale in investments (Stiglitz 1998).

Moreover, individual entrepreneurs or investors commonly lack sufficient capital to proceed with projects on their own. Commercial banks provide an intermediation service that brings savers and investors together, theoretically channeling investment funds to the uses that yield the highest rate of return, thus increasing specialization and the division of labor (Todaro 2003). Risk is pooled, transferred, and reduced by commercial banks while liquidity and information increase through the use of progressively more sophisticated financial products and technology. Neoclassical growth models tell us that an increase in the efficient investment of savings in new and innovative projects is one of the main engines of economic growth.

It should be noted that the previous discussion assumes that markets are free from distortionary policies and therefore adjust automatically to economic change. In examining of the utility of liberal markets, McKinnon argues that flows of savings and investment should be voluntary and significantly decentralized in an open capital market at close to equilibrium interest rates (McKinnon 1973). The pro-liberalization literature of the l980s further points out that in order for commercial banks to operate efficiently and profitably in the role described above, financial markets cannot be repressed by government policies, including interest rate ceilings, directed lending, and corruption (Todaro 2003). At that time, the consensus that liberal markets were a necessary ingredient in the 'growth recipe' gained significant momentum to the extent that market liberalization often became equated with growth.[1]

Proponents of liberalization are quite correct in pointing out that repressive policies and macroeconomic instability can cause severe contractions in the amount of savings and therefore loanable funds. Such contraction often leads to what is referred to as a "credit crunch," which has the inherent danger of leading to a decline in investment (Todaro 2003). Financial repression by developing country governments was widespread up until the 1980s and examples of its negative effects are well-documented. Yet, further research indicates that liberal markets are a necessary, however insufficient, condition for the creation of stable financial markets and sustainable growth.

Financial Sector Depth, Liberalization and Growth

The argument that liberalism alone leads to growth has been challenged by a 2005 empirical study by Rousseau and Watchel. These authors sought to retest the previously entrenched finance-growth theory, pioneered by King and Levine in 1993 and Barro in 1991, which postulated that financial sector development leads to economic growth. In developing their theory, King and Levine used variables to measure a state's level of financial development (ratios of liquid liabilities or claims on the private sector to GDP) with the traditional growth regression for data ranging from 1960-1989. The authors found a strong and statistically significant relationship, which led them to believe that financial development, defined in terms of ratios of liquid liabilities and the level of credit extended to the private sector, was positively related to growth.[2] Their work provided the empirical foundation for the widespread acceptance of the finance-growth relationship.

When Rousseau and Watchel retested the finance-growth hypothesis with more recent data ranging from 1960 to 2003, they found that the relationship disappeared over the period of 1985-89 for the coefficient of M3 as a percentage of GDP and during 1990-94 for the coefficient on private sector credit.[3] It was at this time that numerous developing states, especially in Latin America, went through rapid financial liberalization and opening to world economic markets.

The uninspiring growth performances of the late 1990s in many of these newly liberalized emerging markets, as well as Rousseau and Watchel's findings on the breakdown of the empirical relationship between finance and growth, suggest that in the absence of stable financial institutions, rapid liberalization may be counterproductive and provide perverse incentives for banks to lend imprudently. Such activity may result in a severely strained or collapsed domestic financial sector if imprudent lending leads to non-performing loans, illiquidity, insolvency, and capital flight.[4] Rousseau and Watchel suggest that post-1990 credit and deposit growth in financial markets may have taken place without the requisite development of lending expertise (Rousseau and Watchel 2005). It is therefore plausible that as liberalization was implemented the relationship between it and economic growth disappeared as the weakness of the sector was exposed. Two points follow: (1) the allocation of credit by bankers may require knowledge-based expertise, a point that receives little recognition in the literature pertaining to financial sector development and, (2) the need for expertise arguably increases exponentially in light of the competition and the level of sophistication that exposure to world markets and international firms brings.

The literature on financial sector stability currently focuses on the regulatory regime, access to information, and legal structures such as bankruptcy and creditor protection legislation. Questions of transparency and fair competition and procedures to reduce rent-seeking, cronyism, and corruption also garner considerable attention. While these regulatory and institutional factors are crucial, the role of human capital in banks and other financial institutions has received too little attention.

Human Capital Formation and Financial Sector Development

Outreville was the first to attempt an empirical analysis on the role of human capital in financial development (Outreville 1999). His study was based on a cross-country analysis of developing countries, which is similar to the style of analysis used by Barro in 1991. Although a number of critiques exist regarding the use of cross-country regressions, the paper states early on that because of the difficulties associated with the data used to measure socio-economic variables such as human capital, its intention is only to establish correlation, rather than attempt to attribute causality (Outreville 1999). In conformity with the literature, Outreville utilizes quantity indicators based on monetary and credit aggregates to measure financial depth. For human capital measures, the indictors used include the human development index, the percentage of the labor force with tertiary level education, and "human capital accumulation" which is defined as the capacity of nations to adopt, implement, and develop new technologies. Overall, the Outreville study found high correlations between measures of financial development and human capital. The findings confirmed the existence of significant returns to human resource development, suggesting that action must be taken to develop policies that increase capacity where deficiencies lie. However, it is first necessary to gain a better understanding of the nature of these skill shortfalls in the context of developing states.

The emergence of the global "knowledge-based economy" has in large part been driven by the acquisition and development of knowledge-based skills. Banking is a knowledge-based service industry that has always required specialized training but increasingly demands a more sophisticated skill mix. The expertise required by the industry can be divided into two sub-sets: (1) academic training, and (2) on-the-job skills. In terms of academic training, the required knowledge includes intermediate accounting, corporate finance, business law, economics, and strong written and oral skills (Carlson 1997).

The on-the-job training portion, which relies upon the assumption that an employee has acquired the prerequisite academic education, includes learning how to perform the following skill-driven tasks: credit analysis, credit investigations, and the professional conveyance of unpleasant information. Moreover, training also involves becoming familiar with banking laws and regulations, interviewing customers, and negotiating business deals using sales techniques (Carlson 1997). Finally, post-liberalization, the development of credit granting criteria (credit policy) becomes the responsibility of the bank as opposed to the government. Credit policy development involves the creation of standards around the provision of credit, investments in securities and subsidiaries, choices about the kinds of capital investments to make, and hiring decisions (Carlson 1997). Logically, credit analysis, the process of determining which projects will receive credit, monitoring investments, and the overarching credit policy that guides such decisions require fair mastery of the skills outlined above.

Banks in developing states commonly encounter two problems at the officer and management levels that are relevant to this discussion: (1) difficulty finding candidates possessing the appropriate skill mixes during recruitment, and (2) insufficient staffing, which refers to a lack of skills in employees who are already on-the-job (Carlson 1997). Furthermore, many developing states previously used or continue to use inefficient lending policies that were either left over from colonial rule or the result of government efforts to direct lending toward "priority" sectors (Carlson 1997). It is imperative for banks to have managers who are skilled at objectively assessing credit risk based on market forces by conducting penetrating interviews with prospective clients, performing detailed financial analyses, and judging the validity of available information. These skills are a vital part of the institutional strengthening process and yet are often deficient in pre-liberalized or newly liberalizing states. As McNaughton notes, "Substantial training is needed to support institutional development. In many developing financial markets, particularly in Eastern Europe and the former USSR, scarce skills are a huge impediment to banking development" (McNaughton 1997, 172).

Institution and governance building are processes that often follow liberalization. If banks undergo institutional development and restructuring, they will often overhaul or create policies for credit risk management, financial management, and compliance and control systems. This process must be led by competent managers; however, when management falls short, the process may be compromised. Based on the skills outlined above and the crucial nature of the functions they pertain to, it is not difficult to see the need for both academic and on-the-job human capital development, especially in emerging states that are either on the cusp of liberalization or have already opened up. Unfortunately, such human capital investments have often been neglected to the detriment of the economy.

The policy problem we are confronted with is how to best address: (1) incorrect skill mixes or academic backgrounds, and (2) insufficient staffing. Clearly, the selected policy will need to shore up both the academic and on-the-job training supply shortfalls. In attempting to determine what the most effective options may be, it is useful to first examine: (1) whether state involvement is an efficient option with which to address issues related to academic training, and (2) which actors or institutions are most likely to bear the burden of increased on-the-job training. A thorough analysis of these factors will shape a more informed and effective approach.

Policy Considerations

Developing Academic Backgrounds: Theory

During recruitment employers are often confronted with a lack of candidates possessing the prerequisite skill mix, specifically the relevant academic background. Arguments surrounding the appropriate level of state involvement in the economy can be used to inform decisions its optimum role in the formation of human capital stock related to the financial sector. In the World Bank's discussion of the "East Asian miracle" and in other related literature, it is argued that development assistance should focus on providing universal primary education due to the equity and efficiency payoffs it yields (Todaro 1999; World Bank 1993). Private returns to primary education should lead to demand for secondary and eventually tertiary schooling. The World Bank literature supports private rather than public financing of tertiary education due to the inefficiencies associated with state funded universities and based on the argument that private returns to higher education significantly exceed social returns.

This approach seems suitable for states in early phases of development; however, it is perhaps less suitable for emerging markets where primary and secondary education will not deliver the skill mix the economy requires. The equity returns to primary and secondary school alone are not likely to create an egalitarian society in which all students have financial access to tertiary education. Moreover, one must consider potential barriers, such as the influence of risk and taste, rather than simply assessing the ability to pay for a university education as the sole variable positively influencing enrollment.

The foregoing suggests that states may have different roles to play depending on the development juncture they are at. The idea that two distinct junctures exist, the first where it is optimum to focus investment in primary education and the second where it is optimum to encourage tertiary and vocational skills training, is discussed in the literature as the existence of multiple equilibria (Green et al. 2003). Economic adjustment will create new skill demands within the economy and as a less developed state becomes an emerging market, it moves from low to high-skilled equilibria. Arguably, the state has a role to play in identifying and coordinating the needs of the economy at both of these critical junctures. The question is, "What is the optimum level of state involvement?"

The general debate within the economic development canon about the optimum mix of state and market is well established and, if policy makers wish to be efficient, a close examination of what the state can offer must be balanced against the potential costs. The role of the state as the provider of information, public goods, and services is commonly accepted. However, the role of the state as the central guide for the economy is now generally viewed as undesirable, mainly because the market tends to coordinate economic activity with a lower failure rate than government. This is because the government does not tend to be as flexible as the market in adjusting to the forces of supply and demand.

However, for reasons related to inadequate financing, potential risk and tastes, there is a case for government intervention in human resource development because individual consumers in developing countries tend to underinvest in education (Green et al. 1999). Even when a state moves from a low to high-skill equilibria, pursuit of specialized academic accreditation is invariably a long-term and uncertain investment (Green et al. 1999). It is thus the case that many boundedly rational individuals may opt for comparatively general training to mitigate downside risk (Green et al. 1999). If this tendency is combined with rapid social and economic development during market liberalization, there is a risk of a mismatch between the supply of skills and the demands of the economy (Green et al. 1999). It is at this juncture, *ceteris paribus*, that the state may have superior information about the returns to various types of skill formation (Green et al. 1999).[5]

A second central element in skill formation is the social and economic context. Particularly important is the level of inequality and whether or not education increases social ranking. In the case of South Korea, this factor arguably played a crucial role in generating demand for tertiary education (Green et al. 1999).[6] If government has superior information, it would be efficient for them to coordinate skill matching using market friendly incentives (rather than central planning schemes) and foster a more egalitarian society through development-related policies.

Addressing Insufficient Staffing Through On-the-Job Training: Theory

It is useful to rely on the seminal work done by Becker in 1975 on human capital as well as other research on the nature and characteristics of the banking industry to determine how best to increase on-the-job training for both new hires and current staff that possess insufficient skills. On-the-job training will be defined here as occurring within the firm; however, the nature of the industry and, more specifically, the nature of the skills to be imparted will determine whether or not firms will be willing to bear any or part of the cost.

Becker uses empirical and theoretical analyses to help "fill a gap in formal economic theory" and offers in his general analysis, "a unified explanation of a wide range of empirical phenomena which have either been given *ad hoc* interpretations or have baffled investigators" (Becker 1993 30). Becker's discussion can be used to draw insights into two characteristics of the banking sector in developing countries, namely: (1) why banks are more likely to offer and pay for on-the-job training, and (2) why there is a tendency for firms in underdeveloped states to appear more paternalistic vis-à-vis employees relative to those in developed states (and also display "cradle-to-grave" policies where new hires start at entry levels and are expected to remain with the firm for the duration of the their careers) (Carlson 1997). Becker's analysis shows that firms are more likely to perform and pay for on-the-job training when the training raises the marginal productivity of workers above the marginal wage, but only when the firm can profitably capture these returns. It logically follows that firms are more likely to capture such returns when the likelihood of turnover is low.

Becker, however, makes an important distinction between two types of on-the-job training: general and specific. General training can be used in a number of different firms and across industries (Becker 1975). Although general training increases the marginal productivity of workers in the training firm, it also increases it in many other firms; therefore, perfectly general training raises both the marginal product and wage rate by equal amounts in all firms. In this case, the training firm does not capture a return (Becker 1975). By contrast, specific training raises the productivity of employees more in the firms providing it as opposed to in other firms (Becker 1975). Yet, only perfectly specific training is non-transferable (Becker 1975).

With regard to turnover, economic theory often assumes perfect competition; wages are assumed to equal the marginal product and thus, turnover is not an issue because employees are marginal (they cannot be made better off by switching firms). In the case of more specific training, however, where the marginal product exceeds wages after training, turnover is possible. Recalling that a firm will only provide specific training if it can ensure the capture of sufficient productivity returns to cover the costs of training costs, a wage premium may be paid to keep the employee from transferring (although that premium would not exceed the full marginal difference between the increased productivity and the marginal wage) (Becker 1975).

These initial concepts establish the theoretical underpinnings required to assess whether firms and industries are more or less likely to provide and finance on-the-job training for employees. Becker explains how wage increases can also be used to increase productivity if they increase emotional and physical health. It is argued that in developing states, "an increase in consumption has a greater effect on productivity…and that a productivity advance raises profits more there either because firms have more monopsony power or because the advance [in productivity] is less delayed," (Becker 1993, 57).

Application of these theoretical arguments to the subject at hand leads to two conclusions. First, it is apparent that skills required by the banking industry are more specific. If the theory is applied to intra-industry comparisons, almost all of the skills would be specific in nature aside from interviewing, negotiating, and sales skills. Furthermore, at the firm level, credit policies and procedures are bank-specific and it is likely that familiarization with one bank may not be fully transferable to competing banks. Turnover, however, remains a possibility because the skills are not perfectly specific and because assumption of perfect competition rarely holds outside of models. Therefore, it is fair to suggest that banks would be willing to train and likely pay a wage premium to mitigate the risk of turnover.

Second, the likely reason the "paternalist" tendency is common in less developed countries relates to the way that wage increases affect productivity. Wage increases in emerging economies, be they associated with the desire to reduce turnover after specific training or to obtain increased productivity gains, tend to be allocated to consumption of basic needs. This is because in lower income states wage increases are more likely to be used for staple consumption due to the law of diminishing marginal returns. Thus, the observed tendency towards paternalism or "cradle-to-grave" policies is largely explained by the fact that incentives exist for both firms and employees to perpetuate them.

Policy Recommendations and Rationale

Based on the foregoing analysis of policy considerations, this article proposes two policy options which involve public-private partnering and linking solutions that leverage the potential for a number of actors to contribute to human resource development, rather than making trade-offs. The two human resource challenges faced by banks, "wrong skill mixes" and "insufficient staffing," represent skill mismatches and shortfalls. From the following discussion, it is evident that there are three sector-specific characteristics of the policy problem: (1) banks face skill supply shortages during recruitment and internal shortfalls, (2) banks will be willing to assume the role and cost of on-the-job training, yet lack the capacity to shore up academic deficiencies, and (3) at the juncture when the economy is adjusting from a low to a higher skill based system, state involvement to coordinate skill matching through incentive manipulation may be useful.

Policy Option 1

The first option is aimed at addressing the inadequate mix of skills. This proposal is inspired by the case of Malaysia, where universities opened up to private investment and in some cases corporations were permitted to run universities (Rudner 1997). The infusion of private capital lightened the budgetary burden on government while capturing the management efficiencies of the private-sector. In order to encourage students to enroll in business and related academic programs, meritocratic financing may be offered in part by government and in part by private banks. This kind of targeted public-private sector financing is in the interests of the financiers, the state and the prospective students.

Watson critiques the use of loans and/or graduate taxes at the secondary and tertiary levels by highlighting the burden they place on students and the indirect benefit they provide to the rich (Watson 1996). In the interests of egalitarianism, it is quite correct that programs which indirectly select for wealth are undesirable and normatively unacceptable. However, Watson also states that governments should subsidize higher education unless doing so deprives another sector (Watson 1996).

A program aimed at the development of business program graduates into professional bankers is recommended here, based on the caveat that students would be required to spend a specified period of time with a sponsoring bank. Post-graduation, the individual would commence employment as a management trainee within the bank and move into more sophisticated functions as they progressed. The idea is similar to programs already found in developed economy banking industries. Banks often recruit students directly from commerce programs and streamline them into twelve- to eighteen-month training programs where it is expected that the students will remain with the firm for some period afterwards.

Since firms would be expected to sponsor a portion of students' academic tuition, a front-end post-graduation commitment from students provides an incentive for private-sector participation. From the point of view of the firm, non-recoverable portions of their tuition investment represent the value of being able to source qualified individuals in supply shortage scenarios.

The condition of supply shortages is an inherent assumption of this proposal; however, this condition is dynamic. The policy, therefore, would need to include strong multi-lateral communication mechanisms whereby the state gathers information and consistently consults with representatives from participating banks to stay abreast of the supply conditions at the industry level. The policy should phase out as development increases and as risks are outweighed by rewards to higher education. Rising income levels and increasing economic and social information about the returns to business training would theoretically become so widespread (as in the case of South Korea) that individual consumers would be in a position to pay for their own education and calculate that potential returns outweigh costs as well as other downside risks.

Policy Option 2

The second policy approach is designed to deal with skill shortfalls of current staff, which relates to upgrading "on-the-job" skills that are generally more specific in nature. Recall that firms have an incentive to train when skills are specific, as they are in banking.

While we may hope to rely upon firms to provide "on-the-job" training, not all firms may have the capacity to do so. If there are insufficient skill-levels in higher level positions, as indicated may be the case by Carlson's 1997 study, then it is perhaps logical to question whether emerging market banks, both pre- and post-liberalization, possess the requisite internal level of expertise to train either existing staff or new hires. This issue also calls into question the potential effectiveness of the first policy above, which relies upon the assumption that firms will be able to absorb academically qualified graduates.

In general, during periods of rapid economic expansion, deficiencies in higher level skills are often a reality (Rudner 1997). East Asian countries, realizing their need for access to these skills, responded to widespread and acute shortages of qualified professionals by opening up their education sector to the domestic and international private sector, while simultaneously continuing to inject large portions of public funding into the system (Rudner 1997). One result was the emergence of international exchanges of scholars that improved the quality of research and instruction capabilities within education institutions (Rudner 1997). In some cases, aid dollars were made available to support such exchanges (Rudner 1997). Institutional linkage-building and partnering are two other mechanisms that were used to address shortfalls in curriculum design, technology, and program delivery (Rudner 1997). The formalization of knowledge-sharing through these contractual-type arrangements provides certainty that the skills transfer process will be uninterrupted, therefore providing long-term assurances to policy-makers.

Policies similar in structure to those employed in the market for higher education, as described above, could be used to address analogous deficiencies in banking sectors. In the case of banks, these strategies would attract fewer potential critiques along the lines of the "Westernization" or cultural homogenization arguments mounted against such practices in the realm of education (Rudner 1997). Although the culture of doing business will vary, the nature of the analytical requirements, portfolio monitoring skills, risk assessment, and often the accounting standards are far more culturally neutral and internationally standardized than in many other areas of economic activity, especially with increased adherence to the Basel Capital Accord.

In this context, the idea is to set up a program that institutionalizes professional skills transfer by creating a pool of interested developed state bankers, with a specified level of experience, which could be placed for variable terms in training and coaching roles in emerging market banks. The optimum form for this type of professional exchange would depend on the level of interest on both the supply and demand side and should begin as a *beta* test. The formalization of this stock of professionals could later be embodied in an organization similar to those established by other professionals who desire to make contributions in the field of development.

With regard to a structural model, one may wish to look to the well-known and reputable organization Doctors without Borders, which supplies the skills of well-trained, experienced medical professionals around the world in response to emergencies. The organization relies on public donations for 80% of its financing, with the remainder from international agencies and governments (*Doctors without Borders* 2006). The establishment of an analogous organizational concept, which could be called 'Bankers without Borders,' is one possible way to achieve professional skills transfers for the development of stability in developing country banks. This organization, however, would not likely be in a position to rely on public donations due to the association of banking and the financial industry with high levels of profitability and the near demonization of corporate interests the realm of development.

This is a novel idea presented here for the first time and it is therefore in its infancy. It clearly requires the development of a detailed business case. However, a number of considerations emerge immediately. First, the program would require state support on both the sending and receiving side. Financing this endeavor would depend on the level of interest it elicits amongst experienced banking professionals. In corporate professions, the importance of remuneration is traditionally high and thus may aid funding, but receiving government funds and assistance from multilateral organizations may also be necessary. Ownership on the part of the receiving government is also crucial to ensure that permission for the visa issuance for the incoming professionals is facilitated.

There is also a potential financing role for developed country banks. Corporate sponsorship of philanthropic activity, including sending employees overseas to work on development projects for specified periods of time, does occur. Employee programs, where professionals are sent to facilitate short training seminars overseas, may be feasible if they did not exceed a period of a month.[7] There may also be professional bankers with a number of years of experience who prefer to leave developed country banks entirely due to a lack of personal fulfillment and who desire broader professional experience. These individuals would theoretically be in a position to engage in longer-term placements of six months or more.

Placing structuring issues aside, the rationale behind the idea that professional bankers in developed states could be used to transfer skills is something that has been done in other economic sectors. The literature is clear on the high returns to human capital capacity building for states whose economies possess high skill shortfalls among current employees and that, in some cases, such shortfalls may only be addressed by external sources. Banking professionals in developed states often have extensive internally provided on-the-job training through seminars, direct one-on-one skills coaching, and mentorship experience. As trainees develop, they move into coaching and mentoring roles themselves. It is this culture of continuous learning and development that would make these professionals arguably the most qualified candidates for capacity building roles. Government bureaucrats or staff from independent regulatory organizations cannot offer the skills and expertise possessed by experienced corporate banking professionals.

Conclusion

This article argues that financial sector human capital, in the form of skilled and competent professional bankers contributes to the stability of banks. Unfortunately, developing countries, both pre- and post-liberalization, often suffer from an inadequate supply of capable professionals. This situation threatens the potentially positive relationship between financial liberalization and economic growth. It is therefore urgent that developing states develop policies aimed at addressing the supply and demand side requirements of the sector. Such policies must target the development of professionals with both the appropriate academic background in business and the requisite on-the-job skills. Public-private solutions are advocated as the most efficient and effective approach to the development of comprehensive policies in this regard.

Notes

[1]This method of thinking led to the development of a cache of policies often described as the "Washington Consensus."

[2]Rousseau and Watchel explain how liquid liabilities, specifically M3, as a percentage of GDP, are used as a standard measure of the depth of financial markets and as an indicator of the overall size of financial intermediary activity in cross-country studies.

[3]M3 is a measure of the money supply that includes M2, plus large time deposits and buybacks of maturities in excess of one day at commercial banks and institutional money market accounts.

[4]These outcomes were relatively common in a number of regions after the economic crisis of the late 1990s.

[5]This tendency will increase or decrease depending on state size and the level of state-economy involvement.

[6]The forgoing discussion must be predicated upon relatively low levels of corruption, rent-seeking and inefficiency in the bureaucracy and commitment to a coherent economic growth strategy. Where these conditions do not apply and state-strength is low, the utility of the implied role for the state is significantly diminished. (Please see Green et al., 1999), as listed in the References, for a detailed discussion.

[7]The one month time frame was suggested in an effort to limit the time banking professionals from developed countries spent away from their primary employer.

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