

## **Topic 6: Developments in International Banking**

The landscape of international banking has undergone tremendous transformation over the past three decades shaped by globalization, technological advancement, financial innovation and evolving regulatory frameworks.

As the global economy becomes increasingly interconnected, banks have transitioned from domestic intermediaries into global financial institutions that facilitate trade, investment, and cross-border capital flows.

International banking plays a critical role in the modern economy by enabling countries to finance imports and exports, manage foreign exchange, and access global credit markets. The expansion of multinational corporations, international capital markets, and digital platforms has accelerated the integration of financial systems worldwide. This integration has been supported by liberalized trade regimes, advances in information and communication technology (ICT), and policy reforms by institutions such as the World Bank, IMF, and Basel Committee on Banking Supervision.

In Africa, and Uganda in particular, these developments have opened new opportunities for growth while introducing new challenges in regulation, risk management, and financial inclusion.

African banks have expanded across borders (e.g., Ecobank, Equity Bank, and UBA) and increasingly participate in regional payment systems such as the Pan-African Payment and Settlement System (PAPSS) and the East African Payment System (EAPS). Ugandan institutions, including Stanbic Bank, dfcu Bank, and Centenary Bank, have embraced digital transformation, aligning their operations with global banking standards and Basel III compliance under the Bank of Uganda's supervisory framework.

### **1. Globalization of Banking**

**Definition:** Globalization of banking refers to the expansion and integration of financial institutions across national borders, facilitating global trade, investment, and capital movement.

It allows banks to serve multinational corporations and individuals in multiple countries, contributing to global economic interdependence.

### **Key Drivers**

- a) **Deregulation and Liberalization:** Many countries, including Uganda, have relaxed restrictions on foreign bank entry and capital movement since the 1990s.
- b) **Technological Advancements:** Introduction of real-time gross settlement systems (RTGS), SWIFT transfers, and mobile banking.
- c) **Growth in International Trade:** African economies increasingly integrated through trade agreements like AfCFTA
- d) **Financial Innovation:** Development of instruments such as derivatives, trade finance, and offshore banking products.
- e) **Global Financial Institutions:** Expansion of banks such as Standard Chartered, Citi, and Barclays into African markets.

### **Impacts**

- a) Increased access to international capital and diversification of services
- b) Enhanced financial stability through foreign investment but also increased exposure to global shocks
- c) Integration of Uganda into global financial systems through foreign bank subsidiaries (e.g., Stanbic Bank, Standard Chartered Uganda, Absa Bank Uganda)
- d) Harmonization of regulation through adoption of Basel standards by the Bank of Uganda (BoU) and the East African Community (EAC) framework

**African Example:** Ecobank Group operates in over 30 African countries, demonstrating successful regional globalization.

**Ugandan Example:** Stanbic Bank Uganda, a subsidiary of Standard Bank Group South Africa, leverages regional expertise and digital transformation to support cross-border business.

## **2. Cross-Border and Correspondent Banking**

**Definition:** Cross-border banking provides financial services to clients outside the home country.

Correspondent banking involves a relationship where one bank (the correspondent) provides services to another (the respondent) in a different jurisdiction to facilitate payments and trade.

### **Mechanisms:**

**a) Nostro/Vostro Accounts:** Used to manage transactions in foreign currencies

#### **Nostro Account- “Our account with you”**

- The term *Nostro* comes from the Latin for “ours.”
- It refers to an account that a domestic bank holds in a foreign bank, in the foreign currency
- Example: If Stanbic Bank Uganda holds an account in Citibank New York denominated in U.S. dollars, that account is Stanbic’s *Nostro account*.

**Purpose:** to make and receive payments in U.S. dollars or to settle international trade transactions.

#### **b) Vostro Account -“Your account with us”**

- The term *Vostro* means “yours” in Latin
- It refers to an account that a foreign bank holds in the domestic bank, in the domestic currency

**Example:** From Citibank New York’s perspective, the same account is a *Vostro account* because it’s “your (Stanbic’s) account with us.”

**Purpose:** to hold funds of foreign banks for local clearing and settlement

Perspective	Account Type	Example	Currency
Ugandan Bank (Stanbic)	Nostro	Account in Citibank New York	USD
U.S. Bank (Citibank)	Vostro	Account held for Stanbic Bank	USD

They Matter because they;

- Enable smooth international payments and foreign exchange settlements
- Used in correspondent banking relationships to process trade finance, remittances and cross-border transfers
- Critical in foreign currency management and liquidity operations for banks operating globally

2. **SWIFT Network:** Enables secure communication for international payments

3. **Trade Finance Instruments:** Letters of credit, guarantees and bills of exchange used in export-import transactions.

**Importance:**

- a) Facilitates international trade, investment, and remittances.
- b) Enables smaller banks in developing countries to access global payment networks.
- c) Supports diaspora remittances, which contribute significantly to Uganda’s GDP (approximately USD 1.2 billion annually).

## The Challenges

- a) **AML/CFT Compliance:** Increasing scrutiny under anti-money laundering and counter-terrorist financing laws.
- b) **De-risking:** Large international banks have reduced correspondent relationships with African banks, fearing regulatory penalties.
- c) **Regulatory Burden:** High compliance costs and reduced international access for smaller banks.

**African Example:** The Pan-African Payment and Settlement System (PAPSS) launched by Afreximbank to enable intra-African trade settlements in local currencies.

**Ugandan Example:** Uganda's partnership with SWIFT and the Bank of Uganda's cross-border settlement systems under the East African Payment System (EAPS) supports trade among Kenya, Tanzania, and Uganda

## 3. Technological Innovations in Banking

### Overview

Technology has transformed international and domestic banking, reducing transaction costs, improving accessibility, and enhancing customer experience. The digital transformation wave in Africa has made banking more inclusive and efficient.

### Key Innovations:

- a) **Fintech & Digital Banking:** Rise of digital-only banks and platforms such as Kuda Bank (Nigeria), TymeBank (South Africa), and fintech partnerships in Uganda (MTN Mobile Money, Airtel Money)
- b) **Blockchain & Distributed Ledger Technology (DLT):** Improving transparency and settlement efficiency for instance RippleNet, SWIFT gpi
- c) **Artificial Intelligence (AI):** Used for fraud detection, customer profiling, and risk analysis for instance AI-enabled credit scoring by fintechs like Ensibuuko in Uganda

d) **RegTech:** Regulatory compliance automation through data analytics.

e) **Central Bank Digital Currencies (CBDCs):** Pilots across Africa; Nigeria's eNaira, South Africa's Project Khokha, and Bank of Uganda's research into a potential digital shilling.

### **Benefits**

- Financial inclusion through mobile and digital platforms
- Reduced cost and time of international transactions
- Enhanced data-driven decision-making for banks

### **Risks**

- Cybersecurity threats and data privacy breaches
- Technological exclusion of rural or low-literacy populations
- Lack of harmonized regulatory frameworks

**Ugandan Example:** The partnership between MTN Mobile Money Uganda and Mastercard enabling cross-border payments between East African countries.

**Regional Example:** Kenya's M-PESA as a model of mobile money success replicated across Africa.

## **4. Risks in International Banking**

**Overview:** International banking activities expose institutions to numerous risks due to currency fluctuations, political instability, and cross-border operations.

### **Types of Risks**

- a) **Credit Risk:** Default by international borrowers or counterparties
- b) **Market Risk:** Losses from interest rate or foreign exchange fluctuations
- c) **Operational Risk:** System breakdowns, cyberattacks, and process failures

- d) **Country (Sovereign) Risk:** Political unrest, policy changes or capital controls
- e) **Compliance Risk:** Breaches in AML/CFT or international regulations
- f) **Systemic Risk:** Contagion across financial systems during crises

### **Risk Management Strategies**

- Diversification across regions and sectors.
- Hedging using derivatives to manage currency and interest rate risks.
- Strong governance and internal controls.
- Stress testing and capital adequacy compliance (Basel III and IV)
- Use of risk-based supervision by regulators such as the Bank of Uganda and Financial Institutions Act

**African Example:** Banks in Nigeria and Kenya have implemented currency hedging and capital buffers to mitigate exchange rate volatility.

**Ugandan Example:** The Bank of Uganda's Financial Stability Reports guide commercial banks in risk management, while institutions like Stanbic and dfcu conduct regular stress testing.

### **Key Takeaways**

- a) Globalization connects Uganda's banking sector to the international system but also increases vulnerability to global shocks.
- b) Cross-border banking underpins trade, remittances, and regional integration in East Africa.
- c) Technological innovation is the biggest driver of inclusion and competitiveness but introduces new cybersecurity risks.
- d) Effective risk management and adherence to Basel frameworks are crucial for maintaining resilience.

## Reference Documents

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