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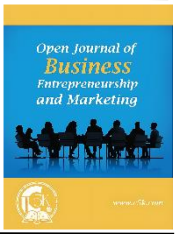

Research Article

Financial Management in Emerging Markets: Challenges and Opportunities

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ABSTRACT

This article examines the future trends and problems of financial risk management. The assessment focuses on the historical advancements and present state of financial risk management. Next, the essential characteristics of the financial sector in the digital economy are examined. The ongoing advancements in technology, namely in computing and telecommunications, are believed to significantly impact the future progress of financial risk management. The utilization of evidence and economic analysis in the formulation of policies is increasing, and this trend is also observed in the establishment of accounting standards and financial regulation. This article explores the potential of evidence-based policymaking in accounting and financial markets, as well as the obstacles and prospects for research that supports this effort. Utilizing sound theoretical principles and strong empirical evidence should ideally result in improved policies and regulations. However, despite its clear attractiveness and significant potential, implementing evidence-based policymaking is more challenging than just requesting it. This text discusses the future trends and problems of financial risk management in the digital economy, taking into account the historical and current practices of financial risk management and the overall trends in the financial industry. Lastly, this section has implications for financial institutions, enterprises, and emerging economies.

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1. Introduction

The adoption of evidence-based policymaking has gained significant traction across various domains, seen from the growth of think tanks and programs that endorse and promote evidence-based policymaking (Karadag, 2015). Evidence-based policymaking refers to the systematic and meticulous process of using scientific and empirical evidence, such as impact studies, cost-benefit assessments, program evaluation, and academic research, to inform policy decisions, such as the implementation of new regulations (Kumar et al., 2024). The allure of evidence-based policymaking is quite apparent. Utilizing scientific knowledge and empirical data to inform policy decisions is highly logical. Policy formulation based on robust theory and empirical evidence is likely to result in superior rules and regulations (Doszhan et al., 2020). Academic research has a crucial role in providing significant empirical evidence and enhancing our comprehension of the impact of policies, both before and after their implementation. Empirical facts and analysis, particularly when based on theory, are believed to impose greater rigor on policymaking, hence enhancing its resistance to political pressures, lobbying, and capture. In addition, research is allocated significant public financing, and hence, it should have a tangible impact on society (Skees, 2003).

In light of these arguments, politicians, regulators, and standard setters are facing mounting pressure to adopt this approach to policymaking and to substantiate their policies with thorough study and empirical data (Hasan et al., 2023). Accounting standard setters, auditing regulators, and financial regulators, including the SEC, are not exempt from this. The accounting standard setters, namely FASB and IASB, have consistently acknowledged their obligation to consider cost-benefit factors in their mission statements and conceptual frameworks (Dafri & Al-Qaruty, 2023). Nevertheless, the standard setters refrain from utilizing traditional or official cost-benefit analysis. Currently, the

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Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) have initiated post-implementation assessments (Ediagbonya & Tioluwani, 2023). Three In addition, the IASB is transitioning towards an approach to standard setting that is informed by evidence. Financial market regulators are also experiencing comparable shifts. As an illustration, the Securities and Exchange Commission (SEC) has encountered significant pressures to do cost-benefit analysis for its rulemaking.Currently, there is no legal obligation for independent U.S. agencies, such as the SEC, to conduct cost-benefit analyses (Falaiye et al., 2024). Nevertheless, there are currently other Congressional measures in progress that would mandate the implementation of rigorous economic research. Financial agencies in the UK are obligated to conduct and publicly disclose cost-benefit studies for proposed regulations. Furthermore, several scholars advocate for the implementation of formal economic or cost-benefit analysis in financial regulation (Jabbouri et al., 2022).

Implementing evidence-based policymaking is a challenging task despite its attractiveness and potential (Sakarya et al., 2007). Research encounters several obstacles in producing data that informs and bolsters policymaking. To tackle these difficulties, significant expenditures are needed in research infrastructure, including data generation, aggregation, and transmission of research findings (Leeds & Sunderland, 2003). This article explores the obstacles and possibilities for research, as well as prospective modifications to the research infrastructure, in order to enhance and methodically facilitate the utilization of evidence in policymaking (Barth et al., 2009). In this post, I primarily discuss studies related to accounting standard setting and financial markets regulation, such as disclosure or securities legislation. However, the insights and discussions presented here may also be applicable to a wider range of economic research.

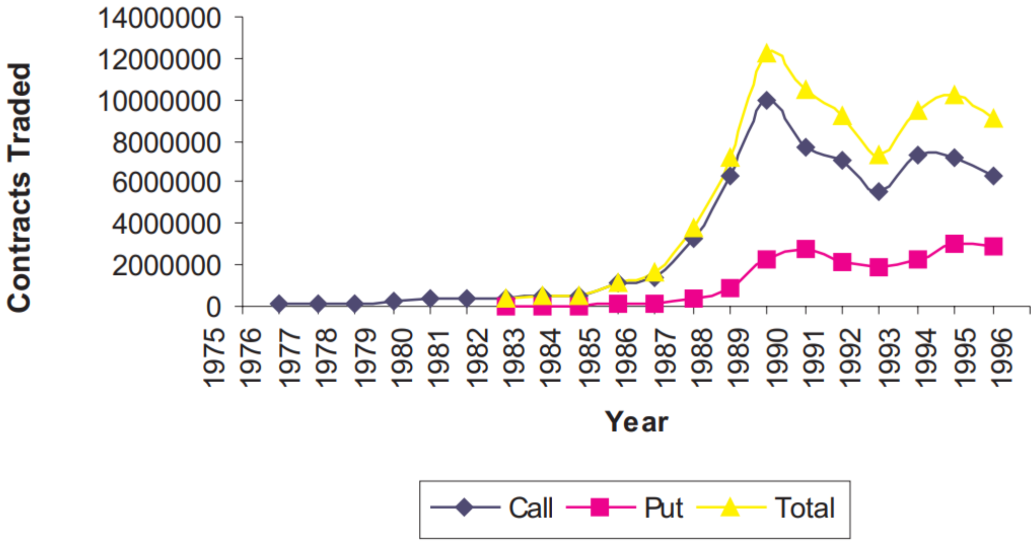

Fig. 1. Past Australian options market (Doszhan et al., 2020)

Fig. 1 shows the Australian options market. With this particular emphasis in mind, I initiate by inquiring about the degree to which accounting and financial markets research provides valuable insights and evidence for policymaking. Financial accounting research is closely linked to policy, namely the establishment of accounting standards. In a broader sense, research on financial markets should have the capability to aid in financial market regulation (Abor & Bokpin, 2010).

This can be achieved by examining pertinent economic connections and relationships, such as the impact of information disclosure on the liquidity of the market. Additionally, accounting research has the potential to provide valuable insights into discussions surrounding disclosure and transparency rules in several fields beyond the primary accounting and financial reporting sector (Marqués et al., 2020). These sectors may include environmental regulation, consumer protection, healthcare, and more. Furthermore, accountants fulfill several responsibilities pertaining to quantification, disclosure, and adherence to regulations beyond the scope of financial reporting. Although I am confident that accounting and financial markets studies provide valuable insights, currently, we lack enough empirical evidence to support these contributions (Khanna & Palepu, 2010). It is advisable to inquire more methodically about the knowledge we have gained from previous studies that can be beneficial to regulators and policymakers. Additionally, this would indicate potential avenues for future investigation (Legesse, 2012).

2. Financial markets research on policymaking

This section examines the degree to which research in accounting and financial markets provides valuable insights and evidence for policymaking purposes. Without a doubt, accounting and financial markets research may provide useful insights to standard setters and regulators. Financial accounting is closely linked to the concept of establishing standards for corporate disclosure and reporting. Early accounting study has a longstanding tradition of including normative considerations. A multitude of accounting studies examine the impacts of accounting rules and disclosure obligations. Financial markets research frequently analyzes the impacts of regulatory modifications (Dekker & Alevizos, 2024; El Amin et al., 2024; Habbal et al., 2024; Minkevics & Kampars, 2021; Wu, 2024). Accounting and financial markets research are frequently intertwined with policy discussions and regulatory matters.

Although it is evident that this research has the capacity to produce significant insights for policymakers and regulators, it remains uncertain how exactly this research has impacted the process of establishing policies. To our knowledge, there is currently no comprehensive record of the contributions made to policies or the effects of this research. There are instances where economists' work has had a significant impact on policy, such as Friedman's examination of an all-volunteer military. In addition, we possess subjective evaluations.

Furthermore, there are studies that examine the effects, but they mostly concentrate on citations and, thus, the influence of research in academia. In addition to citations, numerous authors analyze research impact by utilizing Altmetric's Attention Score. This metric measures the attention that published research receives from online sources such as news sites, policy documents, and social media platforms. While the statistic does not guarantee impact, it does measure the overall level of interest in research. A study has revealed that research conducted in social scientific fields, including economics, finance, management, and psychology, has far less influence or appeal compared to research conducted in the natural sciences. Accounting has the least amount of influence compared to other subjects in business schools, whereas finance has the second lowest impact (although it still receives more attention than accounting). One possible explanation is that accounting and finance are relatively smaller and more specialized fields compared to management, economics, or psychology. In line with this perspective, accounting and finance receive significantly lower attention scores compared to management, marketing, and psychology in the Altmetric categories for news, blogs, and social media. However, they receive higher scores for policy documents. The latter emphasizes, to some extent, the practical importance of accounting and finance research. Fig. 2 shows the depiction of the securitization process.

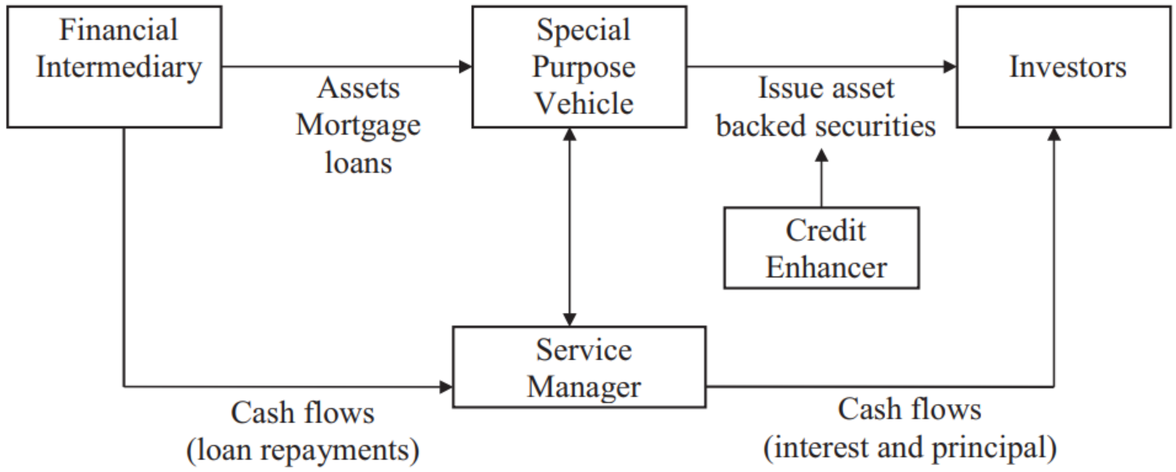

Fig. 2. A depiction of the securitization process (Doszhan et al., 2020).

3. Risks and Opportunities

Similar to any kind of progress, Fintech encompasses not just advantages and opportunities, but also a diverse range of hazards that span across many industries and typically combine both tactical and strategic risk factors. The primary risks and challenges in the FinTech industry stem from worries around operational risk, compliance, liquidity, volatility of bank funding sources, and intense rivalry. The subsequent peril linked to FinTech, specifically in the financial industry.

The possibility of non-bank fintech or BigTech firms rapidly offering bank services separately increases the risks to profitability for individual banks. If new competitors can utilize innovation more effectively and provide cheaper services that better align with client expectations, existing financial institutions may experience a significant decline in their market share or profit margin.

There is a potential for the platform or some of its users to engage in collapse, fraud, or malpractice. There have been instances where platform fraud has occurred.3. Fraud can occur when individuals or entities engage in the buying and selling of securities on the platform.

The increased use of fintech creates more interconnections between market participants (such as banks, fintech companies, and others) and market infrastructures. This can result in a higher risk of IT-related events escalating into a widespread crisis, especially when services are heavily reliant on a small number of dominant players. The inclusion of fintech companies in the banking sector enhances the intricacy of the system and adds new participants who may possess little proficiency and knowledge in handling IT hazards.

The presence of a large number of new goods and services might make it more challenging to manage and control operational risk in financial services delivery. Legacy bank IT systems may lack the necessary adaptability, and its implementation procedures, such as change management, may be insufficient. This type of risk is primarily associated with the reliance on robo-advisers, which can lead to technological challenges such as algorithmic errors, excessively complex algorithms, overly simplistic algorithms, and static client information.

Heightened challenges in fulfilling regulatory obligations, particularly in relation to Anti-money laundering and preventing the funding of terrorism. Anti-Money Laundering/Countering the Financing of Terrorism obligations: The increased level of automation and distribution of the product or service among banks and fintech companies may lead to reduced transparency about transaction execution and compliance duties. The risk associated with performing general solicitation or unlicensed activities has increased. Platforms may argue that they are not involved in regulated activities as they solely provide execution-only services, information services, and matching services. In addition, numerous FinTech platforms may lack uniformity and offer less comprehensive information compared to publicly traded equities. Cyber-risk refers to the potential harm or damage that can arise from activities or events in the digital realm. Increased dependence on application programming interface (APIs), cloud computing, and other emerging technologies that enable greater interconnectivity may heighten the susceptibility of the financial system to cyber-threats and expose significant amounts of sensitive data to potential breaches.

The utilization of modern technologies and aggregators allows clients to automatically switch between various savings accounts or mutual funds in order to achieve a more favorable return, hence increasing liquidity risk and volatility of bank funding sources. Although this has the potential to enhance efficiency, it can also have an impact on consumer loyalty and lead to greater fluctuations in deposits. Consequently, this could result in increased liquidity risk for banks, as shown in Table 1.

Table 1. Potential risks and advantages arising from the implementation of financial technologies and innovation (Saudagaran & Diga, 1997).

	Risks	**Opportunities**
Impact on consumer sector	A. Data privacy B. Data security C. Discontinuity of banking services D. Inappropriate marketing practices	A. Financial inclusion B. Better and more tailored banking services C. Lower transaction costs and faster banking services
Impact on banks and banking system	A. Strategic and profitability risks B. Increased interconnectedness between financial parties C. High operational risk – systemic D. High operational risk – idiosyncratic E. Third-party/vendor management risk F. Compliance risk including failure to protect consumers and data protection regulation G. Money laundering – terrorism financing risk H. Liquidity risk and volatility of bank funding sources	A. Improved and more efficient banking processes B. Innovative use of data for marketing and risk management purposes c. Potential positive impact on financial stability due to increased competition[15] D. Regtech

4. Significance in developing economies

Emerging economies are confronted with several domestic vulnerabilities, including excessive dependence on the export of raw materials, insufficient oversight and capitalization of banks, underdeveloped capital markets, and policy errors made by governments. As a result, emerging economies exhibit greater volatility compared to industrial countries.

Emerging economies are not only susceptible to internal weaknesses, but also confront dangers stemming from global causes that are beyond of their influence. The first factor to consider is the overall state of the global economy, which has a direct influence on both the cost of commodities and the amount of imports that developing countries are requested to provide. Furthermore, monetary policy and its influence on foreign exchange policy are crucial factors. This is because alterations in exchange rates of wealthy nations can have a significant impact on both the trade and capital accounts of developing countries. Trade policy modifications can significantly affect the economic prospects of developing economies. Implementing higher tariffs on imported products and services or completely shutting down borders can have a catastrophic impact on developing nations.

Based on the aforementioned features of emerging economies, it is evident that the aforementioned consequences for financial institutions and enterprises are indeed applicable in emerging economies. In addition, the presence of domestic uncertainty in emerging countries will introduce further complexities to financial risk management in those economies.

In emerging economies, the financial industry is sometimes subject to strict regulations, resulting in limited availability of risk management tools commonly seen in industrialized markets. Currently, the technical infrastructures of emerging economies often fall behind those in industrialized economies. Therefore, the process of managing financial risks in emerging economies still has a significant amount of progress to make.

Conversely, the level of consciousness and readiness of corporations to handle their risks has unquestionably risen in the developing countries as a result of events like the Asian financial crisis. The demand for financial risk management has been increasing, particularly in recent years. Financial institutions from industrial economies are eager to investigate financial risk management in emerging economies due to their significant revenue potential. Consequently, the progress of financial risk management in emerging economies is expected to occur rapidly.

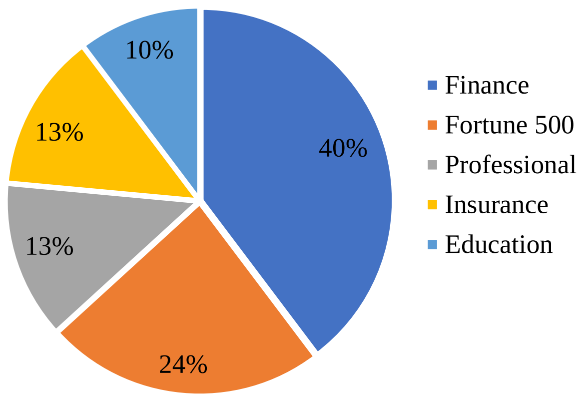

Fig. 3. Opportunities in the financial market (Pilipczuk et al., 2019)

Overall, emerging economies must confront the patterns of financial risk management in the digital economy and thus have comparable obstacles. Fig. 3 shows the Opportunities in the financial market. However, the unique difficulties encountered by each developing nation are also influenced by additional elements, such as rules pertaining to the banking sector and the technical infrastructure.

5. Conclusions

The financial industry is undergoing fast transformation in today's digital economy. We are currently experiencing a rise in the speed of financial advancements, a swift growth in international financial transactions, a quicker transmission of shocks or errors across the global financial system, and a heightened responsiveness of financial market prices to changes in preferences. These changes subsequently dictate the future trends of financial risk management. The field of financial risk management will experience rapid evolution with the emergence of new risk management solutions and ongoing improvements to the financial risk management system.

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