

General Discussion*

In responding to the discussion of Gerald Goldstein, John Chant agreed that principal–agent problems arise when markets for corporate control weaken for Canadian banks. This lack of disciplinary pressure on management could lead to the kind of fraudulent behaviour that we have witnessed in the case of stock options. Another explanation for the linkages might be a reverse-causation argument. For instance, large borrowers are able to secure positions on bank boards and, as a result, extract some of the rents through lower loan rates.

A number of participants offered suggestions for other potential sources of linkages. Raphael Solomon was concerned about whether there could be enough instances of default to use credit ratings as a basis for measuring loan quality. He wondered whether they should consider incorporating large shareholders and loans to expand the sample size or diversity of data.

Sean O’Connor suggested looking at linkages from a perspective of relationship banking in which there may be other fees collected by banks in addition to interest. Consequently, given the expectation of future revenues, a bank may take a lower rate on a collateralized loan up front as part of a long-term relationship package.

In response to Claudio Borio’s discussion, Marc Quintyn pointed out that the empirical project was preliminary and that the data set was still in its infancy. To capture the evolutionary aspects of regulation, more years of data would be needed. He also felt that their measurement of the regulatory

* Prepared by Greg Caldwell.

governance index needed work. He added that they had to develop a better measure of the structure of the banking system.

In the general discussion that followed, John Helliwell began with a question on modelling. Given the parallel effects of regulation and government, he felt there was probably no need for variables of government effectiveness, regulatory effectiveness, and an interaction term. Chenard argued that these were necessary to investigate multicollinearity. In a similar vein, a question was raised about the use of ordinal versus cardinal rankings.

Raising a different issue, John Chant wondered whether accountability would be as precise with multiple goals. For instance, was there a way to measure central bank and regulatory independence? Quintyn pointed out that monetary and financial transparency could measure transparency and other aspects of central banking for the central bank. Banks also had a separate measure for supervisors. If the supervisor was the central bank, there should be a correspondence between the two measures. If, however, the supervisor was separate from the central bank, there should be differences when the supervisors were less accountable. Or, one could also see differences when fewer accountability mechanisms were in place for a particular country.

Charles Freedman asked if it mattered whether or not the regulatory authority was inside the central bank. For banks to be protected from political interference, Quintyn felt that in many countries, central bank independence was much greater than the independence of supervisors. Consequently, for many transition countries, supervision came from within the central bank to allow supervisors to “piggyback” on central bank independence. Meanwhile, in many other countries, this was not the case, and quite often the supervisors were less independent and less accountable.

