Financial sector convergence and corporate governance

Andy Mullineux
Birmingham Business School, The University of Birmingham, Birmingham, UK
Financial sector convergence and corporate governance

Andy Mullineux
Birmingham Business School, The University of Birmingham,
Birmingham, UK

Abstract
Purpose – To explore the implications of financial sector convergence for corporate governance systems.

Design/methodology/approach – Globalisation, regulatory harmonisation and pensions reform are driving convergence of bank and market-oriented systems of corporate finance towards a hybrid model (“hybridisation”). Given the importance of financial systems in corporate governance, this may lead to convergence of corporate governance systems; legal traditions notwithstanding.

Findings – The growth in the importance of funds (pension, insurance, mutual, hedge, venture capital) and the decline in the importance of bank as shareholders has the potential for forcing convergence in corporate governance if the funds actively use their shareholder (or proxy) voting rights. Data on financial institution voting patterns is required to test the hypothesis.

Originality/value – Hybridisation is increasingly widely recognised, although not universally supported by the data. This paper attempts to draw the implication of the hybridisation process for corporate governance given the breakdown of traditional market and bank-based systems.

Keywords Financial institutions, Economic convergence, Corporate governance

Paper type Viewpoint

Introduction
Since, the early 1970s, there has been substantial liberalisation of the banking sector and financial innovation. The process has been facilitated by deregulation of banks (Mullineux, 1992), which continue to lie at the heart of all financial systems (Mishkin, 2004). Quantitative and qualitative controls and guidance have been largely replaced in many countries with a price (interest rate) oriented monetary policy and general prudential regulations (Hermes et al., 1998, 2000). The latter includes: risk related capital adequacy requirements (the Basel I accord); deposit insurance schemes (also risk-related in the USA); rules prohibiting overexposure (to individuals, sectors of the economy, or foreign exchange risk) in order to promote portfolio diversification and risk reduction; and rules requiring the holding of adequate reserves to assure liquidity and to make provisions against bad or doubtful debts.

To inform supervision by the authorities, there are confidential disclosure requirements; and to facilitate monitoring by equity and bond holders, there are public disclosure and auditing requirements. In addition, banks and other financial institutions disclose confidential information to credit rating agencies in order to gain ratings that reflect their credit standing and this in turn determines their cost of capital. Finally, to aid comparison in the increasingly global environment, accounting and disclosure rules are in the process of being harmonised and country-based supervisors.