OPINION

WHO WILL RULE THE FINANCIAL GOVERNANCE SYSTEM?

by Guillermo Kopp
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When economies move down unexpectedly, governments are keen to lift up ailing financial institutions that are deemed "too big to nail down." ***Would the danger of failure by any such big player be greater than the unintended consequences of a government bailout?*** If a government can take stock in a troubled institution and sell such stake later at a hefty profit, why should taxpayers care?

The impact of rescuing a financial institution transcends any particular bailout transaction. The complexity and interconnectedness of the global financial system continues to increase. So does the systemic risk that as a whole affects banks, securities firms (including hedge funds and "tax havens"), insurance companies, and also the treasuries of large corporations. As the entire system shakes, the long term consequences will be felt in both cultural and structural terms.

Over the centuries and after many a crisis, financial markets have learnt how to adapt and reach new points of equilibrium. When the financial system undergoes severe distress, governments may play a stabilizing role as "last resort" providers of credit and liquidity. But would such stabilization promote long term stability across the financial system and the economies that it supports?

To be stable, any system must stand on robust foundations. If governments invest heavily to support stumbling institutions, then new rules must also remove the roots of instability. Otherwise, the notion that a company should be accountable for its own health might give way to a culture of complacency. ***If governments will always come to their rescue, why should companies refrain from taking excessive financial risks?***

Money is fungible so for a troubled company, a dollar "in the red" of appears to be as green as a rescuing dollar. However, governmental cleansing and intestine controls over the burden of bad loans and other rotten financial assets would do little to stop the ingestion of unhealthy funds. Absent a permanent fix to the financial structure that should make funds available to productive uses, big investors could be tempted to bet, and governments would feel compelled to bail them out.

What rules will bring stability? Who should be in control? For starters, a series of domestic rules should mind the big picture of a global and interdependent financial system. A culture of broader alignment and productive purpose should eradicate structural imbalances. To achieve stability, governments and regulatory agencies must aim beyond isolated protective measures and tactical stabilization moves.

Enduring financial stability will require a cultural shift at the Board of Directors level. Corporate directors must act upon their direct responsibilities for strategic direction and oversight. Boards are where "the buck should stop." And regulations must reaffirm the duties and accountability of corporate directors for ensuring that their companies run sustainable businesses. When adopted throughout the financial system, a culture of sound business principles will build up a more dependable foundation.