Corporate Governance and Bank Liquidity Creation: An International Analysis[†]

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This paper employs the measures of bank liquidity creation proposed by Berger and Bouwman (2009) to examine the relationship between corporate governance and bank liquidity creation from the individual bank perspective. The sample consists of the banks and bank holding companies in G20 and Taiwan from 2002 to 2008. We use the degree of independence of shareholders and board size to measure the corporate governance structures. The empirical results show that an inverse U shape relationship between the degree of independence of shareholders and bank liquidity creation exists in the full sample or in the developed countries, but it becomes a negative linear relationship in the developing countries. On the other side, bank liquidity creation increases with the board size significantly for large banks or in the developing countries. We also test the relationship between capital and liquidity creation, the results indicate that bank capital impedes liquidity creation for small banks, supporting "financial fragility-crowding out" hypothesis. However, a higher capital improves banks' ability to absorb risk and create more liquidity for large banks, consistent with "risk absorption" hypothesis.

Key words: corporate governance, liquidity creation, financial fragility-crowding out, risk absorption

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