Does Corporate Culture Affect Bank Risk-Taking? Evidence from Loan-Level Data

Nguyen et al., 2019

Context

Many believe that the competitive corporate culture present in banks is key factor in bank's risk-taking behavior which ultimately has large implications on global financial stability.

Given the lack of empirical evidence on the relationship between bank culture and risk-taking behaviour, this paper addresses that gap by examining whether bank culture affects risk-taking in lending decisions.

The authors use data on loan contracts from 1993-2007 from US lenders and determine bank's dominant culture (control, compete, collaborate or create) by analysing text in annual reports. They examine changes in lending behaviour before and after the Russian default event.

Key Insights

The authors find that compete-dominant banks have riskier behaviour.

Riskier lending practices

Compete-dominant banks have a willingness to take on higher default risk and impose fewer covenants. However, they do charge higher interest rates to compensate for this higher risk.

Greater risk to financial stability

Since compete-dominant banks incur a higher proportion of non-performing loans and hold a significantly lower level of Tier-1 capital this increases the risk of instability in the financial system.

Market conditions affect lending behaviour

Compete-dominant banks show higher loan growth in normal times, but their risky lending behaviour stops in periods of distress when the proportion of non-performing loans starts to increase.

The opposite was found for control-dominant banks

Implications

- How could you use text analysis in your organisation? What behaviours would you want to understand?
- How would you describe the culture in your organisation or team?
- How might your organisation's internal risk culture shape the products you create for your users?

Nguyen, D. D., Nguyen, L., & Sila, V. (2019). Does Corporate Culture Affect Bank Risk-Taking? Evidence from Loan-Level Data. *British Journal of Management*, *30*(1), 106–133. https://doi.org/10.1111/1467-8551.12300