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Revisiting the impact of institutional quality on post-GFC bank risk-taking: Evidence from emerging countries

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Abstract

This is the first attempt to address the impact of institutional quality on post-GFC bank risk-taking behavior. This study is conducted on 730 banks from 19 emerging countries covering the period 2011–2016. We used six indicators of good governance as a proxy for institutional quality. Both static panel and Dynamic GMM estimation are used to identify the impact of these variables on bank risk-taking; measured by Z-score. We evidenced that increasing government effectiveness, controlling corruption, and improving agents' confidence and adherence to the rule of law reduce banks' risk exposure and improve banks' stability. Besides supporting the Z-score model, the robustness test using σ(NIM) also provides evidence of the impact of regulatory quality on reducing bank risk. Surprisingly, both models tend to indicate that improving voice and accountability increase bank risk-taking in emerging countries. Furthermore, our study provides an interesting reconciliation to the major debate on the impact of size on bank risk.