



WAS THE CRISIS DUE TO A SHIFT FROM
STAKEHOLDER TO SHAREHOLDER FINANCE?
SURVEYING THE DEBATE

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Was the Crisis due to a shift from stakeholder to shareholder finance? Surveying the debate

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Abstract

We discuss the literature on the shift from stakeholder to shareholder finance behind the Great Financial Crisis (GFC). Traditional banks generally maximized stakeholder value (STV). But before the GFC also many of them started maximizing shareholder value (SHV). Moving from STV to SHV often meant shifting credit management from Originate-to-Hold (OTH) to Originate-to-Distribute (OTD). Moving from STV-OTH to SHV-OTD increased systemic risk damaging the common good of financial stability. STV-oriented banks seemed to weather the GFC relatively better with more heterogeneous systems proving more resilient. Heterogeneity in banking governance-orientations/ownership-structures seems to add value reducing the probability of financial crises.

JEL Classification codes: G0; G01; G14; G15; G18; G21; G20; G24; G28; G30; G32.

Keywords: Financial and Banking Crises; Bank Governance; Financial Regulation; Financial Institutions and Organizations.

1. Introduction

This paper critically surveys the literature on the change from traditional to non-traditional models in banking corporate governance and credit management, analyzing how this change promoted the Great Financial Crisis (GFC) of 2007-2009. Largely, this change affected the organization of banks shifting their corporate governance model from Stakeholder Value (STV) to Shareholder Value (SHV).

The change from STV to SHV in banks has been largely achieved by having economic organizations maximize SHV and often use an Originate-to-Distribute (OTD) credit management model with respect to banks maximizing STV typically using the Originate-to-Hold (OTH) model. The shift from STV to SHV and from OTH to OTD synthesizes and represents the change from traditional to non-traditional banking. Traditional banks grant credit by using deposits and get revenues via interest rate spread holding credit contracts until maturity (OTH model). Non-traditional banks generate credit not only via deposits but also selling credit. These are banks on the supply side which profit by selling credit contracts to other parties that, through securitization, can generate a higher return for the banks (OTD model). Usually these banks have low Net Interest Margin and Credit/Deposit ratios structurally above 1 meaning that they use other sources of funding such as derivatives, securitization and interbank loans. The OTH-OTD change in credit management is representative of a deeper STV-SHV change in the corporate governance of financial organizations. This change relates to how banks interpret their role with respect to shareholders, borrowers, communities in reaching social valuable objects. In fact, when banks focus on creating relationships with the external environment – producing social valuable goods such as confidence, financial stability, liquidity, macro sustainability, being active part of communities – they more likely enforce relationship banking using an OTH credit management. In this case their management model tends to maximize STV. This is typical of some particular forms of banks such as cooperatives, credit unions, savings banks, ethic banks that have complex systems of relationships with different economic claimants maximizing resources in a long run perspective.

On the other side lie banks maximizing SHV. These banks maximize their position in the short run with reduced possibilities to develop relationships with communities and multi-stakeholders, since they focus on creating more present values for their shareholders as if their shareholders were the only stakeholder in a sort of single-stakeholder model. These banks may develop a system based on OTD, in which they create credit just to be securitized selling it on financial markets to obtain high present revenues. As said, the OTH-OTD change in credit management often parallels an STV-SHV change in corporate governance. However there is also a reverse causality between credit management and corporate governance models. If OTH lets us infer STV maximization and OTD lets us infer SHV

maximization, also the reverse is true.¹ This is showed by the managerial behavior of cooperative banks, savings banks and credit unions that generally have an STV model and through relationship banking apply the OTH model, juxtaposed to the behavior of large banks that maximize SHV based on statistical evaluation of creditworthiness applying the OTD model.

In banking it is accepted that banks do some form of non-traditional activity. But there are many risks when banks apply structured forms of financial innovation such as securitization. Indeed, this is juxtaposed to an OTH traditional model which is not only better able to guarantee efficiency and long run perspective for banks but can also be a tool for an endogenous political economy strategies aimed to macro-financial stability. The differences between STV and SHV oriented banks are represented in their balance sheets and income ratios like Net Interest Margin (NIM). «*Relationship banks still enjoy considerable interest margins*» in the words of Ewijk & Arnold (2013). NIM is one of the measures frequently used to classify the income representation of the banking business, showing the part of a bank's earnings from traditional activities. The data shows a decline in NIM in the run-up to the GFC. That is, banks developed non-traditional activities during the financial globalization phase changing their credit model from OTH to OTD. This shift changed the role of banks in the economy. In fact, while in the traditional STV-OTH banking model banks produce stability, in the non-traditional SHV-OTD banking model banks change their institutional mandate possibly producing instability, breaking the finance-growth nexus and creating the premises for financial crises. We survey the literature relating financial stability to the OTH model stressing that banks can promote stability when they retain an STV-OTH model. In this case banks can stabilize the business cycle and also be instruments for economic growth, while the structure of risks in the financial system can be controlled by regulatory reserves and this can help to stabilize the business cycle (Ferri et al., 2014a; 2014b).

The change from OTH to OTD and that from STV to SHV raised risks for the banking sector, financial markets and macro-financial stability. In fact, in non-traditional banking risks are difficult to calculate, e.g., for non-regulatory reserves banks must build as collateral on non-traditional activities, driven by financial innovation, which, by definition, consists of contracts yet unregulated. The engineering process of creating securities based on credit contracts developed risks with inadequate coverage that drove the banking and financial sector to the crisis. At the same time the more developed screening and monitoring processes in the STV-OTH model can discriminate borrowers excluding those that are just asking for credit to buy low and sell high, as for many during the housing price bubble at the heart of

¹ Even if we can't say that the relations STV-OTH and SHV-OTD have the mathematical meaning of a logic identity.

the GFC with the subprime mortgages mismanagement. So, by shifting from OTH to OTD, banks raise the structure of risks in the financial system and may produce financial instability leading to crises.

Our critical survey is organized as follows. Section 2 analyzes the change from STV to SHV in banking showing how STV relates to OTH while SHV relates to OTD. Section 3 studies the change from OTH to OTD, how this reduced the quality of screening and monitoring, disrupted the process of acquiring information and complete contracts increasing individual and systemic risks. Section 4 analyzes how the shift from STV-OTH to SHV-OTD affected macro financial stability changing the traditional role of banks with respect to the business cycle dynamics and how this contributed to the subprime mortgage crisis. Section 5 surveys the literature on the varieties of capitalism focusing on the comparative analysis of financial systems. In Section 6 we present the main conclusions.

2. The Evolution of the Stakeholder Value vs. Shareholder Value Debate

Shareholder Value (SHV) and Stakeholder Value (STV) are the two corporate governance models juxtaposed in the economic literature (Freeman et al., 2010). The main difference between STV and SHV maximization relates to the different economic constituencies holding subjective rights and legitimate interests to whom the strategic choices of the management are consciously directed. While organizations maximizing STV have the ability to develop management systems counting directly the interests of stakeholders such as employees, customers, and others (Freeman, 1984) affected by the corporation, shareholders make the only deserving stake in SHV maximization. Some managerial scientists have defined stakeholders as the economic actors essential to a firm's survivorship (Stewart et al., 1963), or as those related to the firm for the realization of their personal goals (Rheman, 1968).

Stakeholder theory is an interdisciplinary theory (Freeman et al., 2010). Some authors have questioned whether it is a comprehensive doctrine in the sense of Rawls (1993), rejecting this idea and proposing stakeholder theory as an organizational theory (Orts & Strudler, 2002; Phillips, 2003). Stakeholder theory is divided into three fundamental parts: descriptive, instrumental and normative. Descriptive stakeholder theory illustrates what managers and companies actually do. Instrumental stakeholder theory consists of research on the outcomes of specific managerial behavior. Normative stakeholder theory relates to what managers or corporations should do (Donaldson & Preston, 1995). Freeman et al. (2010) combine these three elements in a libertarian and pragmatic conception of stakeholder theory.

One of the merits generally recognized to stakeholder theory is that it links in a pragmatic framework the old topic of business and society due to the fact that in it all the dichotomies between business and ethics and business and society are overcome in a common cognition enforced in the decision-making

process (Jones, 1995).⁴ From another point of view, business ethicists and philosophers applied to the theory of the firm and economic organizations appreciate Stakeholder theory for having linked philosophy and management (Jones & Wicks, 1999).

In the economic literature the debate between shareholder theory and stakeholder theory is often referred to as the Friedman vs. Freeman (Freeman, 1984) debate. Nobel Prize scholar Milton Friedman proposed that SHV maximization, i.e. present profit maximization, is the only way for corporations to produce social valuable goals. One of the main founts generally reported is a 1970 New York Times Magazine article entitled «*The social responsibility of business is to increase its profits*» where he argues that there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, i.e., it engages in open and free competition without deception or fraud (Friedman, 1970).

Friedman's is considered an article against the stakeholder theory. But we can note that Friedman never cites that theory, since his explicit intent is not to confute it, but to offer arguments against Corporate Social Responsibility (CSR), considered as a normative, collectivist, heteronymous application of rules to business. Friedman stresses the challenge between collectivism and individualism. He views CSR as a normative way to create a sort of collectivized society reducing the freedom of businessmen. Against this collectivist view he proposes his idea of business based on individual freedom in a society defined as «*[...] a collection of individuals and of the various groups they voluntarily form*». So Friedman tries to defend the idea of freedom to choose and the anti-collectivist view that is a sort of self-determination of individuals and groups of individuals in setting their goals and in trying to obtain them. In Friedman's economic thought being free to choose is the main characteristic of the homo oeconomicus as well as the end of his actions, and institutions should be mandated just to preserve this fundamental liberty (Friedman, 1962). Businessmen must be free to manage their corporations making profits.

This idea has influenced the economic literature and inspired legislators (Donaldson & Preston, 1995; Marens & Wicks, 1999). But, as we'll show later, we can't assimilate stakeholder theory with CSR, since while STV maximization is a model that affects directly the cognitive process of rational choice, and in this sense it is based on the freedom to choose, in CSR the cognitive process is instead related to the normative definition of what can be considered a common idea of justice with respect of whom the corporation assumes obligations to. Pedersen (2006) shows that there is no accepted definition of CSR and managers must work to translate CSR concepts in practice, so in this sense STV maximization is a more pragmatic framework. Sacconi (2006) develops a model of CSR that is convergent to stakeholder theory defining the firm as a multi-stakeholder organization, showing that stakeholder theory relates to

decision theory. While CSR is normative, heteronomous and presents some coercive force with respect to individuals' freedom, shareholder and stakeholder theories are positive, they require the autonomy of economic agents that must be free to apply responsibly and consciously choose a strategic management model. Jones (1980) criticizes CSR scholars who prescribe managers to develop a theory of corporate social policy based on a generic principle of public responsibility mirroring the government's public policy. Stakeholder theory still remains a theory of choice in that it considers how firms balance among differentiated stakeholders (Laplume et al., 2008) or assuming single rational choice (Firouzabadi et al., 2008). In the economic literature many authors have showed that STV based decision theory can be used especially in the case of complex external environments (Liebl, 2002; Chou et al., 2006; Henn & Patz, 2007; Mohanty et al., 2005; Lewis et al., 2007; Morgan & Matlok, 2008).

Some business ethicists (Freeman et al., 2010) judge Friedman's view compatible with instrumental stakeholder theory where catering for non-shareholder stakeholders is viewed useful to shareholders (Jones, 1995; Donaldson & Preston, 1995; Jones & Wicks, 1999). In fact, the instrumental theory recognizes primary stakeholders different from secondary stakeholders (Clarkson, 1998).

So, on one hand Friedman confutes CSR, on the other hand Freeman underlines that also STV theory differs from CSR. Stakeholder theory in Freeman's definition is autonomous and based on the freedom to choose by managers and directors. Thus, SHV, in Friedman's definition, and STV, in Freeman's definition, share at least two common characteristics: i) they are autonomous vis-à-vis external norms, such as CSR rules, and ii) they hinge on the freedom of businessmen to apply a strategic management model, or in other words they postulate individuals' freedom to choose. We must consider at first that SHV and STV maximization are models within decision theory (Chang et al., 2007) or in the case of multi-criteria decision-making processes (Bryson & Mobolurin, 1996). Thus, we must view the differences between SHV and STV maximizations, as systems that directly inspire managers' rational choices, and so they are autonomous from other kinds of social, ethical, and normative obligations, such as, e.g., CSR, that are not in the mind of the decision maker, and in this sense are heteronomous.

Many economists have studied CSR arguing that the presence of specified rules for managers' obligations vis-à-vis the economic and social environment could solve the problem of the responsibility of corporations as to negative externalities, e.g. in our case saving disruption or financial instability. There is something positive in the CSR literature in that it has developed mechanisms for social and ethical accounting (Zadek et al., 1997) effectively available to managers in STV decision theory. But the STV-SHV debate still remains open, since while they are both inside the rationality of choices, in this sense they are autonomous, CSR is based on a set of rules that are heteronomous to the decision

maker, and so don't affect the cognitive process of choices. Indeed, CSR can't solve the value creation problem, to manage the way in which firms affect society, since ethics is not viewed as an afterthought in the value creation process (Freeman et al., 2010). In our case many banks and corporations before the GFC had CSR statues but this guaranteed neither STV maximization nor ethical behavior.

Stakeholder and Shareholder managements are instead models that inform directly the rationality and the reasonableness of managers' choice. So, in our analysis of what is the rationality behind those choices we must exclude CSR, because if CSR may produce a debate among managers, board of directors, and other corporate divisions, this debate doesn't affect the rational choice but simply remains as a set of rules, as general reference, as a statutory obligation. CSR is insufficient to address the business vs. ethics relationship in the manager's decision-making process (Windsor, 2006).

On the contrary STV and SHV maximization are models that inform directly governance rationality in developing strategies, in the process of making choices to reach corporate goals. Wood (1991) details the link between CSR and stakeholder theory. SHV and STV theories are both compatible with a society based on individualism and freedom, along an anti-collectivist view, as explained in the paper *Stakeholder theory a Libertarian Defense* (Freeman & Philips, 2001) viewing stakeholder theory as a choice of the management based on individuals' fundamental freedom. Stakeholder theorists remark the libertarian perspective of STV arguing against a shareholder economy (Philips, 2003) proposed as a model of political economy by some authors (Barnett, 1997; Hutton, 1995; Rustin, 1997).

Economists studying the nexus between leadership and stakeholders (Friedman & Olk, 1995; Nwanko & Richardson, 1996; Heller, 1997; Roberts & King, 1989) stress that Stakeholder theory can be seen as a managerial choice theory. Not only the development of leadership features in a single economic organization but also the relationships among different leaders across organizations can be efficiently developed in an STV model. STV decision theory builds ethical oriented efficient leadership (Friedman & Olk, 1995; Andreadis, 2002; Hall et al., 2004; Thomas et al., 2004; Fubini et al., 2006; Stenberg, 2007; Clement, 2005; Covey & Merrill, 2006).

Having seen the commonalities, we can now focus on the differences between SHV and STV theories. To understand the methodologies behind managers' choice, we must refer to the model that directly affects their rationality and reasonableness, referring to STV vs. SHV maximization. The main contrast stems from the diversity and plurality of economic agents that are consciously involved in a firm's strategic management. So, the main difference between STV and SHV theories is that while in the former various groups have a moral claim, such as, e.g., employees, customers, environmentalists, in the latter there is a single group that has a moral claim that is constituted by the shareholders (Freeman,

1984). Indeed, stakeholder theorists separate legal fiduciary and moral non-fiduciary duties (Boatright, 1994). On philosophical grounds the main contrast is that STV can overcome Goodpaster's paradox of a business without ethics and an ethics without business (Goodpaster, 1991). Craig (2002) proposes solving the paradox by overcoming the division between moral and legal duties.

Several managerial and economic theories have been juxtaposed to STV as more prone to sustain an SHV approach. For example, Porter's (1980) idea of management and Williamson's Transaction Cost Economics (Williamson, 1975) have been viewed as opposed to stakeholder theory. But, these two ideas are completely compatible with STV (Freeman et al., 2010). Porter's model of management based on the idea that firms must compete not only in the market but also with suppliers, customers and other subjects (Porter, 1980) is compatible with the idea of STV as a strategic management in which all the persons, groups, constituencies that are affected or affect a firm's life are considered in the decision-making process (Freeman et al., 2010). This means that the stakeholder approach is strategically useful and coherently informed with the principal ideas of Porter's management model.

Williamson's TCE embodies the idea that a firm is a set of contracts (Williamson, 1980) and that have safeguards. Since contracts can self-regulate all the possible risks in the market, in this way managers can optimize SHV. But, in a deeper analysis, Freeman & Evans (1990) showed that it is possible to distinguish two different kinds of contracts, on one side we have contracts with endogenous safeguards, i.e. contracts in which private subscribers can intervene in case some obligations are not respected, and contracts with exogenous safeguards, i.e. contracts in which the cost of the failures are sustained by communities or other stakeholders. Either kind of contract is compatible with STV maximization. In fact, if contracts have endogenous safeguards they can self-regulate the risk of failure also in case of STV maximization. If contracts have exogenous safeguards they produce externalities that are not considered in an SHV model and that only an STV maximization model can manage (Freeman et al., 2010). So we can conclude that the STV theory is compatible with Friedman's idea of businesses' social responsibility, as well as with Porter's model of management or with Williamson's TCE theory.

But probably the strongest opposition to STV theory hinges on agency theory. An agency problem exists if the management works against shareholders' interests. Jensen & Meckling (1976) showed that the best way to solve the agency problem is to maximize SHV. But this is not a strategic solution and finally Jensen (2001) admitted that satisfying multiple stakeholders is essential to maximizing the objective function of wealth maximization for shareholders (Freeman et al., 2010). The reason why STV is compatible with the definition of Friedman, the TCE and the agency theory is that STV is based on pragmatism and libertarianism that are common frameworks in Friedman's definition of capitalism,

in Williamson's definition of the firm as a nexus contracts, as well as with Jensen's definition of agency theory and Porter's system of management (Freeman et al., 2010).

Many authors (Blair, 1995; Zingales, 1998; Blair & Stout, 1999) reject the principle of shareholder supremacy and the reductive principal-agent view of the firm, where managers bear fiduciary duties only towards the shareholders. Other economists argue that STV and SHV maximization must be considered in terms of representativeness and democracy. One of the main distinctions between STV and SHV theories is that in the former the agents are considered as ends in the Kantian sense (Evan & Freeman, 1988). Stakeholders are, in a certain way, investors in the corporation not only in a pure financial sense (Blair, 1998), but also producing social capital (Schlossberger, 1994) as part of the firm considered as a community (Etzioni, 1998). These are arguments that sustain also the participation of stakeholders in the governance of economic organizations as in the theory of democratic stakeholders. That theory states that stakeholders legitimately enter directly in firms' governance. In this sense, Jones & Goldberg (1982) held the legitimacy of corporate governance with democratic principles. In many countries there are forms of stakeholders representativeness such as, for example, in Germany where employees are directly involved in the governance of corporations, or where political representatives are engaged in the administration of local saving banks. The concept of stakeholder democracy differs from the traditional idea of STV maximization since in it stakeholders are not only object of strategic management, but are directly part of the governance via a representativeness mechanism. So, while in an STV maximization approach managers and directors follow a model taking rational and reasonable choices based on stakeholders' interests, in a stakeholder democracy approach stakeholders are part of the board of directors or, more broadly, of the corporate governance setup. But, at the same time, the fact that some stakeholders contribute to the governance doesn't automatically mean applying STV maximization since not all stakeholders are represented. Thus, in a stakeholder democracy managers must apply STV management also vis-à-vis subjects lacking legitimate corporate representativeness. Many different definitions and developments of SHV and STV maximization concepts were proposed but the terms of the debate remain substantially as in the classical Friedman vs. Freeman debate.

2.1) STV and SHV theories and their connections with the OTH and OTD models

The concepts introduced above in general relate to nonfinancial corporations, but we can apply them also to banks. In fact, also banks can be managed in an STV or SHV maximization model.

Drawing a line between nonfinancial corporations and banks can be important since a large part of the literature distinguishes the latter from pure firms and enterprises (North, 1990), due to the fact that

banks are engaged in the administration of savings and affect financial stability that are considered as common goods. The main difference between a bank and a nonfinancial firm is that banks can solve market failures. Some economists hold that banks can be considered as pure enterprises and in this case perfectly free to apply SHV and profit maximization following the idea of the firm as a nexus of contracts (Coase, 1937; Williamson, 1980). But since banking is everywhere subject to particular attention by regulators, in reality, this distinguishes banks from nonfinancial corporations.

We may classify banks depending on whether they follow an STV or an SHV maximization model. Cooperative banks, savings banks, credit unions traditionally apply an STV maximization model while commercial banks and non-banking financial intermediaries apply an SHV maximization model as a strategy to maximize profits (Coco & Ferri, 2010). These different models of management highlight differences in the banks' mandate. In fact, while some banks have in their statutory mandate social valuable objectives such as catering for communities, common goods, stakeholders and persons, other banks are organized to purely maximize profits (Jensen, 2000). The latter don't consider the interests of communities, persons, groups as objectives of the choices of the management (Freeman, 1984). The difference matters in the economics of relationships. While the STV maximization model prompts the manager to have relationships with stakeholders, in the SHV model those relationships don't matter since the objective of the management is simply to maximize the value of the shares (Friedman, 1960). When banks maximize STV, e.g., at cooperative banks, they create value not only for the shareholders but can aim to reduce borrowers' financial exclusion based on the mutuality concepts and at the same time to preserve stability and the savings that are common goods, i.e. they can serve also the general interests of their communities. Interesting in STV theory is the networking among banks and the fact that banks can consider other banks as stakeholders in the interbank market acquiring credibility and sustainable relationships. In all these passages relationships are important among the members of the cooperative, but also between bank and borrower, the bank and its community. The importance of stakeholders is recognized by the US legislator via The Corporate Constituency Statutes enforced in an antitakeover strategy (McDonnell, 2004). Stakeholder theory creates relationships between banks and various stakeholders, suggesting that this theory develops an economics of relationships, in which dialogue and consensus among decision makers is viewed as a strategic feature of the management (Freeman et al., 2010). In the SHV model managers create a system in which the objective is not a relationship but a commodity, in particular profit evaluated by the value of shares. So, while the STV theory takes a non-utilitarian perspective where relationships with persons/groups are factored in the

decision-making process, the SHV theory hinges on a purely utilitarian approach since relationships among persons are immaterial to maximize profits (Screpanti & Zamagni, 2005; Rawls 2008).

These differences in corporate governance between banks able to develop relationships with groups and subjects and banks lacking such ability affect also credit management models. In fact, while banks applying an STV management develop relationships with different stakeholders, especially borrowers, and tend to apply a relationship banking model, where personal relationships produce soft information that are precious to screen and monitor borrowers' creditworthiness, banks that maximize SHV tend to use explicit credit contracts, evaluated on the basis of statistical analyses of risk, and often used to build collateralized contracts, via securitization. The problem of incomplete contracts and markets arises. STV-OTH banks may be more sustainable (Coco & Ferri, 2010). At one extreme, SHV-OTD banks try to optimize the present value of shares. Their model may be less sustainable as it can raise not only the asset insolvency risk – relating just to short term creditors – but also a total credit risk due to the fact that long run investors try to transform future payoffs in present income distorting the traditional role of banks that try to give long run perspective to monetary deposits (Morris & Shin, 2009).

Traditional banks use OTH having higher Net Interest Margin and lower Credit/Deposit ratios with respect to non-traditional OTD banks (Caprio et al., 2014). This means that choosing the OTH or the OTD model is not neutral vis-à-vis corporate governance. When a bank chooses OTD, this shift in the credit management model can change its corporate governance associating with a parallel STV to SHV shift even in front of statutes enshrining CSR principles. Since OTH signals that a bank is predisposed to a relationship banking model, this means also that OTH is the most appropriate credit management model for STV banks. The tendency to a correspondence between OTH and STV descends from the fact that heterogeneous stakes are guaranteed: i.e. shareholders and borrowers at least.

On the contrary, in the OTD model the only stake to be considered is that of shareholders. Maximizing shareholder value, the OTD model can worsen the asymmetric information problem in a principal-agent setup (Jensen, 2000). OTD credit management best suits shareholder value ideology. This is the feature that has been appreciated by banks moving to this method. But, at the same time, we posit that this method can't be based on STV maximization since no stakeholder – other than shareholders – benefits from the application of the OTD model. In fact, neither the interests of the borrowers, nor those of the communities or of the persons excluded from the financial system are weighed in this management model. The strict connection between STV-OTH on the one side and SHV-OTD on the other is well established and we can say that this connection may also feature reverse causality.

2.2) STV vs. SHV maximization in the management of common goods and efficiency

Economic organizations produce externalities and corporate governance models have a direct effect on how economic organizations manage their externalities. Externalities can be positive or negative. Negative externalities are social costs disrupting common goods such as, for example, savings, financial stability and the social order. The classical economic negative externalities generally relate to environmental social valuable goals that can be dealt efficiently with via STV maximization (Wood & Ross, 2006; Klassen, 1993). Positive externalities can sustain common goods such as, for example: trust, financial stability and savings. These common goods are directly affected by whether an economic organization maximizes SHV or STV. Stakeholder theory has showed that STV maximization produces good results in the process of governing externalities. The presence of stakeholders and their involvement in governance can help develop systems to manage externalities.²

In the literature common goods are characterized by positive externalities and absence of rivalry. Traditionally, common goods are managed by public institutions but due to the privatizations of the 1990s (Stiglitz & Hoff, 2005) many of them have been assigned to the market economy. However, this is not the whole story. In the present condition of economic development we have not only the State and the Corporation, something the economic literature presented at length as the State vs. Market debate, juxtaposing public enterprises and private profit-oriented corporations. Indeed, we have also economic organizations that lie in the middle and even if operating in the market are neither private, in the sense of being profit maximizers, nor public, since they are based on the association or cooperation of economic actors. These other civil economic entities generally abide by STV maximization, often applying a model of democratic stakeholders governance. We find these civil economic organizations engaged in the administration of some common goods, such as, e.g., financial stability and savings, in the banking and finance sector. These organizations are, for example, cooperative banks, savings banks, credit unions, micro-finance organizations, ethic banks. All these economic organizations are engaged in the management of common goods and at the same time are neither public, in the sense of state-owned, nor capitalistic, in the sense of profit maximization. These are economic organizations of the market economy without being organizations of capitalism (Zamagni & Bruni, 2005).

The administration of these common goods through banking and financial organizations, such as savings and financial stability, is more rational in the case of STV economic organizations than for SHV economic organizations, since only the former may overcome the problem of the Tragedy of

² Especially environmental externalities as shown in Gonzalez-Benito & Gonzalez Benito (2006), Alvarez-Gil et al. (2007), Moffat & Auer (2006), Grimble & Wellard (1997), Starik (1995).

commons. In the economic literature, especially in the English tradition of economics and political economy, the management of commons has always been a tough question for economists. How to manage common goods efficiently without disrupting them? The public economics literature has produced many classifications of goods along an imaginary line that goes from public goods to purely private goods through club-goods, reporting degrees of quasi-private or quasi public-goods on the basis of the level of positive externalities produced and the extent of non-rivalry. In the economics mainstream public goods should be managed directly by the state with purely private goods assigned to the corporation as capitalistic enterprise, and the goods in the middle assigned to meso-economic organizations based on the cooperative, association, mutual or philanthropic model. In contemporary economies, also following globalization, the number of economic organizations that can afford managing public goods has shrunk, to the less important role of the State vis-à-vis corporations. Nowadays, after the great privatization wave, economists are trying to understand which management models of economic organizations can solve the new version of the old Tragedy of commons problem. The tragedy of commons arises when in the administration of a public good no rule limits access and at the same time no economic organization is responsible for the management of the public good. In the Tragedy of commons some economic actors use the common good without limits and irresponsibly, so disrupting the good over time. Common goods are destroyed when economic agents use them maximizing their subjective utility in a non-tuism scenario.³ The pure utilitarian maximization process applied to the administration of a common good produces the disruption of the good.⁴

Financial crises are cases of Tragedy of commons.

STV model's ability to reduce negative externalities and create positive externalities is higher than in SHV since only in the former all the interests affected by managers' choices are considered in the decision-making process. The literature shows various examples of economic organizations devoted to the administration of common goods that are managed in an STV maximizing approach (Argadona, 1998; Hartman, 1996). To conclude, the STV maximizing model can solve the Tragedy of commons.⁵

In reality, also banks in some ways manage public goods such as savings and financial stability. Based on the economics literature, we posit that to the extent banks engage in managing those public goods

³ Non-tuism is a form of utilitarianism based on the absence of alterity in the definition of the economic game. In Non-tuism economic subjects maximize the relationship with goods in the absence of relationships with other economic subjects.

⁴ The disruption of the good is a "Tragedy" since it means that a resource has been destroyed by unreasonable and irrational behavior of economic actors, and at the same time without any possibility to recover the common good due to the fact that the absence of rivalry and limits in the access produce an absence of costs and prices.

⁵ But if this is considered given in the case of social valuable activities such as, e.g., hospitals (Dey et al., 2006; Gilmartin & Freeman, 2002; Brugh & Varvasovsky, 2000), schools, and similar, it is not clear whether it translates also to banks.

they would benefit from STV-orientation. Many studies show that excessive focus on maximizing profit, along the SHV model, is one of the causes of the GFC (Freeman et al., 2010). Since many public goods were damaged (savings, financial stability, trust; Akerloff & Shiller, 2009), this is a case of tragedy of commons. Public goods were impaired because banks developed an SHV maximizing model. Empirical studies show that countries in which the SHV-OTD model was hegemonic common goods such as savings, stability and confidence were damaged more, while economic systems in which the STV-OTH model was applied more extensively less likely suffered the GFC or performed better.⁶

Another debate in the literature regards the efficiency of STV-OTH vs. SHV-OTD model. Allen et al. (2009) apply a mathematical model to the question finding that stakeholder oriented firms have lower relative output but higher prices, which can lead to higher value. Others hold that maximizing the STV multi-objective function can be less competitive than maximizing the SHV single-objective function (Jensen, 2000; Sundaram & Inkpen, 2004). Many economists assume that maximizing SHV is more efficient than maximizing STV. But some studies show that STV-OTH banks can be efficient.⁷

Juxtaposing SHV to STV must be considered relating to the ability to develop an efficient management system, where the economic organization can efficiently reach its goals. So we must consider also the externalities that these models produce and their ability to develop efficiency in the economic organization. Also in the interbank market, an STV approach can be efficient. In reality, banks can prefer STV banks as interbank market partners since this can raise the incentive to monitoring, where peer monitoring improves efficiency reducing the insolvency probability (Freixas & Holthausen, 2005). To be sure, in the banking and financial sector we must consider the nexus between efficiency and risk, in the sense that efficiency in obtaining profit maximization shouldn't raise risks amplifying market failures, financial crises and bank distress. Profit maximization based on shareholder primacy increases bank failures caused by nontraditional activities, chiefly securitization (Litan, 1985; Wall, 1987; Kwast, 1989; Gallo et al., 1996; Uzun & Webb, 2007; Jiangli & Pritsker, 2008; DeYoung & Torna, 2013).

⁶ Let's exemplify on both theory and empirical evidence. First, Mehran et al. (2011) argue forcefully that banks would gain the most from governance/regulation fostering the role of non-shareholding stakeholders. As to empirical evidence, on individual bank data Beltratti & Stulz (2012) show that banks with more shareholders-friendly governance performed worse during the crisis while Lemzeri (2014) finds that diversified cooperative banking groups that retained the main features of their original model (i.e., STV orientation) contributed most to financial stability throughout European national banking systems. Also, Ferri et al. (2014b) show that STV banks, especially cooperatives, were downgraded less than SHV banks by the credit rating agencies. In turn, on country level data, by augmenting Caprio et al. (2014), Leogrande (2013) finds that countries with larger cooperative bank shares in their national banking system less likely suffered the 2008 crisis.

⁷ For instance, Ferri et al. (2013) find that STV banks, especially cooperative banks, showed no worse, and sometimes even better, performance than SHV banks before the GFC (for cooperatives, see also Birchall & Hammond Ketilson, 2009; Birchall, 2013).

This means that we must reject the hypothesis that SHV (STV) maximization is efficient (inefficient) per se in banking. The GFC of 2007-2009 shows that firms that had maximized SHV, maximizing profit realizing the Wicksteedian nontuistic utilitarian perspectives (Wicksteed, 1910) were at the core of the disruption of common goods such as savings and financial stability and at the same time were inefficient failing and being punished by the market discipline. STV-OTH model banks, applying an economics of relationships, better managed those financial public goods. In this there is now a growing literature asserting the compatibility between STV maximization and the economic performance of economic organizations (Kotter & Heskett, 1992; O'Toole, 1985; O'Toole, 1991; Kaler, 2006).

3. OTH and OTD in screening and monitoring

The economics literature highlights the existence of specific differences in screening and monitoring between the OTH and the OTD model. A banker's ability to acquire information in the OTH model is based on private information that she gets by the process of formal screening and monitoring but also on soft information gained by the implicit contracts typical of relationship banking (Boot, 2000). These hard/soft information and explicit/implicit contracts improve the banker's ability to manage risk. While complete contracts create prerequisites for market efficiency, the incompleteness of contracts creates inefficiency in the interconnectedness of markets producing market failures (Allen & Gale, 2004b).

In the OTD model the process of screening and monitoring is based on pure explicit contracts evaluated via statistical tools by credit rating/scoring. Then, commoditized credit is sold via securitization leading to off balance sheet operations and lower bank accountability. The lower accountability raises risks that credit rating certifications are unable to cover (D'Apice & Ferri, 2010). This can lead to incomplete contracts and markets. In this sense markets and the monitoring system can hinder STV maximization since managers are concentrated on shareholders (Schreuder & Ramanathan, 1984).

While in the STV-OTH model the process of screening and monitoring is coherently part of the banking activity within the relationship banking approach, in the SHV-OTD model the process of screening and that of monitoring are divided. Here banks perform only screening via credit rating/scoring, while monitoring is delegated to financial markets through the process of securitization. The fact that financial innovation lets bankers transfer risks to the insurance sector can create contagion in case of idiosyncratic shocks (Allen & Carletti, 2006). In the SHV-OTD model the bank covers the risks that can be realized on securitized credits sold to the financial market but effectively, since the credit contracts are securitized and sold to financial markets the bank loses the incentive to manage the monitoring process delegating this function to financial markets. Cerasi & Rochet (2008) show that

when banks' main activity is to monitor loans, then credit risk transfer can be optimal. Once credit contracts are sold to the market the bank is no longer able to monitor the risk of these contracts, and this questions the capital requirement and the reserves that banks following the SHV-OTD model should hold. Allen & Gale (2006) and Allen & Carletti (2006) show that the translation of risk from the credit market to the insurance sector can work if contracts are complete, but if contracts are incomplete, credit risks can lead to financial crisis and contagion can occur among different markets.

But also in the screening process there are substantial differences between STV-OTH and SHV-OTD as to the quality of information used to decide on granting the loan or not. In fact, as is common in the literature, STV-OTH (with relationship banking) and SHV-OTD (through securitization) have different abilities to acquire information about the borrower, and to manage the credit risk. In the STV-OTH traditional banks acquire information not only through statistical evaluations and formal requirements that are requested to loan applicants and are explicated in explicit contracts, but also via implicit contracts that are at work in a relationship banking model (Berger & Udell, 2006). On the contrary, in the transactional lending approach (typical of the SHV-OTD model), screening employs only hard information. De Jonghe (2010) shows that the shift from traditional to non-traditional banking activities increases the risk of crisis for banks. This deficit of information in the process of screening produces risks that are difficult to evaluate and that can create contagion transforming individual risk into systemic risk, at the heart of the GFC. In the economics literature it is clear that information may reduce risk. Reducing the riskiness of an asset means in a certain sense acquiring information about that asset, and in this sense the literature shows that the OTH model can produce more qualified information to manage risks than the OTD model. In case of incomplete contracts and information the SHV maximization produces mark-to-market accounting evaluating the level of cash or liquidity in the market rather than reflecting future payoffs. In this case price volatility can affect directly the value of banks' assets causing crisis and contagion (Allen & Carletti, 2008). So while in the OTH model, via the relationship banking approach, a banker can acquire not only formal but also soft information through which she can improve the screening and monitoring of risk, in the OTD model this soft information is not acquired and at the same time the monitoring process is outsourced to the market. Allen & Gale (2004a) show that if contracts are incomplete the risk of default and financial crisis is amplified.

Some economists have argued that the scientific nature of the credit rating/scoring in the OTH model should have been able to offer adequate guarantees to manage risks since the application of these quantitative methods applies portfolio diversification reducing risks through the securitization process. But, as showed in Freixas & Holthausen (2005), the existence of markets for derivatives on securitized

contracts such as repos, reduces the incentive to monitoring and this can lead to market failure through inefficiency. Also, some economists question that, *ceteris paribus*, portfolio diversification can develop a more sustainable structure of risk as, in the dynamics of financial contracting, portfolio diversification can create pyramidal schemes producing market failures and financial crisis (Ferri & Neuberger, 2014). The structure of contracts of the OTH model is linked to the relationship between banker and borrower. Relationship banking is a model where the banker-borrower relationship is based on implicit contracts in a long run perspective, that is a fundamental prerequisite to acquire credibility. Credibility can be used by the borrower to improve his access to credit, but to accumulate this capital the borrower must prove able to respect over time the various conditions in the credit contract. So, on the one side, a banker can acquire information about the activities of the borrower and this is an instrument to manage screening and monitoring reducing risk while, on the other side, the borrower can use this relationship to acquire credibility having access to new credit in the future or to negotiate better terms with the bankers, this means that in a game like Prisoner's Dilemma banker and borrower have incentives to cooperate. This cooperation increases financial stability preserving the efficient allocation of savings. A relevant contribution as to the importance of STV-OTH and SHV-OTD hinges on the interlink between banks and financial markets. Allen & Gale (2004a, 2004b), Diamond (1987) and Fetch (2004) show that individual investors need banks to reduce information and transaction costs for market operations, while intermediaries need markets to share risks. These multiple relations can be managed efficiently by STV maximization (Freeman, 1984). In the SHV-OTD model the fact that banks are purely on the supply side creating credit for borrowers can cause crises driven by credit booms with lower credit standards favored by banks' weak screening and lack of monitoring (Lorenzoni, 2008). If we put together these two effects, i.e., that the credit scoring produces less information than relationship banking and the fact that the monitoring process is delegated by the bank to the financial markets, we have that the level of risks with the SHV-OTD model is greater than that in the STV-OTH model due to the former model producing less information performance with respect to the latter. Being SHV or STV is important for the credibility of a bank in the interbank market too. Banks can opt to use secured or unsecured lending. Fetch & Gruner (2007) show that if there is high liquidity banks choose secured lending, in other cases they choose unsecured lending. Unsecured lending is a strategy to create more relationships among banks in the interbank market, considering other banks as stakeholders, acquiring credibility commits to bail each other in the case of individual crisis (Leitner, 2005).

3.1) Cost of credit in relationship lending and in transactional lending (credit scoring)

An important question in the literature is whether borrowers' cost of credit drop moving from STV-OTH to SHV-OTD. Skepticism on the cost-efficiency of relationship lending has arisen. Some authors argue that relationship lending raises borrowers' cost of credit as the bank gains a sort of informational capture of borrowers acquiring market power and this leads to increasing loan rates (Sharpe, 1990). But others argue that relationship lending can actually lower loan rates due to the fact that the relationship between bank and borrower lowers the information asymmetries between them (Petersen, 1999). In turn, this reduces the risk in the credit contract and, finally, also the cost of credit becomes lower.

In practice, this interpretation is controversial as different authors reach opposite results. Moreover, it seems difficult to judge relationship lending in terms of its impact on the cost of credit since there is exogeneity in the models that can depend on different market competition or regulation. Perhaps, the hypothesis of varieties of capitalism and the fact that regulation and competition vary across markets can help explain the variance in the credit cost under relationship vis-à-vis transactional lending.

Yet another factor might account for a lower cost of credit in the OTD model. In fact, in the SHV-OTD model banks are purely on the supply side. In the economic organization of these banks maximizing the level of credit lent is important, since these credit contracts are collected in pools, these pools are divided in tranches and these tranches are sold on the market, while at the same time the bank subscribes derivatives on what it sells. Thus, to perform securitization banks need to collect credit contracts, and to have more credit contracts they have an incentive to reduce borrowers' cost of credit. If this leads to an artificial reduction in the cost of credit in the SHV-OTD case vis-à-vis the STV-OTH model, the social cost of the former is higher than that of the latter. Relationship lending has important social and private positive effects by expanding relationship capital (McHale, 2006). In fact, viewing banks as institutions to overcome asymmetric information, long run relationships/cooperation can help them solve market failures as in the game theory framework (North 1990, Axelrod & Hamilton 1981).

If we view banks as firms we may consider the borrower as a customer and so relationship lending is a case of relationship marketing (Podnar & Jancic, 2006; Conway & Whitelock, 2007). Long run relationships are more effective than short run ones. Also, having multiple relationships over time is more effective than making a series of unrelated spot exchanges (Zinkhan, 2002; Murphy et al., 2005; Carrigan, 1995). So, both when we define the bank as an institution able to solve market failures and when we define it as a firm, we may conclude that relationship lending increases the value of the bank.

3.2) STV-OTH and SHV-OTD models. What kind of economic game?

The agency problem (Jensen, 2000; Jensen & Meckling, 1976) is important in the governance of banks. Since the separation of ownership and control (Berle & Means, 1932), a feature of American capitalism during the latest 50 years, the information asymmetry between shareholders (owners) and managers, was a research focus in law and economics. This is important also in the literature on banking, where information asymmetry relates especially to the problem of moral hazard. The separation of ownership and control in modern corporations produces asymmetric information that in an SHV-OTD model creates incentives to deviate from cooperative behavior producing inefficiency and market failures (North, 1990). By that deviation, players choose a non-tuistic behavior trying to maximize profits. This non-cooperative behavior rooted in the misalignment of interests between managers and owners creates risks that through moral hazard and shirking create inefficiency and can magnify market failures, making individual risks systemic. Freeman et al. (2004) highlight that a critical part of STV theory is about procedural justice while this issue, in a Rawlsian sense, is not considered in SHV maximization. In SHV-OTD the asymmetric information among managers, owners/shareholders and borrowers are magnified. In fact, shareholders can't control managers due to the separation of ownership and control (Berle & Means, 1932), and at the same time shareholders can't control the quality of borrowers. SHV maximization rhetoric puts shareholders in a condition in which effectively they are formally considered as object of the managers' choices, but effectively they can't control the production function of the bank, neither in screening, nor in monitoring. Shareholder activism should produce mechanisms for management accountability. But if managers perform off-balance sheet operations, the accountability process becomes non-representative of the real condition of the bank. The prescription of shareholder activism doesn't matter anymore, since shareholders are unable to monitor, screen and enforce managers' accountability. Thus, SHV maximization can create volatility in the stock market for shares representing the capital of the banks and induce shorttermism. The possibility for shareholders to cooperate with managers, in reality, is based on the possibility to undertake speculative behavior in the stock market. In fact, if the management under SHV-OTD produces more shareholder value in the short run the shareholders can sell shares on the market obtaining revenues for their initial investment. So the cooperation of management and shareholders is based purely on the shorttermism, managers maximize the present value of shares and shareholders sell shares on the market. Managers try to increase the present value of shares in the market and shareholders speculate on these improvements in share values through stock market operations. But at the same time if managers raise the present value of the shares in the short run, shareholders are incentivized to abandon the ownership of the bank and this means that the managers' strategy in an SHV-OTD model produces changes in the composition of

ownership and these changes are at the same time an incentive to reduce shareholder activism and a strategy to maximize the independence of management from ownership. By this way the management with the rhetoric of SHV maximization wins the game with ownership, increasing its control on the bank as corporation acquiring more freedom with respect to the accountability issue. But in this model the process of screening and monitoring can create conflicts of interests with shareholders. Jensen (2000), Marcoux (2000) and Sternberg (2000) considering the problems of SHV maximization have in mind that STV theory increases the possibility of self dealing and in this case this model shows that the true objective of managers is SHV maximization. Since in SHV-OTD screening is based on the credit scoring and monitoring is delegated to financial markets, a borrower can't interact with the bank trying to realize a cooperative behavior. In fact, also the borrower has incentives to deviate. Since the credit scoring is a statistical tool she can find ways to disguise an administrative application able to match the credit scoring requirements formally, even when she is a bad borrower. So the borrower adopts a free rider strategy and the bank can produce a riskier asset reducing the quality of the borrowing pool.

What STV theory does is to offer a solution to the problem related to the winner takes all mentality (Freeman et al., 2010). This is a direct consequence of the STV-OTH model since in it the management is not interested in creating cooperation between the bank and the borrower. This cooperation creates positive links between social and financial performance (Waddock & Graves, 1997).

In the STV-OTH model information asymmetry among managers, owners and borrowers persists, but is managed in a cooperative way. Here the strategic management of the firm works as an equilibrating mechanism (Venkataraman, 2002). It's the same STV model to solve the conflicts among stakeholders (Ansoff, 1965). These categories of stakeholders choose to cooperate and align the different interests in the economic organization of the firm. Some have argued that the interests of primary stakeholders (the shareholders) should prevail in a zero sum game on the interests of secondary stakeholders (Carson, 1993). The crucial point by which this cooperation is achieved is via the relationships among managers, owners and borrowers. These relationships are viewed crucial in the economic organization of the bank as governance tools to obtain profitability and raise the value of the bank. STV treats persons as ends (Evan & Freeman, 1988) applying the concept of interconnectedness.

The fact that relationships are diversified in the long run is a fundamental element for the longevity of markets and organizations (Beer et al., 1984). So under SHV-OTD players engage in a zero sum game where managers maximize moral hazard, shareholders maximize their positions selling shares in a shortermist view, and (some) borrowers try to obtain credit hiding information on their true economic conditions. But there are also economists who describe STV relationships as a zero sum game (Smith,

2003). The literature shows mechanisms to solve the conflicts among stakeholders in a game theory framework able to transform a zero sum into a positive sum game (Le Cardinal et al., 2001) entrusting cooperation (Den Hengst et al., 2007). STV-management can raise the cooperative behavior among the various stakeholders transforming the game structure in a cooperative and collaborative sense (Sen et al., 2006). But at the same time STV theory remains in the contract theory framework (Freeman, 1994). This means that players view the game not as zero sum but as positive sum game in which participation increases the outcome. Poindexter (1995) argues that a merit of stakeholder theory is that it considers the various constituencies. Also the STV-OTH model creates conditions for applying a concept of happiness and welfare close to that of Amartya Sen, as the STV-OTH favors flourishing by all the players – managers, shareholders and borrowers. All participants to the economic game must flourish to raise the game's output and this is the condition for the STV-OTH model. The higher cohesion under STV can be used also as a strategy against takeovers (Strudler & Orts, 1999; Sarasvathy, 2001). In the STV-OTH the relationships among economic actors are important and single stakeholders' interests directly count as managers' objectives. This relates to the idea of economic organizations as mediating institutions (Fort, 1997). STV management can also obtain the classical goal of the corporation.

4. From STV-OTH to SHV-OTD: the impact on financial stability

The shift from STV-OTH to SHV-OTD has changed the traditional role that banks have over the business cycle. Traditionally this role was producing financial stability by transforming present deposits into long run investments. The STV vs. SHV debate is important also for interbank markets. In fact, banks can view the other banks either as stakeholders (STV-OTH model), or as mere counterparts (SHV-OTD model). The behavior of banks on interbank markets can explain the turbulence during the GFC (Allen et al., 2009; Acharya et al., 2008; Heider et al., 2009; Freixas & Jorge, 2008; Freixas et al., 2009; Diamond & Rajan, 2009; Acharya et al., 2009).

Generally banks perform an important anti-cyclical role over the business cycle helping to stabilize the economy. Their fundamental role is offering long term credit contracts reducing the possibility that financial resources sustain financial bubbles. As in Bryant (1980) and Diamond & Dybvig (1983) banks perform maturity transformation, i.e. raising demand deposit and short term funds in capital markets and investing in long term assets (Allen et al., 2011). The long run perspective of the traditional banking model, related to relationship banking, subtracts financial resources to shorttermism that generally produces crisis by volatility and financial stability. Diamond & Rajan (2001) show that the long term perspective of banks, their ability to ensure that loans are repaid, creates a possible risk.

Since the first bubble buy low and sell high has been the strategy of speculators. Crises may emerge when this strategy is financed by banks. In reality, the method consists in the possibility of getting credit to acquire goods whose value is increasing for speculative reasons trying to sell at a higher price. Prices rise and investors can use credit to buy goods under speculative trends and later sell them at a higher price realizing a profit. This creates an increasing price structure. As Akerloff & Shiller (2009) explain this mechanism was applied to households in the run-up to the GFC. House prices increased disproportionately since these assets were under speculative pressure and investors could buy houses and sell them at higher prices. This mechanism raises market volatility, subsequently creates financial instability and at the end causes a crisis in the market due to the boom and bust of the financial bubble. At a certain point there aren't buyers for the asset. This mechanism is sustained by banks that support speculation, whereby financial bubbles arise naturally. The GFC, to a large extent, came from failures and weaknesses in corporate governance arrangements (Kirkpatrick, 2008). Since they try to maximize short term profits, SHV-OTD banks can raise volatility driving to financial crises. In fact, the credit scoring-based screening couldn't select borrowers effectively able to repay and also the fact that these banks are on the supply side enhanced the credit supply and speculative behavior (Lorenzoni, 2008). There are many problems of adverse selection if investors view liquidity by transforming future payoffs into present income (Eisfeldt, 2004). This is one of the fundamental causes of the GFC. Only few worried about increasing house prices in the US where SHV-OTD banks granted credit to non-qualified borrowers fueling those raising prices, creating the bubble and financial instability. The misalignment between increasing house prices, dropping cost of credit due to the supply side behavior of SHV-OTD banks, created a gap between the banks' reserves and the extent of risk causing bank failures. Also the value of securitized contracts on financial markets dove due to volatility and illiquidity, and individual risks became systemic. During the boom SHV-OTD banks maximize their present shareholder value and this heightens financial market volatility. Beltratti & Stulz (2012) show that larger banks performed worse during the crisis supporting the Small banks anomaly in the GFC (Bongini et al., 2009). But even if they become too big to fail, in the sense that governments recognize public interest in their survival, often these banks are technically bankrupt and need to be saved by governments. During financial crises SHV-OTD banks are more likely to fail or must follow non-SHV-OTD rules set by governments and even markets tend to depreciate them.⁸ For this reasons Hendry (2001a; 2001b) and Van Buren (2001), argue that STV should produce a sort of legal enforcement. Marens & Wicks

⁸ Referring to credit rating agencies, Ferri et al. (2014b) show that STV banks, especially cooperatives, were downgraded less than SHV banks while D'Apice et al. (2014) find that traditional banks were assigned better ratings through 2008-2009.

(1999) consider the corporate constituency statutes with respect to stakeholder theory, showing that the legislator has recognized the importance of stakeholders especially in antitakeover strategies.

On the contrary, STV-OTH banks tend to be anti-cyclical and sustain financial stability. Lim & Wang (2007) use an STV based view of risk management, arguing that financial hedging reduces a firm's systematic risk thus encouraging firm specific investment by stakeholders. This does not hinge on how these banks offer credit tout court but on how they manage credit cutting risk taking, by acquiring also soft information on borrowers. Basley et al. (2006) show how multiple relationships can lower risk.⁹

In reality, during booms STV-OTH banks can increase the supply of credit but as this stays in their balance sheets, and thanks to their strong screening and monitoring, they tend to smooth changes in credit supply (Ferri et al., 2014a). Overall, these banks are better placed to survive the crisis and at the same time to limit speculative behavior and financial bubbles. It is then not by chance that some economists show that cooperative banks have positive effects on financial stability (Groeneveld & de Vries, 2009) and in smoothing the macro-economic cycle. One reason why STV-OTH banks favor financial stability – contrary to SHV-OTD banks – hinges on their strategic management model. Carey et al. (2007) stress that such a risk-based approach is appropriate to deal with uncertainty. Strategies are defined as sets of rules modeling relationships between a firm and the external environment. The STV model best guarantees those relationships. Freeman et al. (2010) show how developing a strategic management relates to stakeholder theory. Since the crisis was due to moral hazard, a key thesis is the separation of business and moral (Freeman, 2000; Freeman et al., 2004; Martin & Freeman, 2004).

As Reinhart & Rogoff (2009) show, every banking crisis builds on a financial bubble. This was also the case of the GFC, created on the house price bubble. Interaction with financial markets cut the liquidity for interbank markets and this can change the level of reserve requirements and of borrowing-lending mechanisms (Bhattacharya & Gale, 1987). In fact, if the banking system lends to speculative borrowers the bubble is sustained and it can engender a macro financial crisis. For example, Washington Mutual was one of the most aggressive players to apply this model. But since that was based on increasing house prices, applying the rule buy low and sell high helping the financial bubble, when this bubble burst the bank failed. But the structure of risks that banks were taking questions the effective use of the SHV model. In fact, the bank's failure is not in the interest of the shareholders who want to maximize at an honest price and having the bank alive. So managers perverted the SHV model, applying it in a rhetoric way raising own compensations in a zero sum game based on the principal-agent model.

⁹ Some STV banks, e.g. Italian cooperative banks, have a mutualistic statutory mandate to reduce financial exclusion and via cooperative behavior, in a positive sum game, they improve equity in access to credit. But this is not true for all cooperative banks, e.g. French cooperative banks are less engaged in financial inclusion (Gloukoviezoff, 2011).

4.1) Which model can be considered strategic in banking?

The now commonly accepted definition of strategic management emerged in the mid 20th century (Freeman et al., 2010) when US Business Schools started courses in business policy (Gordon & Howell, 1959). The development of the economic environment raises the issue of adequate business policies as a discipline, hence the idea of strategic management (Schendel & Hofer, 1979). Among the forerunners, Chandler (1962) defined strategy as the determination of the basic long term goals and objectives of a firm, and the adoption of courses of action and the allocation of resources necessary to carrying out these goals. This definition features three key characteristics: i) developing long-term goals (long run perspective); ii) identifying resources and opportunities that the economic organization can use to reach its goals; iii) considering the importance of the external environment as determined by non-shareholder constituencies in relation with the firm (Learned et al., 1965; MacMillan, 1978).

The STV-OTH model has these three features. In fact, STV-OTH banks have a long-run perspective, organize their resources to obtain long run goals, and at the same time can develop long-run relationships with non-shareholder constituencies. On the contrary, SHV-OTD banks lack a strategic management model. Since they don't maximize in the long run and are concentrated on the short run, they are unable to manage their resources well, as proven by the fact that their screening and monitoring methods increase risks reducing the quality of information. The fact that, instead, the STV-OTH is a strategic model underscores the higher resilience of STV-OTH banks to the crisis. Three key differences stand out. First, the shorttermism of SHV-OTH prevents a bank from projecting for the future, maximizing its resources to obtain long term goals in a complex environment of relationships with diverse economic constituencies. The idea that banks must maximize the present value of shares puts them in a sort of «*damnatio*» where present values are all that matters. Present value maximization and shorttermism as a cognitive model for rational choice-making, destroying the possibility of projecting reactions and modifying the perceptions of risks, makes it impossible to manage resources efficiently. In an STV-OTH model instead all corporate governance relationships are long run ones stemming from the bank's long term goals. Long term relationships prevail among managers, owners, borrowers, communities, and these relationships are projected by the management strategically.

The second feature of a strategic management model is that resources be used by the banks to pursue long-term goals. SHV-OTD banks can't develop an efficient management to obtain long term goals since, as said, the structure of risks and the mechanism of building adequate capital reserves is falsified by the credit management model. By lending in a supply side model they are unable to manage risks

effectively, something STV-OTH banks can instead achieve thanks to their better ability to screen and monitor. In fact, generally STV-OTH banks have higher NIM and lower Credit Deposit ratio (Caprio et al., 2014) and respect capital ratios via a more conservative management system. STV-OTH banks take less risk even in a pure accounting sense by checking borrowers' quality. Companies that put always shareholder's short-term interests first are not likely to prosper for long (Wheeler & Sillanpaa, 1997). Third and finally, the relationships with non shareholder claimants are not strategic in SHV-OTD, as these claimants are considered neither actively nor passively by the decision maker. The cognitive process of rational choice making in the SHV-OTD contemplates no claimant other than shareholders. Quite the opposite holds for STV-OTH banks where the economic relationships with non shareholder claimants are factored in. The issue of strategic management appears vitally related to STV rather than SHV theory. The main difference between is that while STV has strategic value SHV is an operational non-strategic governance model. For these reasons SHV banks can't develop long run relationships and generally are more prone to increase risks without effective reserves, exposed to failure, unable to build relationships with non-shareholder claimants. Thus, we can conclude that the only model that has the three characteristics of a strategic model is the STV-OTH model.

5. STV-OTH and SHV-OTD: the diversity of economics organizations

These differences in banking across the STV-OTH and SHV-OTD models regard corporate governance. STV-OTH banks are generally cooperative banks, savings banks, credit unions and so on while SHV-OTD banks are commercial banks, investment banks, bank holdings. These differences are related to historical, ethno-anthropological, cultural reasons (Screpanti & Zamagni, 2005). A key field of research in economics compares different types of legal, cultural, financial, and banking systems. In reality, many differences arise in the development of economies and some authors refer to this as the Varieties of capitalism. These varieties can be an opportunity for economic systems. After the fall of the Berlin Wall when some pundits evocated «*The end of history and the last man* » (Fukuyama, 1992), others rediscovered that differences exist across market systems (Hall & Soskice 2001).

These varieties arise also for corporate governance models: as showed by Doidge et al. (2007) country characteristics explain much more of the variance in governance ratings (39% to 73%) than observable firm characteristics (4% to 22%). La Porta et al. (2002) show how legal determinants directly affect the finance-growth nexus and financial development. However, others underscore cultural, religious, ethno-anthropological determinants in explaining economic performance (Alesina et al., 2003). In general, diversity is a resource. Barth et al. (2001, 2004) show wide varieties among countries' banking

regulation. We argued that STV-OTH and SHV-OTD are very different methods of corporate governance for banks. While SHV banks are pure corporations on the supply side of credit markets, STV banks are organizations able to both obtain profits and increase social and relationship capital. It is important to preserve the diversity of corporate governance models and economic organizations since this diversity can support systems featuring a certain degree of heterogeneity that can continue to promote economic development and growth even when some models fail, as in the case of the SHV-OTD in the GFC. The fact that not all banks had moved from STV-OTH to SHV-OTD proved valuable for economic systems' stability and functionality. Thus, there are many economic reasons to defend the diversity of models in corporate governance of banks. Also, we must appreciate different qualities in the diversity of economic organizations (Michie, 2014). Commercial banks organized as SHV-OTD corporations led the economic and financial globalization of the Washington and Post-Washington Consensus operating as instruments of market fundamentalism after privatization and liberalization. This model produced many crises started from the periphery and then hitting the center. Cooperative banks, credit unions, ethics banks, following an STV-OTH model managed to survive the hegemonic SHV paradigm and the idea of economic organizations based on non-relational common goods.

6. Conclusions

We can conclude that juxtaposing STV-OTH and SHV-OTD models created diverse ways to solve the classical agency problem between shareholders and managers. We reported literature showing that the STV-OTH model can be less risky for banks' corporate governance. The higher performance of the STV-OTH model owes to its greater ability to develop systems of screening and monitoring using long term relationships, upgrading banks' information. While STV-OTH banks can develop soft information based on implicit contracts, in the SHV-OTD model only complete contracts can be endorsed. This suggests the greater sustainability of the STV-OTH model with respect to the SHV-OTD model.

The separation of ownership and control creates an agency problem between shareholders, principal, and managers, agent. The SHV-OTD model builds a zero sum game where managers have more tools to win over shareholders since they can perform more speculative business generating more risks for shareholders while raising manager compensation. Instead, the STV-OTH model solves the agency problem in a positive sum game. Here managers act in the interest of ownership in a more responsible way out of the strait jacket of maximizing present SHV. This engages banks in long-run relationships with borrowers/communities and sustains all players' flourishing life and ability to raise payoffs.

We also reported literature on the macro impact of the SHV-OTD and STV-OTH models. We argued that SHV-OTD banks are pro-cyclical boosting the expansionary phase of the business cycle, fueling financial bubbles, and when the bubbles' burst causing deeper crises due to bank failures. In this the SHV-OTD model jeopardizes macro-financial stability. Instead, STV-OTH banks favor macro stability as better screening/monitoring cut credit to speculators, dry the bubble and more likely survive crises. We also tackled STV-OTH banks' ability to favor financial inclusion and equity. This is a key point as many STV-OTH banks have mutualistic objectives by statutory mandate, achieved directly by the credit management and corporate governance model especially in cooperative and ethical banks. Instead, financial inclusion is not an objective for SHV-OTD banks that might achieve it only indirectly via CSR. Indeed, some SHV-OTD banks create philanthropic foundations (Porter & Kramer, 2002) to cut financial exclusion but the economic meaning of these organizations cannot deploy the same effects of an STV-OTH model. In fact, the non-tuistic utilitarian view of the SHV-OTD model still persists even when banks pay some philanthropic aid that may produce dependence in the receivers, rather than sustainable financial inclusion as with the long term and personal relationships of STV-OTH banks. We addressed the meaning of the two models in the subprime mortgage crisis too. In reality, the SHV-OTD model amplified speculators' access to credit and this further sustained the house price bubble. We argued that STV-OTH banks could reduce lending to speculators since their credit management and corporate governance models are based on relationship banking and on a complex system of screening and monitoring devoted to develop long-run relationships that are generally non-speculative. Finally, we underlined the importance of diversity of corporate governance models in economic organizations. Diversity in economic organizations can be due to different elements, along the literature on the Varieties of Capitalism and of economic organizations. Indeed, there are many differences across national economic systems generating differentiated capitalism and market economies. This variety applies also in the case of organizations such as banks. For banks variety was generated by legal systems, or ethno-anthropological differences or even by linguistic or religious beliefs. Diversity is a value for economic organizations since it makes economic systems more sustainable and resilient.

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