

The Challenge of Convergence, The Wisdom of Convergence

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The world is grappling with the challenges of coordinating policy – monetary and fiscal – among economically and industrially diverse nations. Some nations need additional stimulus, others need less. Some nations are more at fault, others are less so. Regardless, we are all in the global economic malaise together.

Important as the coordinative effort is, it remains a relatively short-term issue. In the longer term perspective, the pressing question is whether the world and its nations can build a stronger and more resilient global financial architecture. This deeper issue is both legal and institutional, confounded in the international setting by the question of sovereignty and individual nations' jealously held right to steer their own course. My remarks will focus on one particular issue: can, or should, nations converge to a common set of regulatory/supervisory policies and practices for the financial sector?

In a paper that I recently co-authored with two colleagues, we address this question in the bilateral context of Canada and the United States. The title, "Different Roots, Different Routes to Financial Sector Development," seems to tell the whole story. Whereas these two neighbouring new-world nations share the same continent, speak the same language and have similar legal structures, history reveals that when it comes to banking and capital markets, a number of identifiable political, institutional and cultural factors account for the dramatically different routes to financial sector development – and onward to supervision and regulation – in Canada versus the United States.

My remarks will use the stark contrast in the bilateral Canada-U.S. context to draw inference for the potential success of international efforts toward a stronger and more resilient global financial architecture. Two points will receive particular attention. The first is the difference between a "rules based" approach and a "principles based" approach to supervision and regulation and the difficulty that that conflict – rigid rules versus adaptive principles – creates for convergence. As Ralph Waldo Emerson suggested, "A foolish consistency is the hobgoblin of little minds, adored by little statesmen and philosophers and divines." The second issue, to go beyond the search for a common prescription for financial sector stability in diverse nations, is whether one regulatory/supervisory approach dominates others in regard to innovation and dynamism in banking and financial markets.

In the recent times when the rather dull Canadian banking and financial system weathered the storm much better than others, pundits remarked that in the realm of financial institutions, boring is good. However, we ought to be wary of a call to impose restrictive regulatory constraints on every nation's financial system. It is not a matter of simply constraining recklessness, but rather we need to ensure that constructive adventure in finance occurs within the perimeter of effective regulation and not in the shadows.