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James Wolfensohn

Is integrity the key ingredient in financial services?

Camunico in conversation with James Wolfensohn, is an Australian-American lawyer, investment banker and economist who served as the ninth president of the World Bank

Integrity as the key ingredient to be sought within the financial services industry.

In the UK and elsewhere, the financial services industry is in the eye of the storm. The industry probably accounts for around 9.5% of UK GDP. Yet in the wake of the financial collapse, seemingly never-ending penalties for Mis-selling and market manipulation and the continuing public outrage over bankers' compensation, many have come to believe that the industry is both rotten to its core and has become totally dissociated from the society which it is supposed to be serving.

We put this statement to Sir James Wolfensohn, former President of the World Bank. Now aged 80, retired from business and focused on setting up a top quality trans-national educational programme on development, Wolfensohn was keen to point out that he is no longer at the heart of the industry and describes himself more as a knowledgeable observer rather than someone intimately involved with shaping the industry's future. Yet he still knows personally many of the key players and, as a businessman, banker and one of the few World Bank Presidents to have served a two full terms, he was in the thick of it for many years.

Our statement was intended to stimulate a reaction. No such luck. Wolfensohn's response was calm and measured. "I think that is an over-statement," he said. "A considerable overstatement." He went on to list many of his friends and acquaintances who were devoting much of their time to setting up new investment banks and financial advisory firms that are focused on doing business ethically and on stripping out the excesses and conflicts of interest that lay at the heart of the financial services industry. "I am encouraged by how many people are focused on creating something trustworthy and on giving back to society," he continued.

That's all very well, we argued, but these boutique firms are no more than a blip in an industry still dominated by large, oligopolistic companies that seem both focused on their own interests and politically untouchable.

"There was a time when a bank reflected the ethics and personality of the person – or the few people – at the top," said Wolfensohn. "But these firms have become so large, so complex and so widely spread that it is now a much more difficult task to achieve that."

Short of breaking up these behemoths, as the UK Labour Party has vowed to do, that may not bode very well for achieving a change in culture. But surely signals from the top still matter. Barclays has recently announced a 10% increase in its bonus pool despite a 32% fall in profits. JP Morgan Chase CEO Jamie Dimon is awarded, as the New York Times puts it, '$20 million — a 74 percent raise — for 2013, a year in which JPMorgan narrowly escaped a criminal guilty plea and paid more than $20 billion in regulatory fines and penalties?'

Commenting on these pay awards generates different perspectives. Nils Pratley in the Guardian puts it like this "he [Jenkins – Barclays' CEO] is powerless to resist the annual bonus-grab. Pay for performance? Go-To hell, his bankers replied." Commenting on the Dimon case, Professor Larcker, from Stanford University said. "His incentives are aligned with shareholders. There's risk imposed on him. That's called pay for performance, and it's a good thing." Yes. But only if one believes that shareholder value is the only measure of performance while things like operating within the law don't matter at all in assessing performance.

What does this tell us about banking culture and supposed "pay for performance?" "I'm not sure what all this says about the industry but it possibly says something about the Boards of these companies" according to Wolfensohn. "But, at an industry level, we should maybe look beyond compensation," he continued. "We should look at the people who are being appointed to crucial positions world-wide. Central bankers and other regulators.

The people who are being chosen for these positions are not people who have shown themselves to have been able to make a lot of money for shareholders. They are people who are both tough – they have to be in a tough industry – and of high integrity. They have shown the willingness and the ability to take on unacceptable practices and hold firms to account."

We suggested that some may disagree and feel that regulatory and political capture by the industry is almost total and that all attempts at meaningful regulation have been significantly watered down. "Isn't it just an old boys' club where the same people circulate between the banks and the regulators?" we asked.

"Things are not as black and white as you paint them. Look at Ben Bernanke. He's an academic not a banker. He steered the US economy though one of the most difficult phases, forced banks to restore their balance sheets and was instrumental in pushing forward risk reduction strategies. These are important achievements which the Europeans, for instance, have not yet been able to take on."

But what of this question of "integrity" that Wolfensohn brought up? Do we know what that means or is it a matter of interpretation?
Europe is now faced with the situation where the German Constitutional Court has ruled the ECB's Outright Monetary Transaction programme as being incompatible with Germany's primary law. The programme was declared ultra vires and in violation of EU treaties. What does this say about "integrity"? Was the ECB – the top Eurozone financial authority – acting with integrity when Mario Draghi promised to do "whatever it takes" to save the Euro? Was this a courageous and effective move or does "whatever it takes" mean what it says far too literally? The German court finds the purchase of sovereign bonds in the secondary market simply to be a "circumvention" of the explicit legal prohibition against state financing. So is this simply a banker behaving true to form and continuing to reinforce a culture that believes that there is no rule that clever people cannot find their way around to achieve their ultimate aims?

Maybe Wolfensohn is right. We should broaden our focus from rules, regulations and technical competencies and focus much more on this difficult to define question of integrity.

In a financial services industry – and its regulatory structure – that is so central to our society and people's well being, do we have people at the top who have a clear sense of purpose and societal responsibility not only with regards to the aims but also with regards to the means? Can we shake off a perspective of aims that are too narrow and the utilitarian culture that the ends justify any means – whatever it takes? For the sake of all of us who depend on this economic structure, let's hope we can move in that direction and that Wolfensohn's faith in good people with the courage and ability to do good things turns out to be right.

James Wolfensohn was talking to
Joe Zammit-Lucia and
Ron Soonieus of Camunico

This conversation was published in the Huffington Post