From Captain Mainwaring to Gordon Gekko:
Why Bankers need to be a law unto themselves

What do you think of when you think of a banker? For a generation growing up in the 1970s, it was Captain Mainwaring, portrayed by Arthur Lowe in the sitcom *Dad's Army*.[1] In the 1980s, it was the corporate raider Gordon Gekko, played by Michael Douglas in the film *Wall Street*.

Gekko was a powerful role model. A generation of highly paid, mostly white, males grew up admiring Gekko's ruthlessness, his lack of hypocrisy about his motives, and, perhaps above all, the money he made. Film-maker Oliver Stone intended Gekko to be an indictment of the traders on the financial markets who saw themselves as "the Masters of the Universe". Instead, he became the poster boy for the lifestyle and the rewards to which so many talented people became fatally attracted. In a speech on 8 October 2008, Australian Prime Minister Kevin Rudd described the bankers who caused the global financial crisis as the "the 21st century children of Gordon Gekko".[2]

A key reason why Gekko was so compelling was because his slogan, "Greed … is good"[3], was a memorable summary of the teaching of neo-liberal economics. The idea was not a new one. In 1714, Bernard Mandeville had proposed in his *Fable of the Bees: or Private Vices, Publick Benefits*, the idea that invisible hand of the market meant that "private ethics do not matter, anything that happens, be it moral or amoral, contributes to the general welfare", and in fact, "the more vices there were, the more material well-being there could be."[4] What was new was not the philosophy of a need for greed, what was new was its cultural dominance.

Educating for selfishness

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[1] The original series of *Dad's Army* were broadcast by the BBC from 1968 to 1977 and have been repeated ever since.

[2] http://www.theaustralian.news.com.au/story/0,25197,24450662-7583,00.html

[3] The actual line in the film is "Greed, for lack of a better word, is good".

[4] Sedlacek, 183.

This cultural dominance was achieved by the power of education and example. The power of education came from the Chicago School of Economics. This School took its cue from an idea of the 18th century moral philosopher, Adam Smith, who famously said, in *The Wealth of Nations*, that "*It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest."* The Chicago School argued that this meant that the invisible hand of the market will deliver outcomes that are good for most people most of the time even if some people are acting selfishly and disregarding the interests of others. Eugene Fama, developed the efficient market hypothesis according to which market forces could safely be left to produce the most efficient outcome.[5] Milton Friedman taught that business managers' only social responsibility was to make as much money for their shareholders as possible. Generation of short-term profit, regardless of the interests of customers, became the key objective for banks and other big businesses. What Joseph Stiglitz calls the religion of market fundamentalism was lauded,[6] but its legacy was a disaster. The Chicago School ignored, with devastating consequences, that Smith's understanding of self-interest was very different from the selfishness which Mandeville praised as economically efficient and the concentration on short-term profit which was the result of Friedman's teachings.

Changed culture

Banks changed from sleepy, prudent institutions into money-making machines obsessed with short-term gains. The break with the past was symbolised in new corporate headquarters. The new motto was: let's make a profit at all costs and by all means. A striking feature of the defences of their actions mounted by Tom Hayes (convicted for manipulating LIBOR), Kweku Adoboli (whose fraudulent trading cost UBS £1.4 billion) and Jerome Kerviel (whose fraudulent trading lost Société Générale 4.9 billion euros) was their insistence that their bosses knew what they were doing, and tacitly approved it so long as they seemed to be making money, regardless of whether they were breaking the rules. Pay, promotion and prestige were all dependent on their performance in making money, at all costs.

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[5] Longley, 25.

[6] Stiglitz, 134.

This change to a culture where sales were the overriding imperative and it did not matter whether or not the products sold were in the customers' interests has been identified in numerous studies produced after the start of the great financial crisis. In his independent review of Barclays business practices, Anthony Salz laid many of the central failings of Barclays bank in the run-up to the LIBOR scandal on its internal culture: "despite some attempts to establish Group-wide values, the culture that emerged tended to favour transactions over relationships, the short term over sustainability, and financial over other business purposes."[7] McCabe[8] and Kerr and Robinson[9] identified how different banks stopped seeing their branches as bases from which financial services were provided and considered them to be sales outlets instead. Staff were transformed from professional advisors embedded in the community into salespeople with targets to meet. New City Agenda and Cass Business School's 'A Report on the Culture of British Retail Banking'[10] summarises the research as showing that a widespread and aggressive sale culture was one of the central reasons for the numerous failures of banking in the UK between 2007 and 2014 – problems that were particularly prevalent in the biggest banks.

Changed self-image

The Chicago School of Economics offered a model for 'normal' human behaviour and popular culture provided, in Gordon Gekko, an exemplar for the successful banker to copy. The result has been, as other parts of Adam Smith's theory had predicted, a significant change in the behaviour of market participants 'guided by market values, … market values [which have become] are quite different in character from the moral values that are supposed to guide the behaviour of people as members of society.'[11]

In an age of fragile personal relationships, in which a popular expression talks of middle-aged men "trading in" their wives for a younger model, the model human being (*homo economicus*) imagined by economics was an isolated, materialist individual,

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[7] Salz, 2.13.

[8] McCabe, 1551 – 1579.

[9] Kerr & Robinson, 247 – 266.

[10] http://newcityagenda.co.uk/wp-content/uploads/2014/11/Online-version.pdf

[11] Soros.

with no social or moral connections. Such a man was meant to be a description of human nature as it is, on average, having smoothed out the extremes of heroism and malice. In fact, *homo economicus* became a justification for those who chose to live self-centred lives, if necessary at others' expense.

Knights and Tullberg (2011)[12] studied financial services in the UK and Sweden and found that the banking crisis arose partly because of a narrative of the 'masculine autonomous self' – the notion of the self-interested, self-sustaining individual, which led to "poor ethical standards stemmed from the conditioning of individuals to not recognize their social interdependence". Captain Mainwaring served his community, whether behind his desk at the bank or when organising the Home Guard. Gordon Gekko lived for himself, both in the office and away from it.

Changed behaviour

The result of the Chicago School's teachings,[13] the changed culture in banks, and the self-image of the successful banker manifested itself in a variety of harmful behaviour. Three examples will suffice: banks routinely sold Payment Protection Insurance (PPI) to customers who did not need it, who were not told its true cost, were not given the opportunity to shop around for cheaper alternatives, and who, in some instances did not even know that they had been charged for it. All of this was clearly contrary to pages of detailed rules set out in the Financial Services Handbook yet it happened on an industrial scale.

Equally staggering was the sale of Interest Rate Hedging Products (IRHPs) such as Swaps to small businesses. The scale of the non-compliance with the law was such that it deserves to become a textbook example of how all the significant players in a major industry can defy the rules to which they are supposedly subject. In 2012, the banking regulator concluded that the banks had failed to meet the regulatory standards applicable to the sale of IRHPs in over 90% of cases.[14] A Redress Scheme was

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[12] Knights & Tullberg, 385 – 404.

[13] Poole.

[14] Financial Services Authority, 5.

established which dealt with 17,000 claims[15] and provided some degree of compensation in 14,000 cases.[16] The long term profile of the IRHPs and the costs of cancelling the IRHPs early were such that they were, in almost all cases, unsuitable for the customers to whom they were sold. In selling IRHPs, banks were not treating their clients as customers to be served but as unsuspecting counterparties to be taken advantage of.

The third example is the manipulation of LIBOR. Traders, sometimes colluding between different banks, provided false data so that they could make profits by distorting the level at which a supposedly independent benchmark was set.[17]

There were a few commentators who saw the trend before the crisis happened. As early as 2002, Professor Alistair Alcock criticised the increasing emphasis on rules as meaning that whereas in the 1980s people in the financial services sector asked themselves whether what they were doing was right, in the 1990s they asked themselves whether what they were doing was within the rules.[18] In the 2000s, the banks stopped caring about whether what they were doing was within the rules.

In one of the most telling exchanges, Bob Diamond, the CEO of Barclays, was unable to name any of the three founding principles of the Quakers who set up Barclays, when asked to do so by John Mann MP in 2012. Honesty, integrity and plain dealing all seemed to have become wholly alien to the culture of the banks in the run up to the great financial crisis.[19]

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[15] Controversially, the scheme excluded a further 23,000 claims because of the size of the business involved and another 60,000 claims relating to fixed rate loans which had the same economic effect as IRHPs.

[16] Financial Conduct Authority.

[17] McIlroy, 'What effect does regulation have on the culture of banks?', 65-87.

[18] Alcock.

[19] These three virtues are listed in Robert Barclay's 1678 book, *An Apology for the True Christian Divinity*. Books on how the Quakers did business include David Burns Windsor, *The Quaker Enterprise: Friends in Business* and James Walvin, *The Quakers: Money and Morals*. Kenneth Hopper and William Hopper in *The Puritan Gift: Reclaiming the American Dream Amidst Global Financial Chaos*, suggest how those virtues could once again transform the way in which business is done.

Once honesty, integrity, and fair dealing ceased to be valued by the banks, they also ignored the detailed rules whenever it suited them to do so. Bad behaviour became endemic in the banking sector. It was frontline staff who mis-sold PPI. It was the investment bankers who sold IRHPs. It was the traders who manipulated LIBOR. The sales of PPI and IRHPs were carried out in accordance with directions from senior managers, who set sales targets for such products without regard to whether customers would benefit from them or not. The manipulation of LIBOR led to large profits for the banks, and either managers turned a blind eye to the practices or they actively colluded in them.[20]

Technical regulation

Where were the law-makers while all of this was happening? They too were seduced by the Chicago School of Economics. Politicians had delegated the responsibility for making and enforcing the rules to regulators. The regulators saw banking as a technology, and were busy drawing up technical rules, to keep the markets working. The ancient Greeks told a story about Sisyphus, condemned to spend eternity trying to roll a stone up a hill. Such was the regulators' task, as they tried to keep pace with technological changes and financial innovations. As financial products and services became ever more complex, so the laws regulating them grew and grew. The result was that neither the bankers nor the regulators themselves could see the wood for the trees. Like those who Jesus condemned for focussing on the detailed rules but failing to have regard for their overall purpose, they ended up "straining a gnat and swallowing a camel" (Matthew 23:24).

The moment of truth

Whereas before the credit crisis, the efficient market hypothesis and the belief that the financial markets were a-moral was taken for granted, there is now a widespread acceptance that both theses were unsound.[21]

With a touch of hyperbole, Will Hutton, British economic and political commentator,

[20] See FSA Final Notice to Barclays Bank plc, 12-14.

[21] Turner.

declared that "the dominant intellectual ideology of the last 20 years, free market fundamentalism, and the way it was applied in the financial markets, the efficient market hypothesis, was the biggest intellectual mistake this generation has ever witnessed, arguably the world has ever witnessed."

The great financial crisis has revealed once again that markets are dependent on, sustained by and shaped by, the existence of social attitudes, accepted standards of behaviour by market participants, and the enforcement of laws which reinforce those attitudes and behaviours. Jeffrey Sachs wrote in the *Financial Times* on 18 January 2012, a column entitled "Self-interest, without morals, leads to capitalism's self-destruction".

The last 30 years has been an experiment in attempting to control a business sector by focussing on laws and neglecting questions of character and culture. The experiment has been a comprehensive failure. Gordon Gekko was a compelling character, the embodiment of an ideal. It will not be enough to legislate to make his activities illegal or to make his pay subject to approval by the bank's shareholders. What is needed are alternative heroes[22] and institutional cultures which remember them, which nurture them and which promote them.

The ineffectiveness of laws without reinforcement from culture and example should not have been a surprise. The Christian reading of the Old Testament from Exodus to Jeremiah and Ezekiel is that good laws do not, by themselves, make people good.[23] While external standards are necessary in order to make clear the basic expectations people living in society should have of one another, right behaviour has to be internalised if it is to be consistently lived out. This was Jesus' message too. Whereas *Torah* observance focussed on external purity, Jesus made it clear that it was not what was on the outside that made a man pure, but rather what was in his heart[24]. Likewise,

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[22] Though, here too, we need to be careful not to replicate the myth of the self-made man, the rugged individualist, who is a solo success. We need instead to celebrate communities whose shared values and collaboration lead to sustained achievements.

[23] McIlroy, *A Biblical View of Law and Justice*, chapter 7.

[24] Matthew 15:11, 16-20.

the Apostle Paul "expresses extreme skepticism about the ability of an external law-code to control human wrongdoing".[25]

Rev. Stephen Green, formerly Chairman of HSBC, has rightly pointed out that 'regulation and legislation 'are not and cannot be, sufficient without a culture of values', not only for individuals but also for the 'institutions of capitalism – businesses, banks and other institutions of the financial markets'.[26] The urgent question, to which far too few concrete answers have been offered, is how can such a culture of values be rebuilt once it has been lost. The antidote to the banking scandals we have witnessed lies in four "E"s: Education, Empathy, Example and Enforcement.

Education

Thomas Aquinas said that 'the common good of a political community can be rightly disposed only if its citizens, at least those to whom its ruling belongs, are virtuous.'[27] Virtues have to be taught. The financial services regulator (the FSA at the time) in the early 2000s got rid of their training and competence unit. That sent a signal that the regulators were no longer interested in these areas; that was a very bad signal to send to the financial institutions. The Senior Managers Regime introduced on 7 March 2016 does now pay some attention to the attitudes of those at the top of banks and to the culture which they promote but nowhere near enough. The virtues required of bankers need to be taught in Universities, in induction and training courses at banks and repeated following each promotion. What is needed is a new education for business leaders and management consultants, one which recognises that issues of character are key for those who will be in future leadership positions in banks and other large companies.

Empathy

Adam Smith saw self-interest very differently from neo-liberal economists. Smith drew a sharp distinction between greed and selfishness on the one hand, and prudent and

[25] Marshall, 11.

[26] Green, 132.

[27] Aquinas, *Summa Theologiae* I-II.92.1 ad.3.

virtuous self-interest on the other.[28] Smith saw that our self-interest includes concern for others. We are capable of moral actions, and impelled by our self-interest towards them because of our capacity to sympathise with each other. Smith taught that to the extent that we allow our capacity for sympathy and our desire for friendship to inform our understanding of our self-interest, we grow in wisdom and learn to control our selfishness and greed.

Finance should be understood as a service industry, one whose value lies in the services it provides to companies, individuals and public institutions. This means that the primary focus of banks ought to be on the quality of the service provided, in the interest of its customers and counterparties. It is from the provision of good quality services which are in the customers' and counterparties' best interests that the profits of the banks should flow.

This is particularly important because many of those with whom banks deal do not have access to any alternative sources of information and advice about the bank's products.

Example

It matters whether those who behave like Gordon Gekko are lauded or shunned by their peers. As Adam Smith knew and spoke about at length in his *Theory of Moral Sentiments*, the behaviour of market participants is determined by how they think their peers will view their actions. Smith was on to something important when he highlighted that our self-interest includes a strong desire for approbation or esteem. This is a powerful factor in the construction of popular morality and other social conventions: we behave in certain ways because we believe that our actions will be approved of by those whose opinion we value. The vast earnings, the working hours, and the lifestyle of the superstar traders all placed them within a bubble, isolated from any commentary on their actions other than from their peers. Senior bankers and successful traders became their own club, playing by their own rules.

[28] Wight, *Adam Smith and Greed*, 46-58.

The importance of this factor explains a lot of what has gone wrong in the last 30 years. What is striking about the scandal of the manipulation of LIBOR is how brazen and open with one another the traders were about their actions. As Paul Downes QC puts it: "It is clear that from at least 2005, there was a cultural acceptance that LIBOR was simply a variable, to be managed just like any other variable, to maximise the returns being generated by individual traders, for their own personal financial benefit, and to bolster the banks' trading revenue."[29] Requests within banks, and between banks, to manipulate the LIBOR rate became routine. It was not uncommon for a trader at one bank to act in collusion with his counterpart at another bank. They were part of the same club where successfully rigging the rules of the game was a sign of skill. The fact that it was cheating was either lost on the participants or else did not matter.

Moreover, in the run up to the great financial crisis, before the manipulations and deceptions became evident, the bankers received applause for their apparent successes (the knighthood given to Fred Goodwin, the boss of RBS who, in retrospect, ruined one of Britain's oldest financial institutions is, perhaps, the starkest example).

Barclays' decision in 2016 to oust Chief Executive Antony Jenkins, who was trying to reform the size and approach taken by Barclays' investment banking division, sent a powerful message that the banking sector was not serious about reforming itself. The tone that is set at the top of a bank is a signal to the lower levels of the bank about what the Bank really values, and how much of a price it is prepared to pay to live up to its rhetoric.

Enforcement

Regulation alone is insufficient – it is easily circumvented. And even when it is not a case of exploiting a loophole but of flagrant violation of the rules, Richard Samuel makes the obvious point that "the [banking] regulator cannot be expected to see everything or act on everything".[30]

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[29] Downes, 83-85.

[30] Samuel, 2.

That is why it is key that banks themselves enforce high standards upon their staff. If those who cheat their customers are dismissed, and those who build long-term relationships are promoted, then others will copy their example. There is, perhaps, a place for a return to something like the Banking Code, a short statement of fundamental rules of fair dealing, agreed by the banks themselves, applied in the first instance by the industry, but then subject to an appeal to a body representing the public interest.

But in the end, bankers need to be people who do the right thing even when no-one else is looking.[31] The ethical person is a law unto themselves, they act justly not because they are following a rule for fear of a sanction but because they have internalised the fact that acting justly is the right thing to do.

Conclusion

Laws alone will not prevent harmful behaviour in the financial sector, or any other for that matter. Wrongful actions became endemic in banks because of dangerous ideas which led to irresponsibility, because of a culture which pursued short-term profit regardless of the risks and costs, and because the heroes who were applauded were those who were greedy and selfish. Re-building trust in banking will require education which places character at the heart of leadership and actions, a return to the idea that banks are there to serve their customers and to provide them with financial products which benefit them, structures of reward and promotion which do more than measure short-term profit-making, and institutions which are committed to policing their own values rather than focussing on ticking the boxes or pulling the wool over the regulators' eyes.

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