Reforming Global Finance One Banker at a Time

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Introduction

The title of our panel, "Can ethical questions raised by the churches help the international decision process on financial reform?", presumes an exclusively architectural or policy-driven solution to the world's financial problems. I have two principal concerns with this approach.

First and most importantly, the Churches have a direct role to play in the reform of global finance, one not mediated by policy makers. Accordingly, I propose a different question: "Can ethical questions raised by the churches bring financial reform?" The answer to this question is a resounding yes. In fact, raising ethical questions that will truly drive global Financial Reform is something which, perhaps, only the Catholic Church can do.

Second and more controversially, efforts to restructure global finance absent a change in the hearts and minds of financial professionals will likely aggravate the effect of technology and make finance less, rather than more, human. In recent decades, there are many examples of regulation and technology conspiring to dehumanize of finance.

Calling Financial Professionals

Through the Catholic Finance Association, I have had an opportunity to discuss *Caritas in Veritate* with a number of New York City financial professionals. Despite the extraordinary openness to the Church's teaching on finance at a time when secular voices have been largely discredited, *Caritas in Veritate* has not yet sparked a robust discussion in New York City's financial community. Moreover, to the extent that the encyclical was read and discussed in New York City's financial community, *Caritas in Veritate* was overwhelmingly interpreted in political or policy terms.

The reaction in New York City thus far is disappointing because the meaningful reform of global finance will require the active participation of financial professionals, for it is not possible to craft a financial system that will produce just outcomes without the knowing participation of financial professionals themselves. In fact, a financial system that attempts to transform selfish interest into the common good without the conscious collaboration of financial professionals risk the further dehumanization of finance.

Technology and Regulation: The Banker's Perspective

Over the past four decades, banks have used technology to radially concentrate their decision making processes. The extent of this concentration can be clearly seen through a simple analysis of a local bank branch. It used to be that your local bank branch manager was a person of great economic importance in the community. He had standing. He made credit decisions. Maybe his credit decisions were unfair at times, but the underwriting process was essentially human.

Today, by contrast, bank branch managers are in charge of local marketing rather than local underwriting. The core functions of commercial banking have been fragmented. The branch manager advertises the branch's services, gathers deposits and encourages cross-selling of financial products. He may even have responsibility for operating expense management and local hiring, but rarely does he control the key function of the bank, *i.e.,* underwriting.

The central aspect of banking, the credit decision, has been stripped away from the branch. In the instance of corporate loans, the underwriting process has been concentrated in regional offices or even the head office, making it less likely that the loan underwriter will have a personal relationship or community connections with the borrower. In the case of individual loans, the process has been even more radically altered by technology.

In the developed world, the decision to extend credit to a particular person is far more likely to be made by an algorithm than a human being. The amount that a person can borrow against his home or on his credit card is, by and large, not a discretionary decision being made by a banker. Instead, this decision-making process is generally computer driven. This extreme automation, which makes dealing with banks so frustrating, not only dehumanizes the customer, it also dehumanizes the bank employee administering the process. The prevailing mechanism for individual credit extension effectively turns bank employees into execution machines incapable of making the most important decisions about their own business activity.

The extent of automation within today's banks is not constrained to the underwriting process alone. For example, during a recent trip to Poland, I had an opportunity to observe a bank using the latest in statistically driven debt collection technology. While the collection process involves two humans speaking on the phone, one side of the conversation is almost entirely scripted with the collection strategy actually determined by a computer model rather than a human being. The telephone collection process, in this instance at least, is essentially dehumanized while retaining only the veneer of human interaction.

Importantly, the ever increasing number of rules and procedures embedded into bank operating systems tend to aggravate rather than correct technology's dehumanizing force in the banking sector. The Dodd-Frank financial reform act, for instance, when fully implemented will add an estimated 30,000 pages to the rulebook governing American financial firms. While these rules will only be read by a handful of banking professionals, to assure compliance, they will be imbedded into banking technology platforms. They will be translated into computer prompts and applied with uniformity so as to avoid regulatory discipline. Such detailed and specific rules are only imaginable in a highly technology-driven environment. In this way, technology and regulation have been pulling banking in the same dehumanizing direction.

Technology and Regulation: The Investment Professional's Perspective

Technology-driven investing calls to mind the black-box trading programs that dominate the developed world's stock market activity and literally make billions of investment decisions every day without the direct involvement of a person. But, it would be a mistake to see the dehumanization of investing as identical to the dehumanization of banking. For much of the dehumanization of investing has occurred independent of recent advances in technology. Take indexing for example. Trillions of dollars are indexed, allocated according to an approximation of a market rather than at

the discretion of a person, in the name of efficiency. The rapid growth in indexing, however, has not been dependent upon technological advances.

The increasingly systematized modern money management industry can be accurately described as a rejection of the Church's teaching that all economic activity be moral activity. With scant exception, monies are allocated across asset classes and markets with the sole intention of generating a return for the investor. The notion of willfully supporting a particular business or type of economic activity is not common. Furthermore, to the extent that ethics are brought to bear on the investment process, they are almost invariably the ethics of avoidance. While attempts to wash one's hands of harmful investment activity are vastly superior to amoral investing, they clearly stop short of a complete understanding of investing as essentially a moral activity.

With respect to regulatory-driven reform of the investment industry, it should be noted that regulation is reinforcing the systemization and dehumanization of investing. Take the American regulation "Fair Disclosure" for instance. This rule promulgated by the Securities Exchange Commission in August 2000 mandates that public companies provide identical information to all investors at all times. While noble in theory, in practice this regulation has impaired professional fund managers' ability to engage with the managements of publicly traded companies in America. With the personal interaction of investors and managers mandated by regulation to be either public or inconsequential, the value of human participation in the investment process has been reduced. In short, the desire to make everyone absolutely equal has made the investment process far more impersonal.

Conclusion

There is growing evidence that the centralization and automation of underwriting and investing produces inferior outcomes as compared to models of more distributed decision making. Furthermore, distributed decision making requires levels of trust incompatible with the narrowly defined pursuit of profit. Accordingly, the world's financial system and its financial professionals remain open to the Church's call for a more ethically driven financial system. But, Catholic financial professionals need to be clearly called to lead more integrated lives. Absent a call from Mother Church, their bishop, parish priest, or a peer, too many will continue to live the compartmentalized lives to which they have become accustomed.