

Not just politics....

- Regulators had the powers and the evidence, did not act
- Why not? Perhaps 'home field advantage'
- To prevent recurrences, need instant replay for regulators

Clear Warning Signs

- Destruction of information, skewed incentives (Ninja loans, leverage, record growth, pay levels, etc)
- Housing bubbles (US, Ireland, Spain, etc)
- Regulatory abdication across countries...including those in continental Europe

Were the Irish unlucky victims of the U.S. collapse?

We don't think so.

And they don't either: "the crisis was entirely homegrown."

Patrick Honohan,
Governor of the Central Bank of Ireland

Irish crisis was not unforeseeable

The root causes were:

"a regulatory approach which was and was perceived to be excessively deferential and accommodating ... " an unwillingness by the (regulator) to ... "rock the boat" or "spoil the party" ...

Governor Patrick Honohan
Central Bank of Ireland

Regulatory Bias Seems to Continue

- Regulators missed the Whale (not even close)
- Bank of Spain and audit allegations
- Standard Charter/Iran – federal regulators deferred
- **LIBOR lies** – "Through all of my experience, what I never contemplated was that there were bankers who would purposely misrepresent facts to banking authorities," Alan Greenspan.

Why is there a home team advantage?



Is it human nature?

Officials are not necessarily corrupt, but human, and sub-consciously please the home crowd.

- Officials do not *reluctantly* change their *stated* views
- They *genuinely* adopt the crowd's view
- Conformity changes their *actual* perceptions

The financial services industry has the home field advantage.

Lessons from sports

Electronic monitoring of balls and strikes, the challenge flag, and instant replay.

Reduce bias ... ex ante!!



How can we fix the system?

The public needs an informed, expert, & independent assessment of regulation. We need...

- Accountability
- Reduce importance of revolving door, political influence
- Avoid the comforting allure of simplistic ideologies
- Permit an informed debate
- Reduce bias

