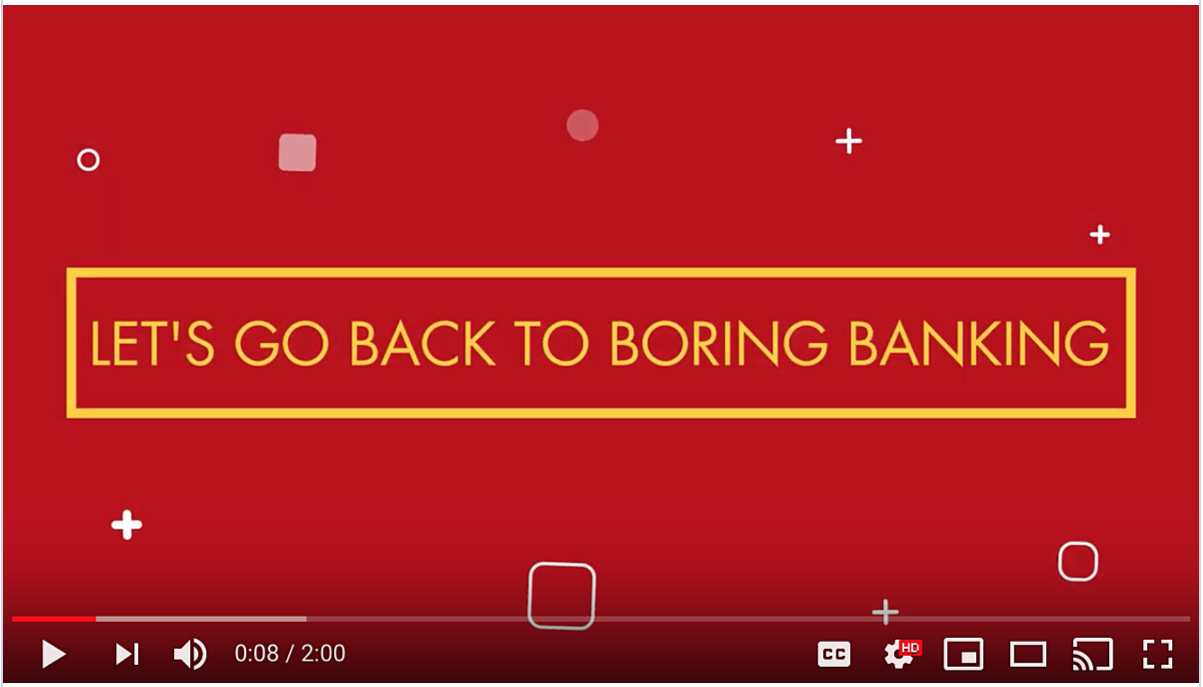
RGM NEWSLETTER

RITA GUNTHER | MCGRATH

Let's Go Back to Boring Banking

April 2019



Dear colleagues,

When even Larry Fink is talking about too much short-termism in our economic lives, you know something important is going on—perhaps an inflection point in the making. A lot of what ails us economically, many smart people say, can be sourced directly to the unwinding of rules that kept the financial sector more or less contained.

How we got here: An end to boring banking and the growth of the financial sector

From the New Deal era right through the Reagan era, banking was boring. Banks were prohibited from many of today's creative financial engineering practices. Bankers, of course, hated that. Aided by a deregulatory ideology and abetted by their political clout, they persuaded policymakers on both sides of the aisle to lift many of the limits the sector operated under, including the repeal of limitations on using government-backed savings to engage in speculative investment, such as Glass-Steagall.

The financial sector made up 3-4% of Gross Domestic Product from the 1940s to the 1970s. It's above 7% today, with some arguing it's as high as 9%. In the era of boring banking, a researcher found that in 1978 the average salary of a worker in the financial sector was $48,300, compared to the average full-time worker salary of $48,100. Stunningly, a recent report found that the average salary of a worker on Wall Street was $422,500. Median household income in the US? $61,372.

Scholars have pointed out that unintentionally, too large a finance sector funnels investment into existing assets, such as housing, and starves productive investment in innovation. Even as efficiency in virtually every other sector has increased, the cost of financial intermediation has ballooned over the decades, from 5% in 1980 to 9% in 2010. As economist Thomas Philippon argues, the benefits of economic growth have flowed disproportionately to the financial sector and to the investing class, which has creatively found new ways to make money by moving money around.

Strangling growth and other unintended consequences

While entire books have been written on this topic, it is worth highlighting a few other consequences. The first is that the bulk of activity in the banking sector isn't funding productive growth. According to research done by Oscar Jorda, Alan Taylor, and Moritz Schularick, only 15% of the money sloshing around the financial industry is funding new investment in productive assets, which is important for innovation.

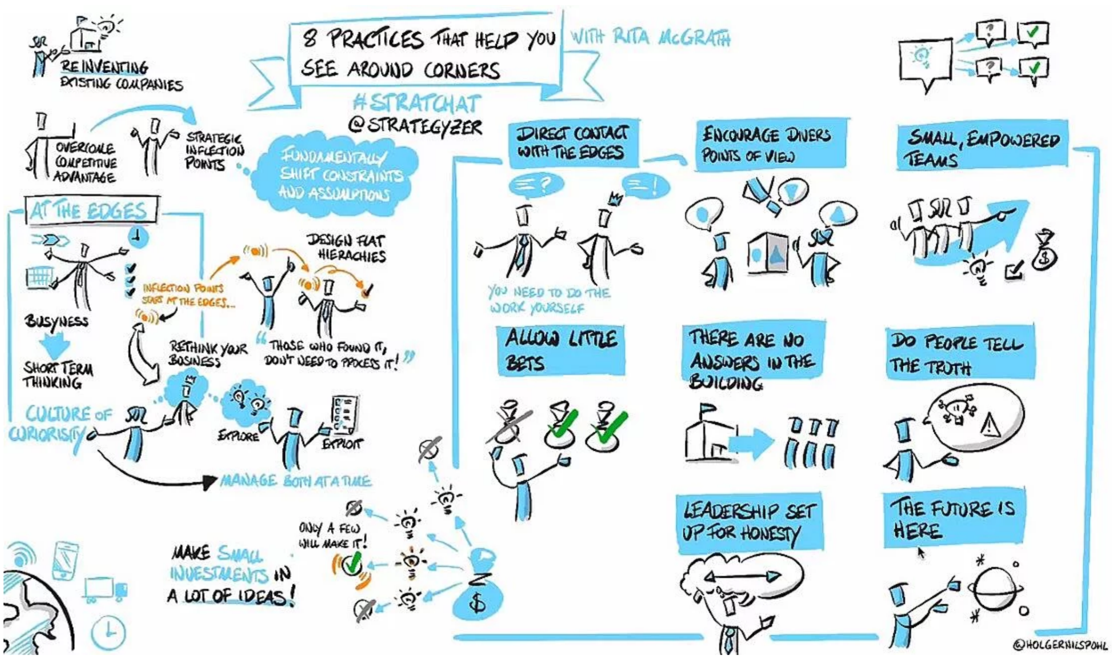
Financialization has been linked to a decline in new business formation, as a financial sector more interested in short-term speculation doesn't provide conventional access to capital for small businesses. It's been linked to "profits without prosperity" as mechanisms such as stock buybacks allow profits to be distributed to executives and investors, without increasing the share of those profits that go to workers. The economist William Lazonick points out that companies are not investing in innovation, but are rewarding executives and shareholders, extracting value from previous investments in building capabilities in ways that do not benefit the other stakeholders.

What is to be done?

If we want to bring back a historically appropriate balance between the financial economy and the "real" economy, there are a few policy changes that could be a start. We could change the way buybacks are regulated, and Congress has started to show some interest. We could require that companies put workers' representatives on their boards, as is common in European countries. We could use some of the funds currently going into buybacks to increase worker pay. We could take a page out of Costco's book and recognize that providing good jobs can actually help everybody.

I'm not at all opposed to people making gobs of money. But I do believe that there should be a balance between returning enough to shareholders via dividends or other mechanisms and investing in the growth of firms, and thereby, our economy.

Read more



In a webinar for Strategyzer earlier this month, I shared eight practices leaders can use to see around corners. You can watch the full recording here.

And in an exciting first, I had the chance to participate in a panel via hologram! Here's my holo-presence at a talk with Bridge Partnership on purpose-driven organizations.

Reading List

A curated roundup of interesting books and articles to get you thinking:

- **182 Questions for Digital Execution: Strategy Implementation Starts with the Right Questions.** Robin Speculand's new e-book enables you to develop an execution plan that sets the organization up for success in a digital world, as leaders are actually getting worse at execution. (Bridges Consultancy)

- **How to Talk to a Co-worker Who's Having a Tough Time.** We all have bad days at work. Deborah Grayson Riegel offers some thoughtful and respectful advice about how to deal with a colleague who just can't "get over it." (HBR)

- **Taking a Human-Led Approach to Navigating Technological Change.** In a workshop with Tracey Zimmerman of Robots & Pencils, we explored a few solutions for how executives can adapt to the modern pace of change. (Blog)

Upcoming Events

April 24-26: Penrose Lectures (London, UK)
I'm thrilled to be delivering two lectures at SOAS University of London, exploring financialization and innovation, along with how digitization is changing theories of growth.

April 23: Women's Network Event (London, UK)
During my visit to London, I'll be visiting the CBS London Alumni Association's Women's Network for a networking event and discussion about my latest research.

April 28-May 24: Advanced Management Program (Columbia Business School)
This transformational program helps executives respond to evolving leadership challenges and create a vision to lead their companies to success.

May 6-10: Leading Strategic Growth and Change (Columbia Business School)
This five-day program focuses on the process of finding opportunities, launching new ventures, and leading necessary organizational changes to revitalize an organization.

May 10: Ascend Women in Leadership Conference (New York, NY)
ASCEND aims to identify and promote the best strategies for advancing women to the C-Suite and the boardroom, and to foster specific commitments for action from companies.

May 21: Best Practice Institute Webinar (Virtual)
Join me for an interactive webinar about how executives can best position themselves to "see around corners" and identify major changes in their environment.

May 22: Women in Innovation Forum (New York, NY)
I'm excited to join this pioneering event, which aims to give women and minorities the energy and confidence to become the most innovative and inclusive leaders they can be.

June 5-7: ScaleCon (Washington, D.C.)
It's the event of the year for growth leaders. At the inaugural Predictable Success ScaleCon, you'll receive an immediately actionable roadmap to scaling your organization.

Interested in having Rita speak at your organization or event?

Learn more

In the Press

- Trust Me: Building a Culture of Trust in an Era of Uncertainty (CNBC)
- Leadership Lessons From a Guitar Hero (Strategy + Business)
- Creating Growth & Competitive Advantage in Consulting (Consulting Success)
- 8 Leadership Lessons From Game of Thrones (Newsweek)

Where there is uncertainty, there is also opportunity.

Here's to your next advantage! - Rita

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Rita McGrath Group, P.O. Box 7286, Princeton, NJ 08543