A chance for bankers to refocus their talents

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A few weeks ago, some science and engineering students at London University lobbed me a question. “Lots of people on our course used to go to work for banks, but now that seems a really bad idea, so where do you think the job opportunities will be in the future for graduates like us?”

Where indeed? It is a question of great import right now – not just for current students but for policymakers across the western world. Until three years ago, smart, numerate students took it for granted that one of the fastest ways to become rich and successful was to dive into the world of complex finance, producing structures such as collateralised debt obligations (CDOs).

Now, however, those CDO dreams have crumbled. By late last year, large western banks had shed more than 125,000 jobs. Thousands more have gone since then, many in high finance. The betting in the management consultancy industry (which is cutting back too) is that some 300,000 global jobs linked to banking could vanish before the crisis ends.

That is striking, given that the City of London was thought to employ some 350,000 financial workers two years ago. An entire financial army, in other words, is being demobilised – of all ages and ranks.

Some optimists (and students) hope the trend will be temporary in nature. History, however, suggests otherwise. Take a look, for example, at some fascinating recent research by Thomas Philippon and Ariell Reshef, two US-based economists, on human capital and wage trends in the 20th century banking and non-banking worlds.

This analysis suggests that between the 1930s and early 1980s, pay and skill levels in finance were roughly comparable to those in the rest of the business and professional world. However, from the early 1990s, pay and skill levels soared until by 2006 bankers were earning 1.7 times what other comparable business employees took home. No wonder graduates flocked to finance.

But – more interestingly – the research also shows that an almost identical rise in the wage and skill levels of finance workers relative to other business spheres was also seen in the 1920s. It was only in the late 1930s, or after the Wall Street crash, that banking pay and skills fell to levels comparable with other industries (where they stayed for almost five decades).

That has two intriguing implications. First, it suggests that the ability of finance to attract smart graduates this decade had little to do with the inherent challenge of the technology of modern finance. After all, CDOs – and “rocket scientists” – did not exist in the 1920s. Instead, Philippon blames extreme deregulation, or a bubble.

But second, the data also suggest that if history now repeats itself – i.e. banking becomes a tightly regulated, low-margin business – then the relative skills and pay of bankers could stay low for years. The next decade, in other words, could look like the 1950s or 1960s, when bankers’ remuneration differed little from everyone else’s.

That might horrify financiers. But it may also carry some seeds of hope. After all, if finance no longer keeps monopolising the brightest and best workers, some of that talent could be diverted into other, more productive, arenas – for the good of the economy.

Some of those financiers now being “demobbed” – or sacked – have strong science or engineering backgrounds, and are sitting on spare capital. In an ideal world, they would be perfect candidates to support manufacturing, information technology or other high-tech start-ups of the kind that Europe in particular so desperately needs.

America, for its part, is also short of engineers. The Society of Manufacturing Engineers, for example, calculates that while the country needs 100,000 engineering graduates a year, it is only producing some 70,000. The SME itself points out in a new advertising campaign aimed at students: “Engineers create real wealth by solving problems rather than creating ‘paper’ wealth by playing with the markets.”

The public sector in both America and Europe could also benefit from an influx of highly skilled, financially astute managers. Expanding the talent base of the regulators, in particular, would seem one obvious place to start. The non-profit and educational sectors also need more smart, highly skilled workers, particularly (but not exclusively) in places such as the UK.

Will these redeployments of talent actually happen? It is still far too early to tell. A few sectors of the economy are already trying to ride the wave. In the City of London, a campaign has been launched to persuade former bankers to become physics teachers. In New York, the mayor’s office is also developing programmes to retrain Wall Street workers.

But thus far, such efforts remain disappointingly sporadic. Most policymakers remain keener to bash bankers than to consider how to use them in an economically rational way. Some shell-shocked bankers, for their part, seem to prefer to sit on the beach, hoping – foolishly – that the current cull is simply temporary in nature.

But the science students who asked me that jobs question, at least, are already voting with their feet. One of them (bravely) says that he still hopes to be a banker. Most of his classmates, though, are looking for jobs in science or industry (working with "green technology" is apparently now ultra-hip, just as derivatives used to be). Fingers crossed that they succeed – not just for the sake of their own careers, but the health of the wider economy, too.

* **www.nber.org/papers/w14644.pdf**

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