

[The truth is, we have no idea how much money bankers deserve](#) [1]

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The daffodils are out and the annual uproar at bankers' bonuses is upon us. The EU's bonus cap is a well-timed, predictably silly play to the gallery, but we shouldn't assume that our own banking rules are much more sensible.

Any rules about what private firms pay their employees are, of course, absurd. Aside from the base illiberalism of interfering in people's privacy, there is the practical problem that a cap on pay would drive bankers abroad. Imagine if there was a cap on footballers' pay? Within a year, the Swiss Premier League would be world class.

A cap on bonuses will also make financial firms more sensitive to downturns in business. The purpose of bonuses is to give firms flexibility in how much they pay, so that they can pay employees much less in bad years than they would in good years without having to sack people.

In a free market, the problem of bonuses encouraging short-term profit maximisation at the cost of long-term sustainability would not be an issue? the firms that pursued that strategy would go out of business soon enough. The problem is that any large firm that acts badly like this is protected from its mistakes by things like deposit insurance and bailouts.

The other problem is that the government has already bailed out quite a few banks, and those banks also want to pay bonuses to their employees. On the one hand, this is perfectly sensible? it's crucial that we have competent executives in government-owned banks to minimise the loss of value to taxpayers.

On the other hand, aren't we against extravagant public sector pay? The big problem with the public sector is that, internally, it lacks the price signals that make markets work relatively efficiently. It's true that the public sector can mimic market prices to an extent, but only very crudely. RBS can borrow money at a significant discount because of the implied promise of government backing. (All banks operate under the promise of an implied government bailout, and explicit deposit insurance.) Without a functioning price system, there's no way of telling how much RBS's CEO deserves.

The reality is that nobody really knows how much to pay RBS's executives. Mimicking the private sector isn't enough? without private shareholders to answer to and a genuine threat of loss, RBS's bonuses are no more wisely spent than [Bury council's iPads for its binmen](#) [3].

Yes, a cap on bonuses is a dumb idea. But so is any state involvement in the banking sector. If the government's going to fight against the latest example of EU overreach, it would do well to get its own house in order as well.

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