

Dean Starkman Interviews Anat Admati:

Q: Why did you write “The Bankers’ New Clothes,” a book for the general public and not strictly for scholars?

A: It was disturbing to me that there was not enough serious discussion about what was going on.

I was not a banking expert, but after studying it, I found that a lot of policymakers and people commenting on it didn’t actually know what they were saying or were saying wrong things or misleading things.

There seemed to be, to take a charitable interpretation, that there were blind spots or confusion or, the most cynical interpretation, there was sort of willful blindness.

Q: So, what’s wrong with banking?

A: What’s wrong with banking is that a lot of people are able to take risks and not be fully responsible and accountable for those actions. They can get away with doing things that are really inefficient and dangerous, somehow. And it works for them but it’s dangerous for the rest of us.

People need to understand that the biggest banks are really, really big, by any measure. It’s also the complexity and sort of breathless scope of what they do and just how much of it is opaque. It remains incredibly fragile as a system.

Q: Why is a bank’s equity important?

A: Equity is like a down payment on a house. It’s money from shareholders, not borrowed, and that’s what most corporations live on primarily.

Q: Is it the same as bank capital, which we usually hear about?

A: Essentially, yes, but think of equity as the best form of capital. Capital is often misunderstood as a rainy-day fund, money that sits on a shelf until it is needed to absorb losses. That's false.

In banking, the word "capital" is meant to represent where the money comes from. And really what regulatory capital means is essentially money that's unborrowed.

Q: Capital requirements, boiled down, amount to a few percentage points of a bank's total assets. What's the right ratio?

A: Current requirements are ridiculous by any normal standards. A supposedly "harsh" regulation would be 5 percent of the total. Corporations just never ever live like that.