Decision Taking, Confidence and Risk Management in Banks in the 19th and 20th Century

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In the aftermath of the recent financial crisis it became obvious that risk management – if there was any - in many financial institutions failed. This encouraged economic and business historians to do renewed research on risk management and decision taking in financial institutions. In this context the organizer, Korinna Schönhärl (Duisburg), convened banking historians from around Europe as well as researchers from different fields such as sociology, behavioral finance and economics in an inspiring workshop to discuss new insights and methodologies relating to decision taking, confidence and risk management in banks from the so-called ‘banking revolution’ in the first half of the 19th century until the end of the 20th century. Contributions at the workshop focused therefore on four questions: (i) what mechanisms of decision taking were established and how did they change over time, (ii) what kinds of risk management techniques emerged and how did they change, (iii) what factors constructed confidence in banking and (iv) what methods would be useful to describe risk management and decision taking processes.

In the first session YOUSSEF CASSIS (Florence) contributed a trenchant paper on the differences of risk between family and joint-stock banks in the 19th and 20th century. Despite the emergence of large joint-stock banks in the late 19th century, family banks persisted throughout the 20th century. He argued that the big City and Wall Street mergers of family and joint-stock banks in the 1990s brought a separation of ownership and control but not a change of habitus. Investment bankers named themselves ‘partners’, overtook the social status and habitus of a ‘partner’ and received remuneration as they were ‘partners’, but without fulfilling one of the most important characteristics of a ‘partner’ in family banks: the risk of the unlimited and personal liability.

With the focus on decision taking FRIEDERIKE SATTLER (Frankfurt am Main) addressed the impracticality of modern economic theory in order to explain decision taking processes. ‘Rationality’ and ‘homo oeconomicus’ should be historicized as concepts, she suggested. Since decisions were future-related and therefore uncertain, assumptions had to be made by the actors. For historians the investigation of the formation of future-related expectations and assumptions would challenge concepts of rationality. She proposed to investigate the change of rationality concepts by looking at institutions, semantics and everyday-practices. In her empirical example she proved the fruitful method in the examination of foreign investment decisions of three large German banks in the 1960s and 1970s.

Further reflections on decision taking were in the center of DANIEL WYLEGALAs (Düsseldorf) contribution. Based on Niklas Luhmann’s systems theory he defined an organization to be only sustained by continuous decision taking, which produced the risk that an organization would suffer from a decision. Further, decision with high risks would be allocated at the organization’s top-level, that is why he investigated the function of a successful top-career. From this point of view he explained the typically long career (‘Hauskarriere’) in German banks in the 19th and 20th century as function to ensure the organization’s capability for decision taking by selecting and socializing the persons who prove that they were able to fulfill the corresponding role.

In the second session the workshop provided a broad overview about methodologies of different research fields. MORTEN REITMAYER (Trier) posed the crucial question if new methodologies would help banking history to greater significance. His reflections on the question brought him to deny it and instead he proposed not to believe in new methodologies as a boost for business, economic and financial history but to actively participate with existing methods and theories in discussions regarding contemporary
history; to cite for example issues like ‘financialization’ or ‘financial market capitalism’.

The interdisciplinary approach of the workshop culminated in the presentation of Behavioral Finance as a specific academic approach within Economics and Finance by VICTOR RICCIARDI (Baltimore). Since the beginning of the 1980s this empirical approach challenged central elements of the so-called ‘rational school’, therefore taking up again core questions of the first session. When taking into consideration concepts as bounded rationality, loss aversion, emotions and feelings and different biases like overconfidence, inattention, representativeness, familiarity or herd behavior in order to explain decision taking in Finance – mostly looking at investors – this showed many similarities with everyday historical (archival) research findings. However, it remained open in the following discussion, how Behavioral Finance could be implemented to a historical perspective in order to explain changes of decision taking and risk management.

A similar discussion came up in the aftermath of the paper of the economist THOMAS P. SYRMOS (Piraeus). He assumed that nowadays banking included more risks than twenty years ago; environmental, social and governance risks. Therefore he asked if sustainable banks were different. Working with a data-set from the US-Social-Investment-Forum he denied any effect on banks profitability but instead found out that sustainable banks did recently invest more in the productive sector than in real estate. Despite the methodological questions, the following discussion pointed out that ‘sustainable’ had to be historicized and to ask for what reason certain banks decided to include environmental, social and governance risks into their decision taking would be more productive to historians.

The third session approached the subject of the workshop again fully historically, concentrating on insights of risk management techniques in Europe. ANDERS L. MIKKELSEN (London) focused on the role of growing competition, reputation and underwriting risks as drivers for the establishment of issuing syndicates among financial intermediaries in London from the 1880s to the Great War; attempts to reduce risk for issuing houses by restrictive market practices.

Addressing risk management and decision taking more generally SEBASTIAN KNAKE (Bielefeld) presented the unpublished dissertation of Monika Pohle-Fraser, where she analyzed risk management techniques and decision taking in German and French banks of the 19th century. Investment decisions until the 1850s were rather based on personal reputation than economic calculation. With the banking revolution the reputation approach lost its legitimacy to justify decisions whereas the reputation approach in every-day banking practice remained predominant in the old banks. Decision taking processes were portrayed by decision takers as based on economic calculations and rational choice, but in fact this was only ex-post justification rather than the basis for decision taking. In his critical reflections he added sociological convention theory to Pohle-Frasers findings. Since the formal existence of rational calculation – whether it was used in decision taking or not – had become the new code of conduct and convention, it was an important element of risk management practices to have such calculations. When a decision had proved to be bad for business, one could blame others for wrong data delivery for example.

In order to understand how certain attitudes to risk were preserved within a financial institution, MATTHEW HOLLOW (York) looked at Barclays from 1900 to 1980. What he described as ‘old fashioned banking’ could be preserved by a corporate structure and culture that saw the bank as network of branches and therefore as big family, also tracing this back to the expansion of Barclays by mergers with different local banks in the beginning of the 20th century. A certain culture was further preserved by long lasting and loyal careers or internal training courses for the staff.

In his comment CHRISTOPHER KOPPER (Bielefeld) proposed to understand reputation and personal relations as means to reduce complexity regarding the decision taking and risk management. When for example accounting practices were not standardized or balance-sheets were subject to fraud and inaccuracy, personal confidence reduced information costs.

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In the last session some methodological problems were addressed again. First ANDREW DILLEY (Aberdeen) suggested in his paper to consider comparative and geographically broad perspectives on risk management and decision taking. He emphasized that risks were constructed within financial centers; distinctive financial centers will have evolved different perspectives on what risks are and how to deal with them.

Two early modern historians, DANIEL VELINOV and NADIA MATRINGE (Paris), problematized the conceptual term of ‘financial intermediation’. When looking at the Florentine Salviati banking house in Lyon and the La Bistrate banking house in Antwerp in the 16th and 17th century, they stated that with growing financial transactions in the early modern period intermediaries emerged but the narrative in the existing literature of intermediaries as middle men who connected demand and offer sides would be problematic. The two respective banking houses, as they showed, acted as agents and principals at the same time; they were not just middle men but players on the financial markets.

Finally BERNARDO BATIZ-LAZO (Bangor) rose up the question of broader implications of technological innovation in banking and how this would challenge banking historians when looking at recent information technology in financial institutions. He encouraged economic historians to deal with computer and technological history and prompted oral history approaches.

In conclusion, the workshop caused fruitful reflections on banking history and the challenges when introducing risk management and decision taking as objects of investigation. When discussing theories and methodologies it became obvious that banking historians follow a rather eclectic perspective which is not to be underestimated in its capability. The workshop further problematized and histori- all sources, an issue still highly unsatisfying in some countries. Further focus on banks as part of financial capitalism that would combine a micro- and macro-perspective wasn’t part of the discussion. For example the historical question where financial institutions could invest when running debts has become undesirable to all participants of the economy, is a challenging question of our time. It is much to be hoped that the attempts to encourage banking and financial history brings forward much more historical studies.

Conference Overview:

Korinna Schönhärl (Duisburg), Introduction

1st Session: The Organization of the Bank and its Implication for Decision Taking, Risk Management and Confidence
Johannes Bär (Frankfurt a.M.), Chair / Dirk Baecker (Friedrichshafen), Commentator
Youssef Cassis (Florence), Family banks, private banks, investment banks: Wall Street and the City of London from the 19th to the 21st century
Friederike Sattler (Frankfurt a.M.), Cooperative Governance in Banking: Consequences for Decision Taking Processes
Daniel Wylegala (Düsseldorf), The Person and the Institution

2nd Session: Evidence from Sociology and Financial Psychology
Friederike Sattler (Frankfurt a.M.), Chair / Youssef Cassis (Florence), Commentator
Morten Reitmayer (Trier), Consideration of Social Capital
Victor Ricciardi (Baltimore), The Role of Judgment and Decision Making: The Perception of Risk in Behavioral Finance
Thomas P. Syrmos (Piraeus), Are Sustainable Banks Different?

3rd Session: Historical Insight in Risk Management Techniques in Banking in Europe and Abroad
Dieter Ziegler (Bochum), Chair / Christopher Kopper (Bielefeld), Commentator
Anders L. Mikkelsen (London), Minimising Risk: Financial Intermediaries and the Bond

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Issuing in London before the Great War

Sebastian Knake (Bielefeld), The ‘reputation approach’ and the justificatory function of economic calculation: Some critical reflections on Monika Pohle-Fraser’s analysis of Risk Management Techniques in the 19th century

Matthew Hollow (York), Investigation Attitudes to Risk in British Banking: A Methodological Survey

4th Session: The Framework of Investment
Korinna Schönhärl (Duisburg), Chair / Boris Barth (Konstanz), Commentator

Andrew Dilley (Aberdeen), Financial Centers and Risk: Reflections on Institutions and Cultures in the Belle Epoch

Daniel Velinov/Nadia Matringe (Paris), Financial Intermediation

Bernardo Batiz-Lazo (Bangor), The Method and Concept of the Digital Bank

Korinna Schönhärl (Duisburg), Conclusion: New Methodological Approaches to International Banking History.


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