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BRITAIN'S BEST SELLING QUALITY DAILY

## Politicians and financial experts team up to calculate bankers' bonuses more accurately

A powerful committee of politicians and financial experts is considering a new pay code for bankers that will calculate bonuses more honestly.

**By Philip Aldrick**

Bank profits have been swelled in the past by leverage, which multiplies income in good times but leaves them horribly exposed in a crisis. Under proposals being reviewed by the Future of Banking Commission, profits made through leverage would be excluded from bonus calculations to provide a more truthful measure of performance.

The idea was first championed last May by Andrew Haldane, director of financial stability at the Bank of England. He described the way in which banking success is measured as "skill multiplied by luck", with "luck" representing "leverage" or debt. "Since 2000, rising leverage fully accounts for movements in UK banks' returns. Good luck and good management need to be better distinguished."

In a submission to the commission, Knight Vinke, the activist investor known for its forensic analysis of banks, has argued

for a more straightforward "return on assets" measure that removes leverage.

"Management compensation schemes should reward real returns on assets, not leverage," Knight Vinke said last week. "Incentive schemes need to be overhauled."

Further analysis by Knight Vinke shows that, without leverage, investment banks often make poor returns. Using its measure, Barclays' investment bank did not beat the average "risk-free" rate in any of the past five years. However, it paid £2.2bn in bonuses last year and awarded Bob Diamond, the investment bank's head, a package worth £60m.

Using the proposed measure, the more boring UK retail bank performed far better – generating returns above the "risk-free" rate.

Should the measure be adopted, it would almost certainly lead to lower bonus levels across the industry.