

Josef Ackermann

CEO and Chairman, Deutsche Bank

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Since 2002, Josef Ackermann has been the CEO and Chairman of the Group Executive Committee of Deutsche Bank. Prior to joining Deutsche Bank, Ackermann worked at Schweizerische Kreditanstalt, now Credit Suisse, and in 1993 became President of the Executive Board. In 1996, Ackermann joined the Board of Managing Directors of Deutsche Bank with responsibility for the investment banking division. Under his leadership, the business unit developed into one of Deutsche Bank's principal revenue sources and entered the top tier of global investment banks. He is a member of the Supervisory Board of Siemens (Second Deputy Chairman), a non-executive member of the Board of Directors of Royal Dutch Shell, and a member of the Board of Directors of Zurich Financial Services (Vice Chairman). He also plays an active role, among various other activities, in the Initiative Finanzstandort Deutschland (member of the Initiators' Group), the Institute of International Finance (Chairman), the World Economic Forum (Co-Chairman of the Foundation Board), the St. Gallen Foundation for International Studies (Chairman), and the Metropolitan Opera New York (Advisory Director). Ackermann was recently appointed Visiting Professor in Finance at the London School of Economics, and Honorary Professor at the Johann Wolfgang Goethe University Frankfurt.



Is the level of inequality in Europe and the U.S. about right, or is there too much or too little? What do you think about the current level of inequality?

In order to answer this question one must look at the prevailing socio-economic environment. Before the financial crisis, inequality was probably perceived differently from what it is today, and once we return to stronger and more sustainable growth the perception might change again. In the current socio-economic environment, there seems to be a broad consensus that the present degree of inequality is too high, less in terms of wealth than in terms of compensation. This certainly holds true for the United States, but also to a lesser degree for Europe. Even in the business community, this view is widely shared, especially regarding the financial industry. My personal view is: To regain trust, we in the financial industry have to make sure remuneration is well-deserved and based on proven and solid lasting performance.

You mentioned the financial crisis; do you think the crisis has had an impact on the level of inequality?

To a certain extent, no doubt. The concentration of wealth and income was mainly driven by the financial industry. As a consequence of the financial crisis, remuneration there as well as asset prices have come down, so the trend of increasing overall inequality should have been stopped if not reversed. However: When you are in a stagnant or recessionary environment, when people have to fear job losses or major salary reductions, inequality is perceived much more clearly. Discussions about income distribution and inequality are always more intense in such times.

If we talk about Deutsche Bank and the inequality of pay, would you say that the pay differentials between different levels of employees are just about right or are there aspects you would like to see changed?

It is essential that pay truly reflects performance and provides the right incentives. Deutsche Bank's compensation system has long been among those in the industry with a longer-term orientation. As a consequence of the financial crisis we have improved our system further by establishing a robust governance structure, introducing risk-adjusted metrics, and ensuring a significant proportion of variable compensation is deferred over three to four years and subject to stringent clawbacks. Having said this, the financial industry is very competitive and our people are our talent so we

have to be cognizant of the actions of other firms in order to ensure that our pay levels and structures remain competitive.

When you read about inequality, you definitely see that there are positive and negative effects. Do you think a different level of CEO or board remuneration at Deutsche Bank would affect the profitability of the bank?

If you want to grow as a company and create profits you have to have the support of the society in which you are operating, you have to meet the requirements of your shareholders, but also of your other stakeholders. One has to take this into consideration when it comes to compensation at the board level in particular. We at Deutsche Bank are fully aware of this. However, I'm a bit concerned that the regulation of compensation systems might go too far. In the end, pay has to be based on merit, and it has to be competitive. There is a war for talent out there, and we see that some banks are losing good people to non-regulated institutions that do not have to disclose compensation packages. That is why regulation has to be industry-wide in order to avoid competitor distortions.

If you follow data like the Gini coefficient, you will find that inequality measured by this indicator has increased in many, but not in all, OECD countries over the past twenty years. What do you think are the reasons for this trend?

Let me take the financial industry. Today we are recruiting talent globally, in New York, London, Hong Kong, and many other places. This has led to higher compensation levels in many countries which were lagging behind internationally, like Germany. Secondly, public disclosures of compensation have made it possible to compare one's own pay with that of others. That again put upward pressure on compensation levels. Thirdly, for many years, our industry aligned executive pay to shareholders' interests by linking a certain portion of the remuneration package to the company's share price. Until the recent crisis, we had seen significant growth in share prices, which created unprecedented wealth for executives.

With the benefit of hindsight, perhaps there should have been more stringent limits to compensation. This is something that our industry has recognized and dealt with by better aligning compensation to sustainable value creation.

But let's not forget: We operate in a very competitive market, and this market situation as well as the compensation practices of our peer competi-

tors also contributed to the rise in senior executive pay. We have to offer competitive packages to attract and retain the most talented people.

Besides executive and high-level compensation, we are also interested in the pay of rank-and-file employees lower in the organizational hierarchy. Is their pay about right or too low?

I think pay here is broadly appropriate and linked to the position, performance, and also seniority of these colleagues. The current discussion is mostly centered around highly paid people, but these are only a small minority. It is wrong to believe that bonuses in general created bad incentives. For many bank employees, their bonuses plus fixed salaries taken together are not more than the salaries they would receive in other industries.

Turning to wealth, which, according to the data, has also become much more concentrated among fewer people, what are the reasons for this development?

Wealth, in my opinion, has become so concentrated because financial assets have experienced this tremendous rise in prices. If you were invested in financial assets, shares, or real estate, you benefited enormously from the inflation in asset prices we had until the crisis hit. Meanwhile that has been corrected, of course.

What do you think about the future? Will this concentration leading to increasing inequality in terms of income or wealth continue, or will we see a reversing trend?

Remuneration as well as asset prices have come down, or will come down. Political and regulatory pressure will increase, and that will probably lead, on a macro level, to a different trend. But overall, as long as we are operating in a market economy, those who have a higher net worth will benefit when asset prices rise again. Therefore, I would not expect the correction we have seen over the last twelve to eighteen months to continue. On the contrary, we will see certain values recover and that will help wealthy people in creating more wealth, which is already starting to happen.

You noted that pressures to regulate remuneration will likely increase. Do you have any suggestions as to practical, effective, and appropriate regu-

lations? Do you have any cautions about types of regulation that might prove counterproductive and should be avoided?

Basically, in a market economy, companies should be allowed to set remuneration levels and structures at their own discretion, governments should infringe as little as possible on private contracts. Therefore, the regulation of remuneration should be limited to setting a framework. The proposals issued by the Committee of European Banking Supervisors (CEBS) on remuneration in the financial industry provide a good basis for this. Essentially, these proposals define the requirements for transparency, the principles for remuneration structures, as well as the minimum standards for setting up remuneration structures within firms. Establishing such a framework is, in any case, better than trying to enshrine specific rules, such as absolute pay limits or caps on the tax deductibility of pay. Experience has shown, such mechanisms will only lead to attempts to circumvent them.

Moreover, as far as the financial industry is concerned, there is also a need to differentiate between various functions. Performance-based pay has a different impact depending on whether it is used, for instance, as an incentive to sell retail products, as an incentive in proprietary trading or risk management operations, or at the board level. The key issue here is the extent to which performance-based pay affects the risk situation of the firm.

Finally, it would also be wise to keep regulation limited to broad principles, as there is a need to differentiate between industries. Arguably, there is greater justification for setting rules on remuneration in the financial industry, where – as we have just experienced – there is a greater likelihood of the state having to step in to prevent a systemic crisis than there is in other industries, which are also less likely to receive state assistance at some stage.

Turning to recommendations, what, first of all, should the private sector do? Are there any practical actions the private sector should pursue?

Again, let me speak about my own industry: The financial industry is particularly dependent on trust. For this, transparency is key. Second, we must take a long-term perspective, remuneration must be based on real, bottom-line contributions to earnings, not on revenues, with vesting over several years. I think the more critical part is really to establish some sort of claw-back mechanism in the system such that if people make a lot of money in one year with very risky activities, they do not get the full payout if the

company loses money on these activities in the following years. In that sense, compensation should be based on a longer-term analysis of your performance. We also have to avoid paying big bonuses to staff making good profits for the company in a year when shareholders suffer. But that is easier said than done when you have high-performing entities on the one hand and loss-making entities on the other. In the end, the bottom-line should restrict the bonuses you are willing to pay.

Do you also have more general advice about how to design better remuneration systems, how to better align performance and pay? Although mention was made of the excessive “short-termism” of compensation packages, are there other problems to address?

As the Chairman of the IIF, I have been advocating more sustainable remuneration practices with a longer-term orientation for quite some time now. There might be different ways to achieve these goals. For example we could use more risk-adjusted metrics and compensation plans structured accordingly. A lot of companies already have such structures in place, but they need additional fine-tuning and alignment with the risk profiles of the business they are in. More generally, I think that all aspects of a performance cycle should be covered. This means you need short-term pay for performance as well as longer-term pay structures to ensure, and compensate employees for, the company’s sustainable success.

If we look at inequality in terms of poverty and limited opportunities for those at the bottom of the income scale, do you think there is anything the private sector should do?

Absolutely. I strongly believe in equality of opportunity and social mobility. If you are a child in a very poor family but very talented, you should be able to go to the best universities and maybe become CEO of Deutsche Bank one day. The feeling is growing, especially in Germany and other European countries, but probably less so in the United States, that people with a modest social background don’t have the same opportunities. This is creating a tremendous amount of frustration. Deutsche Bank therefore contributes to making it possible for hundreds of talented people, children from more modest backgrounds, to obtain a university education, and that is something we will be promoting even more going forward. I believe that programs like these make an extremely important contribution to the very fabric of our society.

What can the government do to address the issue of rising inequality?

The government should invest as much as possible in education. This makes a country more competitive on a global scale, but it also gives its citizens the feeling they have opportunities in life. I think there are a lot of talented people who cannot live up to their full potential compared to other people who can, simply because they are brought up in a different environment where they get better input and are more challenged.

It is also important to invest in the very young (from the ages of one to five). And it is also very important to invest in technology – especially information technology, for example, to improve learning skills.

Aside from investing more in education, are there other recommendations for improving education in ways that would increase opportunity?

Money is not everything, you can and should, of course, invest time and talent, for example, in mentoring programs.

Should the government address the issue of inequality, or focus more on the issue of poverty?

Above all, governments should address the subject of equal opportunity. I believe this is key. To some extent, of course, this also means fighting the root causes of poverty, but it is just as important for people to have the feeling that they have the same opportunity to succeed if they are talented. If that is the case, inequality of wealth and income distribution will be much more widely accepted.

What are some practical ways the private sector and the government can work together to bring about more equal opportunities?

To give you an example, at Deutsche Bank we team up with different institutions to foster the financial education of young students to help them to effectively manage their personal finances. People from disadvantaged backgrounds quite often lack the most basic financial skills, which adds to their disadvantages.

Are there any policy recommendations, any actions of the private sector in the U.S., that could serve as a model for Europe?

With its many private foundations, in the U.S. clearly a lot is done to help the disadvantaged. We are learning from this in Europe. On the other hand, the U.S. is presently running the risk of losing some of its former advantages. For example, the country was always very open to talented people, wherever they came from. Meritocracy always played an important role, as it does at Deutsche Bank, where we look for the most talented people, whatever their background, which was very important for our success. But in the U.S., we are now seeing a trend in the opposite direction. For instance, there are restrictions on hiring highly skilled foreigners. If these were allowed to continue, the benefits of meritocracy and diversity would be lost.

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