Hearing On
WALL STREET AND THE FINANCIAL CRISIS: THE ROLE OF INVESTMENT BANKS
Tuesday, April 27, 2010
10:00 a.m.
106 Dirksen Senate Office Building

Opening Statement by Senator Mark Pryor

I believe Wall Street is always going to be several steps ahead of Congress. Regulators are the "cop on the beat" who are reacting to the next exotic way Wall Street invents to make money. Every year Wall Street devises new types of investments that, in my opinion, are more suitable for Las Vegas than Little Rock. Until recently, I had never heard of a synthetic CDO. It has been reported that John Paulson recommended several of the asset backed securities included in the Abacus 2007 –AC1 synthetic CDO. What I want to know is:

- Is it common practice on Wall Street for hedge funds to recommend securities for CDOs?
- Where were the credit rating agencies when these CDOs were being rated?
- What other types of investments is Wall Street inventing that allow individuals and companies to bet on the market and the direction of the economy?

Over the last 25 years, the United States economy and financial industry has experienced a series of increasingly significant financial crises. Some people believe the only way to prevent financial institutions from becoming "Too Big to Allow to Fail" is to limit their size so that they do not represent a systemic risk to the financial system. The use of Off-Balance-Sheet limited and special investment partnerships have raised concern about full disclosure and transparency and the potential for companies to hide "systemic risk."

In my opinion, one of the main contributors to the magnitude of the current financial crisis was the amount of leverage used in the housing market and mortgage backed securities. Many investment banks were leveraged by a ratio of 30 to 1, and they were dealing with billions of dollars. As you know, when asset prices are rising, this system works like a dream.

Until Wall Street changes its culture and goes back to putting the client first, I am concerned that we will continue to experience these financial crises. Bonuses on Wall Street rose 17 percent last year to $20.3 billion even as the retail investor on Main Street continued to lose money in the stock market. There appears to me to be an inherent conflict of interest between rewarding bankers with outsized bonuses for short term performance and the long term needs of investors to protect their investments and grow capital.