

PETITION TO THE NOBEL COMMITTEE AND SWEDEN'S CENTRAL BANK

In light of the current credit crisis, which has already lasted well over eighteen months and has had the deleterious effects known to all (disappearance of the investment banking industry, tanking markets, untold volatility, monster losses, a freeze-over of the lending system, massive lay-offs, economic stagnation, unprecedented state intervention), we want to make the following statement to the Nobel Committee and the Sveriges Riksbank (Sweden's Central Bank):

- ✓ The main factor behind the unleashing of the crisis was the widespread use of flawed quantitative/theoretical methodology by financial institutions, with the enthusiastic blessing and encouragement of regulators and the academic financial economics establishment
- ✓ We can highlight at least two key culprits: the Value at Risk (VaR) model for "measuring" risk and setting capital charges, and the Gaussian Copula model for valuing and rating Subprime Collateralized Debt Obligations; by avidly abiding by (among other) those two scions of quantitative finance, the financial industry guaranteed that never before was risk so badly anticipated and valuations and credit ratings so hopelessly off-base. The inevitable end result was massively leveraged exposures to impossibly overrated toxic securities, which brought the system down as the underlying mortgage market turned sour
- ✓ The Sveriges Riksbank has had a decades-long habit of rewarding flawed, unworldly, and dangerous theoretical finance constructs with its "Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel" (colloquially known as the Nobel Prize in Economics) thus endowing such machinations with unlimited global credibility and respectability, decisively encouraging their real-life adoption and helping silence any possible skeptics
- ✓ At least two of the theories awarded with the Economics "Nobel" have been behind the very worst financial crises to have afflicted the world since the 1929 crash; Black-Scholes-Merton was the inspiration for the strategies that gave us October 1987's Black Monday, the most devastating one-day drop in the history of Wall Street (which gravely threatened to sink the system); while Portfolio Theory was the inspiration for the creators and adopters of VaR, which outrageously misguided guidance and capacity for forcing destabilizing liquidations were to blame for the 1998 LTCM crisis and the current malaise (both of which, certainly, put us in great peril)
- ✓ It is high time that wildly Platonic, wildly unworldly, wildly dangerous theories (that, by the way, have never solved a previously unsolved practical problem) stop being glowingly rewarded by those who claim to be the torch-carriers for Alfred Nobel (who, by the way, never said anything about a prize for Economics, let alone its financial branch)
- ✓ By rewarding wildly Platonic, wildly unworldly, wildly dangerous theories, the Nobel Committee (as aiding and abetting enabler) and the Sveriges Riksbank (as direct instigator) put the world in great danger and make the possibility of future meltdowns that much more plausible

- ✓ The unhealthy obsession with assigning precise measurements to that which is not amenable to concrete quantification has gotten us in enough trouble already; by relentlessly and consistently embracing and promoting theories that promise precision and concreteness (yet are built upon unremittingly flawed foundations) the Nobel Committee and the Sveriges Riksbank lead us down the path of painful deleteriousness
- ✓ The safety of the global economy should always be far more important than satisfying the ego (and bank accounts) of non-scientists bent on applying dodgy scientific methodology to disciplines that are practical-only in nature, and who never show the humbleness to admit their mistakes and responsibility for never-ending havoc-wreaking
- ✓ Platonic, unworldly, and dangerous finance theories simply cannot go on being endowed with the Nobel stamp of approval! A lot is at stake, drastic action must be urgently taken, and bad practices cannot be prolonged any longer
- ✓ If the Nobel Committee and the Sveriges Riksbank persist in choosing the pleasing of the financial economics politburo over the salubrity of the system, we suggest that they at least drastically modify the name of the award (allow me suggest “Sveriges Riksbank Prize in Platonic Potentially-Lethal Typically-Impractical Financial Economics”). We need those Scandinavians to be incommensurately honest, so that naïve outsiders understand the true nature of what’s being glorified. Finance theory run amok can kill. Adding a big disclaimer onto the “Nobel” that regularly endows the theories with a far-reaching seal of approval would be a reasonably healthy protective step on our part.

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