

# Financial crisis in ireland and groupthink



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## Groupthink and Irish Financial Crisis

- Efstathiou Thalia
- Papaeracleous Elena
- Papoulla Pantelitsa
- Tritas Tasos
- Tsoulli Andri

### 1. Introduction

The complexity of today's modern organizations has increased the need for effective decision-making. The capability of an organisation to develop and progress depends heavily on the ability of its members to arrive consistently at appropriate decisions. There are many forces that affect the decision making process in a group, one of them is groupthink[Thalia Ef1].

Professor Janis L. Irving, a research psychologist introduced the term "groupthink" to explain the phenomenon where people in a group embrace the opinion of other members of the group because they desire harmony and conformity. Members set aside their own beliefs, try to minimize conflict and reach a consensus decision without critical evaluation of alternative solutions. The conformity of the group eliminates the individual's creativity or responsibility for a step forward decision. The members of the group, victims of the groupthink effect, tend to compromise with the decisions of the group, leading to sub-optimized decisions. The repeated non-optimum decisions that are made lead to negative performance which in turn may lead the downfall of the organization.

Groupthink effect can be detrimental for organizations. Individuals suppress their personal thoughts and accept others opinion without further investigation . Groupthink can crush the innovation in an organization. Innovators may be willing to take alternative paths but often those courses of action are not very realistic in a groupthink environment. Due to that many organizations fail to respond to market trends or adopt new technologies. The organization is following a “ safe” direction but in reality is not able to take decision that will extent and empower its presence in markets[Thalia Ef2].

Behavioural research and studies show that behind corporate and public disasters, there is a group of participants responsible for the decisions made , that often are « victims» of the phenomenon called groupthink.

An example of such disaster was observed in the Irish financial crisis. Peter Nyberg was appointed to investigate what went wrong and frequently found behaviour exhibiting bandwagon effects such as groupthink . [Thalia Ef3]

*“ The more amiability and esprit de corps there is among the members of a policy-making in-group, the greater the danger that the independent critical thinking will be replaced by groupthink, which is likely to result in irrational and dehumanizing actions directed against out-group . ” [1 [Thalia Ef4] ]*

## 2. Symptoms

According to Janis’s studies the following eight symptoms of groupthink exist :

### Invulnerability

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The members of the group share an illusion of invulnerability that creates excessive optimism and encourages them to take extreme risks, failing to respond to obvious warnings of danger.

### Rationale

The members tend to construct collective rationalization and so they discount warnings or other negative feedback and as a result they do not reconsider their assumptions.

### Morality

Believing in inherent morality leads the group members to ignore the ethical and moral consequences of their decisions.

### Stereotypes

The group thinkers hold stereotyped views of out-groups, or the "enemy groups". This makes them believe that attempts to negotiate differences are unnecessary and unwarranted.

### Pressure

The members of the group are under direct pressure not to express arguments or doubts against any of the group's views.

### Self-censorship

Victims of groupthink avoid expressing doubts and deviations from the perceived group consensus, " *they keep silent about their misgivings and even minimize the importance of their doubts*".

### Unanimity

The group members share the illusion of unanimity, since the majority of those members who speak have views and judgments which seem to be unanimous, by making the false assumption that anyone who remains silent during a discussion is in full agreement with the others.

### Mind-guards

Victims of groupthink tend to be self-appointed mind - guards, to protect the group and the leader from problematic or contradictory information that might damage the group's cohesiveness, or create doubts about the morality of the group's views or decision

When the symptoms described above exist in a group that is trying to make a decision, there is a reasonable chance that groupthink will happen, although it is not necessarily so. When groups are under pressure and are highly cohesive, groupthink has a greater chance of affecting the decision making process. In addition, when pressure for unanimity seems overwhelming, members find it more difficult to realistically appraise the alternative courses of action available to them. These group pressures lead to irrational thinking and carelessness since groups experiencing groupthink fail to consider all alternatives and seek to maintain unanimity.

Decisions shaped by groupthink have low probability of achieving successful outcomes.

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what went wrong between bankers, regulators and others and frequently found behavior exhibiting bandwagon effects such as groupthink Doctor o .  
[Thalia Ef5]

Commission of Investigation into the Banking Sector of Ireland ,

### 3. Financial Crisis in Ireland and Groupthink

*“ In economics the majority is always wrong ”* - J. K Galbraith [Thalia Ef6]

As with most countries worldwide, Ireland has been facing an economic recession, which has started in 2008. Ireland currently is performing positively and it is considered that it has come out of this recession . However, by analyzing the factors that led the country to this point, groupthink was identified as one of the reasons responsible for the crisis .

The main reason for the crisis in the country was the unhindered expansion of the property bubble financed by the banks using wholesale market funding.

Groupthink in the financial crisis of Ireland, is mostly based on the report that was published from the Commission Investigation into the Banking Sector of Ireland m. Nyberg concludes that bankers, regulators and others were prey to “ groupthink”.

Biases in judgment and decision-making were instrumental in the development and severity of the crisis in Ireland. The rapid financial integration and the lack of relevant past experience may have increased the  
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vulnerability of decision-makers to economic and financial reasoning that proved disadvantageous.

Nyberg uses the term 'groupthink' to describe the mindset that prevailed during the boom years, when banks lent out money indiscriminately. His criticism was not confined to the banks, but to other groups, including the 'mainstream' ???, which bought into the bubble mentality.

Ireland's economy started to grow in the mid-1990s, which is considered as "late" compared to their European neighbours. Ireland's economy took the path of growth by offering a business-friendly environment, namely with low tax rates, a highly educated workforce and perhaps most importantly, land property to invest. *"After joining the Eurozone, Ireland's banks gained increased access to wholesale funding at a relatively low cost as retail and corporate deposits were not sufficient to fund lending growth and enabled the banks to respond to competition."* [Elena [Thalia Ef7] 1]. As a consequence, the need for the Government and the banks to keep up with this new flow became even stronger, leading banks to get carried away by the developments before they even became aware of them.

*Banks and their members started to feel the huge competitiveness by foreign banks and foreign property investment agents and in order to remain in the property market, they began taking risks. They did so with no rational thinking and objective. Those decisions put at risk the entire economy due to the absence of legal supervision and an insufficient regulation policy. They offered low rates and, similarly, other smaller banks and foreign-owned banks felt obliged to do the same. Those decisions put at risk the entire*

*economy due to the absence of legal supervision and an insufficient regulation policy, ignoring ethical and moral consequences and having the illusion that nothing could go wrong, both symptoms with aspects of morality and invulnerability in groupthink mode. [UCY8]*

*Ακίεμα ίνα γεγονίεζ το οποίο ίπαπιξε σημαντικίε ρίελο στην οικονομική κρίση της Ιρλανδίας ίεραν το ίετι οι*

*Banks exposed statements with huge funds and property as assets and became more and more tempting for potential investors. Somehow, both banks and borrowers ignored risks. Borrowers took advantage of the formal lending policy and, as a consequence, lending on credit expanded so rapidly that it led to severe liquidity and solvency problems. As a result, Ireland experienced an economic downturn, fell into deep recession and was forced to request financial aid from Europe. [UCY9] Οι τρέπεζες δεν πίστευαν ποτί ίετι θα ίφταναν σε αυτίε το σημείο αφοί και πίλι υπίρχε η αυταπίτη του ατρίεμητου που σε κίνει να αγνοείς τα σίματα κινδίνου.*

Financial integration in the euro area was deepening, and banks in Ireland had unprecedented access to cross-border funding. This put pressure on bank margins in Ireland. The report investigated the handling of the banking crisis and found that the crisis was essentially “home grown”. It was a result of domestic Irish decisions and actions, and not international developments. [UCY10] PRESSURE

The symptom of unanimity, as described above is occurring again in the case Irish crisis, according to Nybergs report. It has been argued in several reports <https://assignbuster.com/financial-crisis-in-ireland-and-groupthink/>



that human behaviour was a determinant factor in the economic crisis that Ireland faced. As Nyberg states in his report (reference\_1) when the warnings began, the group acted in defensive mode and ignored their existence. It is believed that there were arguments against some of the determinant decisions but they were never expressed because of unanimity and fear to express themselves led them to follow the policy of the group). And if they were indeed expressed, they were ignored. [UCY11]

We could argue that other main symptoms of groupthink such as stereotypes, where each member is completely loyal and dedicated to the group and its decisions and, invulnerability, which forces group members to be over optimistic and delusional, take risks and practice risky management, were also present.

## Conclusions

The financial crisis Ireland faced led authorities and policy makers to question their system. Investigations were conducted and they were forced to make several re-evaluations and establish stricter laws and policy regulators, in order to ensure that a crisis like the one they experienced would never emerge again.

Team leaders and facilitators need to take positive actions to avoid Groupthink, including creating constructive conflict within the group, breaking context to avoid context traps for participants, fostering the role of the devil's advocate, using sub-groups, the 'second chance' method, a heterogeneous group and in general to use tools that foster open expression of all points of view. A leader must also consider that the cohesiveness of a

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group intensifies as time goes by, making its members accept the goals, decisions and norms without reservation. Leaders should also recognize that their early expression of opinion can impact and inhibit an unbiased discussion of a project. Obviously, the culture of an organization impacts the openness with which lower echelon members participate, but even in the most open organizations, people are reluctant to contradict the boss. As Andy Grove astutely points out, "*It takes years to build a climate of openness, but one impulsive act by a senior person to a divergent point of view can quickly destroy it.*" [reference\_2]

What is needed now is a vigorous individuality that participates, takes responsibility and shares in its consequences. The right of dissent must be reinvigorated. We have a challenge to face up to, to exercise the responsibilities of citizenship we have systematically shirked.

Ireland ' s economy started to grow in the mid-1990s- and it is considered as " late" compared to their European neighbors. Ireland's economy had taken the path to growth, by offering business friendly environments low tax rates (i. e.), high educated work-force and perhaps most important they offered land-property to invest. "*Joining the Eurozone, Irelands banks gained increased access to wholesale funding at a relatively low cost. As retail and corporate deposits were not sufficient to fund lending growth and enabled the banks to respond to competition .*" [elena [Thalia Ef12] 1]. Ireland ' s productivity increased followed by, foreign banks and property investors who started to show interest in expanding their business and services in Ireland. As sequence the need from the Government and Banks to keep up with this

new flow became more intense; leading Banks to get carried away by that intensity before they even became aware with it.

Banks and their members [Thalia Ef13] had started to feel the huge competitiveness by other foreign banks and from other foreign investment property competitors. In order to remain in the property market field they begin taking risks; with no rational thinking and objective; nor did they have any second thoughts. The decisions that put at risk the entire economy were established due to the absence of legal supervision and an insufficient regulation policy. They offered low rates and similarly other smaller banks and foreign-owned banks felt emerged to do same. Banks exposed statements with huge funds and property as assets and became more and more tempting for potential investors. Somehow, risks were ignored by both banks and borrowers. Borrowers took advantage of the formal lending policy and as consequence the lending on credit expanded so rapidly that it led to severe liquidity problems and solvency. As result, Ireland falls into an economic downturn, in deep recession and forced to request financial aid from Europe [Thalia Ef14] .

We could argue [Thalia Ef15] that the members of the Banks board who took the crucial decisions were in line with the norms of groupthink. Our example for the groupthink and financial crisis in Ireland, is mostly based on the report that was published from the Commission for Investigation into the Banking Sector in Ireland (Nyberg, 2011), which concludes that bankers, regulators and others were in line with the norms of groupthink. Mr. Peter Nyberg was appointed as the sole Member of the Commission of Investigation. Nyberg use the term ' groupthink' to describe the mindset that

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prevailed during the years of crisis, when banks lent out extensively. [Thalia Ef16]

The illusion that nothing could go wrong, the failure to explore for other alternatives,

According to Nyberg's report (elena 3 [Thalia Ef17] ) as warnings began to alert, the group acted in defensive mode ignoring their existence. It is believed that there were arguments against some of the determinant decisions but they were never brought up, or if they were brought up they were ignored. This is one of the main symptoms of groupthink, where the members of the group have the illusion of invulnerability.

Another symptom that is in line with the above,

A belief in the fundamentals of the Irish property market and in the efficient operation of financial markets led to Groupthink, a psychological process that reduces the likelihood of critical views being aired.

Financial integration in the euro area was deepening, and banks in Ireland had unprecedented access to cross-border funding. This put pressure on bank margins in Ireland. The report investigated the handling of the banking crisis and found that the crisis was essentially "home grown". It was a result of domestic Irish decisions and actions, and not international developments.

Groupthink occurs when a group of decision makers decides on a course of action without questioning underlying assumptions. As the period of prosperity continued, executives took more and more financial risks based on prior judgments.

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[Thalia Ef18] It has been argued by several reports that human behavior was a determinant factor in the economy crisis Ireland faced.

That is from members within their group, we could therefore argue that this group acted and were in the mode of groupthink. “ *As groupthink is characterized by inward-looking, self-regulating and stereotypical behavior that can often lead to distorted and defective decision making* “(elena 2) . In line with this we could also state that the group failed to see other alternatives, failed to filter their data that is to examine them more closely and failed re-examine their evaluation. The financial crisis Ireland faced, led to deep considerations by authorities and policy makers about their system, investigations were conducted likewise they were forced to make several re-evaluations and establish stricter law and policy regulators, all in line, that a crisis like the one they experienced will never be faced again.

[Thalia Ef19]

#### 4. How to avoid Groupthink

Through comparison of practices of successful groups and those of groupthink-style, researchers in this area have been able to come up with ways to avoid or limit groupthink.

#### Open Communication

Firstly, the group leader should encourage open communication within the group and at the same time avoid stating his personal preferences and expectations. [1, 2][Thalia Ef20]An open communication environment provides a platform for objections, disagreements, misgivings, concerns and

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alternatives. Group leaders should establish an environment where every opinion is important and carefully considered. It is more likely for group members to share their ideas when they know that the group they are part of fosters open communication. [1] According to Janis L. Irving a leader should not express his opinion when assigning a task to a group and should be absent from many of the group meetings to avoid excessively influencing the outcome. [2]

### Devils Advocate

Another effective way to prevent groupthink is by instructing a team member to play the role of the 'devil's advocate' within the group. The team member assigned the role takes an opposing view to the majority. This method triggers the discussion of opposing views leading each member to defend his ideas and decisions in order to convince others of their importance. Group members who are unable to support their views should revise them or adopt the views of others. [1]

### Outside Expert

An outside expert is considered a valuable shield to help guard against groupthink. The non-biased viewpoint based on research that the external experts bring, helps the team members to see the subject matter from a variety of angles. The fact that outside experts do not possess an allegiance to the group but seek to act in the best interest of the organization makes this method an invaluable asset against groupthink. An organization should bring in or be consulted by experts on a regular basis to allow group members to open up to the opinion of others. [1, 2]

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### Sub-groups

Furthermore, by breaking up the homogeneous nature of the group members will be encouraged to explore alternatives. This can be achieved by dividing the group into sub-groups, where each sub-group will present its views and then the entire group makes a decision to select one of the ideas presented. [1]

### Second Chance

Lastly, the group can hold a 'second-chance' meeting at a later date that gives the group one last chance to rethink the entire issue before making a definitive choice. [1, 2]

### 5. Empower work teams [Thalia Ef21]

Whether the relationship is with your team, supervisor, manager, customer or coworker, you want to make your interpersonal relationships positive, supportive, clear, and empowering. In all circumstances and situations, working and cooperating with others is important for all kinds of relationships. Whether that is at a personal level, professional level, or even national level as described above. Therefore, it is important to maintain teams that are based on trust and keep the lines of communication between the group members open.

Creating efficient and competent teams is challenging but necessary in order for an organisation to be successful. A comfortable and warm atmosphere is vital, so as the team members will feel free and confident to

express their opinion. However, the level of informality differs, depending on the situation.

The concept of synergy is of pivotal importance in a group, thus the goal setting systems must focus not only on the individual level but on the group level as well. Mutual respect within a group should be promoted by involving everyone in the decision-making process.

In order to have well performing teams, there must be clear goals, clear roles and responsibilities, positive relationships, strong leadership, clear procedures for problem solving, planning, completing tasks and evaluating performance. The development of team spirit is also important for empowering work teams.

In addition to the above, the meetings must be effective, so that resources and energy will not go to waste. The expectations from the team's performance and expected outcomes should be clearly communicated, as well as the reasons why the team was created in the first place.

The team members and especially the leader should pay attention to conflicts that may arise. If people let the problems to come to the surface, but in a constructive way this can be gainful for the team.

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