



SOCIETY OF ACTUARIES

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# Why The Financial Crisis Inspired An Actuary To Be An Author

Does the Actuarial Profession have a wider Public Mandate to fulfil?

By John Gordon

I don't count myself among the small number of people who foresaw the financial crisis that began in 2007 (for those interested in the genuine article I cannot recommend Ann Pettifor's 2006 book *The Coming First World Debt Crisis* highly enough). But it was evident to me that much of the supposed boom we'd witnessed in the years leading up to it was being fuelled by little more than debt and optimism, and it was also apparent to me that the activities of some sectors of the financial services industry were contributing significantly to the problem.

The collapse of Lehman Brothers in particular was a truly seismic financial event, and I remember widespread pronouncements in the immediate aftermath that there can be "no return to business as usual." What I find fascinating is how little has really changed. While it is true that the global economic situation is much improved, achieving that has required state intervention on an unprecedented scale and has taken us into uncharted fiscal waters.

Regarding the blood bath on Wall Street and subsequent self examination, villains and good guys (albeit not so many) were clearly identified. Names have been named and people have been accused, fingers have been pointed and reputations have been tarnished. For me it was interesting that for the Insurance and Pensions industry which did not go unscathed in the Financial Crisis, the financial press has been more lenient—especially in its attitude towards the financial architects and risk management guardians of our industry, not least among them the actuarial profession.

I have thought long and hard regarding why more actuaries have not taken the time to examine the root cause of the crisis and its impact on the insurance and pension industry, and to challenge the actuarial profession to critically self-examine its role in the financial world. In a nutshell I have sought answers to the question of where, how and why have we not undertaken such an exercise.

## PUBLIC ROLE OF THE ACTUARY

What the crisis demonstrated above all else was the degree to which perverse incentives can eat away at the moral backbone of those in positions of responsibility. In that regard, I would note that there have surely now been enough high-profile cases to the contrary to dispel any notion that this particular disease has any respect for professional boundaries.

The crux of the problem is that I believe in recent years my profession could have served the public interest more effectively than it did, and did not serve the public interest as well as the public had reason to expect it to.

One way in which I think the profession could help its members better serve the public interest mandate in the future would be to better clarify what that mandate means in practice. Is it surprising that so few actuaries are effective in serving the public interest beyond the confines of what's required of them in the day job when basic questions such as "who are my public" and "what is the public interest" are left so open to interpretation?

We are keen to promote our risk management credentials as a profession that purports to take a long term view. We should be reflecting on how we can most effectively respond to the threat that unpredictable risks pose to our collective long-term interests and the public interest that we are mandated to serve.

Perhaps the best place to start is by questioning personal motives. What is important to you? Are you happy with the way your profession is representing your interests? Are you happy with the way both it and you represent the public interest? How much time do you spend thinking about public interest matters that reach outside the confines of your day job? How do you feel about the reputational risk of not speaking out on some of those issues, either for you individually or for your profession as a whole?



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## // THE REPUTATION OF A PROFESSION IS MADE OR BROKEN NOT JUST BY THOSE WHO LEAD IT, BUT BY THE DEEDS OF THOSE WHO FILL ITS RANKS. //

### OPPORTUNITIES FOR ACTUARIES IN A CHANGING WORLD

Looking ahead, there are many areas of public interest that could benefit from the application of such vision and skills.

The examples I include below illustrate the range of opportunities that might be open to a profession that was more passionate about the public interest. I would also venture to suggest that most of them represent rather more pressing needs than some of the activities that presently occupy our time.

- 1) Actuaries Can Do Banking (and should)
- 2) Economic & Financial Market Reform: A new economic vision of the future is urgently required. Who better than a profession of risk management experts with long-term vision to help develop and promote it?
- 3) Public Sector Reform: The idea that the public sector is riddled with inefficiency has been with us for so long that it has increasingly come to be accepted by many as a fact of public sector life. As a Profession we could better serve the public by helping to improve the efficacy with which taxes are spent.
- 4) Private Finance Initiatives: As these have a history of providing poor returns to the taxpayer, perhaps there is an opportunity for a commercially-minded profession well-versed in the art of analysis and financial management to assist Government in better expediting them.

- 5) Pensions Reform. The combination of economic and demographic challenges continues to grow across the developed world, and actuaries should rightly be expected to take a lead in confronting them.
- 6) Government Policy Initiatives: We could do much to enhance our own risk management credentials by being more proactive in promoting public debate and formulating policy initiatives in some of these areas (economic reform, population growth, the management of scarce resources, etc.)
- 7) International Collaboration: Global problems, from tax havens to financial crashes to radical overhaul of economic systems to global warming to energy crises, demand global solutions. With a coordinated approach, we are well-placed to assist.
- 8) Tax Reform. Globally and nationally, our system of taxation is overly complex, inadequately targeted and easily exploited. The profession is well placed to help inform a new, more transparent system of taxation that better serves the long-term public interest.
- 9) Renewable Energy and Recycling Policy: Could the profession not bring its risk analysis and projection skills to bear in articulating a longer-term business case based on a more realistic economic cost/benefit model?
- 10) Transport Policy: One doesn't need to look beyond the relative cost of road, rail and air travel, and how the relative cost of each has changed in recent decades, to see that a new vision is required. The actuarial skill set is well-suited to the task of helping to formulate it.
- 11) Carbon Costing: The development of reliable carbon models is growing in importance as the scale of the global warming challenge becomes clearer. Actuaries are well-qualified to provide input both into modelling techniques and to support analysis and projection of long-term costs and benefits.

Some of the later entries in particular are a full spectrum away from our traditional interest areas. I am not suggesting for a moment that the profession should seek to embrace them all even if its investment would be welcomed. But if the profession is to be seen as a force for good in a brave new world, these are the kind of initiatives it would help for it to be seen supporting. They are also the kind of public mandate initiatives that the world desperately needs to be supported.

## IN SUMMARY

I conclude and strongly endorse the view that the world needs actuaries, or to be more precise the view that the world needs people who have the kind of skills that actuaries' typically possess. But we need to question individually and collectively whether those skills are presently being utilized to best effect. I believe that as a profession we need to invest our skills, training and intellectual capital rather more wisely than we presently do if we are ever to convince the public that it needs us.

If we can rise to the challenge, I see at least four big benefits to the Profession in doing so:

- The profession has a clear public interest mandate to fulfil.
- The profession clearly sees risk management as a growth area, but it will convince few of its credentials in this area until it can find something meaningful to say about the risks that matter.
- The profession is by its own admission one whose members are trained to take an objective long-term view, an attribute that elsewhere looks to be as scarce as ever. Finding a long-term voice to match its long-term vision would enhance the profession's reputation and might help to promote longer term thinking where it is most needed, namely in the minds of those who govern us.
- The Profession has talked much over the years about applying its skillset to areas beyond the traditional



insurance and pensions comfort zone, but with limited success. A paradigm shift of the kind I advocate would help to turn this aspiration into reality, to the benefit of the public interest and to our own employment prospects.

I am under no illusion as to how what I advocate will be received by some of my professional colleagues. The result will, I expect, leave me accused of many things—arrogance, temerity, precociousness, presumptuousness, insolence or disloyalty all seem possible—but at least a lack of ambition should not be among them.

The reputation of a profession is made or broken not just by those who lead it, but by the deeds of those who fill its ranks. How will history judge us? I would like actuaries to think long and hard about if we need to chart a different course; we must each take individual responsibility for effecting a paradigm shift. If you too believe that your Profession could improve how it represents the public interest, what are you going to do to help it do so? ■