Editorial

MEGATRENDS

BY RONALD POON-AFFAT

JOHN NAISBITT, in his best-seller *Megatrends*, defined a megatrend as a general shift in thinking or approach affecting countries, industries and organizations. An actuary is a professional that uses mathematics, statistics and financial theory to study uncertain future events. Such professionals evaluate the likelihood of those events and design creative ways to reduce and/or manage the risk of adverse events.

So it would appear that the actuarial professional could be counted on to offer an informed opinion about megatrends.

Let us first consider some examples of what is not a megatrend. According to PricewaterhouseCoopers' Insurance Banana Skins 2009 Report, the top three identified risks were liquidity, credit risk and credit spreads. However these are basically short-term issues that probably have more to do with "not delivering" annual budgets (reading between the lines—not receiving annual mega bonuses) rather than long-term creeping financial issues.

Another example of what's not a megatrend is the oldie but goodie story about the relationship between the farmer and the turkey. If the turkey were to extrapolate his past relationship with a farmer, he would infer that the farmer is his best friend as he is provided with food, shelter and health care with no strings attached. Until of course Thanksgiving comes around. The turkey naturally would be dead wrong regarding any forecast made in its lifetime.

John Maynard Keynes said, "It is better to be vaguely right than precisely wrong," and this is where I am convinced that actuaries have the distinct upper hand compared to bankers, lawyers and accountants. Actuaries are still more comfortable being vaguely right. We can still be in our comfort zone pricing whole life policies which include long-term financial, economic and actuarial assumptions. Of course we are often accused of being like the guy standing at the back of a fast-moving train with a high-powered telescope; precisely analyzing where we came from but having no idea about where we are going or even where we are at the moment; a useful reminder that our job description includes peering into the future.

I recently gave a presentation on megatrends and discussed the following:

1) The possible effect of longevity. Everyone thinks that we are all going to be a generation of centenarians, so I decided to shake things up a little bit by referring to the marked rise of diabetes, obesity and pandemics which have the potential to temper future mortality improvements.

2) The increasing financial clout of the older consumer. We need to cater for this growing economic force and alter underwriting and benefits to accommodate this increasing cohort of potential clients.

3) The increasing cost of capital. I undertook a historical tour starting in 1776 when William Morgan undertook the first actuarial valuation of the United Kingdom's Equitable Life all the way to Solvency II, noting that the cost of capital was a lot less expensive in 1776 and going forward it was not going to get any less expensive, and

4). The consolidation of insurance companies all over the world. Even in the most competitive markets, the top 10 companies still occupy 75 percent of the market share. I urged the smaller companies to consider reviewing their product ranges and distribution channels so as to avoid competing head-on with the industry's giants.

After that presentation, I came across an interesting and provocative actuarial paper by John Gordon, FIA; John is an actuarial consultant and emerging best-selling author. The paper challenged "the role of the actuary in a changing world." In his wide-ranging paper John identifies some real megatrends which include risks that pose global threats and threaten societal collapse; issues that hold the key questions for tomorrow.

John thought that it would be rather interesting if actuaries gave a shot at including the following off-the-charts factors within their risk maps and discussed their potential impact. For example, the following:

1) Continuing global population growth,
2) Global warming,
3) The risk of alternative fuels not being able to compensate for the end of oil. Global fuel shortages and an ensuing energy crisis,
4) Shortage of food and potable water,
5) Escalation of conflict, and
6) The end of continuing economic growth as we know it.

There is always a lot of discussion of the role of the actuarial skills in a wider social context. Why is it that we do not consider such risks within our models or academic discussions? Is it that we think that we are not qualified (if not us, then whom)? Is it that we believe it is not in our profession's mandate to do so? Is it that we think that such risks are unimportant? I reckon that if we started to address such global issues, then we would get an invitation to appear on Fox News, quicker that Bill O'Reilly can say, "the spin stops here."

What could be more important than the analysis of risk factors mentioned above? Let's allow ourselves the luxury to daydream a little. Imagine if the slighted, brainy guy in a future Hollywood summer blockbuster is an actuary. He correctly identified the risk that was threatening the world's existence and projected the ultimate consequences. He then designs a creative way to reduce the likelihood and decrease the impact of such an adverse event. Our actuarial hero then ends up saving the world and gets the beautiful girl.


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For more discussion and information on John Gordon's paper "On the Role of the Actuary in a Changing World" visit *www.acturage.com*