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Bill Sharon

There is an assumption that one of the fundamental purposes of government is to provide for the safety of its citizens. One could argue that Americans enjoy that safety. There have been no terrorist attacks in the US since 9/11 and the crime rates in most cities have been declining for years. Although the world seems to be as uncertain a place as we have ever known in this generation we all operate as though we can get through our lives relatively unscathed. Yet we have more people in prison than any other country in the world and we manage to shoot and kill each other at rates that dwarf those in any other developed nation. Safety, it would seem, depends on your perspective.

That desire for safety has expanded into many other areas beyond just the physical. As the consumer society took off after World War II many of us became focused on securing our possessions as much as our persons. Avoiding loss became a cultural preoccupation and was manifested in products that promised a range of security from ensuring our attractiveness to the opposite sex to tracking our kid's whereabouts via cell phones. We built mighty fortresses in our minds as though we could protect ourselves from any eventuality.

Over the last several decades we shifted the focus of our desire for safety from our persons and possessions to our money. Mutual funds became the primary destination of 401k's and we convinced ourselves that there were people who were smarter than we were who knew how to grow our money. We continue to do this regardless of financial catastrophes and in the face of numerous reports that tell us that the DJIA continues to outperform these funds nearly 2 to 1. The perception of safety has become more important than the reality. We pay others to make less money on investments than we could make on our own and we do it because we are convinced that it is safer to let someone else make the decisions.

Derivatives have their origin in that kind of thinking. Originally, before they became a source of wealth creation, they were designed to provide a hedge against a future transaction. That was a reasonable and prudent goal. In their current incarnation they have become the source of misery – their promise of safety shattered by the improbable assumptions on which they are based.

Within the risk management community there is an increasing debate on the utility of mathematical modeling. On one side, there is the argument that the crisis has served to strengthen the models and they are now more robust than ever. On the other side, there is insistence that recent events demonstrate the futility of predicting much of anything.

It's reasonable to assume that there is more than a shred of truth in both positions. The real problem lies in our motivation; do we want to ensure safety or pursue opportunity? Pursuing opportunity certainly sounds like a loftier goal but it is a messier process and it is foolish to think that outcomes can be guaranteed.

In the end, we are stuck with our own subjective judgment. Despite the protests of my quant friends that they can drive bias out of any model I would submit that as long as human beings are involved that goal will

always be elusive. And so it should be. The purpose of life is not the avoidance of death – the purpose of life is life! It is the same for a company.

The current economic crisis has caused most corporations to adopt a defensive posture. They are cutting jobs and expenses. Some of them will survive but we should not be surprised if others, some of them well known brands, do not. The experience of the automotive industry tells us that poor design and substandard quality is difficult to turn around. Those companies and those people, however, who understand that the only reasonable goal is the pursuit of opportunity will not only survive, they will thrive. They see risk as the necessary ingredient that propels their ideas from concept to reality. They understand that strength comes from organizing people towards a goal and that uncertainty perceived as opportunity is much more powerful than pondering the list of possible calamities.

Which leaves us with the challenge of redefining or at least expanding the role of the risk manager. Instead of being the arbiters of what is or is not a risk based on mathematical models or regulations never intended to manage risk within an organization, risk managers need to ask the legitimate authorities within their organizations to align operational capacities with strategic goals.

Asking operational and business managers what they need to achieve success and then synthesizing that information into useful business intelligence, parameters to work by and clear goals to strive for is the real challenge for the risk management profession.

Frankly, it's a tougher job definition than the one we have today, but it is much more interesting and the intelligence it generates can have a much more profound effect on the ability to assess the likelihood of success rather than the probability of failure.

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