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The future of the investment industry

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The aging profile (a.k.a. agenda)

A little light narcissism



Define our terms

Descriptive

Normative

The big five

- Whither capitalism?
- Pension property rights
- Next financial crisis
- Complexity
- Collaboration



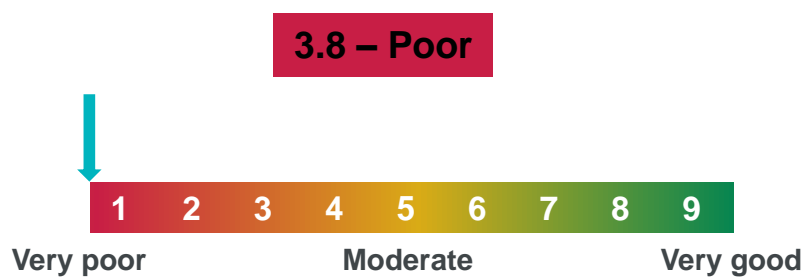
Tackling the issues

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Please score the current state of the investment industry's overall value proposition



Source: Towers Watson London iX conference 18 March 2015



3

As time goes by...



4

When I'm 64

Is it: "Yours sincerely, wasting away"

or

"Sunday mornings, go for a ride"



Likely

- Descriptive outcome
- Simple projection



Desired

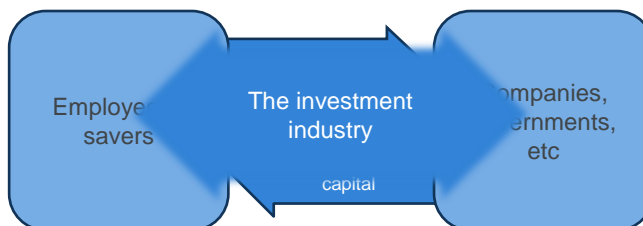
- Normative outcome
- Demands appropriate action



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5

The purpose of the investment industry



Fundamental purpose: connect suppliers of capital with users of capital
The 'why' and the 'how' is poorly understood/communicated

6

A mission statement for the industry

Why develop an industry mission statement?

- What is the investment industry for?
- Does society know?
- Would it be better if industry participants and society agreed on this point?

Suggested mission statement

The industry's mission is to compound wealth – getting clients / customers from under-funded to fully-funded over time – **the 'why'**

The 'how'

- Asset owners: 'invest to meet (explicitly) agreed goals securely, affordably, sustainably, equitably'
- Asset managers 'Align themselves with the needs of the client, incur necessary *Costs*, and convert those costs into outcomes *Efficiently*'



7

How well is the industry serving its purpose?

Last 20 years: Industry has gone from **Moderate** to **Poor**

Next 20 years: Industry will go from **Poor** to ???



8

Challenges to the industry's value proposition

Five overarching issues shaping the development of the investment industry






Whither capitalism?

Likely	Desired	Actions
Modified market fundamentalism <ul style="list-style-type: none"> Primacy of profit remains Systemic risk controlled through self-interest Small role for governments/regulation to correct major abuse 	Toward inclusive capitalism <ul style="list-style-type: none"> Externalities properly valued Focus on sustainability... ...and stakeholders Rise of universal owners 	<ul style="list-style-type: none"> Collaborate/Achieve scale Widen assessment from short term, pure finance
		

Pension property rights



Likely	Desired	Actions
<p>Benefits paid in full in most cases, but:</p> <ul style="list-style-type: none"> Persistent low bond yields put pressure on balance sheets Sponsors default (e.g., U.S. public funds) Past rights are renegotiated Loss of trust 	<p>Secure pension delivery through:</p> <ul style="list-style-type: none"> Rising bond yields + strong investment returns → <i>not controllable</i> Improved pension governance (including smart use of LDI and insurance) → <i>controllable</i> 	<ul style="list-style-type: none"> Improve governance Revamp balance sheet management 



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11

Next financial crisis



Likely	Desired	Actions
<p>Status quo continues:</p> <ul style="list-style-type: none"> Misaligned incentive structures Poor cultural conditions Systemic complexities 	<ul style="list-style-type: none"> Better financial institutional culture and practice <p>+</p> <ul style="list-style-type: none"> Improved effectiveness of regulation <p>=</p> <ul style="list-style-type: none"> A more stable financial system 	<ul style="list-style-type: none"> Strengthen culture Improve meta-understanding Lobby for better regulation
<p>Risk in next 10 years</p>  <p>25-50%</p>	<p>Risk in next 10 years</p>  <p>< 25%</p>	





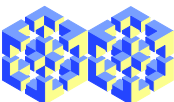


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12



Complexity

Our industry is:		Likely	Desired
Volatile Uncertain Complex Ambiguous		Business as usual: <ul style="list-style-type: none"> Forecasts projected from past outcomes Over reliance on linear models 	Required actions: <ul style="list-style-type: none"> Extreme clarity of mission Self-understanding Meta-understanding Adaptation Strengthen culture Build investment intelligence: <ul style="list-style-type: none"> Capabilities Beliefs Processes
			
			
			



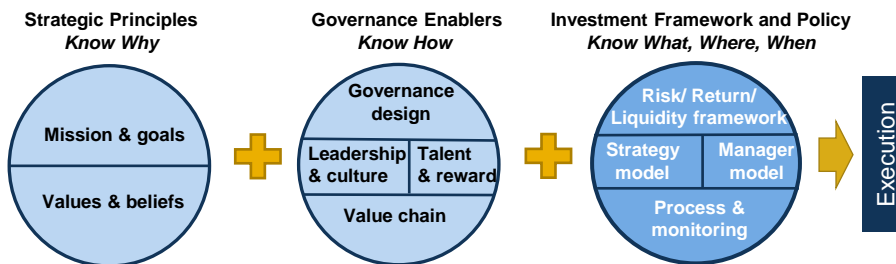
Collaboration

Balanced score-card - system assessment factors		Likely	Desired
Alignment	1. Trust measures	Poor	
	Financial services ranked last out of 15 global industries in the 2014 Edelman Trust Barometer		
	4. Incentives structuring	Poor	
	5. Cultural condition	Moderate	
Costs	6. Effective regulation	Moderate	
	7. Aggregate costs	Poor	
	8. Cost structure and transparency	Poor	
Efficiency	9. As	Poor	
	10. A	Good	
	11. Sustainability	Moderate	
	12. Beta vs. alpha focus	Poor	
Too much attention is given to alpha		Poor	Good

Changing the investment industry for the benefit of the end saver

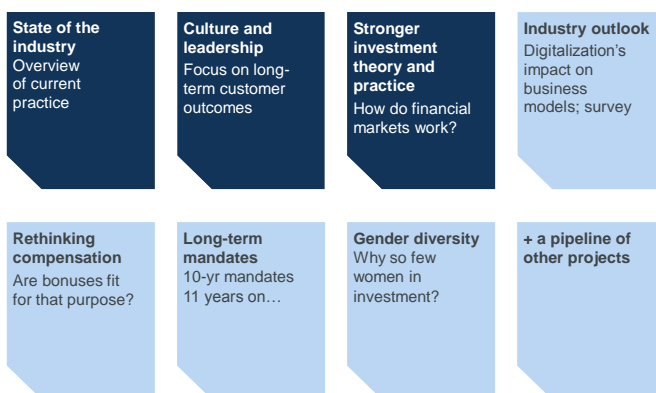


Moving to a more holistic view of investment



- Traditional investment advice focuses on the third disc
- A more effective industry demands that issues in discs 1 and 2 be addressed

Thinking Ahead Institute's research agenda



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17

Questions

Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.



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18