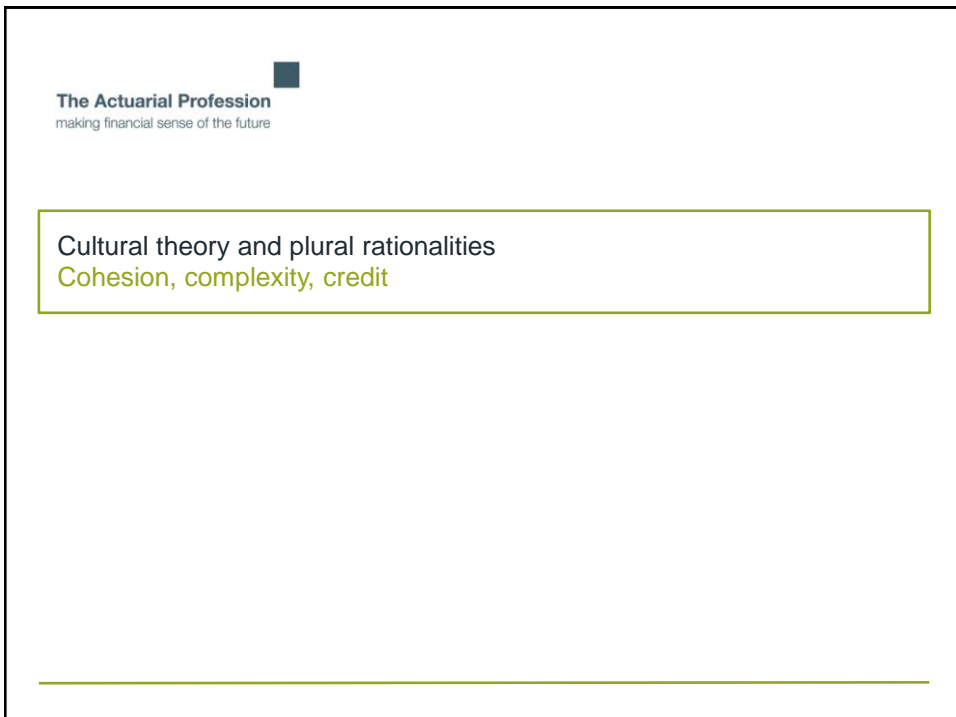


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**Cohesion, complexity and credit:
Studying people to understand risk**

Gillian Tett, Financial Times
Michael Thompson, IIASA
Alice Underwood, Willis Re

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Cultural theory and plural rationalities
Cohesion, complexity, credit

Gillian Tett

- Commentary

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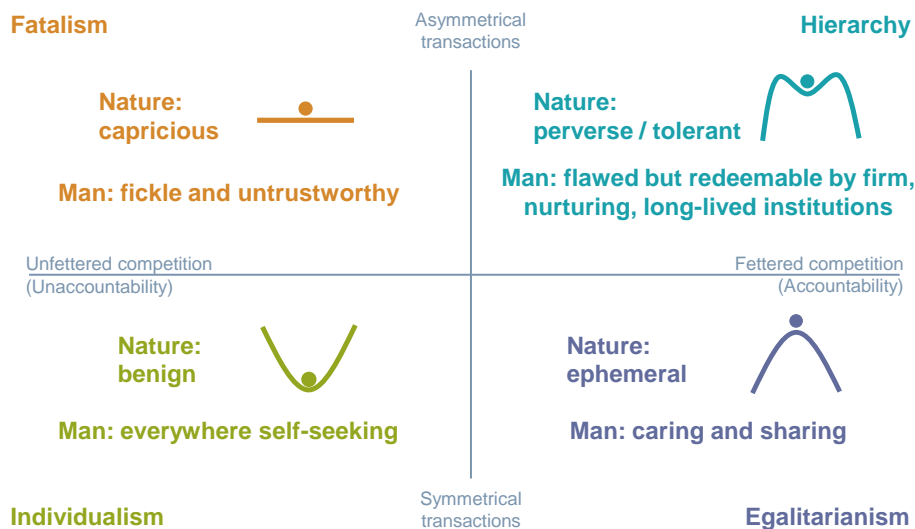
Cultural theory and plural rationalities
Cohesion, complexity, credit

Cohesion creates complexity

- Cohesion
 - “The different ways in which we bind ourselves to one another”
 - Theory of plural rationalities holds that there are four ways of doing this
- Leading to complexity
 - Self-organising system
 - Discontinuities arise when one of the ways of organising manages, for a while, to drive out all the others

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Four paradigms of cohesion



Relabeled as “Risk Attitudes”



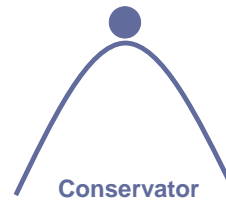
Pragmatist



Manager



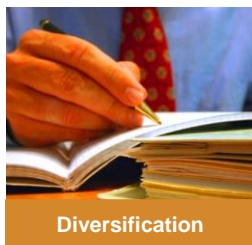
Maximizer



Conservator

6

Risk management strategies



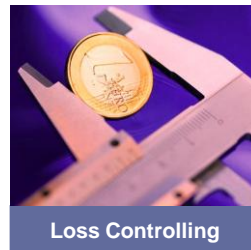
Diversification



Risk Steering



Risk Trading



Loss Controlling

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Favorite risk strategies



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Complexity

- Two-fold schemes yield simple dynamical systems
 - If you leave one regime, you're in the other
 - Keynes (hierarchies) and Hayek (markets)
- But introduce a third (and a fourth!) possibility and complexity appears: behavior is
 - Unpredictable
 - Non-deterministic
 - Sensitive to initial conditions ("path dependent")

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Limitations of models in a complex world

- Predictions based on simple models can be wildly misleading
- Orthodox, top-down models typically assume an equilibrium that does not exist in the real world
- Bottom up models can shed some light
 - A plug for our breakout session on Agent-Based Models!

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Credit

- Varying loads of trust set out in the plural rationality diagram
- Credit will flow where trust is in place, stable or growing
- Credit on the retreat whenever distrust starts to seep in
- Where distrust is rife, credit is absent

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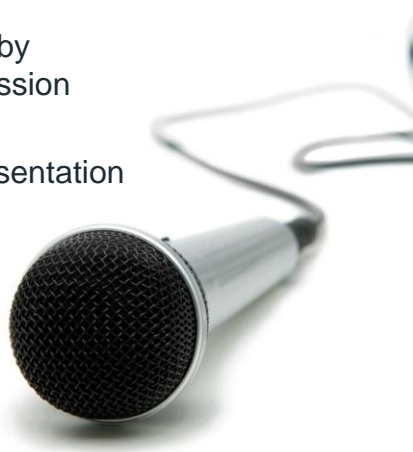
New directions

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Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

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