



## IFoA response to Scottish Government Advisory Group on Economic Recovery: A request for your knowledge and insights

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

### Key points

- The financial services sector plays a key role in the Scottish economy, both as an employer but also in the provision of critical services to the economy. This sector, covering life, health and general insurance, has a vital role to play over the coming years in helping the UK economy manage its way through the Covid-19 period and beyond.
- Actuaries help to steer not only insurers but also other financial entities such as pension funds and friendly societies, with a view to helping them meet the expectations and needs of those that rely on them for financial security; a role that will take on increasing importance through the economic recovery.
- The policy and economic response by governments should seek to avoid exacerbating intergenerational unfairness. The health and economic effects of the virus will be felt very differently by different generations and sectors of society, although the long-term consequences could span decades.
- The IFoA is also concerned about the effects of the virus on the growing trend that sees financial risks transfer from institutions to individuals; individuals who are now required to navigate the uncertain economic future - exacerbated by recent events - for themselves. It is, in our view, a matter of public interest that the stability and durability of the financial system is maintained – and that individuals are suitably equipped and educated to understand and manage these risks if they are to shoulder increased responsibility.
- We welcome the Advisory Group's focus on how to restart the economy in a greener and more sustainable manner, in order for Scotland to "Build Back Better" and meet the Scottish Government's target to go net zero by 2045.

Should you want to discuss any of the points raised please contact Henry Thompson, Head of Public Affairs ([Henry.Thompson@actuaries.org.uk](mailto:Henry.Thompson@actuaries.org.uk)) / 07519106714) in the first instance.

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## Introduction

1. The IFoA is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide and oversee their education at all stages of qualification and development throughout their careers.
2. The IFoA and its members have, throughout its over 150-year history, made significant contributions to the Scottish economy, most notably through the insurance and pension industries but increasingly in the areas of investment, climate change, health and data science. Actuaries are well known for their mathematical, risk management and data analytical skills, using their technical expertise and experience to try and make financial sense of the future on behalf of, among others, insurance company policyholders and pension scheme members
3. The IFoA has over 1,500 members based in Scotland and the activities of the IFoA in Scotland are coordinated by its Scottish Board. In addition to providing a professional community space for its members, the Scottish Board supports various outreach activities to the Scottish educational community through a number of regular contributions to mathematical education at various levels. These include assisting the Scottish Qualification Authority as it developed proposals for a new Higher Applied Mathematics exam, offering, in particular, guidance on what financial mathematics content should be included. We also sponsor prizes for performance in higher maths and in various university courses as well as supporting the annual enterprising mathematics competition.

## The actuarial context

4. A core focus of the actuarial profession is long-term financial provision for individuals. For example, the insurance sector plays a key role in the Scottish economy both as an employer but also in the provision of critical services to the economy. This sector, covering life, health and general insurance, has a vital role to play over the coming years in helping the UK economy manage its way through the Covid-19 period and beyond. As actuaries, we help to steer not only insurers but also other financial entities such as pension funds and friendly societies, with a view to helping them meet the expectations and needs of those that rely on them for financial security.
5. The IFoA has done extensive thinking on intergenerational fairness issues, both in our own right and as a convener of external views<sup>1</sup>. This is an important issue in relation to the economic impact of coronavirus as the health and economic effects of the virus will be felt very differently by different generations and sectors of society, although the long-term consequences could span decades.
6. The IFoA has also, recently, initiated a debate on the growing trend for individuals to have to provide for themselves. This was contained in our theme of “The Great Risk Transfer”<sup>2</sup>. As an institution we are also concerned with the challenges to individuals to navigate the uncertain economic future for themselves, clearly exacerbated by recent events. It is, in our view, a matter of public interest that the stability and durability of the financial system is maintained. This needs an approach that recognises the inter-dependencies that exist within complex systems, as well as sometimes the unintended consequences, for behaviour, of regulation and state intervention (e.g. moral hazard).
7. The IFoA is also contributing to the debate about the implications of climate change and how to avoid these. The IFoA’s Resource and Environment Board has a particular remit to consider these issues and ensure that all actuaries are aware of the risks resulting from climate change. We are pleased to note that your request is framed in a context of looking for opportunities to carry on the journey towards a greener economy, particularly given the Scottish Government’s commitment to go net zero by 2045.

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<sup>1</sup> <https://www.actuaries.org.uk/news-and-insights/public-affairs-and-policy/intergenerational-fairness>

<sup>2</sup> <https://www.actuaries.org.uk/news-and-insights/public-affairs-and-policy/great-risk-transfer>

8. The IFoA is also an investor in research carried out both by actuaries and in collaboration with universities, including Heriot-Watt University in Edinburgh. We would be happy to discuss future possibilities for collaboration on relevant projects. The IFoA is a member of the Scottish Financial Risk Academy.
9. Long-term financial provision and stability requires that the economy works well for everyone. In particular, that the wealth creation processes are working as effectively as possible. We are supportive of an approach to business that considers not only the necessary expected returns to meet the needs of investors but also the impact on society, including both employees and the self-employed, where personal development, fulfilment and ultimately employability are an important outcome.
10. Although most actuaries work in some part of the financial sector, we do not believe it wise to rely too heavily on this sector. Having an economy that is more diverse should make it more resilient and productive as well as being better able to foster the life chances of the population as a whole.

#### **The broader context**

11. Our responses are framed in the context of the current relationships between Scotland and the rest of the UK, with the EU and with the wider international community. Whilst these relations may change with time, the responses we provide are based on Scotland's current position. These relationships affect Scotland's fiscal, monetary and legislative flexibility. Our responses also take into account Scotland's current demographic structure.

#### **Structure of our response**

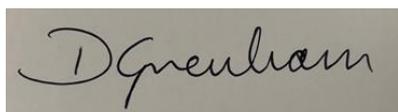
12. We have provided responses under your six main headings. There is though significant overlap between the topics covered as would be expected as they are looking at the whole of the complex system that is the Scottish society and economy. Focusing on just one aspect while ignoring others could lead to making decisions with benefits that are outweighed by the negative effects of unintended consequences. We therefore recommend taking a holistic view, recognising that the economy is only one part of the wider Scottish society.
13. We would be delighted to have an opportunity to discuss our ideas further with you and your colleagues on the Advisory Board. Should you wish to, or if you have any questions regarding our response, please contact Henry Thompson, Head of Public Affairs ([Henry.Thompson@actuaries.org.uk](mailto:Henry.Thompson@actuaries.org.uk)) in the first instance.

Yours sincerely,



John Taylor

**President, Institute and Faculty of Actuaries**



Dermot Grenham,

**Chair, Scottish Board, Institute and Faculty of Actuaries**

## Macro/fiscal considerations

**Significant macroeconomic and fiscal implications will change the economic context for the foreseeable future. What will be the shape and form of the recovery and what will be the implications for the future growth and structure of the economy?**

14. At this stage it is probably too early to know with certainty what shape the recovery will take (U, V or W or some other shape) and over what period. It is possible that Scotland may be harder hit than other parts of the UK as a result of the impact coronavirus has had on tourism and also due to the recent steep fall in oil prices. Politicians and other civil actors need to consider and articulate what sort of society we want in Scotland after the recovery and how economic developments can help achieve this. This may need considerable emphasis to be placed on issues such as equity, both across society as it stands today and through time, in order that policy actions and economic stimuli are just.
15. An open trading economy such as Scotland's is a complex system and therefore care needs to be taken that focusing on one area does not cause greater damage elsewhere. This is not a reason to avoid making decisions but rather to make sure that they have been properly thought out and clearly explained.
16. There is a risk that countries will try and reduce their reliance on international trade by shortening supply chains and developing more national manufacturing capacity. There are certainly options for Scotland to do likewise but at the same time there will be constraints on what we can achieve over the short term. Even longer term, Scotland is likely to suffer if it were to try to create an economy which is too closed in on itself. Nonetheless, developing more industrial or manufacturing national champions could, in the right circumstances, be to our advantage. Scotland has been successful in attracting investment in the IT industry, both in terms of programming capacity and electronics. Building on these and other current strengths, for example in the areas of data science and machine learning, could be more effective than trying to develop new champions. However, we need to make sure that our economy is sufficiently diversified so that it is not overly reliant on a narrow set of skills which could quickly become redundant in a fast-changing world. There may also be opportunities to revitalise parts of the economy that have languished in recent years. This is not to propose a return to heavy industry but light electronics could be an area to look into.
17. To achieve this will require significant investment in education, especially in the STEM subjects, although not forgetting about the importance of a rounded education. Scotland has lagged behind some other countries in a few areas of education which might have an impact on the ability to make full use of the post-coronavirus opportunities that arise. Education may also need to be provided to those who would need to retrain to be employable in the growing sectors of the Scottish economy.
18. Ideally, Scotland needs to be a place where people want to come and live, work and raise families and that businesses wish to invest in. This means, among other things, having a world class education system and health and social care systems and a proportionate level of business regulation and taxation. Due to the fluidity of capital and also of people, Scotland is in competition for both the brightest and best people and for inwards investment. We need to build on our current strengths and look for other areas where we can compete internationally; recognising that this competition is not a zero-sum game but rather should be to the benefit of all parties.
19. We note that dealing with the aftermath of the Covid-19 pandemic is likely to present challenges around maintaining current productivity levels whilst 'social distancing'. This may result in the acceleration of some current trends to towards greater automation and use of IT. We view this as a potential opportunity boost to the productivity of the Scottish workforce through increased training in IT and computer programming although care has to be taken that greater automation does not simply displace jobs..
20. In addition to the IT sector, Scotland has a large financial service sector, although many of the companies in this sector are headquartered outside of Scotland. The Scottish Government may wish to

consider ways in which the financial services sector, while remaining profitable and providing good quality jobs, could be encouraged to help with the recovery and provide services across a much wider sector of society.

21. In deciding which sectors to support, consideration should be given to the export potential, particularly the future potential to export skills.
22. Scotland has a different demographic structure to much of the rest of the UK. Scotland currently experiences more deaths than births each year and currently relies on migration to maintain its working-age population. In recent years, this has been achieved by encouraging immigration into Scotland. With Brexit and now with COVID-19 related travel restrictions, this may not be so easy in future. To the extent that coming out of the recession that is expected to follow on from the COVID-19 lockdown requires a dynamic, energetic and imaginative population, it will be important to recognise the potential demographic challenges when considering appropriate policy responses.
23. Many firms have seen their profits and, in some cases, even the whole business collapse. This may deter future entrepreneurs from taking risks in future. Government can help by supporting start-ups, accepting that a number of these will fail but that others will go on to become successful businesses. The new Scottish National Investment Bank could have a key role to play here. Institutional investors could also be “crowded in” to support infrastructure and business developments if they meet their risk appetite requirements. This may also provide the Scottish government with some policy levers to direct private investment towards activities that will provide net benefits to society, for example, ensuring more greener companies, in terms of both operations and products or services provided, are established. This could also include enhanced reporting requirements around environmental, social and governance issues. These “green strings” could also be applied to any funding support provided to existing businesses emerging from the crisis, in the form of conditions attached to loans or grants. In particular, prudential regulation on financial services companies could be redesigned in a way to encourage greater investment in activity enabling economic recovery.
24. In assessing the potential impact of different options, the Scottish Government should be open to different economic models, such as that being explored in the Netherlands<sup>3</sup>, which may lay out very different paths for the future development of our society. The recovery from the crisis could be an opportunity to fundamentally adjust the economic model to best align with the changing needs of Scottish people and businesses.
25. In considering resilience of the economy in its recovery and in its longer term state, we may learn particular lessons from the impact of this current crisis which appears to have caught many countries off guard. Actuaries practising in the financial sector are familiar with assessing risk through quantitative modelling but also through the use of skilled qualitative assessments and wide-ranging extreme ‘scenario tests’. These aim to understand exposures of entities (insurers, banks, pension funds etc.) to events which appear highly improbable but which might cause extreme impacts. It is unlikely to be wasted effort if specific resources were dedicated to thinking deeply about as-yet unseen risks and following the likely impacts through various facets of the economy and society. This would give any government additional comfort and confidence in the robustness and resilience of any chosen pathway.

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<sup>3</sup> <https://www.kateraworth.com/2020/04/08/amsterdam-city-doughnut/>

## Micro/ Enterprise

**Different sectors and businesses will be impacted in different ways. What are the medium- to long-term consequences of the lockdown on businesses, including loss of employees, debt overhang, loss of markets, reduced investment and unemployment?**

27. It is clear that the immediate impact on businesses across the whole of Scotland is likely to be pretty severe. What is not so clear is what will happen in the medium to longer term. A number of businesses will not survive, but some will be replaced by new entrants. Others will survive, at least for some time, but with additional debt obligations and may not be able to survive in the longer term if the economy does not pick up. In the same way as there is a fear of a second wave of the virus following the opening up of society, there could be a second wave of companies and businesses going under in 12 to 18 months' time. These second wave failures will include city and town-based small retail outlets who may have a reduced level of business if people remain working from home and use larger supermarkets in person or via their delivery services for their food requirements.
28. There could be a loss of productivity in many industries as a result of social distancing measures and parents having to look after children while working at home. This could stoke inflation or lead to a loss of international competitiveness. Maximising productivity will be important in facilitating the recovery, particularly in light of the demographic challenges referred to in the previous question.
29. Impacts within Scotland are likely to vary in severity. Rural areas and the areas of greatest deprivation in and around Glasgow, Dundee and parts of Edinburgh will experience the most severe economic shocks. Policies to promote appropriate training and the availability of decent work should be made a priority.
30. The Government has a clear role to play in encouraging lending and risk taking, perhaps taking some of the risk itself although avoiding undue moral hazard. There will be many opportunities to support small scale operations although this will require that the funders are close to where the needs are and spread widely across the whole of Scotland and not concentrated only on our major cities.

## Labour Market and Inequalities

**The crisis will impact differently on different groups in society, and on different parts of the labour market; and, has already revealed some thorny issues about relative wages across key occupations. What will the implications of the recovery be for different groups, unemployment and on the nature of work? How is the recovery likely to impact on socio-economic inequality as a whole?**

31. These are crucial questions that don't unfortunately admit of easy answers, at least not in the short term. Public support of key workers during the crisis may not extend uncritically to the post crisis situation and it cannot therefore be assumed that there will be political support for radical changes in wage differentials. It will be important to look at a long-term horizon when making policy decisions, something many actuaries are used to doing in the daily work.
32. We think that investment in education and skills should continue to be at the heart of the Scottish Government's strategy. This should include retraining in IT and digital skills for those that have lost jobs and livelihoods as a result of the pandemic. For those for whom retraining is not possible, additional support should be given. Having a well-trained workforce will attract companies to want to base their operations in Scotland and the Scottish Government can facilitate both the entry of international companies and new local start-ups. Given the greater experience that many people have had over recent weeks of providing and using online material and activities, there is likely to be greater scope for providing good quality education to a wider range of people by harnessing the power of technology. We acknowledge though that not everything can be taught online and that not everyone will have access to the hardware needed to access online courses and training. Care should be given to ensure that sections of the population are not increasingly disadvantaged due to digital poverty.
33. With regard to investment, be it in education and skills or infrastructure, Scotland's relatively small geographical size means that it may be possible to promote a diversification in the locations for deployment of investment in the economy. This would support areas beyond the two main cities and bring the expected benefits to a wider and more diverse population. This may also consequently lead to a more stable and diverse economic base, spread more evenly (and equitably) across the whole country and potentially with positive implications for local communities in relation to internal migration and population decline.

## Wellbeing, Inclusive Growth and Net Zero

**What can be done now to ensure the transition to a wellbeing-oriented, inclusive economy on a transition to net zero. How can the wellbeing of the people of Scotland flourish and how can a wellbeing economy approach be embedded to bring distinct benefits to Scotland?**

34. As a first step to achieving a wellbeing-orientated, inclusive and net-zero economy, it will be necessary to articulate clearly how these can be translated into specific, measurable, achievable and realistic targets
35. We need to develop ways of measuring progress in meeting these targets that are objective, transparent and published regularly, with politicians and civic leaders taking responsibility for outcomes. These targets and measures need to have broad support across the whole of society so that they are not subject to change.
36. Even an economy as small as Scotland's is difficult to turn around in a short period of time, therefore we are not going to achieve these goals overnight. In the same way as we have a phased approach to getting out of the lockdown, there could be a phased approach to achieving a recovery.
37. Given the challenges facing the Scottish economy, there may well be significant headwinds in trying to achieve such a wellbeing-oriented, inclusive net-zero economy. It needs to be costed out and the way of paying for it needs to be made clear so that there is social consensus. There may be some fiscal and monetary headroom for additional spending or keeping taxes at their current levels but robust economic analysis will be required to ensure that whatever financial decisions are taken do not lead to high inflation or a languishing economy. In the transition to a green economy maintenance of a secure and robust energy supply will be crucial.
38. Improving the public transport system will both be important in getting a greener economy, even if more people are working from home. Scotland's transport system, even within larger hubs such as Glasgow is uncoordinated. The model of transport for London which integrates rail, bus and underground could be applied across the whole of Scotland and a contactless payment system introduced across the whole of the system. Reaching the more remote parts of the country including the islands will need to be part of this plan. Connected with this would be to encourage the greater use of bicycles through city-based cycle schemes and cycle to work schemes.
39. To support more home working there is a need to ensure the reliability and speed of the broadband infrastructure. Care should also be given to ensure that this does not increase the some of the lifestyle changes brought about by the pandemic could improve wellbeing but this will need to be assessed carefully as any short-term benefits may be outweighed by unforeseen longer-term problems. For some people, home working has been beneficial while for others it may not have been possible or has been problematic. Care has to be taken that trying to entrench new ways of working does not exacerbate existing inequalities or reduces access to decent work and livelihoods.
40. It may be appropriate to consider whether it would be possible to bring forward planned changes in building regulations to make the housing stock more energy efficient, or to focus investment on retrofitting existing housing stock to accelerate change at a domestic level.

## Government, Policy and Delivery

**There will be big changes in the form, nature and interactions between different institutions. How will the crisis change the role and relationships between the UKG/SG/LAs, business and other institutions?**

41. This question goes to the heart of what we expect the relationship between government, institutions and civil actors to be in future. We may, however, find that things change far less than we might expect, and so we should be prepared for this as well. Previous crises, e.g. the two world wars, the depression of the 1920 and the depression of the first decade of the 20<sup>th</sup> century lasted longer and may have had a limited direct impact on social relations. However, the years following the Second World War were a time of significant social changes, with the introduction of the NHS and significant educational reforms among other developments, the war was possibly a catalyst rather than a direct cause of the change.
42. One of the few, potentially positive aspects of the pandemic has been the re-blossoming of local community spirit. The need for isolating vulnerable people to receive food and medical supplies has often been met by family and community groups. This localisation of support networks is something that ought to be encouraged. There may also be an opportunity to capture the current sentiment in the population for the benefit of the wider society: Many of those who end up suffering less financial hardship as a result of this crisis may be willing to forego some income and/or wealth in recognition of their particular good fortune in these extreme times. The Lockdown has been a great leveller across society as the traditional trappings of wealth (e.g. greater consumption) have been much less accessible while much of the population has been focused on the fundamentals of daily life. This may lead to greater support for a marginally higher tax burden across society or a marginally more progressive tax structure or both, particularly if it can be shown what specific benefits the additional revenues would support
43. The current crisis could be a catalyst to get institutions at various levels talking more openly with each other and sharing knowledge and learning to avoid each one having to develop their own solutions to the similar problems they face. To the extent that such forums do not self-organise, Government could seek to convene appropriate groups in order to facilitate the necessary dialogue.
44. There may need to be an open discussion about the need to do more with less or quite limited financial resources.
45. As mentioned previously, education will be vitally important in supporting a strong recovery. Colleges and Universities should be encouraged to focus on providing training to develop skills that are relevant to growing areas of the economy in each region. This will facilitate an increasingly strong pool of workers, with the skills relevant to support local recoveries. Colleges and Universities could also have an important role to play in retraining those who find themselves out of work. With the potential reduction in funded students arriving from the EU following Covid-19, the Government may have the opportunity to redistribute funding in order to up-skill parts of the current working age population.

## Lessons/Data Insights

**The pandemic is a shock which will provide insights and data across a range of areas. How do we ensure that we learn from the impact of the crisis and respond accordingly?**

46. The pandemic and more particularly the policy responses that followed, both in the UK and globally, have been significant shocks to the economy and society more broadly. Gathering and analysing data, both qualitative and quantitative, will be important. However, what will also be important is to have perspective. For example, the impact of more home working may have short term effects but also longer-term ones which may be quite different.
47. The IFoA and its members have been very active in providing and helping to interpret data relating to the health impacts of the coronavirus. The IFoA has set up a network of over 550 volunteers willing to apply their professional skills in this area. There is an active C19 Actuarial Response Group on LinkedIn that has been producing well-regarded newsletters. The IFoA's Continuous Mortality Investigation Bureau is producing a weekly update on mortality statistics<sup>4</sup>.
48. It would though be worth analysing the impact of the daily provision of data on cases and deaths. Has this coupled with the broader communication efforts of the Scottish Government strengthened people's trust in governments or has the difficulty in making national and international comparisons and hearing different scientists take different positions, cause a reduction of trust?
49. One area of trust that may need to be restored is precisely over the care for the elderly and vulnerable. The high number of deaths in care homes and comments, from some scientists, that COVID-19 deaths are just a short acceleration of the inevitable will have given the impression that in fact there is a lack of real concern for the more vulnerable members of our society. A recent video on the IFoA website<sup>5</sup> refutes this argument.
50. It will be important to commission longitudinal cohort studies of young people affected by not being able to go to school, college or university and having to learn online. Similarly, research should be done into the mental health issues arising as a result of lockdown.
51. We see the greater use of technology as one of the benefits to come out of the current situation. It has forced organisations and individuals to embrace new ways of working and socialising.
52. Over time if there is a significant recession and many people suffer financially and in their overall well-being, the decisions taken regarding the lockdown to protect the NHS and vulnerable people may begin to be seen in a different light. It will be important to reflect on the outcomes of the virus and the lockdown over the longer as well as the shorter term.
53. Life and health insurers can, through the provision of insurance products, contribute to making society more robust in the face of future perils although this will require greater understanding on the part of the public of the need to protect themselves against future financial shocks. This is where developments in financial education would be invaluable.

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<sup>4</sup> <https://www.actuaries.org.uk/learn-and-develop/continuous-mortality-investigation/other-cmi-outputs/mortality-monitor>

<sup>5</sup> <https://www.linkedin.com/school/the-faculty-and-institute-of-actuaries/videos/>