



Business School

Never Stand Still

Business School

Risk and Actuarial Studies

# Investments (in small developing nations)

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# Agenda

Background and some principles

Our role in investment governance

Getting hurdle rates right

Caribbean issues and options

“All men are ready to invest their money  
But most expect dividends.  
I say to you: Make perfect your will.  
I say: take no thought of the harvest,  
But only of proper sowing.” TS Eloit

# The Structure of the Financial Sector

## Standards:

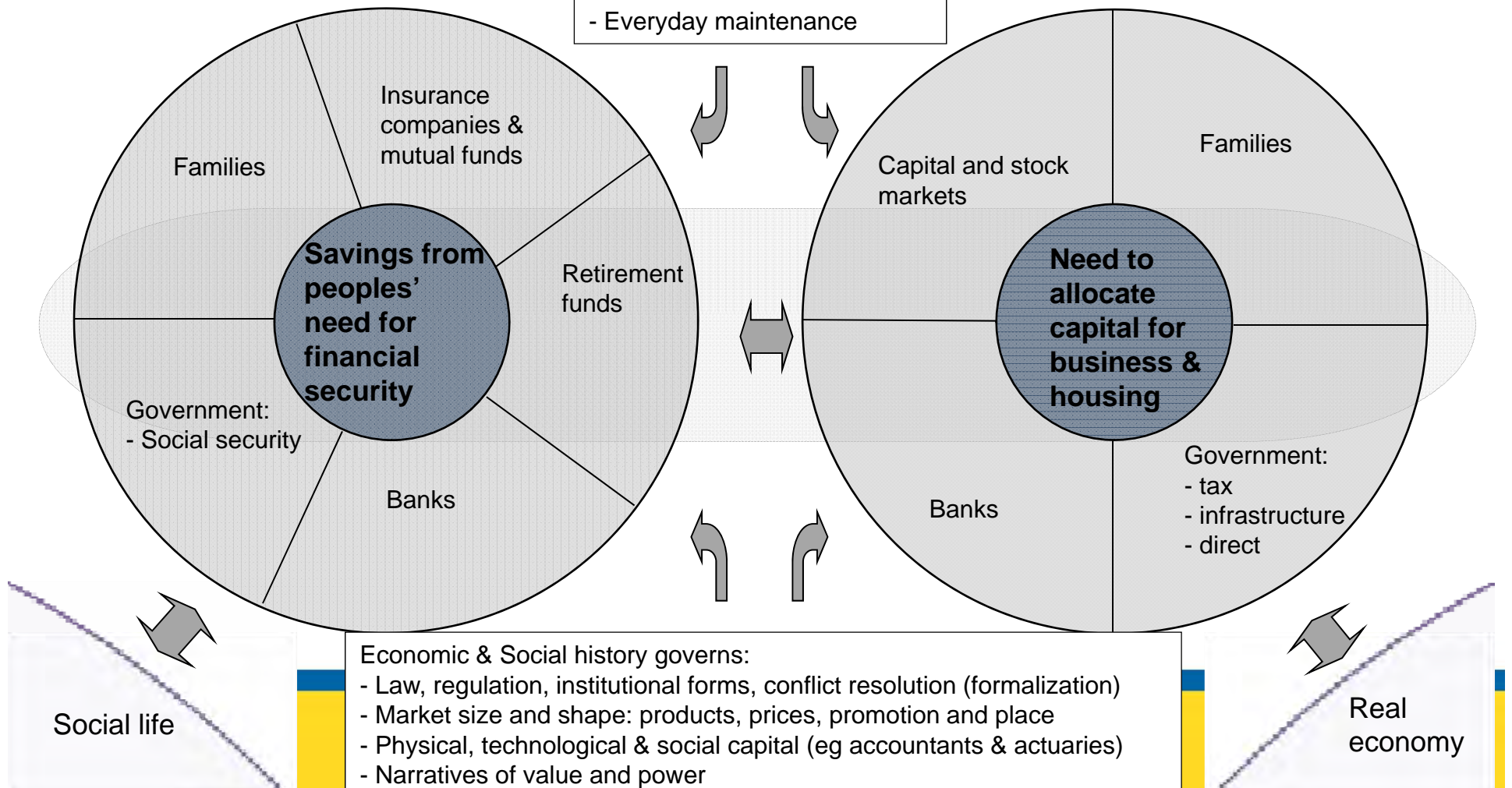
- Just: freedom & equality
- Effective & efficient
- Robust

## Systematic risks:

- Economic (Oil, China ...)
- Societal (Families, war ...)
- Physical (Global warming ...)

Personal initiatives:

- Entrepreneurial
- Ethical
- Everyday maintenance



# Financial Institutions and Investment

Actuaries are involved in financial institutions that mobilize savings.

The savings have to be invested:

- but there are risks
- and potential unintended economic and social consequences
- if the investments are not controlled appropriately.

The aim is to first to ensure that they are applied:

- Such that the proceeds are available when needed - by beneficiaries (savers and pensioners)
- In line with the beneficiaries have preferences as to risk / return tradeoff
- Productively
- Minimizing (negative) externalities
  - Impact on company governance
  - Environment, labor security and productivity.

# Justice – applied to investment

Blindfolded - to  
personal and  
vested interests

Swathed  
woman with  
scale  
emphasises  
process

Sword  
indicates  
legitimate  
power



"Justice is the bond of society ... the condition under which I and every man can identify with society, feel at one with it, and accept its rulings as my own." JR Lucas

## In the scales:

- All the stakeholders
  - Capital markets
  - Companies in which invested
  - Taxpayers
  - Government
- Major criteria
  - Just deserts
  - Liberty
  - Equality
  - Individual need
  - Efficiency

# Actuarial role in investment governance

Ensuring that all expenses and returns are fully reported

- Conflicted payments to service providers
- Secret profits from custodians
- Compare with market rates / VWAP

Benchmark with local and international peers

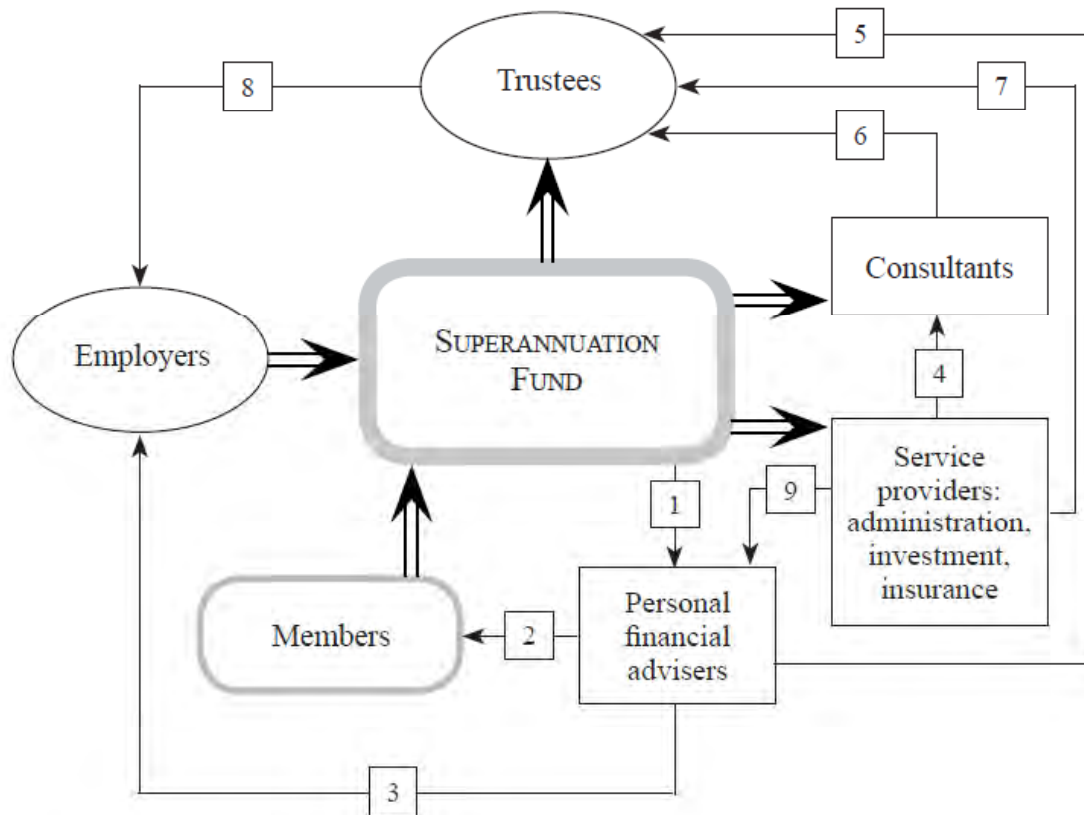
Risk framework reporting and compliance

Asher, A (2016) Efficiency and Competitiveness of the Superannuation System – Issues Paper/March 2016  
[http://www.pc.gov.au/\\_data/assets/pdf\\_file/0003/198075/sub021-superannuation-competitiveness-efficiency.pdf](http://www.pc.gov.au/_data/assets/pdf_file/0003/198075/sub021-superannuation-competitiveness-efficiency.pdf)

Institutions should protect their contractual rights

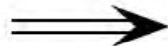
- Strict covenants for loans
- Adequate power to elect directors for equity (proportional representation)

# Conflicted payments



Key:

Essential cashflows



Potentially conflicted cashflows

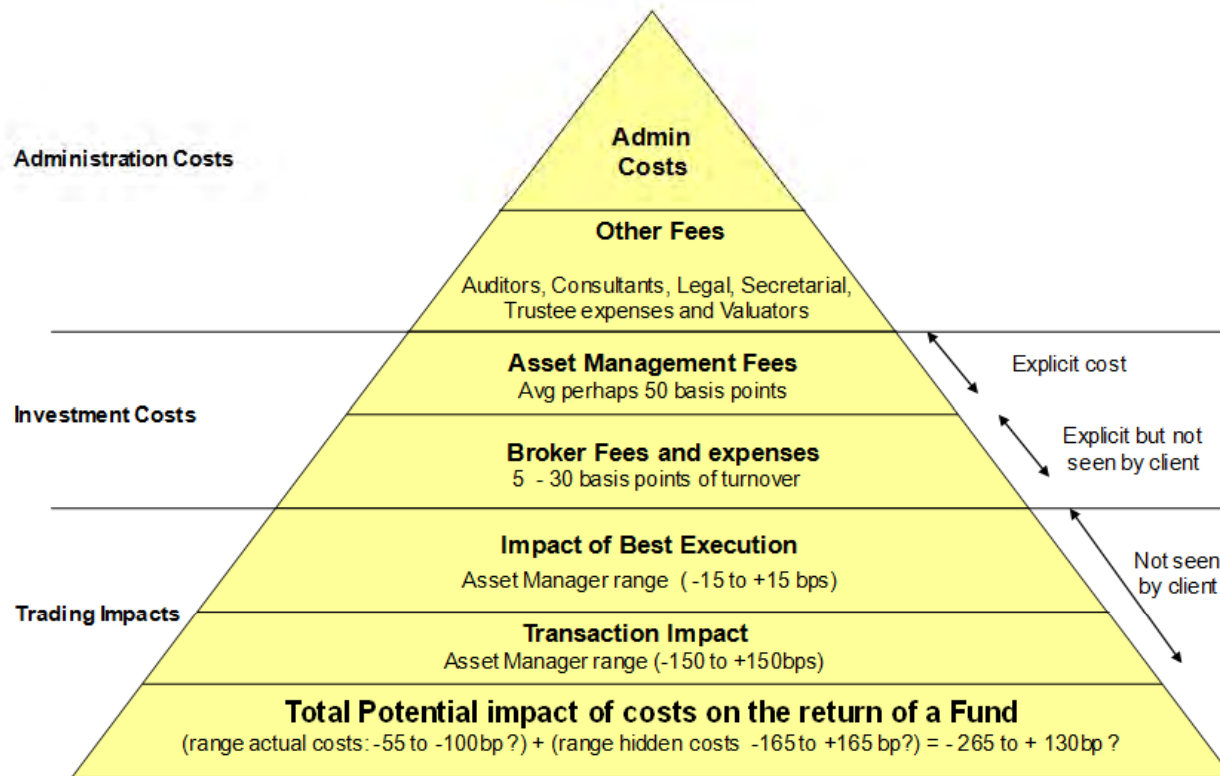


Asher A (2008) "Conflicted super structures: Are Australian Investors being Short-changed", in Pension Fund Governance Ed Evans, J, Orszag M and Piggott J Edward Elgar



# Creating transparency

## Explicit and Implicit Costs



Source: Deloitte/Telemetron



# Getting hurdle rates right

Setting hurdle rates higher than the cost of capital means that viable projects are turned down

This is worse for longer term projects – with long term renewable energy particularly important

The problem of short-termism appears to be getting worse, and the response to lower interest rates is slow.

<http://www.rba.gov.au/speeches/2015/sp-dg-2015-05-18.html>.

[www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2011/speech495.pdf](http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2011/speech495.pdf)

Lewin C.G., A. Carne, N. F. C. De Rivaz, R. E. G. Hall, K. J. Mckelvey and A. D. Wilkie, (1995) “Capital Projects” *British Actuarial Journal* 1.2 pp. 155-249.

# Caribbean issues

Very different from large developed economies:

- Economies are small, less formal, relatively undiversified and more volatile
- Investment markets are small and necessarily illiquid, which means that voice is more important than exit when making investments
- Large rural and informal sectors inhibit specialization, has limited access to law and capital
- Skills are in short supply – in government and industry
- There are fewer autonomous centres of power, which means that governance is more easily subject to corruption or expropriation

Investors would like to invest overseas to diversify

A great need for local investment

# Caribbean options?

Acknowledge need for diversification of political risks:

- Membership of international funds
- Legal overseas investment

Active in sourcing international investments for local economies:

- Need strong local governance protection for international investors
- Support local regulators
  - Close links to CAS / IAA
  - Ask for help
    - Retired actuaries (See movie: “About Schmidt”)
    - Actuaries wanting to give back (Actuaries Without Borders)
- Highlight diversification opportunities
- Look for opportunities to create formal investments

Thanks to Kyle Rudden for suggestions

# CARIBBEAN VULNERABILITIES



*ECONOMIC COSTS OF A CHANGING CLIMATE IS PROJECTED AT \$10.7 BILLION ANNUALLY BY 2025, \$22 BILLION BY 2050 AND \$46 BILLION BY 2100 OR 5%, 10% AND 22 % of GDP WHICH IS EQUIVALENT TO CAUSING A PERPETUAL ECONOMIC RECESSION IN EACH OF CARICOM MEMBER STATES*

[http://www.oas.org/en/sedi/DSD/Biodiversity/Sustainable\\_Cities/Sustainable\\_Communities/Events/SC%20Course%20Barbados%202015/ModuleII/Yolanda%20Alleyne%20AS%20-SUSTAINABLE%20CITIES%20Workshop%20Aug%202015.pptx](http://www.oas.org/en/sedi/DSD/Biodiversity/Sustainable_Cities/Sustainable_Communities/Events/SC%20Course%20Barbados%202015/ModuleII/Yolanda%20Alleyne%20AS%20-SUSTAINABLE%20CITIES%20Workshop%20Aug%202015.pptx)



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# A Caribbean vision?

Educated population

Jobs for everyone

Families live together in their own homes

Financial security with three pillar retirement system

Clean, efficient urban areas – with access to the country

Power widely distributed

The elements of action

- Personal vocation
- Mutual collaboration

....

# So what do we build?

“The good man is the builder, if he build what is good.  
I will show you the things that are not being done,  
And some of the things that were long ago done,  
That you may take heart, Make perfect your will.  
Let me show you the work of the humble. Listen.

In the vacant places, we will build with new bricks  
There are hands and machines, and clay for new brick  
And lime for new mortar.

Where the bricks are fallen we will build with new stone  
Where the beams are rotten we will build with new timbers  
Where the word is unspoken we will build with new speech  
There is work together:  
A Church for all and a job for each

Every man to his work!

# CIRCLE OF ACCOUNTABILITY

