

Should The Government Regulate Risk Taking?



How much risk was this woman taking? How would one measure it? There were 40 some people in our group when my wife had this picture taken and nobody got gored. So, was this a riskless transaction? Just because you don't know how to measure it doesn't mean it wasn't risky. That goes for Rhinos and hedge funds and treasuries. Yes, investing solely in treasuries will guarantee failure to produce the needed retirement income for over 90% of retirees. That is a hidden risk. Risk is situation specific and should be related to what is at stake. Default risk is not what is at stake when investing in treasuries.

When we check into a hospital we know full well they are full of germs, viruses and sick people. We also know that people are dying every day in hospitals, sometimes from infection but sometimes we hear that the operation was a success but the patient died. Those are the risks that society is willing to take because we all know there would be a lot more deaths and illnesses without them. It is not society's duty or responsibility to eliminate risk associated with medical care. That risk cannot be eliminated but it can be managed by ensuring that hospitals meet certain standards and that the staff and physicians have the proper credentials. What patients

should expect is that the action taken by the physician is consistent with the diagnosis and the diagnosis determines the necessary amount of risk.

Similarly, there is always a certain amount of risk associated with investing money and some portfolios die every year. But those who now want to terminate 401(k) plans and replace them with a government plan that guarantees 4% ignore the relevant risk, that most people will never be able to retire with dignity unless they earn more than 4%. The Government should not attempt to regulate something they are not trained to understand. Removing the tax deductibility of 401 (k) plans for an inadequate guarantee would hurt more hard working investors than the financial crisis of 2008; except that it will take them a lifetime to discover it. The key is to require a professional diagnosis of the client's needs and investible assets and ensure that the actions taken by the financial advisor are consistent with that diagnosis.

I believe this approach will eventually lead to a more professional way of attending to the needs of investors and the health of their portfolios. Framing all investment strategies as an asset management problem should eventually give way to a framework that recognizes most investments are made for some future payout.