

Prevent the Next Crisis: Demand Risk Management Education

by Etti Baranoff

Our financial celebrities and biggest Wall Street earners have long been identified by their ability to generate windfalls. In the midst of our present dire circumstances, a key question emerges: Shouldn't we place the same star status on those who prevent disaster?

Does it astonish anyone, in light of the mess we have seen on Wall Street, that most business schools do not require students to take risk management classes? Is it remotely surprising that graduates of most university programs never learn a valuable shred about how to manage risk?

Many of these grads are the financial wizards who have brought us credit default swaps and mortgage-backed securities. It is clear that these innovative minds and their managers delivered risky products to the financial markets without risk management actions.

Why? Perhaps because they did not have the opportunity to learn the art of managing and mitigating risks. They created the bundling of mortgage-backed securities as towers of cards. The bottom card – the quality of the borrower – was insufficiently checked, underwritten or verified. The card was pulled away, and the tower crumbled.

Was it willful blindness? No. Smart people would never undertake such risks voluntarily. It was ignorance.

These technicians, the Wall Street modelers who arrived from the quantitative fields to change our financial landscape, used risk measures in their pricing of new financial instruments, but that was far short of sufficient. They did not play the devil's advocate's role and do a genuine scenario analysis, which is central to an effective evaluation. Even worse, they did not create risk mitigation tools for avoiding collapse. Neither did their managers and regulators, who did not know what questions to ask.

What we saw was the following: In finance and

asset accumulation and management, no underwriting took place. Mortgages were given to the unqualified. Underwriting of risks ceased to exist. Banks and mortgage companies did not behave cautiously. Some ceased to even utter the word underwriting, as if it was a term that belonged only to insurance. The operators who bundled these mortgages did not check the premises of the bundles.

So little basic prudence for such high stakes.

With all of the emergency solutions and the political haggling designed to avert a possible depression, the biggest call for clarity of our future should be: Demand and ensure that our educational institutions teach the capacity

to understand risks and the tools to mitigate them.

Few universities around the country have risk management and insurance majors or concentrations in their business school curriculum. Most are large state universities. The business world, eager for some intelligence in risk understanding, underwriting, evaluation and mitigation, snatch these graduates fast.

However, these grads too often do not become the ballyhooed gurus of Wall Street – the ones with the fawning profiles and kingly compensation — and that is reflected in academia, where no risk management education is a mainstay.

Accreditation bodies demand aspects of ethics and global studies in university courses. Both are important. But it is risk management that is our best bet of averting another calamity in the fast-moving, incredibly complex financial system of our day and age. It should join them as a required component of any business education.

We must overcome a deep misunderstanding of risk management that is frightening in its persistence. ■

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