



u21Global
Graduate School For Global Leaders

Risk Management

**What was never taught
in the classroom**

Acknowledgement:

The Black Swan – Nassim Nicholas Taleb

Presented by Mrinmoy Das

- Before 1606, Europeans believed that all swans were white.
- In 1606 Australia was discovered.

- **History is what is narrated by observers**
 - Holocaust during World War II
 - Did it happen?

- **Events are observed not causes**
 - 5 star dining experience
 - Don't go into the kitchen








- **The illusion of understanding**
 - World is too complicated
 - CEO of a big bank understands the banking business
 - Jerome Kerviel happens

- **The retrospective distortion**
 - Credit crises was inevitable?








- **The overvaluation of factual information**
 - The Curse of learning

- **Scalable events are disproportionately larger than their cause**
 - J K Rowling's books
 - Madonna's albums
- **Non-scalable events are proportionate to their inputs**
 - Dentists
 - Brain Surgeons
 - Risk Managers

Mildly Random

-  Non-scalable
-  Typical is the median
-  Winner takes a small share
-  Subject to known constraints
-  History crawls
-  Normal or similar distributions
-  Easy to predict

Wildly Random

-  Scalable
-  Atypical: giants or dwarfs
-  Winner takes all
-  Not subject to constraints
-  History jumps
-  Mandelbrotian or intractable
-  Hard to predict

- We seek evidence to confirm our theory
- We focus on pre-selected segments of the seen and extrapolate to the unseen
 - “Most rich people are intelligent”
 - “Most intelligent people are rich”

■ Life of a turkey – Bertrand Russell

But in all my experience, I have never been in any accident ... of any sort worth speaking about. I have seen but one vessel in distress in all my years at sea. I never saw a wreck and never have been wrecked nor was I ever in any predicament that threatened disaster of any sort.

E. J. Smith, 1907

Captain, RMS *Titanic*

A BIRD IN THE THE HAND IS WORTH TWO IN THE BUSH

- “Stocks have gone down”
- “Stocks have gone down due to FED raising rates”
- Human beings are naturally pattern seeking

- **Frederic Bastiat's Broken Window Fallacy**
"What we see and what we don't see"
- **What we see:**
"High Oil prices are bad for the economy."
- **What we don't see:**
"High Oil prices have reduced green house gases, reduced global warming, created new industries, forced us to rationalize our energy usage and saved the lives of inhabitants of tiny Pacific atolls from flooding."

- Lets play a game: Let's toss an unbiased coin
- For the first 27 tosses, we get heads.
- What is the probability of getting a head in the next toss?

Don't believe everything you are taught in the classroom or read in the textbook.

Think for yourself.