© *The Journal of Risk and Insurance*, 2008, Vol. 75, No. 4, 1081-1085

Book Reviews

Reforming Early Retirement in Europe, Japan and the USA, by Bernhard Ebbinghaus, 2006, New York: Oxford University Press. Pp. xvii + 331.

Reviewer: Norma L. Nielson, Chairholder in Insurance and Risk Management, Haskayne School of Business, University of Calgary, Canada

The author of this book, Bernard Ebbinghaus, is described on its jacket as a Professor of Macrosociology. Although my computer's spellcheck does not care for that term, it does provide a very accurate description of the perspective that permeates this book. For example, the book purports to examine both macro and micro views. However, the author defines these terms from an extremely high level with his macro view looking at global trends and national economies. His micro view, which differs considerably from how that term might be used by an economist, considers the role of the private sector in an extremely broad sense. In some instances he discusses the experience of a specific industry, but most discussions concerning the private sector role aggregate the impacts of all employer-sponsored benefit plans. The micro views presented in this volume do not examine data regarding individuals.

That said, the book is built on the extremely solid premise that both supply and demand matter. Separate chapters examine the pull factors generated largely (but not exclusively) by government policies and programs and the push factors generated largely by the need to maintain and enhance productivity in firms. Ebbinghaus explicitly examines whether early retirement serves primarily the interests of firms—at the public's expense. Although that is sometimes evident, he finds that the expansion of retirement at increasingly young ages in many countries is the result of unintended consequences of social policies for older workers. Following an extensive comparative-historical analysis of the evolution of early retirement, he rejects *both* the one-sided views put forth by authors who argue that the trends in early retirement are explained fully by the pull factors (e.g., the introduction of external incentives into the labor market that he calls "politics against markets") and the views of other authors that push factors (e.g., firms' efforts to remove less productive workers from their workforce in a "politics for markets" explanation) fully account for the trend. Simply stated, his work strongly supports continued belief in the previously stated premise: that both supply and demand matter.

The overarching and well-supported conclusion is that it is the multiple pathways that have been created—separate policies designed to deal with unemployment, disability, and retirement—that played an integral role to the extraordinary expansion of earlier exits from the labor force. Furthermore, it is those multiple pathways that have made it extremely difficult for subsequent attempts to unwind that trend to produce any meaningful reversals.

This book is well researched and contains a wealth of global data. There are occasional instances where the reader will notice that the book is not written by a native English speaker, but these in no way limit the book's contribution. The policymaker looking for a simple solution will, however, be disappointed. Ebbinghaus concludes (p. 78) that "there is hardly a 'best solution' for all systems. Even if there were, each nation state will have to pursue a particular path given its different starting position."

Risk Intelligence: Learning to Manage What We Don't Know, by David Apgar, 2006, Cambridge, MA: Harvard Business School Press. Pp. ix + 210. ISBN: 978-1-59139-954-4

Reviewer: James Jackson, University of Illinois at Urbana-Champaign, IL, USA

In *Risk Intelligence: Learning to Manage What We Don't Know* (2006), David Apgar develops a framework of risk management best practices for nonfinancial firms, based on his experience as a financial firm risk manager. Throughout the book, Apgar translates and applies financial risk management methods to general business risk management. Based on his research findings, Apgar asserts that by separating financial from nonfinancial risk management techniques, business managers will improve their decision-making processes, as well as the end results of their respective decisions in a world of growing risk and uncertainty.

Throughout *Risk Intelligence*, Apgar presents his arguments in a readable fashion toward the general business risk management audience, although others will certainly benefit from the ideas presented. Stories, examples, risk management theory, and best-practice methodologies provide readers with an examination and critique of current risk management methods and provide steps for action to correct the flaws that currently exist in the methodology that is presently being employed in the world of business. In each chapter of the book, Apgar first presents a research question or problem, followed by an answer or solution as it relates to risk management methods for nonfinancial risk managers. The author clearly defines the terms and definitions presented in each chapter, gives examples to support his argument, and offers a solution that is both practical and theoretically sound. The logical manner in which the information is presented contributes to a greater understanding of the arguments presented and aids in the overall readability of the book.

In the first chapter, "Changing Your Approach to Risk," Apgar relates the story of a businessman who seemed to be randomly affected by both the start and the conclusion of the U.S. Civil War in order to illustrate the seemingly unpredictable and uncontrollable nature of risk. According to the author, even though risk may appear to be unpredictable and uncontrollable, it is in fact manageable. Apgar defines risk as "the possibility of a loss or reversal—or gain or advance—different from what we expect from a decision or an activity" (p. 11). But, equally as important as Apgar's definition of risk is his assertion that managers should be concerned with risks that affect them and their firms the most. Based on this framework, the author then enumerates what he defines as the "four rules of risk and the myths that each of these rules explode" (p. 13) in the subsequent chapters of the book.

In "Separating Learnable Risks From Random Ones in Business Decisions," Apgar refutes the myth that "all risks are random" with his first rule, which states: "recognize

which risks are learnable" (p. 14). In this chapter, the author draws the key distinction between nonrandom, learnable risks, which can be managed through increased knowledge and information, and random risks, which are stochastic in nature (p. 26). To illustrate this point, Apgar uses the example of the early 2001 jumbo jet development competition between Boeing and Airbus to demonstrate the concept of the economics of learnable risks. In this episode, Boeing ended up canceling a 3-year development plan because Boeing senior management was unable to estimate the ability of Airbus to design jumbo jets and because it doubted its own ability to understand the competitive market forces at work in the this lucrative market. While Boeing struggled, Airbus proceeded to win contracts from major Asian airlines at least partly due to the fact that Airbus management seemed to understand how to assess market risks, how to address the evolving needs of potential customers, and then how to proceed accordingly. In the end, the loss of this competition and its economic cost caused Boeing CEO Phil Condit to step down from his leadership position.

Apgar argues that the economic cost of capital to any given firm can be reduced by developing strategies that reduce the uncertain nature and magnitude of the risks facing the company by increasing the risk assessment ability of business managers (p. 42). Apgar asserts that nonfinancial risk management and its economic cost of capital needs to be measured as a relative factor. Learnable risk management varies depending on who is making assumptions and analyzing the information. Therefore, the outcome of risk management methods depends not only on what the company does but what the company's competitors do as well (p. 56).

Next, in "Scoring Your Risk Intelligence (or Risk IQ)," Apgar explains and provides methods that relate to his second rule, which is to "identify risks you can learn about fastest" (p. 64). In this chapter, Apgar recommends that the business manager identify which type of risk assessor he or she is based on the strengths and/or weaknesses of the three stages in the life cycle of risk assessment skills and experience (p. 93). According to Apgar, impressionists', encyclopedists', and amnesiacs collect, retain, and recall risk assessment information in different ways that can improve the overall risk intelligence score of the firm, and, if used properly, can reveal patterns of risk assessment that can be detrimental to the overall risk profile of the firm (p. 83). By following this identification method, Apgar contends that the risk managers of the firm can use a Bayesian probability framework that takes into account new information or evidence that can support or refute a given hypothesis. Apgar's goal is to use the risk intelligence score to provide a tool that can account for the evidence that can alter the Bayesian probability of a given business scenario (p. 103).

In "Conducting a Risk Strategy Audit," Apgar explains the methods for implementing his third rule, which is to "sequence risk projects in a learnable pipeline" (p. 107). In this chapter, Apgar provides examples to support his argument in favor of conducting risk strategy audits by describing the steps of conducting audits, which units of the firm should conduct an audit, and four distinct risk strategy patterns. The overall goal of the risk strategy audit is to identify learnable risks and to learn about new risks faster.

Additionally, Apgar offers four risk strategy patterns named winter, spring, summer, and fall, which correspond to the different development phases of a firm from a start-up to a conglomerate to a mature firm that dominates the market share of the industry to a firm that is mature but has risk threats to growth and or market share. For each of these risk pattern strategies, or seasons, the author provides a characteristic description, an example of the problems that a given firm is likely to face due to these seasons, and a solution to each of these likely problems.

Continuing the development of his risk management strategy in "Building Networks That Can Adapt to Risk," Apgar first describes the problems identified by employing a learnable risk management methodology and then offers the solution of knowing which learnable risks can be understood and tracked properly. The author's problem and solution identification methodology leads to the development of Apgar's fourth rule: "keep networks of partners to manage risks." The goal of the fourth rule is to divide known risks into those that are random and those that are learnable.

To demonstrate how his fourth rule should be implemented, Apgar states that the network should be composed of more than simply a casual two-way relationship with like-minded partners, but rather with strong allies positioned throughout the business marketplace. The network exposure is driven by two risk-role factors of "how well you can diversify the exposure" and "the breath of the exposure to the risk" (pp. 145–146). These two factors combine to form Apgar's risk ecology, which is the network of business partners and counterparties that are affected by common related risks. Once the risks have been sorted and the pipeline of learnable risks and risk network has been constructed, Apgar asserts that this structure should be used by managers to identify where a competitive advantage lies and can be taken advantage of by the firm at the expense of its competitors (p. 145).

In the final chapter, "Raising Your Risk Intelligence Systematically," Apgar summarizes his story of risk by asking, "how learnable and random risks differ" (p. 183) and then listing and distilling the 10 steps of his story of risk. The list starts with "step one: choose projects, problems, and ventures with learnable risks in mind" (p. 184) and concludes with "step ten: look for opportunities to break the compromise between risk and growth" (p. 196). Of all of the steps in his list, the second step is perhaps the most significant because, according to Apgar, if strategists take the time to measure and score their respective risk intelligence profiles, the firm will be better able to match the key trade-off between growth opportunities and risk management.

The significance of the second step in the story of risk is that Apgar completes his discussion of risk intelligence by returning to the foundation of investment and business management in the current world of increasing risk and uncertainty. The foundation of investment management revolves around the key trade-off between risk and return, while the foundation of business management revolves around the trade-off between risk and growth. Knowledge of these tradeoffs is significant. As Apgar accurately observes, if business firm managers mismanage the key trade-off, then a given firm runs the risk of either underperforming due to the possibility of high-growth companies taking on unnecessary risks and gaining little additional growth, or high-risk intelligence firms continuing to operate in low-growth industries or sectors that provide little opportunities for growth.

Risk Intelligence is recommended for those who are presently practicing risk management and/or studying nonfinancial business risk management methods at the graduate school level. The author's critique of the current use of value-at-risk (VAR) methodologies and other risk management strategies is consistent with recent articles in *The Economist* (2007a,b) and *Plight of The Fortune Tellers* by Rebonato (2007), both of which discuss the limitations of the use of the VAR methodology, as well as overly complex quantitative methods that are designed for the purposes of employing risk management techniques and achieving risk reduction outcomes.

Throughout *Risk Intelligence*, Apgar adeptly translates and adapts the language and tools of financial risk management into the language and tools of nonfinancial risk management. To some readers this adaptation may seem insignificant; however, by choosing this strategy for his book, Apgar demonstrates that he is aware of the flaws and complexities related to the problem of using financial risk management techniques to solve problems presented in a business management setting. Perhaps it is for this fact alone that Apgar demonstrates that he truly understands the concept of measuring and using *Risk Intelligence*.

REFERENCES

The Economist. 2007a, Spooking Investors: Financial Markets Remain on Edge Because the Credit Crunch Has Not Been Solved, October 25.

The Economist. 2007b, Heart of Darkness: The Peril for Markets When Computers Miscalculate, October 25.

Rebonato, R., 2007, *Plight of the Fortune Tellers: Why We Need to Manage Financial Risk Differently* (Princeton, NJ: Princeton University Press).