



Actuarial  
Research Centre

Institute and Faculty  
of Actuaries

# Call for Research Proposals

**Project:**

## **Behavioural Aspects of Institutional Investment Decision-Making**

Date of issue: 20 February 2017

Closing date for proposals: 21  
April 2017, 5pm UK Time (British  
Summer Time)

## 1. Summary

This document is an invitation to submit a research proposal for a project commissioned by the Institute and Faculty of Actuaries (IFoA) through its Actuarial Research Centre (ARC) and under the instruction of the IFoA's Research and Thought Leadership Committee (RTLTC).

The aim of the overall project is:

To explore the decision-making of institutional investors, in particular insurers and pension schemes, especially the biases that may affect their investment decisions. This could include, but not be limited to, emotional, psychological and political biases. It is expected that the project will first explore what "rational" or "optimal" behaviour could be expected from an institution in certain economic scenarios, based on its investment objectives and underlying values.

It will then explore whether there is solid evidence that "behavioural" factors, such as human psychology, company culture, corporate politics and conflicts of interest, cause them to deviate from optimal behaviour. The research should then make practical conclusions that could be used by actuaries working in investment and related areas. For example, one possible output of the research could be a suggested governance structure an organisation could put in place to manage these biases and conflicts.

The IFoA has allocated funding of up to £200,000 to this proposal. This grant may be split across more than one research team depending on the scope and content submitted by respondents.

A key requirement of the research arising from any grant from the IFoA is that the outputs are placed in the public domain for all to access.

## 2. Background to the project

To date, a substantial volume of work has been undertaken in the field of behavioural finance to explore the psychological factors affecting investment decisions made by individuals. In contrast, "behavioural" factors (such as politics or human psychology) affecting decisions and actions made by institutional investors, such as insurers or pension schemes, are less understood. This could be significant for actuaries working in the areas of investment advice, asset-liability matching, liability-

driven investments and investment risk management, within institutional investors, such as insurance companies and defined benefit pension schemes.

A significant number of actuaries work today as advisors to institutional investors' key decision-making bodies. Typical roles could include:

- Investment advisors to occupational pension schemes.
- Professionals setting the investment strategy for assets of insurance companies.
- Investment strategists for assets backing long-term life insurance liabilities, such as with-profit or annuity funds.

Investment objectives and asset allocation decisions for the types of organisations mentioned above would typically be expected to be driven by the long term relationship between the value of assets and the actuarial or accounting value of liabilities.

In setting a long term investment strategy, investment actuaries are often required to form judgements and make assumptions (explicit or implicit) based on commonly accepted economic theories. This usually relies on the expectation of rational behaviour, in line with stated public objectives of these organisations and efficient market hypothesis in various forms.

The objective of this research is to test whether the actual decisions made by organisations, as groups of individuals, are influenced by a wider set of factors, such as emotions, human psychology, company culture, corporate politics and conflicts of interest. This could provide a better tool kit for actuaries and other professionals in managing risks and making financial projections for these organisations.

It is also possible that research forms the basis of more extensive research in this area in future, which the IFoA may wish to pursue at a later date.

### **3. The proposal**

The expected output of this project would be to explicitly draw out some of the key assumptions made about how institutions should behave rationally in certain scenarios and then test their validity. Research methods should be specified as part of the proposal and the IFoA currently has no preferred approach.

Possible examples of the output from the research project could include:

1. A list of statements made about the assumed reaction from an institutional investor (or another key organisation, such as central bank or a rating agency) in certain scenarios, based on their public objectives and traditional economic theories.
2. Discussion of other wider factors which may affect these organisations' decisions in practice. For example: external political pressures, internal culture within the organisations, governance, conflicts of interests (agency aspects), psychological pitfalls exhibited by employees of these organisations as a group of humans, or the way market participants absorb new information. It is expected that this list will be wider than that from traditional behavioural finance theory developed for individuals.
3. Validation of whether the assumptions made about future decisions by the organisation are materially impacted by these wider characteristics or not, assessing their validity and reliability.
4. Consideration of path dependency, where the research is dynamic, rather than simply looking at static examples. For example, some sequences of behaviours may trigger cascade effects which could in turn overwhelm other tendencies or reduce available actions.
5. Practical recommendations based on the above analysis which actuarial investment practitioners could use in their work.

### **Motivational Examples**

Below are some examples of topics that this research could focus on. They are just motivational examples, rather than specifying the proposal:

1. How are investment decisions made in institutions? In particular, are they made by individuals or by committees / groups? And what is the group structure (hierarchical, democratic)?
2. If they are made by committees, how does committee behaviour affect these decisions?

3. If they are made by individuals, how does the cultural context change the decisions they would otherwise make? Does this lead to a different outcome from more “traditional” behavioural biases (and just straight-forward incentives)?
4. Is there any difference between strategic and tactical decisions? Do institutions exhibit similar behavioural biases as individual investors?
5. The importance of agency aspects (conflicts of interest) for different types of institutional decisions. Role of external advisors. External and internal conflicts.

### **Related Academic Disciplines**

There is a preference to support research proposals that cross various related disciplines, in addition to behavioural finance. This could include:

- organisational theory
- psychology
- sociology
- decision making
- corporate governance
- agency theory

### **Funding**

Funding of up to £200,000 has been made available for this research at this stage. This grant may be awarded to a single party or split across more than one team, depending on the proposals submitted. For example, the grant could be awarded to two complementary proposals if the IFoA sees an appropriate fit. Applicants are also welcome to include other funding partners in their proposal, where appropriate.

### **Timescales**

The IFoA envisages that the research is like to last 1-2 years and is open to proposals from interested parties.

## **4. Project management**

The successful party will be accountable to an oversight group (within the IFoA), who will closely monitor the progress of the research to ensure that it aligns to expectation and to act as a practitioner sounding board for the research team. Throughout the work, the principal research team will be expected to regularly meet and discuss progress and planning with the oversight group for this project.

We expect that documentation and supporting work to describe progress, results, and limitations of results, would be provided from time to time as part of the project management. Ultimately, all research outputs arising from the research grant would be placed into the public domain via the IFoA website.

In addition to the milestones and deliverables for the project, the IFoA would like the successful party to commit to wider dissemination of the results, through presentations at relevant industry conferences and presentations to IFoA members, as well as wider publicity activity.

## 5. Eligibility

Proposals would be welcomed from any effective research-led organisations within the university, not-for-profit, public or private sector. Organisations may be based in the UK or elsewhere in the world. The IFoA is also encouraging submissions from multi-discipline research teams.

## 6. Submission guidelines

Submission should be in the format of an A4 document in no more than 12 pages in length and 11 point Times New Roman font. The response should cover the following items:

<b>a. Principal researcher(s) and institutions</b>	Please include contact details
<b>b. Outline of proposal</b>	Please provide a description of the expected research approach and anticipated deliverables. This could also include any initial ideas regarding potential lines of research and a demonstration of how they would support the project aims.

	Please also provide a work plan that demonstrates the expected research delivery
<b>c. Dissemination and Knowledge Exchange</b>	Please provide a draft plan for disseminating and exploiting the project's results, with IFoA members and beyond.
<b>d. Planned, or potential, impact</b>	<p>Please provide a description of the expected and potential impact of the research findings. This could include:</p> <ul style="list-style-type: none"> <li>- how investment choices in aggregate are not consistent with the optimal strategy</li> <li>- the financial impact on the insurer or pension fund</li> <li>- recommendations about how to work with, reduce or remove any biases</li> </ul>
<b>e. Resources and timing</b>	Please describe the proposed resourcing for the project including named individuals, the level of seniority of the persons involved, and the suggested time each person would dedicate to the project.
<b>f. Costs</b>	<p>Please provide a detailed estimate of costs including a breakdown of the time and cost of each resource expected to be employed on the project. Please include all expected expenses.</p> <p>The successful party will be required to commit to a binding quote following more detailed discussion of the work plan.</p>
<b>g. Summary of experience</b>	Applicants should provide details of relevant experience and a demonstration of previous advances made in this topic.
<b>h. Communication</b>	Applicants may wish to suggest an optimal structure for the involvement of the oversight group in the project (e.g. frequency and format of meetings) and the subsequent

	communication of those meetings content via appropriate IFoA channels.
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## 7. Key considerations for selection

Submissions will be assessed on a range of criteria, including evidence that the research team will produce work that:

- is aligned to the objectives outlined in sections 2 and 3;
- is theoretically sound and statistically robust;
- can be applied easily and consistently by practitioners;
- is clearly explained and well documented.

Proposals will also be assessed against:

- Existing relevant skills and experience in the individuals working on the project;
- Evidence of a track record of research projects in cognate areas
- Confidence that the aims of the project can be met within the timescales specified;
- Willingness to promote and support the work post project completion;
- Ability to communicate results;
- Value for money.

Other considerations of the selection will be evidence of innovative thinking in relevant areas, quality of vision and enthusiasm for the project.

## 8. Next steps

Date	Activity
20 February 2017	Call for research proposals opens (for 8 weeks)
21 April 2017	Deadline for submissions 5pm GMT
End April 2017	Shortlisting

Start May 2017	Discussion with short-listed parties, if required
Mid May 2017	Award announced
June 2017 onwards	Research commences

Please submit your proposal to [arc@actuaries.org.uk](mailto:arc@actuaries.org.uk) by **5pm** UK Time (British Summer Time) **on 21 April 2017** at the latest.

Further enquiries about an application may be directed to Catherine Gauld, Research Project Manager, through [catherine.gauld@actuaries.org.uk](mailto:catherine.gauld@actuaries.org.uk)



## Actuarial Research Centre

Institute and Faculty  
of Actuaries

### **About the Institute and Faculty of Actuaries**

The Institute and Faculty of Actuaries (IFoA) is the UK's only chartered professional body dedicated to educating, developing and regulating actuaries based both in the UK and internationally. We represent and regulate over 28,000 members worldwide for the benefit of the outside world and oversee their education at all stages of qualification and development throughout their careers.

As a Learned Society a key objective of the IFoA is to promote and support a wide range of research and knowledge exchange activities with members, external stakeholders and international research communities. The IFoA places the advancement of actuarial science at the heart of its activities by commissioning and funding research that:

- advances actuarial science as a subject
- supports industry practitioners
- helps inform evidence-based public policy development.

### **About the Actuarial Research Centre**

The Actuarial Research Centre (ARC) is the IFoA's network of actuarial researchers around the world. The ARC seeks to deliver research programmes that bridge academic rigour with practitioner needs by working collaboratively with academics, other actuarial bodies and the end user community. The ARC supports actuarial researchers around the world in the delivery of cutting-edge research programmes that aim to address some of the significant challenges in actuarial science, ultimately offering business solutions.