



# Stanford eCorner

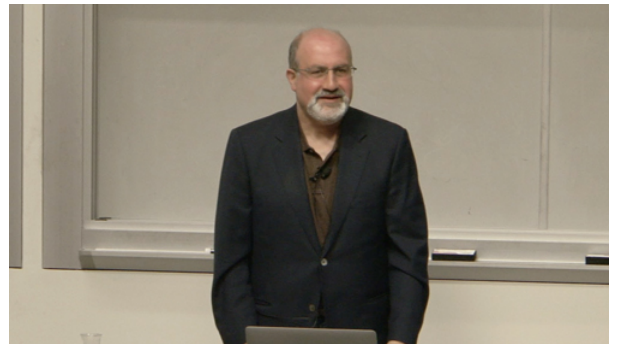
## Skin in the Game

Nassim Taleb, *Author*

April 10, 2013

Video URL: <http://ecorner.stanford.edu/videos/3125/Skin-in-the-Game>

Blending his views on modern day investment risks with effective risk management techniques from earlier in history, author Nassim Taleb explains the value and moral purpose of requiring all investors to have "skin in the game."



### Transcript

I believe in something I call skin in the game, okay, skin in the game is defined skin in the game is most moral and effective to remove risks is that nobody should ever put someone else at risk. I don't really care about compensation, okay. I don't really care about ranking, because you can't have a trading competition because someone has a strategy that pays off very rarely, okay. He would lose in the competition, he would lose every battle and win the war, you see. So, I can't really rank traders, but there is one rule I have, I call, skin in the game is that nobody should put others at risk, without having harm to himself, okay. In other words if you lose money to your clients, you should be exposed to the same risk, that's sort of - it boasts moral and risk management rule. Risk management because in Hammurabi's code, it was simple as the architect builds the house and the house is fragile, but hidden fragilities in a basement, you get the idea when the foundation like in the bank system, banking system they look very stable when they have the cut corners that nobody will see okay to make the bonus and if the house collapses the architect is penalized that was in Hammurabi's code. Actually, he's put to death, if the house collapses and kills the owner of the house. So, this system, okay, is the best, this is the best risk management rule, because as Hammurabi discovered that something they forget today in Washington, the architect or engineer knows a lot more about the risks. He doesn't know a lot about the risks, but he definitely knows a lot more than the inspector, you see, so if you make people eat their own cooking, you see they are lot better off, okay and someone sent me, read my book and sent me something, a story in Brazil where they discovered that they can lower the rate of helicopter crashes by forcing helicopter engineers randomly to take a ride, a half an hour ride once a month in a helicopter, alright.

Now for example something the Romans knew and Victorian knew that you make engineers sleep under the bridge, alright. Okay, so in trading what do you do, so long as whoever is involved in a strategy has losses, small, okay, it doesn't matter, alright has losses, if they can harm others, in other words you have some incentive, but some disincentive then we should be okay. It's when people don't have disincentive when they lose that the system blows up.