

TAIL RISK HEDGING: AN INVESTMENT CONSULTANT'S PERSPECTIVE

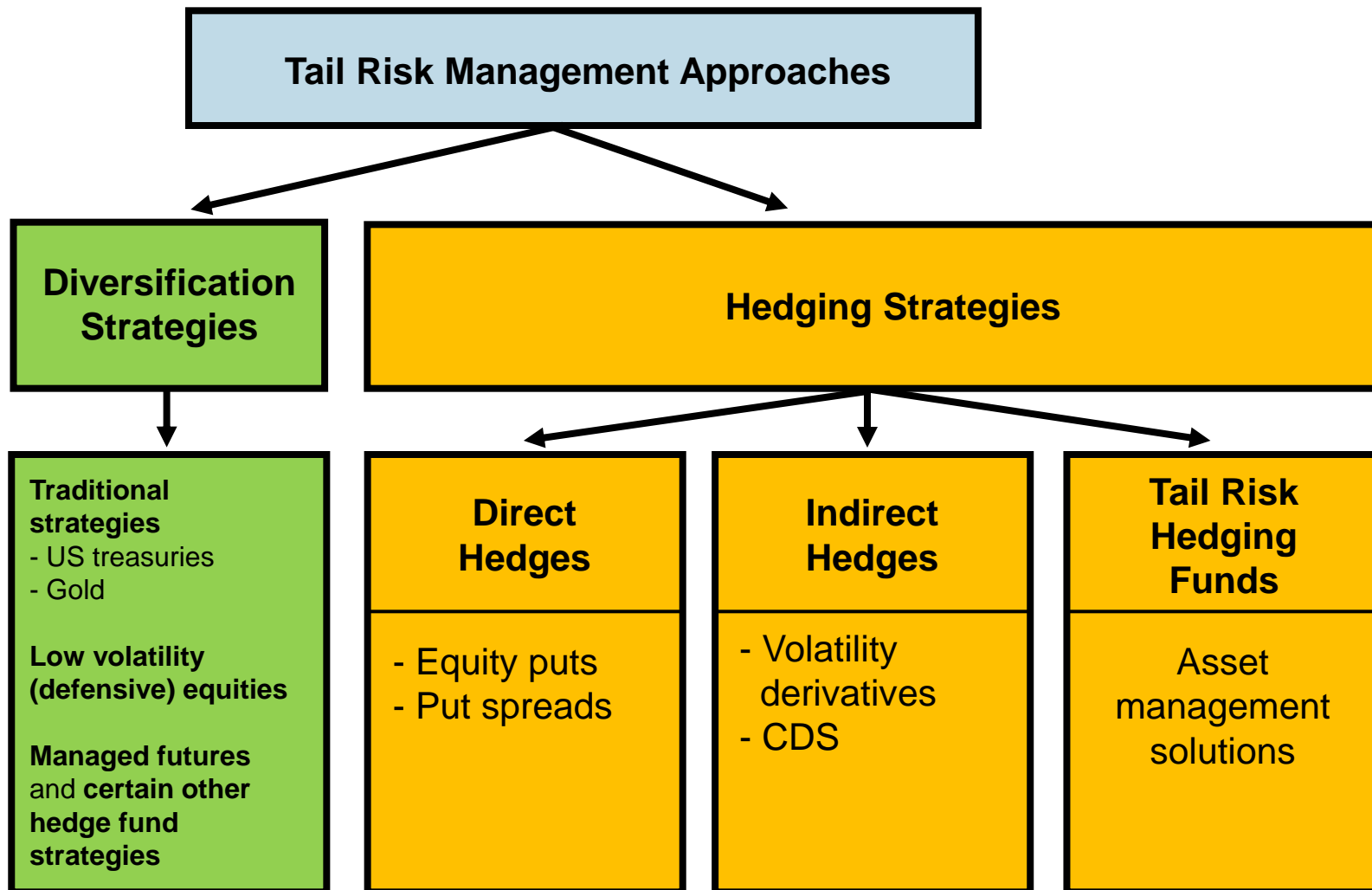
16 APRIL 2015

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Agenda

- Tail risk management framework
- Client experiences
- Client (and consultant) perspectives and challenges

Approaches to tail risk management



Key investor considerations

Portfolio Rationale

**Effectiveness
(as a tail hedge)**

Cost of carry

and / or

**Opportunity cost
(relative to equities)**

Governance and Implementation Factors

Complexity

Transparency

Peer practices

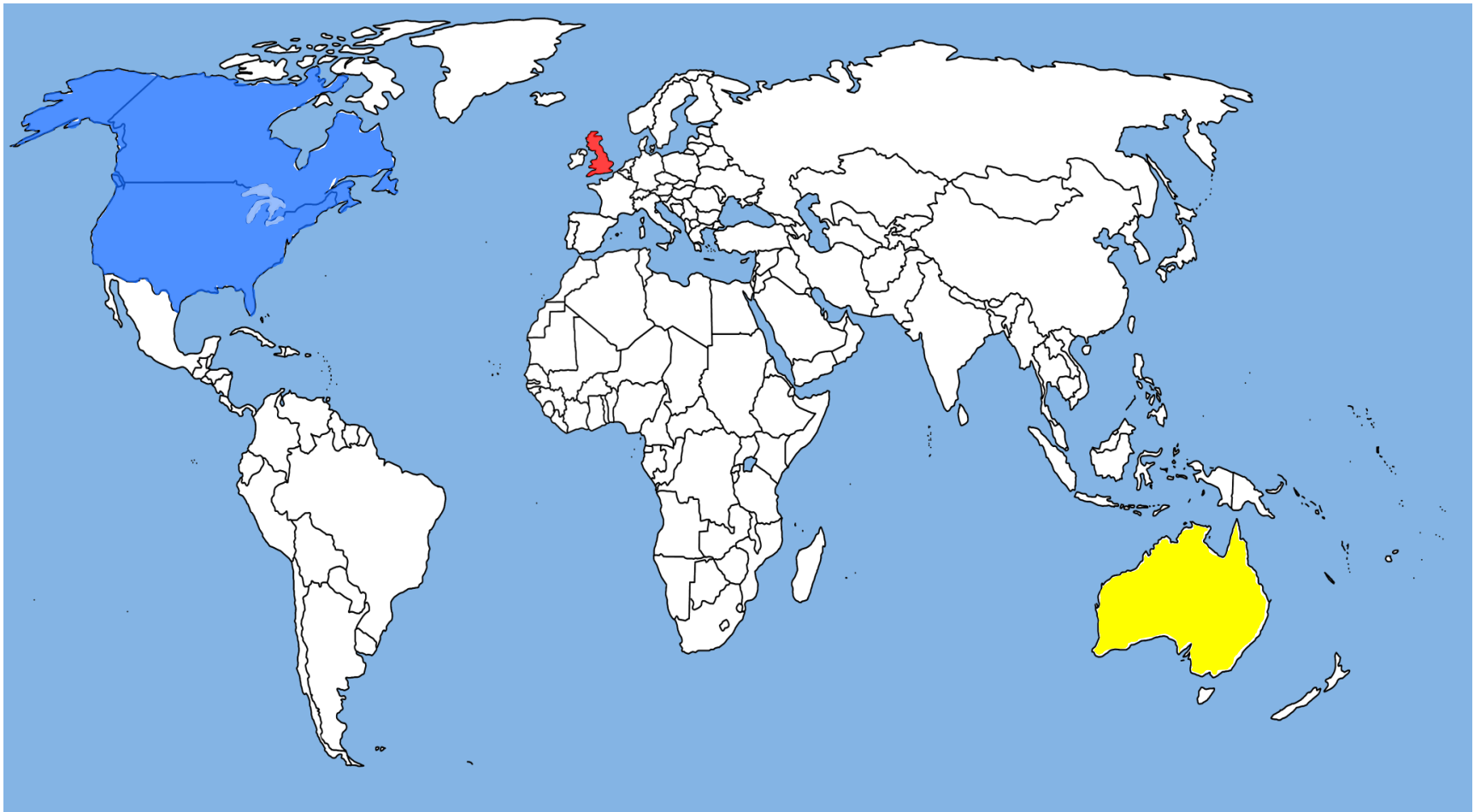
**Counterparty risk /
Liquidity**

**Implementation,
monitoring, benchmarking,
etc.**

Comparison of tail risk management approaches

Approach	Effectiveness	Cost of Carry	Opportunity Cost	Complexity	Transparency
<i>Diversification Strategies</i>					
Cash / T-Bills	Low / moderate	Nil	Very high	Low	High
US Treasuries	Moderate	Nil	High	Low	High
Gold	Low / depends	Nil	Very high	Low	High
Low volatility equities	Low	Nil	Low	Low	High
Managed futures	Depends	Moderate	Moderate	Moderate	Moderate
<i>Hedging Strategies</i>					
Simple put options	Excellent	High	Low	Low	High
Put spread collar	Moderate	Nil / low	Low / moderate	Moderate	High
Indirect hedging strategies	Good	Moderate / high	Low	High	Moderate
Tail risk hedging funds	Very good	Low / moderate	Low	High	Low / moderate

Client experiences



Common client (and consultant) perspectives on tail risk hedging

1. Unconventional / unfamiliar

“Paying for insurance?”, peer practices, derivatives (VIX, CDS)

2. Not for long-term investors

**“Equity markets eventually recover”,
“Our SAA is established accordingly”,
“The ERP is partly a payment for taking on tail risk”**

3. Too expensive

Cost of simple put options, cost of carry generally, tail risk hedging fund fees

4. Volatility risk premium

“Long-term investors should be natural sellers of tail risk insurance!”

5. Strategic or tactical?

Strategic (too expensive / “Why not just de-risk?”); Tactical (“I’m skeptical about timing skill”)

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