Communicating Investment Risks
to Boards & Trustees
Image captivates the challenges of investment risk—e.g. an angry mob—put yourself in their shoes. Use GFC demo photo in June 2013 Gazette.
What we’ll cover

- Investment risk. Communication
- Top 10 different investment risks
- Investor’s risk appetite
- Tailor to your audience
- What to communicate?
- How to communicate?
- Conclusions & recommendations
Introduction. Definitions.

▼ Investment risk

*the risk that the outcomes of an investment strategy and its execution do not meet the goals of the investor.*

▼ Effective communication

*Effective communication means being successful in getting the message across - it must be heard, understood and believed by the receiver.*
Top 10 investment risks

**Strategic/Indirect**
1. Failure to understand investor’s risk appetite
2. Matching risk
3. Inflation
4. Operational risk
5. Liquidity

**Direct**
1. Asset allocation
2. Market risk
3. Stock selection
4. Fund manager selection
5. Credit risk

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Failure to understand investor’s risk appetite
Matching risk

- Nature and duration of assets to match liabilities = needs (goal) of investor

- Communicate via:
  - Scenarios / “what ifs”
  - For a Super fund - by segment
  - Past and future best estimate
Tailor to your target audience

- Tailor communication strategy
- Investor / Trustee / Member - $5K to $50bn
- Board members – range of skills and experience – numerate and not
- Explain in terms relating to the organisation’s strategic intent so decisions easier
- Consider levels of investment risk awareness
- Consider investment risk appetite – e.g. charitable trust.
What to communicate?

- That you understand your Board’s /investor’s specific circumstances, time frames goals and risk appetite

- Which risks matter most and why

- Implications of risk versus return trade-off:
  - price volatility & variability of returns by asset class / option
  - e.g. standard deviation of return, Sharpe Ratio

- Clarity on costs of investment management and reporting services
How to communicate? #1

Mehrabian’s Rule – Part true, part myth

Elements of Personal Communication
- 7% spoken words
- 38% voice, tone
- 55% body language

http://www.rightattitudes.com/2008/10/04/7-38-55-rule-personal-communication/
How to communicate with boards - generally

▼ Develop trusted adviser relationship
▼ Tailor to organisation; its strategic objectives
▼ Tailor to board members
▼ Simplicity / Clarity, Consistency, Relevance
▼ Set reasonable expectations
How to communicate with boards - on investment risks

- Recognise risk = uncertainty & ambiguity
- Quantitative = distributions of investment returns over time
- Qualitative = people’s comfort with understanding current position, needs and goals + likely future behaviour
- Scenarios past + future; stress + reverse stress tests – encourage discussion
- Communication = education. Share good practice examples, non investment risk analogies
- Keep it simple; pictures, colour, graphs.
- Put time into your communication preparation
Conclusions & Recommendations

1. Assist the Board/investor to understand their investment goal(s) and risk appetite
2. Communication of investment risk is as important as identifying and managing it.
3. Pay extra attention to the strategic / indirect risks
4. Tailor to your audience - numerate and not naturally numerate
5. Use pictures and words, familiar insurance analogies, scenarios and discuss
6. Put communication preparation time in.
Questions

Q & A
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