QIC Media Release

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VOLATILITY EXPOSES "RISK MANAGEMENT" STRATEGIES

Superannuation funds need to significantly boost their risk management infrastructure as investment markets expose flaws in conventional diversification and portfolio management strategies.

This is the view of QIC's Capital Markets Division, which stated that superannuation funds which do not effectively manage risk at both a macro and micro level increase the prospect of significant underperformance by the fund.

Troy Rieck, QIC's Managing Director, Capital Markets, said the recent trend to increasingly complex layers of manager and asset class specialisation has seen risk increasingly being managed only at a micro level.

"Risk management is not simply a reporting function – it's a focussed and continually evolving set of actions. Not having the infrastructure to manage both macro and micro levels of risk is extremely dangerous," Mr Rieck said.

"The events of the past 18 months have shown that diversification doesn't work when it is most needed.

"Superannuation funds that solely rely on diversification to manage volatility and drawdown risks are setting themselves up for a failure to meet member expectations.

"Funds can underestimate the size and potential impact of risk as a similar economic factor risk may be spread across multiple portfolios.

"For example, a fund might have had multiple exposures to Lehman Brothers spread across equity, bond, cash and derivative portfolios, as well as indirect exposure through prime brokerage and futures clearing relationships.

"An integrated, client-focussed business would not tolerate large amounts of unmanaged risk – superannuation funds needs to think in the same way.

"QIC's approach centres on a macro-focused risk management infrastructure that complements risk management processes at a micro or portfolio level.

"This macro risk management infrastructure manages the fund's day-to-day asset exposures, supports the many requirements of the fund for liquidity and not only aggregates but effectively mitigates counterparty risk.

"Having this risk infrastructure in place has now allowed us to develop a range of derivative-based investment strategies that provide a true negative correlation with equities. This approach provides strategic tail risk management for our clients and will ensure that they have strategies in place that will benefit should the market downturn continue" he said.

The QIC 'Red Paper' – *Portfolio Rebalancing – Managing risk in volatile markets* can be downloaded in full from the Knowledge Centre of QIC's website - www.qic.com.

QIC is one of Australia's largest institutional fund managers with $70 billion[1] under management for its Australian and overseas clients.

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[1] As at 31 October 2008