Premium Alternatives News
OPALESQUE

Understanding tail-risk hedges & funds - part five - survey results

Bailey McCann, Opalesque New York:

Over the course of this series, we have examined the history of tail-risk, including the strategies employed by various risk experts, funds, and fund of hedge funds, in order to protect investor wealth during a tail event. Now, we bring you the results of a survey in which we asked our readers to share their thoughts on tail-risk. Please note: the survey was entirely opt-in, and is not scientific. The results outlined below reflect only the opinions of those who responded.

We asked 13 questions on the various aspects of tail-risk. The first question asked how much of a premium investors were willing to pay for their tail-risk hedges. As noted in the introduction of this series, investors have paid anywhere from 50-200bps for tail-risk strategies, and prices can vary widely depending on when investors opt into a tail-risk strategy. Survey data also reflects this variance, 75% of respondents said they were willing to pay a premium of between 2-10%, while 25% said they would be unwilling to pay a premium to hedge tail-risk.

When asked what types of products investors would consider purchasing, the most popular products included - out-of-the-money puts, collars, and VIX products. 75% of respondents said they would prefer separate managed accounts for their tail-risk strategies and all respondents wanted a high degree of transparency.

100% of respondents said that the liquidity of the underlying investment was an extremely important consideration in their tail-risk product choices. 50% said that they wanted monthly liquidity, and 50% said they wanted daily liquidity. 100% of respondents said they planned to increase their allocations to tail-risk strategies.

We also asked investors how they perceive the current tail-risk environment and what they are doing to respond to current risk factors. 75% said that they see the European debt crisis as the tail-riskiest event in the market right now, while 25% said that tail-risk events by their nature are unknowable. More than half of those surveyed said that they are taking a proactive approach to portfolio management by rebalancing on a monthly basis in response to increases in risk factors.

For the final question we asked which books are currently undergoing stress tests. Half of respondents said they were currently using stress tests for their banking and trading books on a daily basis. No respondents said they were using stress testing for structured products.

Conclusions

Evolution is one of the key themes in this space. Many of the people I spoke with noted how managers and investors alike have changed their response to risk over time - moving from more generic market views into dynamically sized strategies that seek wealth preservation and cost efficiency. Not surprisingly, the slow recovery from the 2008 crisis has helped to keep tail-risk hedging front-of-mind for market participants. However, managers are quick to point out that they expect these conversations to become more challenging as soon as market conditions start to improve and investors once again feel comfortable with their investments.

Included below is a list of the firms that participated in the series and links to more information. We also welcome additional feedback in the comment section.

References:

- 36 South Capital Advisors - a UK-based investment firm.
- Attalus Capital - a Philadelphia-based investment and trading firm specializing in fund of hedge funds and active core equity and bond strategies.
- Diversified Global Asset Management (DGAM)- a Canadian fund of hedge funds, which manages a proprietary direct tail-risk hedging strategy.
- Investor Analytics- a US-based risk management firm.
- Lionscrest Capital - a Canadian firm offering access to the Universa tail-risk strategy, as well as Horizons black-swan ETFs.
- Symphony Financial Partners - a Tokyo-based investment firm focusing on Asian investments.
- VelocityShares - a US-based firm offering volatility and tail-risk strategies to institutional investors.

Full article link (subscription required): hhttp://www.opalesque.com/643229/Understanding_hedges_funds_part322.html