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# Sustainability of Performance vs Downside Risk

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## Etymology of “Risk”

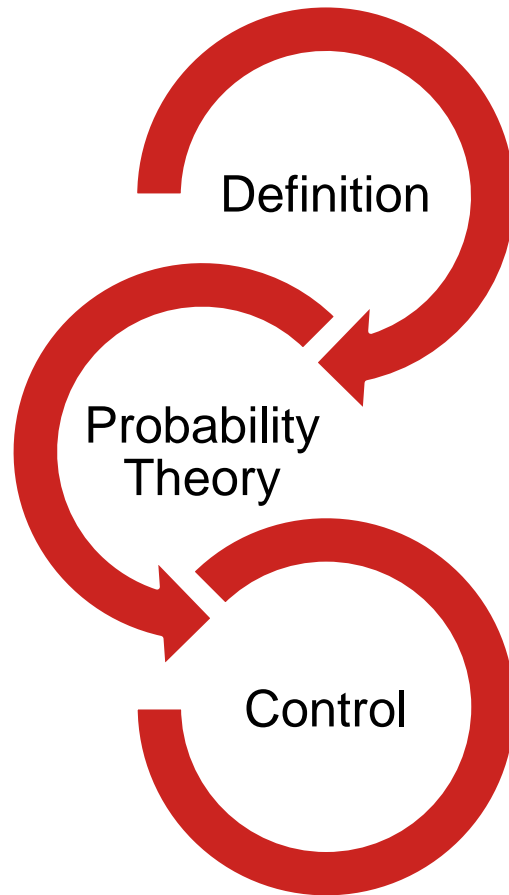
1660s, *risque*, from French *risque* (16c.), from Italian *risco*, *rischio* (modern *rischio*), from *risicare* "run into danger," of uncertain origin.

Source : Online Etymology Dictionary, [www.etymonline.com](http://www.etymonline.com)

“There is no consistent definition of risk”,  
but “taking a risk was often considered a virtue and associated with courage”.

Source : Cline, Preston B., “The Etymology of Risk”, 2004; MacAlister, Jamie, “Risk Strategy: Understanding Risk to Improve Strategic Decisions”, Bloomsbury Publishing, 2016.

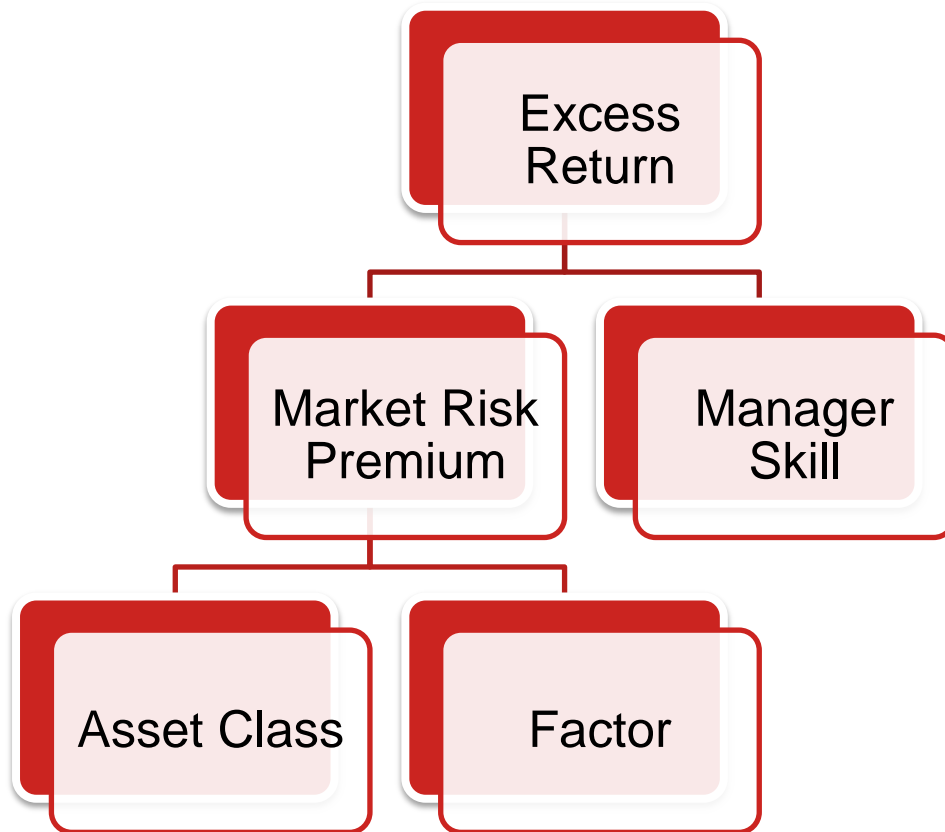




Proper **governance structure** to manage risk is also important

## Risk Taking to Seek Excess Return in Investing

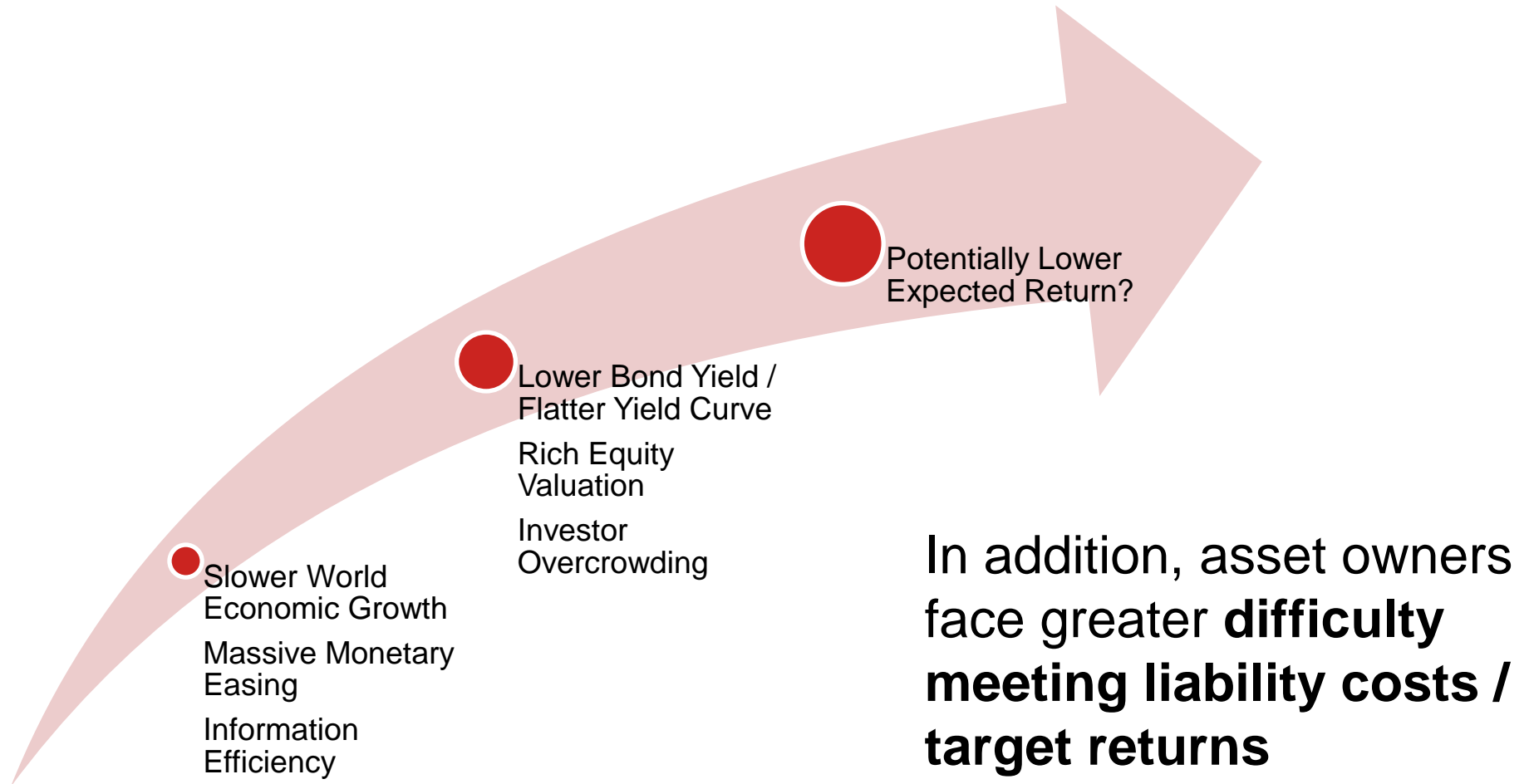
### Sources of Excess Return



Risk taking should depend on the investor's belief about **market inefficiency**

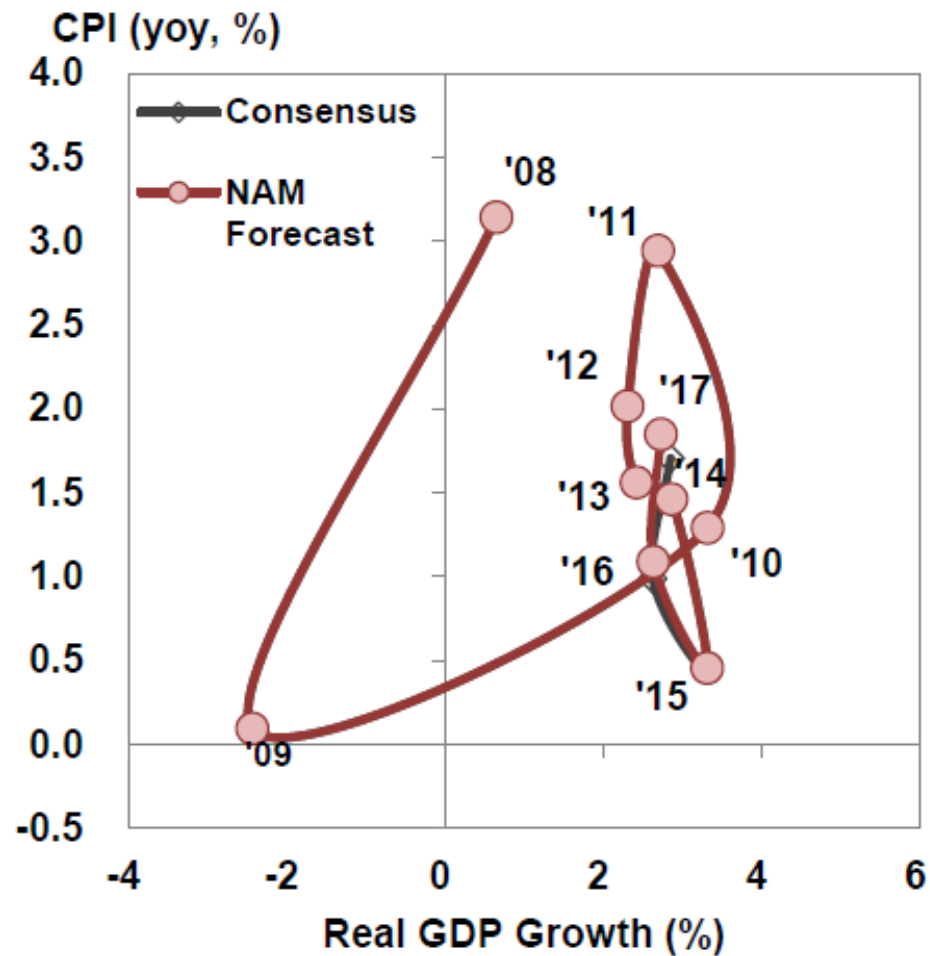
## Why Is Performance Sustainability in Question?

### Challenging Investment Climate



# Has the World Economy Become Unstable?

## World Real GDP and CPI Inflation Cycle



# Risk Factor Analysis Using Proprietary Risk Model

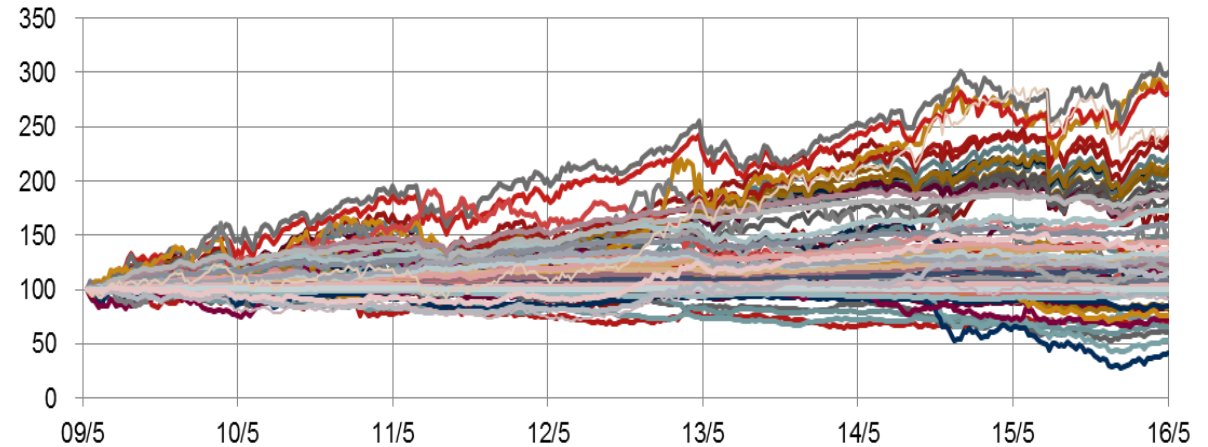
More than 70 financial  
market data series

Principal  
component  
analysis  
(PCA)

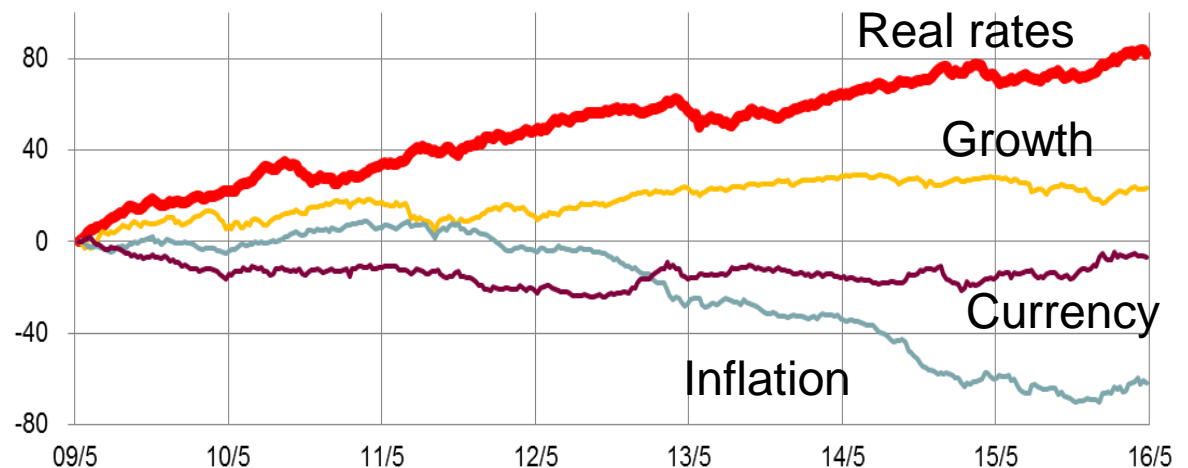
## Risk Factors

- (1) Real Rates
- (2) Growth
- (3) Inflation
- (4) Currency

Cumulative Asset Class Returns

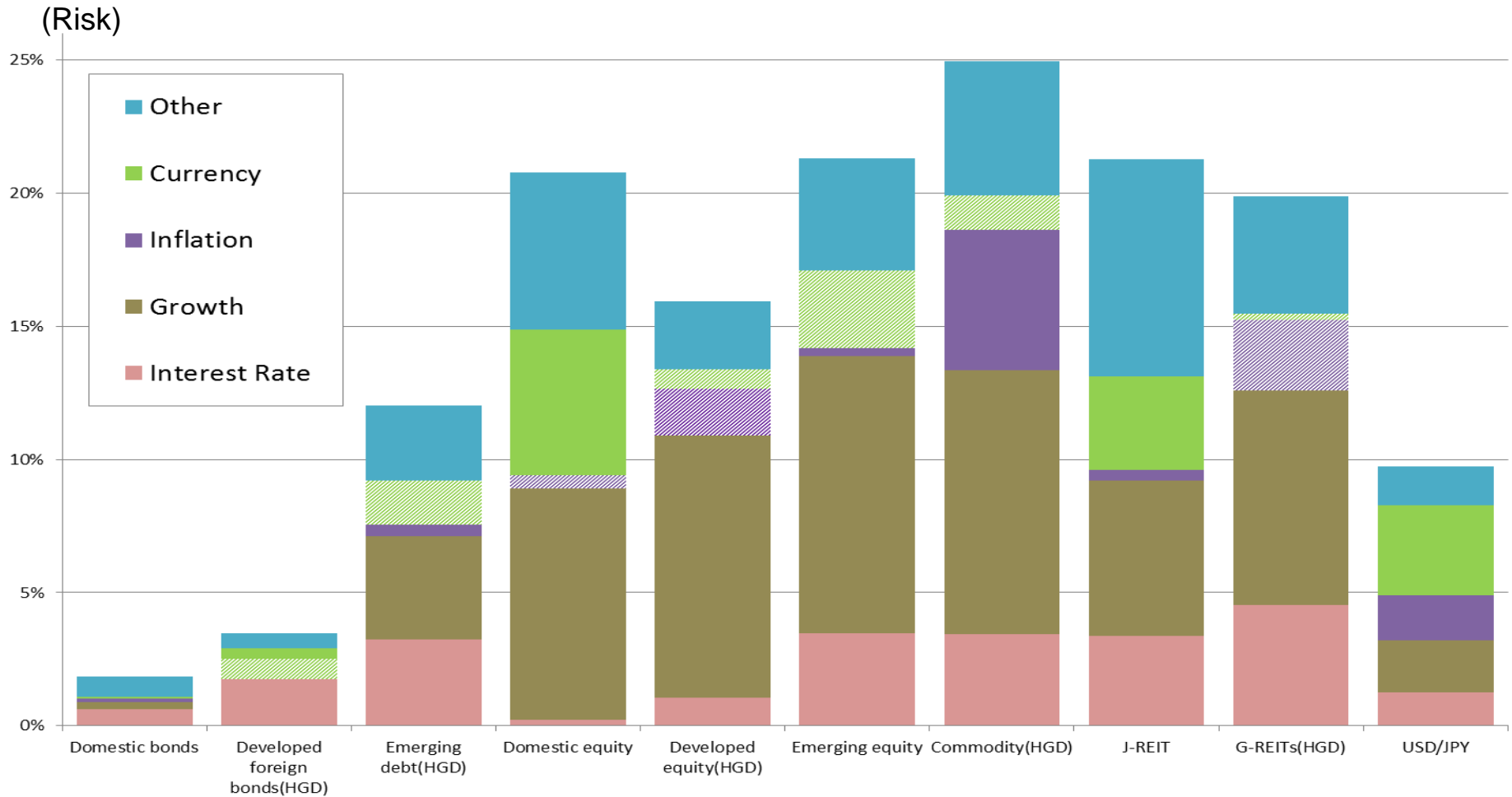


Cumulative Risk Factor Returns



# Breakdown of Asset Classes by Risk Factor

## Factor Mapping to Asset Class





Bond Duration

Credit Market

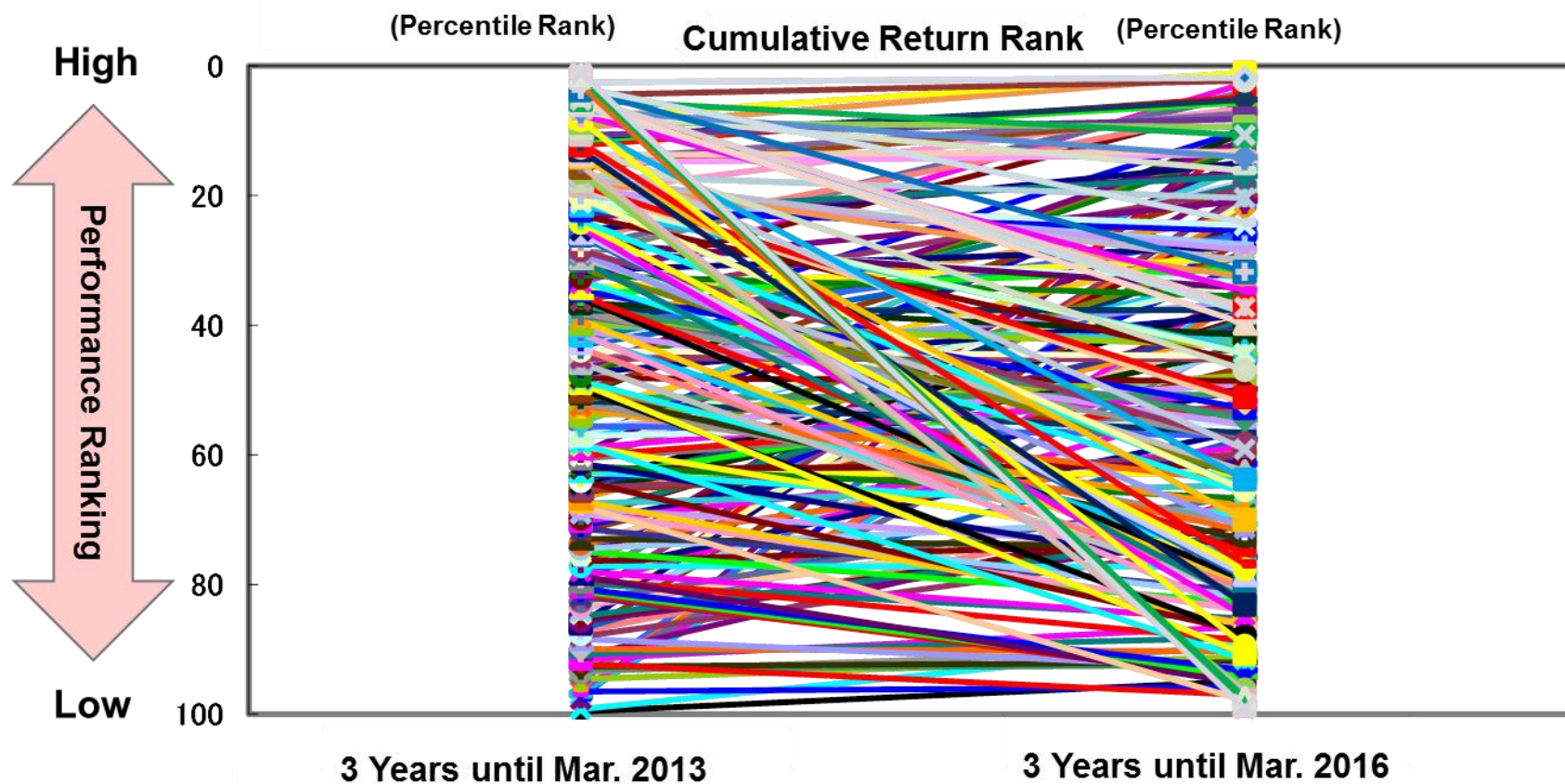
Low Volatility  
Equity Strategy

Illiquid Assets

Absolute Return  
Strategy with  
Low Equity  
Correlation

# Risk Management in Manager Selection

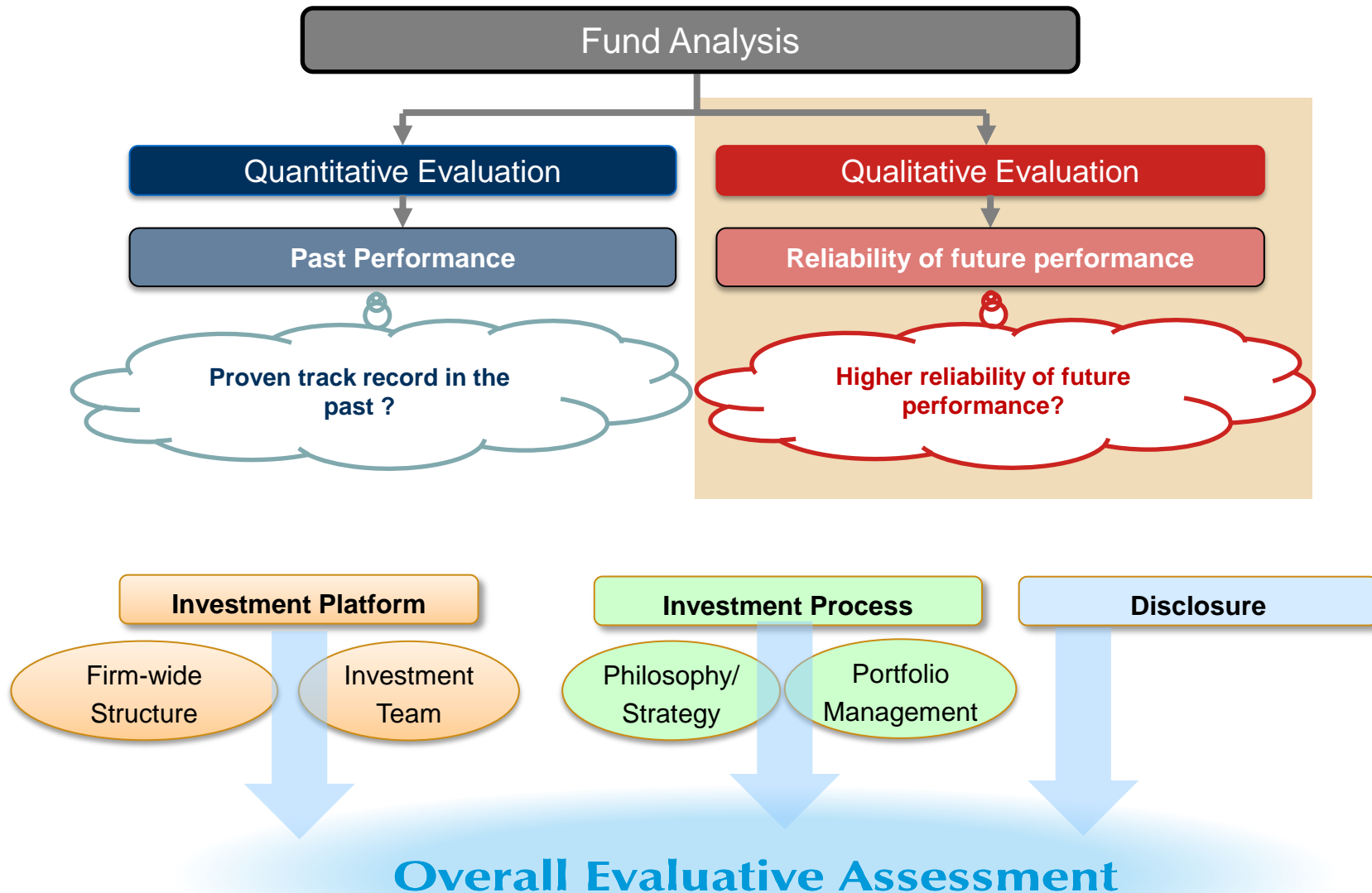
Before/after comparison: 3-year return rank of Japanese equity funds in Japan



Source : NFR&T

\*Above chart shows the cumulative return changes of the individual funds which have more than 6 years track record among domestic equity general free category by Fundmark. Return Rank is the relative ranking among the funds which have 3 years' track record as of each period.

# Assessing Manager's Performance Sustainability



**High Sharpe ratio naturally tends to protect downside**

**Diversify asset classes for higher Sharpe ratio**

**Analyze downside nature in manager selection and monitoring**

**Trend-following dynamic hedging may become costly**

**Potential use of option strategies**

#### IMPORTANT INFORMATION

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