

Portfolio Risk Management

Management of risk is primarily the role of the portfolio manager, who is supported by the Asset Allocation Committee, Stock Selection Committee, Performance Review Committee and our independent Performance & Risk monitoring team.

Performance Review Committee

The role of the Performance Review Committee (PRC) is to review, challenge and escalate significant findings that have been identified by the Portfolio Dispersion Review Committee (PDRC) or the Portfolio Risk Review Committee (PRRC). This is in relation to portfolios or investment funds that have been identified as possibly falling outside Waverton's coherent investment process. The PRC meets quarterly and reports to the Management Committee.

We have outlined below some of the controls and checks we have in place.

Quantitative Checks

Investment Guidelines

- Asset Allocation Committee
- Recommended Stock List
- Asset Class Ranges Monitoring

Portfolio Construction

- Statistical Risk Monitoring (Ex Post)
- Volatility/Style Factor Monitoring,
- Statistical Risk Monitoring (Ex Ante) – VaR, Volatility, Tracking Error, Liquidity, Stress Testing and concentration risk

Dispersions

- Portfolio Outliers
- Performance Dispersions
- Risk Dispersions

Qualitative Checks

- Peer Reviews – conducted annually by the secondary portfolio manager

Investment Risk

Establishing the Measurement Framework for Risk Control

A mandate risk level is selected from our Strategic Asset Allocation framework for a client according to the Waverton 'Know Your Client' on-boarding process, this includes responding to a detailed questionnaire to help effectively judge suitability. It also relies on dialogue to build up knowledge regarding risk appetite not captured in questionnaire responses. Investment ranges are set around the neutral point, or the Strategic Asset Allocation for equities, fixed income and cash. This enables calculation of an implied risk range, derived from historical observations of volatility and associated maximum drawdowns for each mandate and clients will observe these periods as part of the assessment process.

The asset class weighting framework is the primary driver of investment risk and the implied volatility ranges are a result of investment weightings, (see our volatility bands in our [Investment Mandate Guidelines](#)). All invested portfolios at Waverton are managed and monitored in context of these ranges. The volatility ranges are used to flag risk but are not the primary cause to reduce risk. Should a volatility range be breached, Waverton will take a holistic and pragmatic approach to managing client assets. This is to mitigate against crystallising a permanent loss of capital that can result from following hard rules. Further explanation is detailed in the following sections.

Understanding and Interpreting Risk and Risk Ranges

We recognise that the plurality of risk depends on the perspective of the individual client and his or her own interpretation. Our view of risk incorporates volatility and other statistics but is best described as a permanent real loss of capital.

This differentiates Waverton from other investment houses, since we rely on our assessment of capital loss and do not operate hard limits on any one specific risk measure. Waverton seeks to understand whether there is permanence to a sharp move in market price by understanding the changes in the future revenue streams of the assets we own. Therefore, we will not necessarily sell risk assets in volatile periods. This is a deliberate feature in order to avoid crystallising losses at times of maximum uncertainty. The Financial Crisis is a good example of this approach working successfully for our clients and the long term value of their portfolios.

Risk of Permanent Capital Loss

We aim to prevent the risk of permanent capital loss at portfolio level by:

- Applying appropriate diversification
- Investing in quality companies which have an enduring franchise and predictable cash flows
- Managing the time horizon and liquidity requirements of the portfolio

These criteria are observed in conjunction with quantitative portfolio risk measures generated by our systems. The data informs portfolio managers and is an integral part of the independent review process.

Risk Systems and Measures

The primary risk analysis technology we utilise is the FactSet Multi-Asset Class system supported by proprietary software. These systems may provide risk statistics on both an ex-post and ex-ante basis. The quantitative measures used in the investment process are listed as follows:

- Volatility (standard deviation)
- Value at Risk (VaR)
- Tracking Error and Active Share
- Sharpe and Information Ratios
- Maximum Drawdown
- Correlations (asset class, sub-asset class, intra sector, stock-to-stock)
- Concentration Risk and Beta
- Liquidity (Time to liquidate)

Currency Risk

Currency management is necessary to protect the income in the base currency in fixed income securities. These instruments do not benefit from the self-correcting characteristics which equities enjoy. We therefore undertake hedging within our in-house bond funds in order to ensure that the returns are secure in the base currency.

We will not typically hedge currency exposure of our equity investments at the portfolio level. Currency exposure of a company will be considered but we believe hedging is often imperfect or even counter-productive due to the international nature of companies' earnings and balance sheets. The hedging policies that the companies themselves have in place can also distort accuracy. Furthermore, it can be demonstrated that in the long term, currency investment is a 'zero sum game' and the expected return on different developed equity markets should be unaffected by currency considerations over the longer term.

With regard to emerging markets, where currency volatility is a bigger issue and where listed companies do not tend to have the same international reach as they do in developed markets, we will avoid exposure if we are concerned about the outlook for the currency. Our bottom up approach to equity selection will aim to identify the source of revenues and locality of costs, as well as the company's policy toward hedging. Should a company be identified to carry significant currency risk, this would form part of the investment case and be evaluated in conjunction with the other parts of the investment case.

The information provided does not constitute investment advice and it should not be relied on as such. It should not be considered a solicitation to buy or an offer to sell a security. It does not take into account any investor's particular investment objectives, strategies, tax status or investment horizon.

