



Alternative viewpoint

Volatility and risk – what matters?

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# Questions for asset managers



1. What measure of risk most drives your investment process?

- Tracking error
- Other risk budget
- Absolute volatility
- VaR
- Risk vs some measure of liabilities
- Other

# Questions for asset managers



2. What measure of risk matters most to your clients?

- Tracking error
- Other risk budget
- Absolute volatility
- VaR
- Risk vs some measure of liabilities
- Other

# Pause for thought

Why aren't I losing sleep  
about market volatility?

Why do I care about  
the price of gilts?

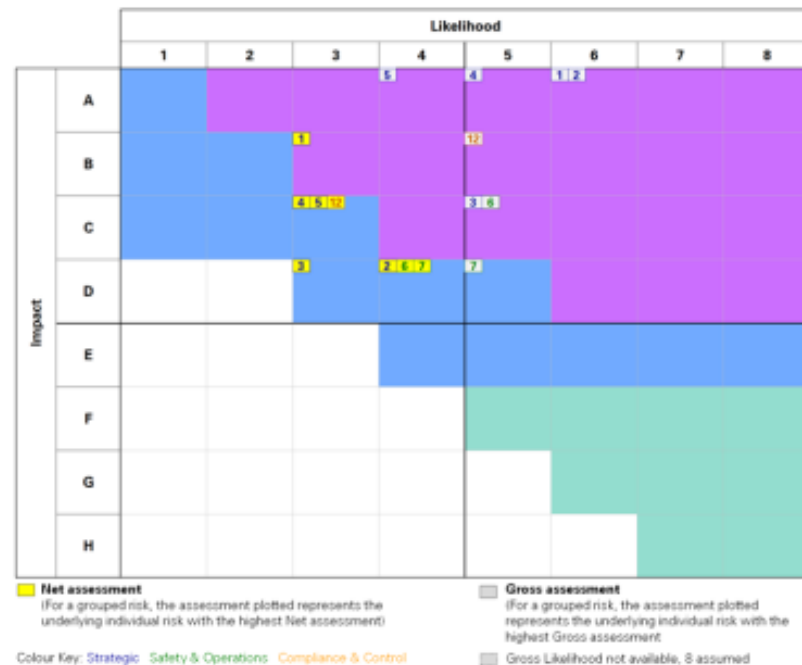
What is the meaning of risk?



# Risk – beyond volatility



- Risks include
  - covenant
  - asset values
  - investment income
  - implementation
  - controls and compliance
- Mitigations and contingency plans



# Strategy – designed to reduce risk long term



- Aligned Income
  - Improved connection between investment income and members' benefit payments
- Stronger Balance Sheet
  - Reduced reliance on investment growth and the sponsor
- Refocused Capabilities
  - Ability to make investment decisions focused on progressively improving benefit security



# UK pension industry investment evolution



- 1980s - Peers
  - actuarial asset values and peer group benchmarks
- 1990s - Markets
  - asset classes, mark to market values and scheme-specific benchmarks
- 2000s - Purpose
  - return seeking, liability matching and derisking flight plans
- 2010s – Hedging
  - pricing risk and cash flows



# Questions in search of an answer



If what I really care about is cash flows ...

... why do I focus so much on asset values, funding levels?

... what investment benchmarks should I use?

... how do I choose different investments and construct a portfolio?

... how do I assess risk and diversification?

... what tail risks matter in the long term?