

What kind of measures a fund undertakes to control risk?

On the individual fund level:

Each fund has its own investment objectives and restrictions. A fund management company would invest for a fund based on the pre-set objectives and restrictions. A fund typically invests in a number of securities, which may be stocks, bonds, money market vehicles etc. and may be exposed to different types of risk.

There is typically a risk management team where risk management systems are employed to measure market risk, security specific risks and liquidity risk, etc. In general, portfolio asset allocation, deviation from the reference benchmark, volatility, risk indicators and investment style are monitored on an on-going basis. Fund management team will continuously monitor the risk level of a fund. Various risk monitoring reports are regularly generated for fund management team to monitor what risks are being taken in a portfolio, and consider if any further action is needed.

There is pre-trade and post-trade compliance monitoring. Before the fund manager sends an order to the dealing desk for trading a security, the fund manager needs to run through a compliance monitoring procedure against investment restrictions that apply to a specific fund. Only when the order complies with all the restrictions that it will be passed to the dealing desk for execution. The compliance department of the fund management company also has post-trade monitoring measures to check on the trades on a regular basis (typically on a daily basis). If there are any breaches, the compliance department will advise the fund manager to rectify the case as soon as possible.

Besides, the fund management companies will monitor the liquidity of the fund and maintain an adequate level of cash for daily trades and redemptions. Fund management companies will also conduct stress test to assess the risk level of the fund under different circumstances. Senior management would typically review the performance and risk profile of the fund on a regular basis, or more frequently when the market is volatile. Referencing various risk parameters, senior management will determine whether the current risk profile is acceptable in accordance with fund investment objective and policies.

On the fund management company level:

The fund management company must have the requisite competence, expertise and appropriate risk management and internal controls systems. There needs to be adequate internal controls and the existence of written procedures, which should be regularly monitored by its senior management for compliance.

As part of risk management, a fund management company also monitors the aggregate exposure of all managed assets to specific securities, to avoid undesirably high exposure to specific securities. Typically, a fund management company would maintain an authorized brokers list to minimize counterparty risk. Dealers will not undertake any business with any broker who is not included in the authorized brokers list. Counterparty risks of the brokers are assessed before authorization to ensure that the brokers are suitable, financially sound and provide good settlement and administration services.

(Investment involves risk. Please refer to the offering document for further details including the risk factors.)

Hong Kong Investment Funds Association