

COGNITY® CASE STUDY: GLOBAL ASSET MANAGER

Global asset management firm seeks to reduce VaR exceedances over multi-asset, multi-currency funds.

SITUATION

Risk Model with Multiple VaR Breaks

The Head of Risk for a large global asset management company had to solve for more than 20 Value at Risk (VaR) exceedances in one year within two funds. The UCITS boundaries for validating a risk model, dictate that a VaR risk model is good so long as the number of losses exceeding the VaR within one year are between zero to six at least 95% of the time. In the case of this particular client, the huge number of VaR breaches indicated the risk model and risk platform used for estimating the risk of the two multi-currency, multi-asset funds did not provide an accurate estimate, as indicated by losses exceeding the acceptable boundaries.

Regulators and Board Demand Immediate Action to Address Risk Breaches

The number of VaR exceedances meant added stress for the risk team in terms of regulatory compliance. The team had to take immediate measures to remedy the risk process and models used for the two funds. The regulators, and thereby the Board required an explanation of the breach, as well as an executed plan to remedy the breach. The risk team had just a limited amount of time to develop a new model and platform for measuring the risk of the two particular funds, and then report those plans back to the Board and regulators.

AT-A-GLANCE

COMPANY

Global Asset Manager

Challenge

Address breach in VaR exceedances, in accordance with UCITS requirements, and instill confidence in regulators and Board for the new risk management measures.

Solution

The Cognito risk model, when backtested on the customer's portfolios resulted in an acceptable number of VaR exceedances - meaning within confidence bounds - to prove the quality of the model and its adaptiveness to varying market regimes. Cognito provided a clear lens into the firm's portfolio risk, utilizing an open and transparent "real world" risk modeling approach that understands the structure of financial asset distributions and adapts to all markets regimes.

Benefits

- Reduced number of VaR breaks to an acceptable level
- Enabled Risk team to meet regulatory requirements and Board demand to adequately remedy the large number of exceedances
- Added a significant amount of additional analytics and functionality, including the Cognito Risk Reporting Services - a fully automated provisioning of daily risk reports along with validation and monitoring of the process.

PROCESS

Collaboration

The Head of Risk and the risk team were already acquainted with the BISAM Cognition platform and the benefits of the patented Cognition fat-tailed risk modeling approach, as several other of the firm's funds under management were already implemented within the Cognition risk reporting framework. So, the customer approached BISAM to support them in the situation and present VaR backtests of the Cognition models both for meeting regulators' requirements, and for reassuring the Board that adequate measures were being put into place to prevent future VaR exceedances outside of the acceptable confidence levels. The BISAM team delivered comprehensive analyses with backtests and bias tests of the risk measures that were taken within the two funds. The results suggested that any exceedances within the BISAM risk model were within the confidence bounds for the same period of time when the alternative risk solution resulted in 20 exceedances. The entire set-up and testing process was completed within two weeks and all backtest experiments were executed directly in the Cognition platform which provided additional transparency.

Reliable and Accurate

The Head of Risk selected Cognition for the two funds, satisfied that Cognition had proven the quality and accuracy of its models

during the years of usage elsewhere within the company. Implementation of Cognition for the two funds not only replaced the existing risk model, but also added a significant amount of additional analytics and functionality. In addition to this, the client was also able to leverage risk reporting services within Cognition - a fully automated provision of daily risk reports, as well as validation and monitoring of the process.

PRODUCT SUCCESS

Advanced "Real World" Risk Models Adaptive to Market Regimes

Implementation of the patented Cognition Fat-Tailed models allowed the customer's risk team to fully utilize the comprehensive full-repricing model for risk of multi-currency and multi-asset class funds and to be confident they were using an approach that incorporates the most advanced statistical methods for modeling extreme events, volatility clustering, regime switching and correlation shifts in times of market crisis.

Met Regulatory and Board Requirements

BISAM's unique combination of Cognition product capabilities and staff expertise meant that the risk team was able to deliver comprehensive risk results, meet regulatory requirements and satisfy Board expectations.

About BISAM

BISAM is the leading provider of sophisticated digital solutions for performance, attribution, market risk, portfolio construction, GIPS composites management and reporting. Many of the world's largest asset managers use BISAM's best-in-class portfolio analytics platforms to evaluate and enhance their investment strategies and better service their clients, while maintaining high levels of security, transparency, process control and operational scale.

For more information or a Cognition demo, please contact us

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For more information or a Cognity demo, please contact us

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