Volume 1, Issue 1 | Oct 21, 2018

SAGA STRATEGIES

SAGA Views and News

Welcome to SAGA Strategies' newsletter! In this issue, an important brief on balancing risk and reward as well as some interesting links for you to browse through.

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Risk is the Other Side of the Coin

More often than not, the investment portfolios being managed in family offices, foundations and endowments target a linear and absolute rate of return without much attention paid to **risk – the other side of the return coin** . As we discussed in the last newsletter, the GFC (Global Financial Crisis) of 2007/08 caught almost everyone in the GCC by surprise. Most family and investment offices incurred substantial losses. It took years to recuperate their lost returns. And some family offices went further by taking on riskier assets in the hopes of catching up on the lost value.

Keeping in view the frothy stance of global markets, the timing of the 8-12 year business cycle, and the relative mismatch of risks-returns, we could essentially see the next downturn to be broader and deeper. So it makes sense that family offices ensure they are better prepared this time.

Risk is not bad. Risk drives the correlated return expectations. Even from an Islamic perspective, investors are encouraged to understand the inherent risks in their business decisions. In fact, taking risk head on is the key to ensuring family offices (and their portfolios) are not caught off-guard. To this effectively, there are three basic principles when considering a risk framework:

1. *identifying* the risk
2. *mitigating* the risk (where possible)
3. *managing* the risk (where not mitigated)

Before embarking on the development of a risk framework, **family offices should consider a Strategic Risk Plan** outlining in clear detail the risk appetite including:

1. How much of the principal is the family office willing to lose?
2. What are the limits to market risk, credit risk and investment drawdown?
3. What are the parameters for leverage both at the asset and portfolio levels?
4. What kind of non-financial risks (reputational, operational, corporate) should be considered?

The answers to these can come from a well-developed and executed Investment Policy Statement (IPS) – a key component of a methodical investment strategy.

The next step is to ensure the governance of risk and return processes is fully integrated in the investment approach and is well-functioning. Without the proper risk governance, a family office can not possess the capabilities to act strategically, and act in a timely and decisive manner about risks when they arise.

Key risk processes should also include the ability to assess risk when making new investments and how the specific risks associated with a specific investment integrates into the overall portfolio level risk.

On top of all the details that go into the above, perhaps the most important aspect of risk management for family offices is the independence of the risk manager. The function needs to be distinctly separate from having any direct or indirect responsibility in selecting or managing the investments as well as being unduly influenced one way or another when identifying and managing risks.

While the above may sound very prescriptive, the fact of the matter is that a family office should inculcate the awareness that risk and return are two sides of the same coin without either no portfolio is truly balanced.

Learn more here

Interesting News

- **(Forbes) Three Critical Mistakes In Establishing Single-Family Offices** - A useful overview of the errors commonly made when establishing family offices. Among these are clarity of goals, operational and structural relevance, and an executable agenda. The right advisor with the requisite experience helps mitigate these mistakes.
- **Private Wealth Systems Launches Industry-First Digital Ecosystem for Family Offices**- In the GCC, systems and operations are often overlooked in the design and development of family offices and investment platforms. This is an interesting news release about the development of a family office digital ecosystem seeking to provide a unified solution.
- **New Research: Family Office Portfolio Performance More Than Doubles From Previous 12 Months**- A new report has been released by UBS and Campden Wealth on the performance of family offices in the last 12 months. Key findings include a marked increase in family office investment performance, private equity leading allocations, and increased investment in sustainable ventures and deals.