DATA MANAGEMENT

Riskdata Introduces ShockVaR Measurement

By Maureen Nevin Duffy

Riskdata, a supplier of risk management solutions to the alternative investment industry, is aiming to improve hedge fund transparency by teaming with Hedge Fund Research to publish daily value at risk (VaR) indicators, including a new measurement—ShockVaR.

During a market crisis, says Riskdata, VaR calculations, or how much a portfolio might lose over a particular time frame, may not accurately account for risk. "Unlike more traditional VaR measurements," said Riskdata chairman Olivier LeMarois, "ShockVaR indicates the possible over- or under-estimating of risk during periods of extreme market stress."

ShockVaR shouldn't be solely relied upon any more than traditional VaR, but it's an interesting tool in determining "where hot spots are in terms of risk," said LeMarois, adding that a lack of risk-related information amid market turmoil can cause panic.

During the last two weeks of September and all of October, hedge funds were buffeted by historically high volatility, noted Ken Heinz, president of Chicago-based Hedge Fund Research. His firm's role in ShockVaR "is just an effort to reflect the reality of performance dynamics."

As an example of the effectiveness of the new measurement, Riskdata points to its calculation of the Nikkei 225 index—which tracks equities on the Tokyo Stock Exchange—on Oct. 20 and Oct. 21, when its ShockVaR rating rose from negative 15 percent to negative 13 percent, compared to the S&P 500's negative 14.5 percent and the Stoxx 50 and FTSE indexes, which hovered around negative 16 percent. On Oct. 22, the Nikkei's ShockVaR reading fell to negative 19.3 percent, which coincided with the Nikkei's 9.6 percent market drop and ran contrary to positive movement in the other three indexes. Since the most recent turmoil began in Tokyo, Riskdata calls this evidence of the indicator's ability to anticipate increased stress and pin-point its source.

Olivier LeMarois

"With the backdrop of global recession, short-term turmoil is building up in various markets around the globe and in various asset classes," said Ingmar Adlerberg, CEO of London-based Riskdata, which also calculates risk for bonds, equities and commodities. "The least that can be done in such a situation is to monitor closely global risk parameters, to anticipate as much as possible the source and consequences of the next possible shock."

A commonly used tool, VaR has been heavily criticized in light of the market meltdown, with several academics attacking its usefulness and dependability. Nassim Nicholas Taleb, author of "The Black Swan," a book that examines the difficulty of predicting events based on past observations, has declared that "VaR is charlatanism, a dangerously misleading tool."

"There is some truth in the criticism of VaR," said Riskdata's LeMarois, "if it is relied on as only one figure for the measurement of risk. VaR should be considered only in conjunction with other risk indicators. If you oversimplify reality, one day reality gets you." Historically the industry has relied simply on VaR and volatility, in an isolated process, contends LeMarois. "This has been a major flaw in the market—VaR is not the alpha and the omega of risk. We can give much more, as in the new ShockVaR."

"If you oversimplify reality, one day reality gets you."

Riskdata's VaR and ShockVaR measurements are available for free on its Web site, where theoretical portfolios comprised of hedge fund indexes—supplied by Hedge Fund Research—are used to demonstrate its capabilities over a range of strategies. ■