

FUND RISK INDICATOR

What is the Fund Risk Indicator?

1. The “Fund Risk Indicator” indicates the risk of your MPF fund. The higher the Fund Risk Indicator, the higher the risk. You can find it in the Fund Fact Sheet and on the MPF Fee Comparative Platform on the website of the MPFA.
2. There are many possible ways to measure risk. The risk measure that has been adopted for MPF funds is a measure called standard deviation, which is calculated over a three-year period. Technically this shows the volatility of price as a percentage around the average price over the measurement period. In effect this shows how much the price of the fund has moved, upwards or downwards, over that three-year period.
3. The risk of a fund is important because research suggests that there is a strong relationship between the level of risk and the likely returns over the longer term. The higher the risk, then generally, the higher the expected return over the long term. The downside is that the higher the risk, the greater the chance of large downward price movements in the shorter or even medium term.
4. The risk indicator is of most value when making comparisons between funds. A single risk indicator figure, by itself, may not be of much use to you, but by comparing the risk indicator as between funds, you will get an idea of their relative risk.

Some examples of risk and return of MPF funds

5. The examples below show the relationship between risk (measured by the Fund Risk Indicator) and the investment returns of 4 real MPF funds.

Risk and return of MPF Funds (1 July 2004- 30 June 2009)

FUND TYPE	FUND RISK INDICATOR AS AT 30 JUN 2009*	ANNUALIZED RETURN	HIGHEST MONTHLY RETURN	LOWEST MONTHLY RETURN	RANGE OF HIGHEST/ LOWEST RETURN	NUMBER OF MONTHS WHERE RETURN DROPPED MORE THAN 5%
Fund A Asian Equity Fund	26.35%	7.02%	13.65%	-20.84%	34.49%	11
Fund B Mixed Assets Fund	16.41%	4.94%	8.76%	-13.41%	22.17%	6
Fund C Bond Fund	3.95%	2.13%	3.37%	-2.07%	5.44%	0
Fund D MPF Conservative Fund	0.37%	1.62%	0.37%	0.00%	0.37%	0

* Annualized standard deviation based on the monthly rates of return over the past 3 years (1 Jul 2006 – 30 Jun 2009).

6. As you can see from the above, the Fund Risk Indicator was highest in the case of Fund A which is an Asian Equity Fund, at 26.35%, followed by that of Fund B, the Mixed Assets Fund (16.41%), Fund C the Bond Fund (3.95%) and Fund D the MPF Conservative Fund (0.37%).

7. Fund A, the Asian Equity Fund had the highest risk indicator (i.e. its price fluctuated the most). It also had the highest return of the four funds. Those returns were however very volatile: the fund went up 13.65% in one of the months and down as much as 20.84% in another. In the five years under review, there were 11 months where the price of Fund A dropped by more than 5%.

8. At the other extreme, Fund D, the MPF Conservative Fund had the lowest risk indicator, and correspondingly had the lowest returns at only 1.62% per year. The fluctuations in monthly returns were however very low; the best month was +0.37% and the worst month was 0%. This fund had no months where the price dropped by more than 5%.

9. As you can see from the table, the other two funds, B and C, were between the two extremes in all respects. Fund B was the second most risky; it also had the second

highest returns, the second highest range of fluctuation and had 6 months (the second highest) where the price of the fund dropped by more than 5%.

10. The above should illustrate to you the relationship between the risk of a fund and its performance attributes under normal market conditions. Higher risk funds are likely to deliver higher returns over the long run, but you should be prepared to bear some periods of losses and even a few months of quite significant losses. The probability of higher long-term returns is the reason why financial advisors generally recommend that younger investors should consider investing in higher risk funds. Younger investors have the time to ride out shorter-term volatility and gain the benefits of higher, longer-term returns. Conversely, MPF investors who are closer to retirement may need access to their benefits quite soon and so might not want to invest in a way that might produce significant losses in the short term.

11. The risk of a fund is one of the important factors in making investment decisions as between different funds. Other factors such as your own circumstances, personal finance and savings, years to retirement and the fees applicable to each fund will also be relevant.

12. If you are interested in the details, the formula for calculating the Fund Risk Indicator can be found on the website of the MPFA at www.mpfa.org.hk under “Standards” in “Legislation and Regulation”.