



Press Release

Nice, June 18, 2009

EDHEC research shows that institutional investors' short-term constraints are less costly than the lack of genuine risk management strategies

The results of a new study by EDHEC entitled "Measuring the Benefits of Dynamic Asset Allocation Strategies in the Presence of Liability Constraints," drawn up by Lionel Martellini, scientific director, and Vincent Milhau, research engineer with the EDHEC Risk and Asset Management Research Centre, suggest that **it is not so much the presence of funding ratio constraints that is in itself costly for pension funds as their reluctance to implement risk-management strategies that are optimal given such short-term constraints.**

According to EDHEC, dynamic risk-management strategies can turn irreversible contributions into reversible contributions and short-term constraints into long-term constraints, hence the severe opportunity cost for pension funds that do not follow them.

Institutional investors in general, and defined-benefit pension funds in particular, are currently facing a profound dilemma. The desire to alleviate the burden of contributions leads them to invest significantly in equity markets and other classes that are poorly correlated with liabilities but offer better long-term performance potential. However, stricter regulations and accounting standards give them significant incentives to invest most of their portfolios in assets that are highly correlated with liabilities. Only dynamic allocation strategies that are contingent on the state of markets and therefore on the outperformance or underperformance of the investor's performance portfolio in comparison with their liabilities allow this dilemma to be resolved. The idea is to implement genuinely dynamic management of asset-liability risk budgets, as is already the case in asset management with portfolio insurance techniques.

EDHEC's empirical tests at a 10-year horizon show that implementing a risk control strategy while respecting a maximum funding ratio of 130% (a level beyond which the pension fund's utility is assumed to be nil), in addition to a minimum level of 90%, would allow the conditional mean of the funding ratio to be brought down to 110%; it would also allow for savings of 17.885% in terms of initial contribution under the assumption of irreversible contributions.

This study was sponsored by BNP Paribas Investment Partners.

The publication "Measuring the Benefits of Dynamic Asset Allocation Strategies in the Presence of Liability Constraints" can be downloaded by clicking on the following link:

http://docs.edhec-risk.com/mrk/000000/Press/EDHEC_Measuring_Benefits_Dynamic_Asset_Allocation.pdf

EDHEC

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About EDHEC

EDHEC Business School, founded in 1906 and among the select few institutions to have garnered international recognition through the triple crown of EQUIS, AACSB and Association of MBA accreditations, offers management education designed to meet the needs of companies. With its three campuses in Lille, Nice, and Paris, its 5,000 students, more than 25% of whom are from abroad, and its 110 full-time faculty, EDHEC has been ranked among the top European business schools for several years.

EDHEC Business School is recognised as a centre of excellence for asset management and alternative investment research and several of its professors are regarded as international experts in the fields of asset management, fixed income securities, alternative investments and risk management. The aim of the EDHEC Risk and Asset Management Research Centre is to produce research that meets the most stringent academic standards and to facilitate corporate use of this research. In partnership with large financial institutions, the research centre brings together 46 researchers and implements six industry-sponsored programmes and ten research chairs focusing on asset allocation and risk management in the traditional and alternative investment universes. Adopted by managers and investors, the EDHEC Alternative Indexes are superior measures of performance of the various hedge fund styles.

About BNP Paribas Investment Partners

BNP Paribas Investment Partners brings together the full palette of asset management expertise of the BNP Paribas group.

Through a unique platform that offers immediate and simplified access to a broad range of specialist Partner companies, BNP Paribas Investment Partners has become a leader among the multi-specialist asset managers. At 31 March 2009, assets under management amounted to €325 billion*, nearly half of which was managed for institutional clients.

With 2,600 professionals serving clients in 72 countries, BNP Paribas Investment Partners draws on over half a century of asset management experience and has seen ten years of steady growth through acquisitions and joint-ventures.

** assets under advice included*

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