PERFORMANCE PERSPECTIVES

with David Spaulding

VOLUME 2 – ISSUE 7 MARCH 2005

Since 1990, The Spaulding Group has had an increasing presence in the money management industry. Unlike most consulting firms that support a variety of industries, we focus on the money management industry.

Our involvement with the industry isn't limited to consulting. We're actively involved as members of the CFA Institute (formerly AIMR), the New York Society of Security Analysts (NYSSA), and other industry groups. Our president and founder regularly speaks at and/or chairs industry conferences and is a frequent author and source of information to various industry publications.

Our clients appreciate our industry focus. We understand their business, their needs, and the opportunities to make them more efficient and competitive.

For additional information about The Spaulding Group and our services, please visit our web site or contact Chris Spaulding at

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OUR NEW LOOK

We decided to undergo a facelift. Our designer, Cybill Conklin, put this together for us and we're quite pleased. She's done lots of work for us and we're always amazed by her creativity. We hope you like the new look, too.

MANDATORY VERIFICATION – WILL IT EVER END?

I had mistakenly thought that we (those who oppose mandatory verification) had successfully won over the hearts-and-minds of the members of the Investment Performance Council (IPC). However I was mistaken. At their semi-annual meeting earlier this month (in Hong Kong), they decided to pursue making verification mandatory at some point in the future. I will continue to oppose this.

Why? Let's start with our survey evidence: over 60% of the North America-based respondents to our 2002 survey opposed making verification mandatory for GIPS. The vast majority of those who favor mandatory verification are based in Europe.[1] In addition:

- verification doesn't verify compliance
- verification is very costly and can be a *barrier for entry* for many firms
- verifiers often get it wrong (*i.e.*, many firms that have received a positive report from their verifier are later found to be out-of-compliance)
- in the U.S., the SEC offers "free verifications"[2] – you just don't want to fail them
- the market has caused many firms to get verified.

While a couple countries made verification mandatory as part of their *Country Version of GIPS*, the vast majority didn't. And while many local sponsors support mandatory verification, it's clear from our survey results that this is hardly a universal opinion. Something that's going to cost firms a great deal of money on an annual basis should be left voluntary. Hopefully it will be – I haven't given up the fight.

1 *Performance Presentation Standards Survey – 2002 Detailed Results*. Page 24.

2 To clarify, the SEC doesn't actually offer verifications; however, when they come in to do a review of a firm that claims compliance, they will often attempt to validate that the firm is, in deed, complying.

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IS DAILY ATTRIBUTION NECESSARY?

Our recent attribution survey showed that most firms calculate attribution on a daily basis.[3] But why? I suspect there are two possible reasons:

1. Some people like to look at daily attribution results
2. Daily attribution will increase the accuracy of monthly, quarterly, and annual results.

The first possible cause is easy to deal with: why? Why would you want to look at daily attribution results? In most cases, the effects will be microscopic (*i.e.*, less than a basis point). I shouldn't really be so hasty to dismiss the value of daily. Some have said that daily will help identify problems or issues that may arise. However, I suspect that this isn't that common a situation…but I could be wrong.

Now, to the second reason: to improve accuracy. If you're using a holdings-based model, then daily should improve the accuracy as it will pick up the impact[4] of intra-period transactions. Ideally, you should insure that the daily data is accurate (reconciled), otherwise the results may be spurious.

What if you're using a transaction-based model. In that case, I would argue that daily will not make much of a difference in the accuracy. In a transaction-based model, we want to pick up the activity, to insure that the security and sector returns are accurate. In addition, we need to insure that our weights are correct, and this can be determined by knowing the trade details.

Since we learned in our recent attribution survey that most firms prefer a transaction-based model,[5] the justification for a daily system seems to be lacking, at least as a justification for improved accuracy.

A disadvantage to a daily system is the increased amount of data you will need to store, especially if it's a security-level system. Your data storage needs may quickly go from *billions* to *trillions* of bytes, meaning increased costs.

If you're considering a daily system, you should consider the tradeoffs, and determine if this step is justified.

PERFORMANCE SOFTWARE VENDORS IN THE NEWS

Two large software vendors with sizable products devoted to investment performance have recently been in the news.

3 *Performance Measurement Attribution Survey – 2004 Detailed Results.* Page 12.

4 Granted, they're picked up a day late and this approach will not recognize day-trades (purchases in the AM, followed by sales in the PM), but it's an improvement over relying solely on the beginning of month holdings and assuming they're constant through the period.

5 *Performance Measurement Attribution Survey – 2004 Detailed Results.* Page 22

…since in many markets settlement date is T+3, we could have you using both trade date and settlement date accounting simultaneously!

You may have heard that Financial Models was "in play." It had a few suitors and SS&C Technologies has apparently won out.[6]

SunGard is undergoing a $10.8 billion leveraged buyout.[7] While the *WSJ* article I cite as the source focused on "the relatively humdrum business of backing up computer data," one could hardly call the world of investment performance "humdrum." While Xamin's percentage of SunGard's overall revenues is probably not that great, those of us in performance measurement are aware of this firm's impact on the industry.

Granted, in both of these cases performance was just a piece of the firm being bought. However, it still gives testimony to the attractiveness of this market. We believe that similar events will continue to occur as this is definitely a growth area.

WHAT DOES "TRADE DATE" MEAN?

When we say that we're using "trade date accounting," what does this mean (as opposed to "settlement date accounting")? Well, for many it means that we're recognizing the trade on "T" or on "trade date." And settlement date accounting would mean that we won't recognize the trade (in our system) until settlement date, which can vary by market. Because the AIMR-PPS recommended trade date accounting for periods prior to January 1, 2005, there was a requirement that firms disclose if they used settlement date.[8]

So, it might surprise you to read: "The principle behind requiring trade-date accounting is to ensure there is not a significant lag between trade execution and reflecting the trade in the performance of a portfolio. For the purposes of compliance with the GIPS standards, portfolios are considered to satisfy the trade-date accounting requirement provided that transactions are recorded and recognized consistently and within normal market practice--typically, a period between trade date and up to three days after trade date (T+3)."[9] This means that trade date can be T, T+1, T+2, or T+3. And, since in many markets settlement date is T+3, we could have you using both trade date and settlement date accounting simultaneously! Interesting. And no doubt, confusing. I hope to see some clarity on this as we move to the next version of the standards.

6 See www.fmco.com/news/2005-02-25.asp and www.ssctech.com/about/press.asp?N=209.

7 "SunGard Deal Is Near as Field of Targets Shrinks for Bulging Buyout Funds." *The Wall Street Journal*. March 28, 2005: Page C1.

8 *AIMR Performance Presentation Standards*. 2001. Page 16, paragraph 4.A.4.

9 See www.cfainstitute.org/programs/standards/gips/faqs/gipsresults.asp?term=Trade%2DDate+Accounting &sequence=1

NEWS RELEASE...

FOR IMMEDIATE RELEASE

For Further Information, please call: Patrick Fowler, The Spaulding Group: 001-732-873-5700

THE SPAULDING GROUP TO CONDUCT SURVEY ON THE PERFORMANCE PRESENTATION STANDARDS

Research Project Coinciding with Release of the Latest Version of the GIPS® Standards

Somerset, NJ – April 5, 2005. The Spaulding Group, Inc. (TSG) announced today that it will conduct it's sixth survey of the Performance Presentation Standards. The "presentation standards" began with the Association for Investment Management and Research's Performance Presentation Standards (AIMR-PPSR Standards), which went into effect in January, 1993. With the introduction of the Global Investment Performance Standards (GIPSR Standards), as well as various country-specific standards, the term has taken on a much broader meaning, and this survey addresses the full breadth of the standards. "This is an exciting time for the standards" said TSG's senior vice president, Patrick Fowler, who heads up the research area. "This is the third time we will address the global standards and the first time there has been any significant change to them. We want to see how the industry is going to respond to the changes."

TSG was the first firm to research the industry's attitudes about the AIMR-PPS Standards and this recent effort will mark the sixth time TSG has surveyed the industry on these standards.

There are four distinct surveys on TSG's website, each tailored to a particular segment of the investment industry: investment managers, plan sponsors, investment consultants, and verification firms. The surveys are available in MS/Word and PDF format. Survey participants will receive a complimentary copy of the survey (a US$395 value) for assisting with this research effort.

CFA Institute (formerly AIMR) has agreed to assist with the survey content as well as make its E-mail alert list subscribers aware of this research effort. We greatly appreciate all the support and insight we have received from the survey cosponsors: Advent, CAPS, Eagle Investment Systems, Financial Models, First Rate Investment Systems, Informa Investment Solutions, Kreischer Miller, Performa, StatPro and Wilshire Associates.

"We are very excited that our cosponsors have agreed to support this effort," said David Spaulding, TSG's president. "The standards have had a major impact on the industry over the past thirteen years and it's fitting to see where we stand today, especially in light of the changes to the GIPS Standards and the move to convergence."

"This is a global research project," said Patrick Fowler. "We encourage money managers, plan sponsors, consultants, and verifiers from around the world to participate and provide their input during the coming months, as we will process the data this summer, and publish the results in August/September. Even if a firm doesn't currently support or comply with the standards, we want to hear from them."

The Spaulding Group, Inc. is the leader in investment performance measurement products and services. TSG publishes *The Journal of Performance Measurement®*, a quarterly publication they launched in 1996, and hosts the Performance Measurement Forum. The firm conducts the annual Journal of Performance Measurement Performance Measurement, Attribution and Risk (PMART) conference in New York. Through the Institute of Performance Measurement, the firm offers performance measurement training, including an introductory course on performance measurement, a course on performance attribution, and a performance measurement class specifically designed for plan sponsors and consultants. The company was founded in 1990 by David Spaulding and provides services and products to financial institutions throughout the world. Other details about TSG's services may be obtained from its website: **www.SpauldingGrp.com.www.SpauldingGrp.com.**

TRAINING...

Gain the Critical Knowledge Needed for Performance Measurement and Performance Attribution

TO REGISTER:

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INTRODUCTION TO PERFORMANCE MEASUREMENT

A unique introduction to Performance Measurement specially designed for those individuals who require a solid grounding in all aspects of performance measurement. The Spaulding Group, Inc. invites you to attend Introduction to Performance Measurement on these dates:

May 9-10, 2005 San Francisco, CA

July 19-20, 2005 Chicago, IL

September 12-13, 2005 New York, NY

October 17-18, 2005 Boston, MA

November 14-15, 2005 Los Angeles, CA

December 6-7, 2005 Washington, DC

15 CPE Credits upon course completion

PERFORMANCE MEASUREMENT ATTRIBUTION

A day and a half devoted to this increasingly important topic. The Spaulding Group, Inc. invites you to attend Performance Measurement Attribution on these dates:

May 11-12, 2005 San Francisco, CA

July 21-22, 2005 Chicago, IL

September 14-15, 2005 New York, NY

October 19-20, 2005 Boston, MA

November 16-17, 2005 Los Angeles, CA

December 8-9, 2005 Washington, DC

11 CPE Credits upon course completion

These programs may qualify for the CFA Institute's Professional Development Credit. If you are a member of the CFA Institute, please refer to their website to determine whether this program meets the criteria for CFA Institute PDP credit, to calculate credit hours, and to verify documentation requirements. www.cfainstitute.org/pdprogram

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