

# PERFORMANCE PERSPECTIVES

with David Spaulding



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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, our focus is 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 [CSpaulding@SpauldingGrp.com](mailto:CSpaulding@SpauldingGrp.com)

*"I'm late! I'm late! For a very important date!  
No time to say hello, goodbye! I'm late, I'm late, I'm late!"*<sup>1</sup>

And yes, I AM late with this issue...but only by a very few days (if that really matters): late is late. I won't offer any excuses...just an acknowledgment of my tardiness and the hope that it won't happen again.



**"RISK IS BACK IN STYLE."**<sup>2</sup>

So began an article in the most recent issue of the *Wall Street Journal's* weekend edition. You've probably heard that economists are in general agreement that the recession is ending. We also know that consumer confidence is up and unemployment numbers are easing. All good news. But to hear that "risk is back in style" is quite a leap, not that I would want to discourage such boldness.

What were the ingredients for this remarkable turnaround? I don't think that a new U.S. President and the press deciding to stop bashing the economy hurt: negative thoughts breed negative behavior and more negative thoughts. Let us hope that the complete turnaround is a swift one.

## PMAR VII...A HUGE SUCCESS

This month (okay, it was actually last month, but this IS the May issue) we held our seventh annual Performance Measurement, Attribution & Risk Conference. While our attendee total was down (no surprises there), everyone agreed that it was a phenomenally successful program. We assembled some great speakers to tackle some very interesting topics. In this issue I will share with you some of what was presented.

## A FEW HIGHLIGHTS

We introduced two new topics for PMAR: *Fast Performance* and *Mad Performance*.



John Simpson chaired a panel of performance measurement professionals who addressed a variety of topics in a fairly short and crisp fashion.

<http://www.SpauldingGrp.com>

<sup>1</sup> Carroll, Lewis. "Alice's Adventures in Wonderland." Spoken by the White Rabbit.

<sup>2</sup> Frangos, Alex. "Dow Gained 4.1% For Month of May." *The Wall Street Journal*. May 30-31, 2009

# The Journal of Performance Measurement®:

## UPCOMING ARTICLES

### Determining the Optimal Mutual Fund Style Classification Methodology

– David M. Blanchett, CFA and  
Craig Israelson, Ph.D.

### 101 Ways to Measure Performance

– Philippe Cogneau, and  
Georges Hübner

### Risk Attribution

– Philippe Grégoire, Ph.D.

### Refining the Sharpe Ratio

– Craig L. Israelsen, Ph.D.,  
Brigham Young University

### On Turning Three: Reflections on the CIPM® Program

– Philip Lawton, CFA, CIPM,  
CFA Institute

### Performance Analytics Systems

– In House or Vendor Package  
– Kyle Ringrose, CFA,  
Wilson HTM Investment Group

### A Global Investment Attribution Analysis Based on a Symmetrical Arithmetic Attribution Model

– Yuri Shestopaloff, Ph.D.,  
SegmentSoft Inc.

### A Comparison of Plan Sponsor Attribution Methodologies: Multi-Level Brinson Attribution vs. Macro Attribution

– John D. Simpson, CIPM,  
The Spaulding Group, Inc.

I took on the role of the *Mad Performer*, with perhaps the highlight being my suggestions on ways to improve returns.

Victorious for the second time in our seventh annual *Battle Royale* was Carl Bacon, who bested his contender, Austin (from Austin) Long in a battle of wits regarding the benefits of the Internal Rate of Return.

## PAST SPECIFIC RECOMMENDATIONS

Steve Stone of Morgan Lewis provided one of our best discussions on compliance issues, as he addressed numerous topics relating to performance measurement. For me one of the revelations was his discussion on the subject of “past specific recommendations.” Historically, SEC-registered firms were prohibited from advertising the results of specific investments; and while some thought that as long as there was a balance (e.g., “top 5,” “bottom 5”) it would be okay, the general response often was a simple “no.”

Steve discussed a recent SEC no-action letter regarding TCW Advisors<sup>3</sup> whereby there has been some relaxation on this topic, provided firms follow the rules.

If this is of interest to you, please review the documentation and consult your compliance officer and/or outside counsel.

## VAR...ARE YOU CONVINCED THAT IT'S VOODOO YET?

In last year's *Battle Royale*, I was severely defeated by Robert Mackay (I threatened to ask for a recount but when you lose by double digits it's kind of hard to justify the time and expense). I argued that VaR was voodoo while Dr. Mackay held to the argument that there's much value in this risk measure.

He graciously accepted our invitation to return, this time to spend an entire session discussing VaR. The basis for his talk was the “carry trade strategy,” which he summarized as follows:

- The Basic Carry Trade: Borrow for a month in a low interest rate currency (the “funding” currency), convert the borrowings at the spot exchange rate into a high interest rate currency (the “target” currency), and then lend for a month in the target currency at the higher interest rate
- If the spot exchange rate does not change or if it depreciates by less than the interest rate differential, this strategy earns a positive return
- Repeat this strategy each month choosing a new interest pair depending upon how rates have changed over the month

He demonstrated the results of employing this strategy using a hypothetical scenario. For a long period the results were quite good. And VaR's predictions as-of 3Q08, even at the low-end of the range, weren't necessarily horrendous. However, even Robert had to acknowledge that what has transpired since that date wasn't anticipated: the losses were much greater than predicted.

<sup>3</sup> <http://www.sec.gov/divisions/investment/noaction/2008/tcwgroup110708.htm>.

## ATTENTION:

To help aid those looking for employment PerformanceJobs.com is waiving its listing fee from now until July 31, 2009. If your firm has any jobs it would like to post on PerformanceJobs.com please contact us today!

## PERFORMANCEJOBS.COM WEBSITE

We're pleased to announce that our new website is now available for PerformanceJobs.com. Take a visit and you'll also see that we already have jobs posted. We're very excited with the initial interest this new venture has caused and look forward to it becoming the major resource for individuals seeking employment as well as firms looking to hire. If you know of someone who is looking for a career in investment performance, please direct them to our site and encourage them to submit their resume today.

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In the accompanying figure the blue dashed lines show the 95 percentile range for the Carry Trade Strategy while the red dashed lines show the range for the S&P 500; the solid lines depict reality.

During the Q&A portion I asked Robert if anyone predicted the terrible market

we witnessed and he acknowledge one group: Moodys. However, while they predicted the poor securities and housing markets they did so for the wrong reasons, so do they get any credit?

If there's a lesson to be learned it's that when predicting the future a great deal of caution must be exercised and the recipients of the information must be informed of what the projections are based on and the risks inherent in the measure itself.



## PERFORMANCE MEASUREMENT FOR PENSION FUNDS

A number of speakers touched on this topic, including our custodian panel, Auke Plantinga, and Steve Campisi.

There is increasing agreement that pension funds, when assessing how they did (as opposed to how their managers did) shouldn't rely on time-weighted measures. We're clearly not even close to a majority on support for this, but the numbers are definitely increasing.

## MULTI-CURRENCY ATTRIBUTION

Jose Menchero has successfully established himself as an innovator and forward thinker in our industry. He's now tackling multi-currency attribution and provided a methodology which he contends improves upon the Karnosky-Singer model.<sup>4</sup>

While I am not able to opine in any detail on his approach, I can tell you that a forthcoming article by Jose will go into much detail on this methodology.

Multi-currency attribution is a topic that needs more attention, especially in this global investing world we find ourselves in. While not everyone requires a complex model to capture the effects of changes in the FX rates, for those who do, new ideas should be welcomed and encouraged.

## A BLOGGING WE WILL GO

I created a Facebook page just a couple months ago and am finally getting the hang of LinkedIn, and so it's probably not surprising that I'm finally getting around to setting up a Blog. This is something that Patrick Fowler and I have been discussing for the past few months and we finally decided it was time to enter this new world of communicating.

<sup>4</sup> Karnosky, Denis & Brian Singer. *Global Asset Management and Performance Attribution*. 1994..

## THE SPAULDING GROUP'S 2009 INVESTMENT PERFORMANCE MEASUREMENT CALENDAR OF EVENTS

| DATE                  | EVENT  | LOCATION                |
|-----------------------|--|-------------------------|
| June 11-12, 2009      | Performance Measurement Forum                    | Stockholm, Sweden       |
| July 21-22, 2009      | Introduction to Performance Measurement Training | New Brunswick, NJ (USA) |
| August 24-25, 2009    | CIPM – Principles Level Preparatory Training     | New Brunswick, NJ (USA) |
| August 26-28, 2009    | CIPM – Expert Level Preparatory Training         | New Brunswick, NJ (USA) |
| September 15-16, 2009 | Introduction to Performance Measurement Training | Boston, MA (USA)        |
| September 17-18, 2009 | Performance Measurement Attribution Training     | Boston, MA (USA)        |
| October 20-21, 2009   | Introduction to Performance Measurement Training | San Francisco, CA (USA) |
| October 22-23, 2009   | Performance Measurement Attribution Training     | San Francisco, CA (USA) |
| November 12-13, 2009  | Performance Measurement Forum                    | Rome, Italy             |
| November 18, 2009     | Trends in Attribution Symposium (TIA III)        | Philadelphia, PA (USA)  |
| December 3-4, 2009    | Performance Measurement forum                    | Orlando, FL (USA)       |
| December 8-9, 2009    | Introduction to Performance Measurement Training | New Brunswick, NJ (USA) |
| December 9-10, 2009   | Performance Measurement Attribution Training     | New Brunswick, NJ (USA) |

*For additional information on any of our 2009 events, please contact Christopher Spaulding at 732-873-5700*

### KEEP THOSE CARDS & LETTERS COMING

We appreciate the occasional e-mail we get regarding our newsletter. Occasionally, we hear positive feedback while at other times, we hear opposition to what we suggest. That's fine. We can take it. And more important, we encourage the dialogue. We see this newsletter as one way to communicate ideas and want to hear your thoughts.

The reality is that ours is an extremely dynamic industry, with much happening on an almost daily basis. This blog will allow me the opportunity to voice my thoughts, reactions, and ideas in an almost real-time manner. And you're invited to offer your own reactions and insights, too.

The blog is fairly "bare bones" right now, but it's at least a start. You can find it at <http://investmentperformanceguy.blogspot.com/>.

Please let us know your thoughts.

Oh, and the newsletter WILL continue; the blog is simply a supplemental way to communicate.



## TRAINING...

### *Gain the Critical Knowledge Needed for Performance Measurement and Performance Attribution*

#### TO REGISTER:

**Phone: 1-732-873-5700**

**Fax: 1-732-873-3997**

**E-mail: [info@SpauldingGrp.com](mailto:info@SpauldingGrp.com)**



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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:

July 21-22, 2009 – New Brunswick, NJ

October 20-21, 2009 – San Francisco, CA

September 15-16, 2009 – Boston, MA

December 7-8, 2009 – New Brunswick, NJ

15 CPE & 12 PD Credits upon course completion

The Spaulding Group is registered with CFA Institute as an Approved Provider of professional development programs. This program is eligible for 12 PD credit hours as granted by CFA Institute.



#### PERFORMANCE MEASUREMENT ATTRIBUTION

Two full days devoted to this increasingly important topic. The Spaulding Group, Inc. invites you to attend Performance Measurement Attribution on these dates:

September 17-18, 2009 – Boston, MA

December 9-10, 2009 – New Brunswick, NJ

October 22-23, 2009 – San Francisco, CA

15 CPE & 12 PD Credits upon course completion

The Spaulding Group is registered with CFA Institute as an Approved Provider of professional development programs. This program is eligible for 12 PD credit hours as granted by CFA Institute.



#### IN-HOUSE TRAINING

The Spaulding Group has offered in-house training to our clients since 1995. Beginning in 1998, we formalized our training, first with our Introduction to Performance Measurement class and later with our Performance Measurement Attribution class. We now also offer training for the CIPM program. To date, over 2,000 individuals have participated in our training programs, with numbers increasing monthly.

We were quite pleased when so many firms asked us to continue to provide in-house training. This saves our clients the cost transporting their staff to our training location and limits their time away from the office. And, because we discount the tuition for in-house training, it saves them even more! We can teach the same class we conduct to the general market, or we can develop a class that's suited specifically to meet your needs.

The two-day introductory class is based on David Spaulding's book, Measuring Investment Performance (McGraw-Hill, 1997). The attribution class draws from David's second book Investment Performance Attribution (McGraw-Hill, 2003). The two-day Advanced Performance Measurement Class combines elements from both classes and expands on them.