PERFORMANCE PERSPECTIVES
with David Spaulding

VOLUME 7 – ISSUE 9 | MAY 2010

GIPS® 2010 NOW AVAILABLE AT A BOOKSTORE NEAR YOU!

Okay, maybe not a bookstore, but it is available from the CFA Institute! "Soft" copies (which obviously, through the use of a printer, can be converted into a "hard" copy) have been available, but "official" hard copies are available as well. We haven't heard yet when the handbook will be available, and I expect it's likely a 4Q10 /1Q11 event, but we'll have to wait to see.

At this month's Performance Measurement, Attribution & Risk (PMAR) conference, Jonathan Boersma, Executive Director of the Global Investment Performance Standards (GIPS) at the CFA Institute Centre for Financial Market Integrity, gave a presentation on the changes; obviously, time didn't permit an exhaustive review, but he covered many of the main areas. In addition, he provided copies of the recently adopted Q&As, which provide much needed answers to questions many of us have pondered.

MONEY WEIGHTING IS TAKING OFF…SLOWLY, BUT DEFINITELY HEADING TO NEW HEIGHTS!

We had a conversation recently with a brokerage firm that wants to develop their own performance system. They asked us to comment on their planned approach. And I was fully prepared to hear "we will use time-weighting, because that's GIPS compliant." We've heard this from several other BDs, and so fully expected we'd hear it again. But alas, we were wrong; they got it right! They plan to implement money-weighting through the internal rate of return! Hurrah for them!!!

A few of us have been pushing money-weighting for several years now, and it's great that many individuals have discovered that it's the formula that often makes the most sense.

START-OF-DAY, END OF DAY

For some time I've been encouraging firms to adopt the following approach to handle cash flows:

- Inflows = Start-of-day
- Outflows = End-of-day.

Well, we hit upon an exceptional example of why this approach makes sense, at least for the outflow part. I blogged about this recently but want to spend a bit more time on it.

Here's essentially the scenario that I was presented with:

The Journal of Performance Measurement®:

UPCOMING ARTICLES

Performance Outsourcing 2010 – Broadening the Debate
– Mark Goodey and Jim Trotter

GIPS 2010: Highlights of Forthcoming Changes
– Todd Juillerat

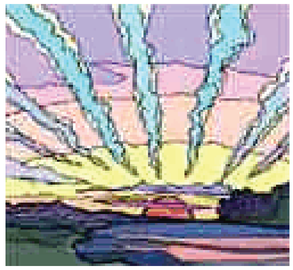
Extreme Risk Analysis
– Lisa Goldberg, Michael Hayes, Jose Menchero, Indrajit Mitra

Determining the Optimal Benchmark Indices for a Domestic Equity Returns-Based Style Analysis
– David Blanchett

Advocating a Trade/Strategy Approach to Attribution
– Jem Tugwell

- Beginning market value = $327,000
- Cash flow = $337,000
- Ending position = $940.

So, the portfolio begins the day with $327,000. To meet a client request, assets are sold, resulting in an intraday boost in value of $10,940. As can be seen, $10,000 of this amount goes out, along with the portfolio's start-of-day value, leaving $940 in the account.



In a start-of-day approach, we are backing the outflow out immediately, which basically puts the account into a $10,000 deficit; magically, it grows to $940 by the end of the day. The return is a totally nonsensical -108.87 percent. The software that our client uses doesn't know what to do with such a return (who would?) And so they don't report anything. Fortunately, they have discovered the error in their approach and are correcting it.

The end-of-day result is 3.35%; makes a lot more sense, yes? It reflects the appreciation that occurred during the day; the outflow is an event we want to ignore for return purposes, thus the end-of-day approach is the way to go.

If we want to measure the daily return of a portfolio, what could possibly be our reason for wanting to use a start-of-day option?

An inflow could, in theory, be invested; and, even if it isn't, it should result in some income from a sweep. Thus, treating the flow as a start-of-day event is appropriate.

I'm confident that most firms choose either start- or end-of-day for both inflows and outflows. However, I have also witnessed more and more managers, as well as more and more vendors, adopt the mixed approach.

NOT SO OBVIOUS...

As noted earlier, at this month's PMAR VIII conference Jonathan Boersma provided an overview of the upcoming changes to the GIPS standards. One item in particular is worthy of addressing: risk and the composite description. Recall that the GIPS 2010 Exposure Draft proposed to require a description of the composite's risks; however, the feedback from the market wasn't very positive on this so it was dropped. However, in his presentation Jonathan offered the following:

Risk was deleted; however, the EC feels strongly that risk(s) should be addressed in the composite description. Sample composite descriptions are included as Appendix C and risk considerations are included in most sample descriptions.

This isn't the first time I heard that the sample descriptions are being used to imply that risk should be addressed in the composite descriptions. As a verifier am I to require my clients to have risk? Based simply on a sample? That, to me, seems a challenge. If the EC felt strongly that risk should be addressed, then one would have thought it would be

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clearly stated as a requirement. The challenge, I believe, is that this is a very difficult subject. Some who saw their proposal felt that to satisfy it they'd need a very lengthy description, possibly extending more than a page; others felt that there was risk to the firm if the description wasn't deemed satisfactory. Thus, if there's no requirement for risk, then I'm not obligated to include anything and therefore aren't at risk (sorry for the less than ideal phrasing).

In the past samples have never been used to say "this is what we expect to see." Rather, they serve as examples of what one might provide. I'm curious how others feel about this approach to defining rules.

FROM OUR READERS

Philip Lawton, who runs the CIPM program for the CFA Institute, responded to last month's post about this certification:

Dear David,

Thank you for speaking up in support of the CIPM program in the April issue of Performance Perspectives.

The exams do evolve as they must in this changing industry. However, we strive to maintain a uniform level of difficulty from one administration to the next. After each exam period ends, our consulting psychometrician applies statistical techniques to distinguish between the relative difficulty of the exams and changes in candidate preparedness. This procedure allows us to monitor exam performance over time. Standard setters evaluate the difficulty of each exam in recommending the minimum passing score.

In short, while the CIPM curriculum will change, we take measures to hold steady our means of evaluating a candidate's knowledge of that curriculum.

There are many sound reasons for prospective candidates to get started as soon as possible—enrollment for the October 2010 exam window is open through 31 July—but a belief that the exams will grow harder is not one of them.

Best regards,

Philip.

Recall that I speculated that the exams will only get more difficult; apparently I was mistaken.

During this month's PMAR VIII I made a rather passionate plea for performance measurement professionals to pursue this certification. If you consider yourself a "PMP," why wouldn't you want to demonstrate this by having these four letters appear after your name? I used our friend Carl Bacon as a perfect example: clearly, Carl has no need to obtain this certification as he's known internationally for his knowledge about performance measurement. But he was one of the first to obtain the certification.

If we all get behind this program it will only grow in value and importance.

THE SPAULDING GROUP'S 2010 INVESTMENT PERFORMANCE MEASUREMENT CALENDAR OF EVENTS

DATE	EVENT	LOCATION
September 13-14, 2010	CIPM™ Principles Exam Preparation Class	Los Angeles, CA (USA)
September 15-17, 2010	CIPM™ Expert Exam Preparation Class	Los Angeles, CA (USA)
September 20-21, 2010	CIPM™ Principles Exam Preparation Class	New Brunswick, NJ (USA)
September 22-24, 2010	CIPM™ Expert Exam Preparation Class	New Brunswick, NJ (USA)
September 27-28, 2010	Fundamentals of Performance Measurement Training	Boston, MA (USA)
September 29-30, 2010	Performance Measurement Attribution Training	Boston, MA (USA)
October 4-5, 2010	CIPM™ Principles Exam Preparation Class	London, England (UK)
October 6-8, 2010	CIPM™ Expert Exam Preparation Class	London, England (UK)
October 19-20, 2010	Fundamentals of Performance Measurement Training	San Francisco, CA (USA)
October 21-22, 2010	Performance Measurement Attribution Training	San Francisco, CA (USA)
November 16-17, 2010	Fundamentals of Performance Measurement Training	Chicago, IL (USA)
November 18-19, 2010	Performance Measurement Attribution Training	Chicago, IL (USA)
December 7-8, 2010	Fundamentals of Performance Measurement Training	New Brunswick, NJ (USA)
December 9-10, 2010	Performance Measurement Attribution Training	New Brunswick, NJ (USA)

For additional information on any of our 2010 events, please contact Christopher Spaulding at 732-873-5700

Save the Date!

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PMAR

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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:

September 27-28, 2010 – Boston, MA
October 19-20, 2010 – San Francisco, CA
November 16-17, 2010 – Chicago, IL
December 7-8, 2010 – New Brunswick, NJ

15 CPE & 12 PD Credits upon course completion

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

September 29-30, 2010 – Boston, MA
October 21-22, 2010 – San Francisco, CA
November 18-19, 2010 – Chicago, IL
December 9-10, 2010 – New Brunswick, NJ

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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, close to 3,000 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).

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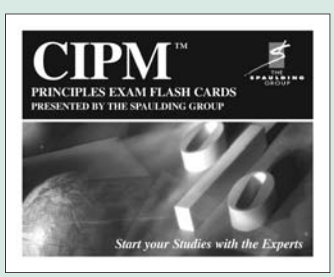

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