

# PERFORMANCE PERSPECTIVES

with David Spaulding



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APRIL 2018

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 Patrick Fowler at [PFowler@SpauldingGrp.com](mailto:PFowler@SpauldingGrp.com)

## ENHANCING YOUR GIPS® POLICIES & PROCEDURES

As you're probably aware, last year we initiated the **world's first** GIPS P&P contest, and just recently announced the winners.

We encouraged everyone (even our non-clients, a few of whom joined in) to participate. Not surprisingly, not all of our clients did, despite the fabulous policies they have.



One item that one of our clients has, that many do not, is a list of the revisions they've made to their policies, by date. This is very helpful, not just for the verifier, but the firm's personnel, as well. A good item for you to add, if you don't already have it.

Another item that many P&Ps are missing is a Table of Contents (ToC), ideally with page numbers. This should be helpful for the firm, and definitely is for the verifier.

Some formats for P&Ps don't lend themselves to having ToCs, however. I'm thinking of an Excel based format, which one of our competitors used to provide to their clients. I have it on good authority that this approach was considered potentially problematic and perhaps bordering on a conflict with verifier independence, but am not aware that this was ever formally addressed. That said, I even question whether it really is a P&P, as it's really a series of answers to questions.

More importantly, I find it a bit cumbersome to work with. But, a few of our clients (who carried it over from their time with the prior verifier) still use it, though some are making the switch to a narrative format, which is easier to deal with.

Consider adopting a policy that defines how frequently your policies are reviewed. Doing so at least annually makes sense, does it not?

If you're going to have a ToC, you'll want to number your pages; and, you should number them, anyway. Standard convention is not to number the first page, which presumably is a cover page. And so, the first page would begin after the cover. No, there is no "page numbering police" that will penalize you if you do start page one with the cover (though some verifiers might point this out).

Page numbering makes it easy for the verifier to point out issues (e.g., on page X you have "xxx"...). Without page numbers, it can be difficult to point to where items need to be addressed.

<http://www.SpauldingGrp.com>

# The Journal of Performance Measurement®

## UPCOMING ARTICLES

### Residuals on Duration-based Fixed Income Attribution

– *João Sousa Dias,  
Eagle Investment Systems*

### GIPS 20/20

– *Carl R. Bacon, CIPM, StatPro*

### The Journal Interview

– *Nick Sharp, Ph.D., MSCI*

### Net-of-Fee Performance Calculations

– *Andre Mirabelli, Ph.D.,  
Opturo and Krista Harvey,  
CFA, CIPM, TIAA*

### A Measure for Evaluating the Distributions of Ex-Ante Forecast Returns

– *Masahito Shimizu,  
Tokyo Institute of Technology*

### Confronting the Challenges of Multi-Level Attribution

– *David Spaulding, DPS, CIPM,  
The Spaulding Group*

You will, of course, be using the term “non-discretionary” (or, if you prefer, “nondiscretionary”) in your policies. Since this is one of the most confusing aspects of the Standards (the conflict between the term meaning that the client has not granted the manager the authority to trade on their behalf and the GIPS meaning, that the portfolio is not representative of the composite’s strategy), you should include an explanation of the term. I prefer qualifying it with something like “GIPS non-discretionary,” but this may be a bit unwieldy at times.

Note that I recommended<sup>1</sup> that GIPS 20/20 replace the terms “discretionary” and “non-discretionary” with “representative” and “not representative,” which is more accurate and eliminates the confusion. We’ll have to wait and see if this idea is adopted.

Look for more commentary on GIPS P&Ps!

Oh, and to get copies of the contest winners’ policies and procedures, please go here: <https://www.spauldinggrp.com/gips-policies-and-procedures-contest-winners/>

## PREPARING FOR YOUR GIPS VERIFICATIONS

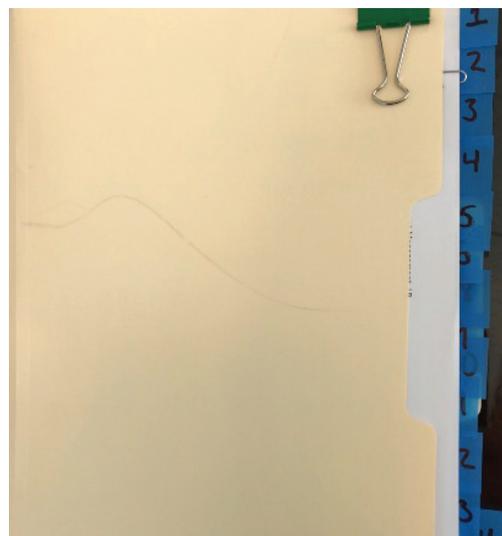
We issue our verification clients a numbered list of items that we will want for the verification. I can’t speak for our firm’s other verifiers, but I like everything delivered in “soft” (i.e., electronic) format, and certain items to be printed. Some of our clients number the files, which is helpful, not just for them, but also for us, too. And, when it comes to the hard copies, some will do different things to organize them for us.

Perhaps my favorite was from our dear friend, Sandra Hahn Colbert, who headed performance at O’Shaughnessy Asset Management (OSAM) until the time of her death. She went to great lengths to make the material as organized as possible, including additional items she anticipated that I would need.

Another client, Chris Duke of Miller Investment Management, LP, presented me with a file folder, with the items nicely labeled (see accompanying photo). This, too, was very helpful. The numbers align with the numbers in our list of requests.

Our information requests have changed a bit over the years, but we try to be pretty consistent, so our clients can get used to what we’ll require.

Will be offering more ideas in the future. If you have ideas you wish to share, please do!



<sup>1</sup> See [https://www.gipsstandards.org/standards/Documents/Guidance/gips\\_2020\\_consultation\\_spaulding\\_group.pdf](https://www.gipsstandards.org/standards/Documents/Guidance/gips_2020_consultation_spaulding_group.pdf)

## 2018 PERFORMANCE & RISK MEASUREMENT HALL OF FAME

We began honoring outstanding contributors to our profession quite some time ago, and this year's inductees are:

David Carino, Ph.D.  
Dugald Eadie  
Lee Price, Ph.D., CFA  
Timothy P. Ryan, CIPM, FRM, CAIA

Each has made significant contributions to our profession. We thank *The Journal of Performance Measurement*'s Advisory Board for voting on individuals who are definitely deserving of this honor. We look forward to presenting them their awards.

Prior inductees:

### 2013

Gary Brinson, CFA  
Peter O. Dietz, PhD  
William Sharpe, PhD

### 2014

Eugene Fama, PhD  
Harry Markowitz, PhD  
Jose Menchero, PhD, CFA  
David Spaulding, DPS, CIPM  
Jack Treynor

### 2015

Brian Singer, CFA  
Denis Karnosky, CFA  
Franco Modigliani, PhD

### 2016

Carl Bacon, CIPM  
Stephen Campisi, CFA  
Frank Sortino, PhD

### 2017

Fischer Black, PhD  
Michael Jensen, PhD

With this year's inductees, we bring the total honored to twenty.



## OUTSTANDING WOMEN IN PERFORMANCE & RISK MEASUREMENT

We recently announced that we wanted to recognize the outstanding women in performance and risk measurement. The reality is that women make up, we'd estimate, less than 25% of those working in this field. We believe the number is rising, though have no real evidence of this.

Our firm has been a supporter of women in the industry for quite some time. A few years ago, *The Journal of Performance Measurement*<sup>®</sup> ran a series of interviews with women in performance. When possible, we include women on panels and as speakers at our events. And, this new award will further serve to recognize those who have made outstanding contributions, and will hopefully encourage others to join the profession.

We thought it appropriate to ask the journal's Advisory Board members to vote. We announced that we were accepting nominations, and received over 20 names. The Board voted, and the top nominees were:

- Frances Barney, CFA
- Sandra Hahn Colbert, CFA, CIPM
- Leah Modigliani, CFA
- Leslie Rahl
- Elske van de Burgt, CFA
- Karyn Vincent, CFA, CIPM



Some of these names are, no doubt, familiar to you, while some may not. I've had the pleasure of knowing all of them, and working with a few in one capacity or another.

Sadly, one is no longer with us. Sandra passed away a few years ago following elective surgery. She was a client of ours, as well as a dear friend.

We will present each of them with a trophy to commemorate this achievement. At the upcoming PMAR North America conference, we will honor Sandra, Leah, and Elske. We will make arrangements to honor the others at a future date.

## HOW TO PASS THE CIPM... (OR, AT LEAST INCREASE YOUR LIKELIHOOD OF SUCCESS)

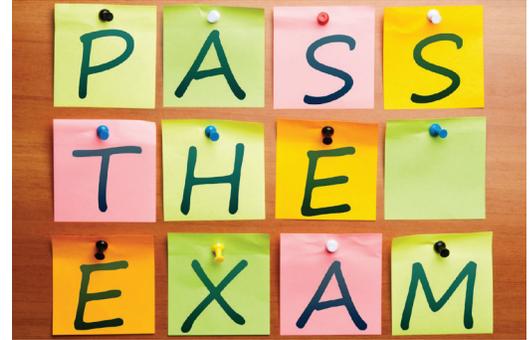
A client recently sent me the following note: "By the time I finish my daytime job, I'm either bleeding numbers or have very little time to read about more numbers until 9:30 PM. Also: young kids. Any suggestions besides sleeping less?"

Here were my initial thoughts:

1. It's very important that you have the full support of your spouse or partner. I obtained three graduate degrees part-time (the first when we were DINKs,<sup>2</sup> the second when we had one, then two small children, and the third when we were "empty nesters"). In each case, my wife supported me, and understood that I'd need to devote time to my studies. When I got

<sup>2</sup> Double Income, No Kids. This term didn't exist back then, but applies.

my CIPM, our children were adults, though I still needed her support. By support I mean not only allowing time to study and prepare, but understanding that I wouldn't be participating in everything that I might otherwise be doing (e.g., kid stuff, watching television with her, etc.).



2. I think setting aside a reasonable amount of time, per day, is ideal. I started the CFA a couple times, and each time failed to do that, so that I simply didn't get through the materials, so didn't bother to take the exams. Committing to, let's say one hour a day, is probably a good start. Somewhere the CFAI will tell you what the average amount of time folks devoted to studying. The Expert has, as I recall, twice the material as Principles. If you can carve out that hour (e.g., 8-9 PM) as a start, that'd be good, I'd think.
3. You need a powerful reason to do this. I didn't have a powerful enough one for the CFA (I guess because I had the MBA in Finance, and that's it's definitely not required; it was always a "nice to get" for me, which isn't very powerful). My doctorate, in comparison, was a goal I had had for decades, so once I found a program that would work, there was absolutely no question, I was going to get it. The motivational speaker, Anthony (Tony) Robbins speaks of needing "leverage" to make things happen. If the lever's board isn't long enough (i.e., doesn't have a strong enough reason), you won't move much. If, however, by getting the CIPM you can articulate what the benefits will be (if your firm will grant you a raise, for example; or, perhaps position you for promotion; or, that the education you'll obtain will have great value; or, if by getting it other "doors" will be open), you can start to improve the need. I've started French lessons multiple times, but never go very far, even though I'd really like to learn French. But, it's still a "like to," not a "must."
4. Wants vs. needs is important, I think. "Oh, I'd like to get the CIPM" doesn't carry the weight of "I really want the CIPM" or "I feel that I must have the CIPM" or "I need the CIPM to reach my goals."
5. You might want to see if your firm will allow you time, perhaps during the day, to study, too. We won a verification from a firm whose verifier was apparently studying instead of doing the verification: not a good idea.
6. I took off a week in advance of the exam, to review all my notes and materials, and to practice. I did the same for the Advanced exam. I think this helps, too. It's better to over-prepare than under, I'd say.

We are HUGE fans of the CIPM® exam. Taking and passing the exam will (a) identify you as someone who has obtained a high level of knowledge and expertise and (b) further the importance of the performance measurement department's role in our industry.

If you have other suggestions, please let us know! Hope these are helpful.

## KEEP THOSE CARDS & LETTERS COMING

*We appreciate the emails we receive regarding our newsletter. Mostly, 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.*

## PUZZLE TIME!

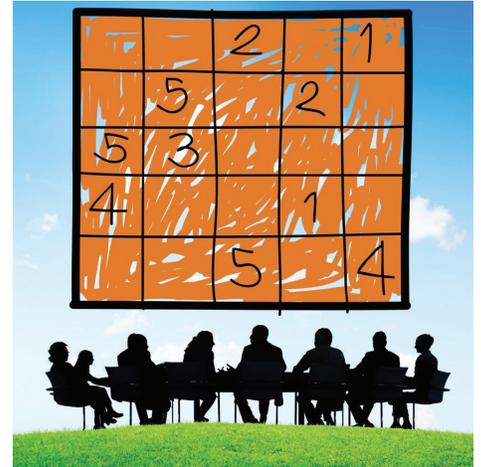
### February Puzzle

*As I explained when I posted this one, it came from my own head!*

*I awoke one morning realizing that it came to me through a dream: weird, right?*

*Anyway, here it is:*

*Put the numbers 1 to 5 in order, in the simplest way, such that each number is not larger than the one to its left, nor smaller than the one to its right.*



This really isn't difficult. What is difficult is to get over the negative wording: "is not larger than the one to its left, nor smaller than the one to its right."

A few decades ago, I did a lot of programming. I would sometimes encounter someone's code that was all written in negative terms. "If X is Not *this*," and I came to realize that such wording can get us a bit confused. It's better, I learned than and still believe, to have expressions in positive tones. Our brain wants to think positively, not negatively.

And so, let's rework that earlier bit of verbiage.

*Put the numbers 1 to 5 in order, in the simplest way, such that each number is smaller than the one to its left, and larger than the one to its right.*

So, we're simply sorting these numbers from the highest to the smallest, right?

5, 4, 3, 2, 1.

Let's go right to the middle.

The number 3 is (a) smaller than 4 and (b) larger than 2.

We can now also check with the original wording.

*Put the numbers 1 to 5 in order, in the simplest way, such that each number is not larger than the one to its left, nor smaller than the one to its right.*

The number 3 is not larger than 4 and it is not smaller than 2.

We often encounter situations where we say "it's a matter of semantics," especially when something isn't clear. Speaking in negatives is one way to confuse: just turn it around, and speak positively, and it'll be clearer!

Our brain apparently doesn't particularly like negative thought. For example, if you are carrying a full cup of tea and wish not to spill any, by saying to yourself "don't spill the tea," you may actually do just that, as the "don't" will be ignored. Well, at least that's what I've heard.

The moral of this exercise? Be positive!

Daniel Kempf, Mark Rothermel, Malcolm Smith, and Dan Lehrer got it right!



### March Puzzle

The difference between two numbers is 66; the sum of these two numbers is 88.  
Find the greater number.

Well, I suppose that if you find the greater, you'll find the lesser, too, right?

This is pretty much algebra. We can construct it as:

$$X + Y = 88$$

$$X - Y = 66.$$

Starting with the second, we can change it to:

$$X = 66 + Y$$

Substituting into the first:

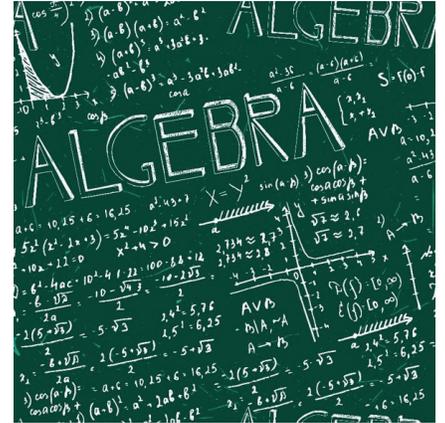
$$66 + Y + Y = 88$$

$$66 + 2Y = 88$$

$$2Y = 88 - 66 = 22$$

$$Y = 22/2 = 11$$

We can then see that  $X + 11 = 88$ , so  $X = 77$ .



Nice to know that my algebra skills are still in tact!

Peena Modi, Tom Stapleton, Neil Riddles, Daniel Kempf, Malcolm Smith, John Gordon, Dan Lehrer, Anthony Howland, Hans Braker, and Stephanie Manter got it right! Congrats!

### April Puzzle

What is the maximum number of triangles you can form within the following rectangle:



Please describe them, as well.

### **FROM OUR READERS**

I found David Spaulding's example of an attribution in a puzzle of a different sort thought-provoking, as his articles usually are.

I would like to offer up a couple of alternative perspectives on the attribution conundrum he quotes.

One perspective is that the return based on NAV is 9.09%, and that if the cash comes out at the start, then it comes out at the start, so should be treated as such. What then is the overall return to be attributed (which is the most important figure of the lot)? The

perspective I am offering is that the \$205 at the start, is split into two components: \$95 cash which returns 0%, and the invested assets which return 9.09%. It so happens that the weighted average of  $\$95 * 0\%$  and  $(\$205 - \$95) * 9.09\% = 4.88\%$ , the number that David Spaulding suggests we attribute.

The first attribution hangs together, and adds up to the correct (in my view) outperformance. The only anomaly is that the return of equities is -100%, but that return is only a concept, as there were no equities throughout the day, so there wasn't even an equity return for the entire day. So it can only be used as a tool for attribution. And, arguably, the return for equities during the time they were held was indeed the 5.26% used in later tables, as they went up from \$95 to \$100 in the twinkle of time between the start of the period and when they were sold.

Incidentally, table 5 is based on the implicit assumption that the equities would have returned 0% from the moment that they left the portfolio to the close of the period. There is no reason to suppose that that would have occurred, though it's a reasonable neutral assumption.

The second perspective is that as there was a very substantial cash flow, it might be appropriate to split the period at the instant of the cash flow. That might seem odd, as the debate is about whether the cash flow should properly be treated at the start or end of the period, and there is a valuation at both instants. However, we are told that the cash flow occurred at the start. The equities were sold for 100, but were valued at 95 at the start. That is the heart of the anomaly. There can't be two values for equities at one instant, \$95 at the start, and \$100 at the sale, both exactly at the start of the period. So it seems reasonable to invoke the idea that the sale occurred an instant after the start. So the period could have two sub-periods, from the start to the instant later when the sale was made, and from the instant of the sale until the end of the day.

Hope these perspectives add something to the conversation. Unit valuations mismatching the sale or purchase values of underlying assets can give rise to serious performance anomalies, with those who trade units benefitting (or losing out) at the expense of (or in favour of) those who continue to hold the units. It is often unappreciated how large the impact can be. So a massive topic.

Regards

**Malcolm Smith**

*Director of Research*

**INALYTICS**

**THE SPAULDING GROUP'S 2018  
INVESTMENT PERFORMANCE MEASUREMENT CALENDAR OF EVENTS**

DATE	EVENT	LOCATION
May 15-16, 2018	PMAR North America	Philadelphia, PA
May 17, 2018	Bacon vs. Spaulding	Philadelphia, PA
June 11-12, 2018	PMAR Europe	London, England
June 13, 2018	Spaulding vs. Bacon	London, England
June 14-15, 2018	Performance Measurement Forum	Dublin, Ireland
July 16-20, 2018	Performance Measurement Boot Camp	New Brunswick, NJ
August 14-15, 2018	Fundamentals of Performance Measurement	Chicago, IL
August 16-17, 2018	Performance Measurement Attribution	Chicago, IL
October 15-16, 2018	Fundamentals of Performance Measurement	San Diego, CA
October 17-18, 2018	PMAR West Coast	San Diego, CA
November 15-16, 2018	Performance Measurement Forum	Luxembourg
November 28, 2018	Asset Owner Roundtable	Orlando, FL
November 29-30, 2018	Performance Measurement Forum	Orlando, FL
December 5-6, 2018	Fundamentals of Performance Measurement	Mumbai, India
December 11-12, 2018	Fundamentals of Performance Measurement	New Brunswick, NJ
December 13-14, 2018	Performance Measurement Attribution	New Brunswick, NJ

*For additional information on any of our 2018 events, please contact Patrick Fowler at 732-873-5700*

## 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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#### FUNDAMENTALS OF 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 Fundamentals of Performance Measurement on these dates:

August 14-15, 2018 – Chicago, IL

December 11-12, 2018 – New Brunswick, NJ

October 15-16, 2018 – San Diego, CA

15 CPE & 12 PD Credits upon course completion

CFA Institute has approved this program, offered by The Spaulding Group, for 12 CE credit hours. If you are a CFA Institute member, CE credit for your participation in this program will be automatically recorded in your CE tracking tool.



#### 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:

August 16-17, 2018 – Chicago, IL

December 13-14, 2018 – New Brunswick, NJ

15 CPE & 12 PD Credits upon course completion

CFA Institute has approved this program, offered by The Spaulding Group, for 12 CE credit hours. If you are a CFA Institute member, CE credit for your participation in this program will be automatically recorded in your CE tracking tool.



#### 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.

#### WORKING ON YOUR 2018 BUDGET?

Don't forget to make room for conferences. And why not the Trifecta of Performance Measurement Conferences?



PMAR, Performance Measurement, Attribution & Risk, is the #1 performance measurement conference. If you've never experienced it, you owe it to yourself and your firm. And if you have, then you know the great value it is. And now, there are three to choose from!

So please set aside funds in your 2018 budget to participate in PMAR!