

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, 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 CSpaulding@SpauldingGrp.com

CGIPS...THE EXAM

It's over! I took it! Finally.

I didn't wait until the very end because (a) I wanted the extra time to prepare or (b) because I'm a natural procrastinator (my income taxes were filed April 17th). My travel schedule and client commitments were just too crazy to afford me the necessary time to prepare. Well, once I settled down to study, I spent a considerable amount of focused time (several nights; two half-days taken off from work; plus time on the weekend leading up to the exam).¹

Having studied and conducted the review course (not to mention using our handy CGIPS flash cards), I'd say the exam wasn't overly difficult. It consists of 100 questions and lasts 3 hours. The on-line system that supports it is quite powerful. You can check off questions you want to return to. It's about as low-pressure as I think you can get.

I won't know if I passed for two months (two months!). I, along with the 400 or so people who are taking it will have a long 60 days to wait. I'll let you know, either way.

Oh, and if you'd like to offer your own comments on CGIPS, please do so...we'll include them in a future issue.

COFFEE AND PERFORMANCE MEASUREMENT

What does coffee and rates of return have in common? Now that's probably a question you haven't heard (and, it wasn't on the CGIPS exam, but perhaps should be).

The answer: well, we have decaffeinated coffee, which essentially involves the removal of caffeine; when we annualize returns, we're decompounding the returns...that is, we're removing the compounding effect. Take for example, the situation where we have these three annual returns: 1%, 3%, 5%. We could *arithmetically* link them (i.e., add them together), which yields 9%, but this would be incorrect since we know we want to compound them. And when we compound, we get 9.23% (i.e., we've got 23 basis points of compounding).

<http://www.SpauldingGrp.com>

¹ Please don't get the impression that I only recently began reviewing the materials; I read them in their entirety early on, because of our CGIPS Prep Classes. I also had the advantage of teaching a few classes, which helps reinforce the material. But I still needed to spend additional time to confirm what I thought I knew. A word of advice: make sure you give yourself plenty of time to review this stuff...it's pretty massive.

The Journal of Performance Measurement®:

UPCOMING ARTICLES

How to Build Your Own Linking Formula – A Unified Linking Theory on Contributions
– Gary Kahan

Obstacles to Overcome in Performance Measurement
– Stefan Tangen

Actual Results Achieved by 401(k) Investors over a Market Cycle – Surprising Conclusions
– Colin Fernandes, Shiv Mehta

Performance Attribution Method – Update
– Teri Geske

Fixed Income Attribution – a Flexible Approach
– Per Sögaard-Andersen Ph.D. and Lars Bjerre Hansen

The Attribution of Portfolio and Index Returns in Fixed Income
– Timothy Lord

The Journal Interview
– Gary Brinson

Now we want to come up with an average return to show our clients. We can't simply divide by three, as that would overstate the average (remember, there's some compounding that went on). So, we have to remove the compounding (as in removing caffeine); and how do we decompound our returns? By annualizing! (And, of course the answer is 2.99%).

I think the analogy with coffee can be a helpful one when trying to explain what we're doing; hope you agree.

GIPS...IS IT WORTH THE TIME AND MONEY?

In the May 2005 issue of *Inc. Magazine*, there was a reference in their "Priority" section on the International Organization for Standardization or ISO: "So many standards to follow, so little payoff." The subtitle got my attention: "Companies have spent a lot of money to comply with ISO's popular management standards. Now, many wonder why they bothered."

Within the piece we read "Getting an ISO certification is expensive and time-consuming...But if you don't go through the process, you often can't work for the big guys."

Elsewhere: "The payoff? That's a tough one. The certification probably helped Delaware North win some contracts and certainly burnished its environmental standards. Employee morale also rose, as workers took pride in their newfound status as a certified environmentally friendly operation. But as for concrete financial rewards, there has been no spike in sales."

I know that some firms have questioned whether or not compliance with GIPS® is worth the time and money. We've heard this especially in Europe, where there has apparently not been the virtual requirement that we've seen in North America. Well, we still strongly recommend compliance:

1. It's better to become compliant in advance of the market demand...it will only become more challenging if you wait.
2. The market will come around to GIPS, so forearmed is forewarned.
3. Compliance doesn't just have to do with gaining business; it's also about supporting a great set of standards, which benefit the industry tremendously.
4. And, many firms have commented on how compliance has helped them improve their processes and controls.

I don't know about the ISO certification, but GIPS is something worth pursuing.

CELEBRATE!

April is Mathematics Awareness Month! And since investment performance measurement is about math, we should celebrate, right? So grab a calculator and calculate some returns, information ratios, tracking errors, etc.

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.

COPERNICUS, PTOLEMY, AND PERFORMANCE MEASUREMENT

I recently read William T. Vollmann's *Uncentering the Earth – Copernicus and The Revolutions of the Heavenly Spheres*. And at some point while reading it, it occurred to me that there may be a parallel in performance measurement.

To refresh your memory, Ptolemy fostered the belief (as many others did) that the earth was the center of the universe...that everything revolved around the earth. Copernicus, on the other hand, placed the Sun at the center. Granted, he wasn't exactly correct, either, but the idea of *uncentering* [sic] the earth was not terribly well received by many. Had it not been that Copernicus was dying when his *On the Revolutions of the Heavenly Spheres* was published, he (like, for instance, Galileo and Kepler) would have been excommunicated.

Anyway, what does this have to do with performance measurement? Some, I believe, have placed the wrong thing at the center of the performance universe! Some, for example, might argue that GIPS is at the center. Now, we're big fans of GIPS, we do a lot of work in the GIPS-world, including consulting and verification, and we've been involved with these standards (and the AIMR-PPS® which preceded them) for some time. However, the notion that GIPS is at the center strikes us as incorrect...if you will, Ptolemaic.

So, what's at the center? Returns. More specifically, portfolio-level returns. Without returns, we wouldn't be bothering with attribution, risk, GIPS, or a lot more.

In my view of the performance universe, what we see at the center is the sun labeled "returns." How about you?



THE SPAULDING GROUP'S 2006 INVESTMENT PERFORMANCE MEASUREMENT CALENDAR OF EVENTS

DATE	EVENT	LOCATION	DEADLINE TO REGISTER
May 22-23	Performance Measurement, Attribution, & Risk Conference	Philadelphia, PA (USA)	May 19
June 15-16	Performance Measurement Forum	Dublin, Ireland	June 9
June 20-21	Introduction to Performance Measurement Training	Vancouver, Canada	June 13
June 22-23	Performance Measurement Attribution Training	Vancouver, Canada	June 13
July 11-12	Introduction to Performance Measurement Training	Chicago, IL (USA)	July 5
July 13-14	Performance Measurement Attribution Training	Chicago, IL (USA)	July 5
July 18-19	Introduction to Performance Measurement Training	Denver, CO (USA)	July 11
July 20-21	Performance Measurement Attribution Training	Denver, CO (USA)	July 11
August 7-11	Performance Measurement Boot Camp	New Brunswick, NJ	August 4
September 12-13	Introduction to Performance Measurement Training	Boston, MA (USA)	September 4
September 14-15	Performance Measurement Attribution Training	Boston, MA (USA)	September 4
September 18-19	Introduction to Performance Measurement Training	Los Angeles, CA (USA)	September 11
September 20-21	Performance Measurement Attribution Training	Los Angeles, CA (USA)	September 11
October 9-10	Introduction to Performance Measurement Training	New York, NY (USA)	October 2
October 11-12	Performance Measurement Attribution Training	New York, NY (USA)	October 2
October 18	Fixed Income Attribution Symposium FIA	TBA	October 17
October 23-24	Introduction to Performance Measurement Training	Dallas, TX (USA)	October 16
October 25-26	Performance Measurement Attribution Training	Dallas, TX (USA)	October 16
November 9-10	Performance Measurement Forum	Milan, Italy	November 3
November 14-15	Introduction to Performance Measurement Training	Portland, OR (USA)	November 7
November 16-17	Performance Measurement Attribution Training	Portland, OR (USA)	November 7
Nov. 30 - Dec. 1	Performance Measurement Forum	Orlando, FL (USA)	November 24
December 6-7	Introduction to Performance Measurement Training	Chicago, IL (USA)	December 1
December 8-9	Performance Measurement Attribution Training	Chicago, IL (USA)	December 1

For Additional information on any of our 2006 events, please contact Christopher Spaulding at 732-873-5700

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Fourth Annual International*

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The Spaulding Group is registered with CFA Institute as an Approved Provider of professional development programs. These programs (Introduction to Performance Measurement & Performance Measurement Attribution) are eligible for PD credit hours as granted by CFA Institute.

Customized In-House Training is also available. Please call or email for additional details.

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:

June 20-21, 2006 – Vancouver, Canada
 July 11-12, 2006 – Chicago, IL
 July 18-19, 2006 – Denver, CO
 September 12-13, 2006 – Boston, MA
 September 18-19, 2006 – Los Angeles, CA
 October 9-10, 2006 – New York, NY
 October 23-24, 2006 – Dallas, TX
 November 14-15, 2006 – Portland, OR
 December 6-7, 2006 – Chicago, IL

15 CPE 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

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:

June 22-23, 2006 – Vancouver, Canada
 July 13-14, 2006 – Chicago, IL
 July 20-21, 2006 – Denver, CO
 September 14-15, 2006 – Boston, MA
 September 20-21, 2006 – Los Angeles, CA
 October 11-12, 2006 – New York, NY
 October 25-26, 2006 – Dallas, TX
 November 16-17, 2006 – Portland, OR
 December 8-9, 2006 – Chicago, IL

11 CPE Credits upon course completion

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