PERFORMANCE PERSPECTIVES
with David Spaulding

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CROSSING INTO UNCHARTERED TERRITORY

"The chief business of the American people is business"
– Calvin Coolidge

For some, October 19, 1987 is a day they can recall where they were, as that was the day of the huge stock market "adjustment" which saw the Dow Jones Industrial Average (DJIA) drop by more than 500 points. I was at a Q Group meeting in Colorado Springs. Because of the two-hour time difference with the East Coast, our meeting began with an announcement of a fairly large drop in the Dow: more than 200 points by that time. I recall that several of those in attendance thought this was funny; I didn't. We had a break that allowed me to go golfing and so I was golfing as the market was tumbling. That evening my wife, who usually doesn't pay much attention to the market, was caught up in the frenzy. Having never lived through such a huge drop, I, like many, thought of the crash of 1929 and wondered if that was what laid ahead. The following day I decided to return home early rather than stay for the full event; even though there wasn't much my presence could do back at my office, I still felt that it was wrong that I was in Colorado Springs. At that time I was working for a NYC-investment advisor.

I learned a valuable lesson that year: markets go up and markets go down. We recovered in fairly short order and many new high points in the DJIA were to be reached.

Now, we're in for yet another huge drop, but of proportions never seen since 1929. From the reactions of investors it appears that just about everyone is in "panic mode." Unlike those who a couple days after October 19, 1987 saw the drop in prices as buying opportunities, we only seem to be seeing further selling, which puts further downward pressure on the markets.

The government takes action to stem the fall and people respond by thinking that if the government is acting, the situation must be extremely bad: but how much worse would it be if the government failed to act? We expect our leaders to have answers when we're faced with something that has never occurred before. Fortunately, the leaders are taking action, which to me is a sign of good leadership. Some are pointing fingers and there's no doubt that there are plenty of folks who deserve being pointed at, both in the public and private sector, and on both sides of the political arena. Bad decisions were made and now we're faced with the troubles that followed. But survive and prosper we will, have no doubt.

It probably sounds odd but I'm not panicking. I haven't looked at any of my investments since the drop began: since I have no reason to sell, why bother? I know they're all down. And, I have confidence they'll recover. Perhaps not as quickly as some would like but they'll still be back. I have confidence in our markets. Some might accuse me of "wishful thinking," and perhaps they're right. But I'd much rather have a positive attitude than one of doom-and-gloom. So far our business hasn't suffered from the drop, and hopefully this won't occur. We suffered through the post-dotcom bear market and made it to today, so I have hopes that whatever lies ahead we'll be able to handle.

Too many politicians like to bash "big business." But "big business" is what has allowed our government and many other economies to prosper: would India and China be the darlings of the 21st century without capitalism? In my home state (New Jersey) we've witnessed governors who have attacked businesses and championed tax increases for them, only to see more and more companies depart for friendlier shores (even we're thinking of relocating). The result has been increased unemployment, reduced corporate tax revenues, and increases in property taxes. Such foolishness by our elected officials shouldn't go unpunished; unfortunately, these politicians usually escape the scrutiny they deserve. When I was mayor I made it clear that our town was "open for business," and I worked with our local businesses. Fostering a positive relationship with those who often are the highest tax payers only makes sense, unless you're looking for votes and think that attacking corporations is a good idea.

The business of America is business, and it has become the business of the world, too. Our prosperity is the result of innovation, hard work, risk taking, creativity, and a desire to succeed. Steps to stifle this will only result in a world with less prosperity, less new product development, and more government involvement. Having witnessed how poorly the government runs virtually everything, why would we turn over anything more to them? If only businesses could tap into an endless supply of revenue whenever they decided to spend beyond their means. Politicians, who have never run anything, too often think that they are in a position to criticize those who have succeeded in making something and being successful.

While it's great to be able to turn to our government in times of need, we cannot allow them to grow in power. Such action will not be good in the long term.

Perhaps what best captures my view on the current situation is a full page advertisement that Merrill Lynch ran in the *Wall Street Journal* in their weekend edition, October 11-12, 2008:

> In America, when we get knocked down, we don't stay down.
> In the last 80 years, America has experienced 13 economic recessions.
> And fought back with 13 economic expansions.
> It was never easy, but it was always possible.
> If you're bullish on America, and we are,
> then you're bullish on getting up and coming back.
> That's not a belief. That's history.

I am bullish on America and the world. We will get through this difficult time and prosper. And, we'll look back at these challenges and be glad that we were able to endure and succeed.

PERSPECTIVES

I was invited to give a talk at DSTi's annual user conference this month; this marks the second time I've spoken at this event having been there last year (terrible location: the Wynn Hotel in Las Vegas; oh, well, I'll manage). My topic is basically my perspectives on where I see performance measurement going. In preparing for this I thought I'd begin with where we've been.

As with much of what we encounter today, some people only know what they see today and assume it's always been this way (e.g., cell phones, the Internet). In the case of performance, it might be daily performance, returns at multiple levels, various ways to measure risk, etc. However, the changes in this industry have been huge!

Are You Currently Facing Staffing Issues?

Can't find enough qualified help? Need an extra hand to roll out quarter end/ year end numbers?

As firms realize the enhanced function that performance teams now play in the overall investment process, the market for qualified staff has become more and more competitive. The Spaulding Group can help your staffing needs with our "***just-in-time***" staffing resources for all of your performance needs.

TYPES OF ASSIGNMENTS

The Spaulding Group can help your firm in many ways including:

- GIPS® Related work
- Performance Analysis and Numbers Preparation
- Operational Issues
- Data Issues
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- System Design

Advantages of Utilizing The Spaulding Group's Staffing Resources:

Cut Benefit Costs – Given the rising cost of benefits and the fact that workers comp and disability continue to rise, the hourly cost for a consultant or temporary staff figures in substantially below that of a full time worker of comparable skill set.

Eliminate Training Costs -Our staff comes ready to roll up their sleeves and help you as soon as they walk in the door.

Eliminate Hidden costs of Overtime - There is substantial evidence that despite the short-term benefits that make overtime attractive to employers, a growing body of research shows that working long hours over long periods of time is not necessarily cost-effective because of diminished quality, increasing mistakes and reduced productivity.

Reduce Costly Hiring Mistakes - Using The Spaulding Group employees eliminates the cost of mistakes in hiring and using marginally productive workers because employers get temporary professionals with the right skills and the best personality for the job. In fact The Spaulding Group assumes the risk for the firm, that is, if our staff does not perform the work is free.

Staff Up and Down at your Convenience - Have to get those quarter-end numbers done? Staff out on vacation or maternity leave? Bring us in for a day, a week, a month, or a year – our staff is ready to assist whenever you need us.

The Spaulding Group arrives ready to work, focused on doing the job and meeting project goals.

For additional information, please contact Chris Spaulding at **732-873-5700** or **CSpaulding@SpauldingGrp.com**

It wasn't that long ago that firms only reported returns at the portfolio level and just for the past year; today, we report at all kinds of levels and for a variety of time periods. Risk measurement used to only mean standard deviation, and most firms didn't even bother with this; today, we have a variety of risk measures as well as risk-adjusted measures available to us. We've also moved into *ex ante* (forward looking) risk. "Attribution, while not new, is still an evolving discipline" was written in 1986 in the famed Brinson, Hood, Beebower *FAJ* article. Well, hardly anyone was doing attribution back then but today it's essentially a given, with the possible exception of fixed income where the most growth is taking place today. And while the presentation standards have now been around for over 15 years, what started out as a U.S.-only idea has spread to many countries with the GIPS® standards. We had no "performance measurement analysts" 15 years ago, but today they're found in virtually every money management firm; and many of these firms have created a new position: global head of performance! Our recent Performance Measurement Professional Survey provides a great deal of details on what's going on from an organizational standpoint.[1]

So, where are we going? Here are just some of my thoughts:

- expanded use of money-weighting over time-weighting (as people understand the difference, they see the wisdom in adopting money-weighting)
- a move to more accurate returns, either by adopting daily performance or adjusting returns for large flows
- greater use of transaction-based attribution
- the adoption of attribution by hedge funds
- risk attribution becoming more common

By the way, I don't see outsourcing becoming common, although it works in some cases. I will shortly be writing an article on this topic and will discuss it further here, as well.

GLOBAL FIXED INCOME ATTRIBUTION: IS ONE CURVE ENOUGH?

When reconciling a fixed income manager's performance to his/her excess return through performance attribution, a critical piece is a look at the manager's "management of the yield curve." This is often referred to as the "duration" or "treasury" effect. For a domestic manager, we would typically use the appropriate risk-free curve (e.g., for the U.S. it would be a treasury curve). But what if a manager is global, will the single curve work? I posed this question to a couple colleagues who agree that it won't.

Because each country's curve moves independently of one another we would expect that a manger will invest within each country based on his/her expectations on what the future might hold. Also, from a pure analytical standpoint, consolidating to a single curve can blur the results. Simple example: a manager invests in two countries and holds all its assets with a duration of five years. In one country, the curve moved up while in the second it moved down by an equivalent amount. Overall, we will see no change in the curve, however, in one case the positioning worked to the manager's advantage while in the other case it hurt. Using a single curve will not provide the insights we require.

1 To learn how you can obtain a copy, please contact Patrick Fowler (PFowler@SpauldingGrp.com; 732-873-5700).

PERFORMANCEJOBS.COM WEBSITE

If you have two to five years experience and are looking for career advancing opportunities submit your resumes to PerformanceJobs.com.

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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This topic is of particular importance for us because we're designing a global fixed income attribution system for a client and wanted to ensure that we were addressing this issue correctly: we are! Your thoughts are invited.

VERIFIER'S CORNER

We encountered a recent situation which speaks to the need for some guidance: what does "since inception" mean?

The GIPS standards have these two important paragraphs:

- ¶ 5.A.1.a: "At least 5 years of performance (or record for the period since firm or composite inception if the firm or composite has been in existence less than 5 years)
- ¶ 5.A.1.b: "Annual returns for all years."

So, what do we do if a composite is created in June 2007? Do we show the third and fourth quarter 2007 results or begin reporting in January 2008? The "since inception" wording suggests we'd begin with the mid-year 2007 numbers; however, the "annual returns for all years" would suggest that we're prohibited from showing partial year results.

We've always encouraged firms to begin with the mid-year results and believe that this is what's intended; however, no clear guidance has been provided: hopefully it will. For now, it's a matter of interpretation.

In addition, what is a "sub advisor"? I think some clarity is needed here, too. Let's take the following examples:

1) Firm A doesn't manage emerging market equities and so establishes a relationship with Firm B to do the investing for Firm A's client. Firm A (a) decides what emerging market equity manager to use, (b) has the right to terminate this relationship, and (c) decides on the allocation (i.e., how much of their client's money to invest in emerging markets).

2) Firm C doesn't manage emerging market equities and decides to use Firm B's emerging market mutual fund for these investments. They (a) decide what emerging market equity manager to use, (b) have the right to terminate this relationship (i.e., sell Firm B's fund invest in some other fund), and (c) decide on the allocation.

While I don't want to stir up any trouble, I also believe some guidance is needed.

Both of these situations look similar. The difference is that with scenario #1, there's a formal relationship established between the managers whereby Firm B subadvises to Firm A. In the second scenario, there is no formal relationship; Firm C is investing in a security for their client (the fund) which happens to be a mutual fund.

I would say that a disclosure of the subadvisor for the first scenario is required but not the second. Agree? Am I creating more problems? Hopefully not.

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.

REMINDER!

We're doing our 7th survey on the presentation standards. Please join in!!! All participants will be entered into a raffle for a chance to win a Nintendo Wii or Ipod Shuffle.

Visit our website at:
http://www.spauldinggrp.com/gipssurvey2008.htm to download your copy today.

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Conference

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Save the Date!

THE SPAULDING GROUP'S 2008-2009 INVESTMENT PERFORMANCE MEASUREMENT CALENDAR OF EVENTS

DATE	EVENT	LOCATION
November 13-14	Performance Measurement Forum (Europe)	Amsterdam, The Netherlands
November 19	Trends in Attribution Symposium (TIA)	Philadelphia, PA (USA)
December 4-5	Performance Measurement Forum (North America)	Orlando, FL (USA)
December 8-9	Introduction to Performance Measurement Training	New Brunswick, NJ (USA)
December 10-11	Performance Measurement Attribution Training	New Brunswick, NJ (USA)
February 17-18, 2009	Introduction to Performance Measurement Training	London, England
February 19-20, 2009	Performance Measurement Attribution Training	London, England
March 17-18, 2009	Introduction to Performance Measurement Training	Boston, MA (USA)
March 19-20, 2009	Performance Measurement Attribution Training	Boston, MA (USA)
April 21-22, 2009	Introduction to Performance Measurement Training	New York, NY (USA)
May 12-13, 2009	Introduction to Performance Measurement Training	Chicago, IL (USA)
May 14-15, 2009	Performance Measurement Attribution Training	Chicago, IL (USA)
May 20-21, 2009	PMAR VII Conference	Philadelphia, PA (USA)
July 20-24, 2009	Investment Performance Measurement Bootcamp	New Brunswick, NJ (USA)
September 15-16, 2009	Introduction to Performance Measurement 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 18, 2009	Trends in Attribution Symposium (TIA III)	Philadelphia, PA (USA)
December 8-9, 2009	Introduction to Performance Measurement Training	New York, NY (USA)
December 10-11, 2009	Performance Measurement Attribution Training	New York, NY (USA)

For additional information on any of our 2008 events, please contact Christopher Spaulding at 732-873-5700

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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:

- December 8-9, 2008 – New Brunswick, NJ
- February 17-18, 2009 – London, England
- March 17-18, 2009 – Boston, MA
- April 21-22, 2009 – New York, NY
- May 12-13, 2009 – Chicago, IL
- September 15-16, 2009 – Boston, MA
- October 20-21, 2009 – San Francisco, CA
- December 8-9, 2009 – New York, NY

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CFA INSTITUTE PROFESSIONAL DEVELOPMENT QUALIFIED ACTIVITY 12 CREDIT HOURS

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:

- December 10-11, 2008 – New Brunswick, NJ
- February 19-20, 2009 – London, England
- March 19-20, 2009 – Boston, MA
- May 14-15, 2009 – Chicago, IL
- October 22-23, 2009 – San Francisco, CA
- December 10-11, 2009 – New York

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.

CFA INSTITUTE PROFESSIONAL DEVELOPMENT QUALIFIED ACTIVITY 12 CREDIT HOURS

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.