

# 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)

## PERFORMANCE MEASUREMENT BOOKS ... JUST WHEN YOU THOUGHT IT WAS SAFE TO STOP COLLECTING

In 1997 I wrote my first book on performance measurement. I was unaware of any that had come before it, though I've since collected a couple. Unbeknownst to me at the time, William Bain was hard at work writing a book, which beat mine to the press by a few months. Since that time I've written, edited, or coauthored a few more, as have several of my colleagues, including Carl Bacon and Bruce Feibel.



I just added to my collection Bernd Fischer and Russ Wermers' *Performance Evaluation and Attribution of Security Portfolios*. And Andrew Colin is in the process of writing quite an in depth book on attribution, which he kindly asked me for an endorsement for.

I will prepare a list of the books I have, in order to demonstrate how the frequency of such books has definitely picked up over the past 20 years. But seriously, how many books do we need and how many deserve to be on your bookshelf?

Well, we need at least one more, because I'm in the process of completing one; actually, at least three more, since I have two more titles I hope to work on in the next few years. And no doubt others are either writing or thinking of writing.

As to how many your library should have, it partly depends on the depth of your pockets and the size of your shelves, but perhaps more important, your commitment to your profession.

Writers tend to have many, many books on writing, as well as a collection of dictionaries and other reference materials. Having been in the offices of many investors, I know that their shelves tend to be lined with many books on the subject that they've devoted their career to. If ours is a profession, which many of us believe it is, then one should never stop collecting. The reality is that there are different approaches to what we do, as well as new ideas that surface on a regular basis.

Must you read each of these books? Only if you have time. For me, they're typically a reference that I can call upon when facing a challenge, preparing a lecture, writing an article, conducting research, etc.

As to my list of books, I'll try to have that ready for next month's issue. I will invite others to share their lists, as I'm sure my library is lacking.

# The Journal of Performance Measurement®

## UPCOMING ARTICLES

### Mind the GAP: Questioning the Investment Manager's Stated Benchmark

– Panagiota Balfousia, CFA

### The Journal Interview

– Jenny Lor, CIPM, CFE, FRM

### Residual Interaction Compounding: A New Term in Multi-Period Arithmetic Attribution

– Joseph D'Alessandro

### Puzzles in Risk and Performance: Part 2

– Marcus Hedbring

### Contribution of Initial Holdings and Transactions to Performance

– Laurent Cantaluppi

### Exact Multi-Period Performance Attribution Model

– Carsten V. Berg

## IS IT ARITHMETIC VS. GEOMETRIC ATTRIBUTION THAT WE CARE ABOUT?

I gave a lecture in Sydney earlier this month, and followed that up with an attribution workshop. In each I emphasized the following: we shouldn't be debating arithmetic vs. geometric attribution, but rather, what our view should be regarding excess return.



What is the role of attribution? To explain the sources of excess return. We want to know how each of the manager's decisions contributed to the portfolio's return relative to the benchmark's. We should ideally reconcile to 100% of our excess return. Whether we use arithmetic or geometric should lie solely upon how we define excess return. And there are two ways we typically do this:

$$\text{Excess Return}_{\text{Arithmetic}} = R_P - R_B$$

$$\text{Excess Return}_{\text{Geometric}} = \left( \frac{R_P + 1}{R_B + 1} \right) - 1$$

The reality is that most of the world likes arithmetic, so it's not surprising that arithmetic attribution rules.

During my lecture I asked why people buy saws.

The answer: they want shorter pieces of wood. Granted, there are some "tool guys" that simply want to amass a collection of all the gadgets they can, but practically speaking, saws are used to make pieces of wood shorter.

We don't use geometric or arithmetic attribution because we like the way they work, but rather because we want to reconcile to our excess return. The excess return should be the driver as to which approach we use.<sup>1</sup>

## PUZZLE TIME

### September Puzzle

Last month's puzzle was submitted by our friend, colleague, and regular puzzle participant, Anthony Howland. The accompanying table was provided, and the solution sought.

€	+	\$	+	€	+	¥	=	19
+		+		+		+		
¥		¥		\$		\$	=	26
+		+		+		+		
\$		\$		€		£	=	18
+		+		+		+		
€		€		\$		€	=	14
=		=		=		=		
19		21		16		?		

Anthony suggested that "the trick is actually in HOW to solve it, not simply finding the solution. If you work out HOW to solve it, it should take less than 20 seconds."

<sup>1</sup> I realize that there are some who use geometric models and then adjust the results to fit an arithmetic excess return construct; the wisdom of this approach has always escaped me, though it's probably a reflection of my ignorance or failure to devote enough time to fully grasp the benefits. So while most of what I'm writing here is accurate, there are, as with many things, a few exceptions.

## BEHIND THE SCENES AT TSG

Douglas Spaulding



I'm the editor of *The Journal of Performance Measurement* and The Spaulding Series of books.

I have been with the firm for 11 years.

I have known several of my co-workers since I was a young kid, so we really are like a family here. We take care of each other, and while we all take our jobs very seriously, we find time for a little fun, too.

In 2012, I completed my MFA in creative writing at Fairleigh Dickinson University. I received my B.A. in Theater Arts and English from Centenary College in 2003.

My family is very important to me. I have two wonderful nephews and a beautiful niece.

My hobbies include running, acting, reading and writing. My 5 year old nephew recently reintroduced me to LEGOS.

This November I will be competing in World's Toughest Mudder, a 24-hour obstacle race in Las Vegas, NV.

Several individuals participated, and most solved the *Howland way*. I'll quote Neil Riddles' response:

*Since we are adding the same members then they should add up to the same thing when added vertically and horizontally.*

*Adding rows:  $19+26+18+14=77$*

*Adding columns:  $19+21+16=56$*

*Since  $77-56=21$  then 21 must be the missing value.*

Let E=Euro, D=US Dollar, P=Great British Pound and Y=Yen

(i)  $2E + 1D + 1Y = 19$

(ii)  $2Y + 2D = 26$

(iii)  $2D + 1E + 1P = 18$

(iv)  $3E + 1D = 14$

(v)  $2D + 1Y + 1E = 21$

(vi)  $2E + 2D = 16$

Take (vi)  $2D=16-2E$  thus  $1D=8-1E$

Substitute for D in (iv) gives  $3E+8-1E=14$  gives  $2E=6$  thus  $E=3$

Substitute  $E=3$  into (vi) gives  $D=5$

Substitute  $D=5$  into (ii) gives  $Y=8$

Substitute into (ii) gives  $P=(18-10-3)=5$

**Thus  $1Y+1D+1P+1E= 21$**

I did it the long way, by using linear algebra. Oh, well. We thank Anthony for his submission, and ask that anyone else who wishes to submit a puzzle do so.

### October Puzzle

Purrer, the cat, has decided to take a nap. He dreams he is encircled by 13 mice: 12 gray and one white. He hears his owner say "Purrer, you are to eat each 13th mouse, keeping the same direction (i.e., clockwise or counterclockwise). The last mouse you eat must be the white one."



Which mouse should he start with?

To ensure that the CIPM Program Candidate Body of Knowledge (CBOK) stays relevant and up-to-date, CFA Institute needs input from industry experts involved with performance and risk measurement, performance and risk attribution, and/or performance appraisal on what knowledge, skills and abilities are important. Feedback to this survey serves as critical input in CFA Institute's continuous practice analysis process.

**Survey Link:**

[https://cfainstitute.qualtrics.com/SE/?SID=SV\\_9NVd7PsvhGb01eZ](https://cfainstitute.qualtrics.com/SE/?SID=SV_9NVd7PsvhGb01eZ)

## Juha Soininen

Head of Middle Office, Keva

### **Bio:**

Juha Soininen has been working in the asset owner side of the investments sector for 15 years.

Juha is Head of Middle office at Keva, a Finnish pension fund with a global, multi-asset class investments portfolio of over 40 billion euro.

Juha has been involved in performance, reporting and systems development and implementation projects as well as developing and introducing new internal processes to meet requirements stemming from the fund's wide instrument coverage, regulation, new services and various other needs. Juha's middle office team is responsible for e.g. performance, risk, allocation and portfolio reporting to the board, finance, investment and risk management and portfolio management.



## CLIENT'S CORNER

### *1. How long have you been involved in performance?*

I started with performance as a part of a system implementation project 14-15 years ago.

Performance has been a big, and ever interesting and challenging part of my job ever since in varying degrees.

### *2. What do you enjoy most about it?*

Performance measurement is one the key focus points in monitoring and tracking the fund's success and meeting our long term goals. The performance measurement methodologies and also the needs for performance measurement and reporting are constantly developing, which keeps things interesting and challenging. As the investment products and portfolio management evolve, new needs and points of view for performance also arise.

### *3. What role does The Spaulding Group play at your firm?*

Spaulding Group's forums, trainings and conferences are excellent sources to keep knowledge up to date. Spaulding Group provides brilliant venues to meet and exchange ideas with leading industry professionals and share experiences with colleagues all around the world and from different kinds of companies. As the industry changes and develops all the time, it is important to be able to challenge and change old solutions and ways of doing things.

## THE SPAULDING GROUP'S 2014 INVESTMENT PERFORMANCE MEASUREMENT CALENDAR OF EVENTS

DATE	EVENT	LOCATION
November 11-12	Fundamentals of Performance Measurement	Dallas, TX (USA)
November 13-14	Performance Measurement Attribution	Dallas, TX (USA)
December 9-10	Fundamentals of Performance Measurement	New Brunswick, NJ (USA)
December 11-12	Performance Measurement Attribution	New Brunswick, NJ (USA)

*For additional information on any of our 2014 events, please contact Christopher Spaulding 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:

November 11-12, 2014 – Dallas, TX

December 9-10, 2014 – 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.



### 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:

November 13-14, 2014 – Dallas, TX

December 11-12, 2014 – 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.

**UPDATED CIPM Principles and Expert Flash cards are now available on our web store. Please visit [www.SpgShop.com](http://www.SpgShop.com) today to order your set.**

Our performance experts have created a study aid which can't be beat: *flash cards!* These handy cards will help you and your associates prepare for the upcoming CIPM Principles Exam. Unlike a computer-based study aid, you can take them anywhere to help you test your knowledge.

Benefits of Flash Cards:

- Work at your own pace
- Immediate feedback
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These cards are a *must have* for anyone preparing to take the CIPM Exams.

