

INSIGHTS FROM CFA SOCIETY SINGAPORE

Issues around performance attribution

AS THE year comes to a close, we shop around for the best priced staycation. For those who wish to travel, we shop around for the best holiday package or flights. We also compare between alternative gifts for Christmas. But shoppers must be able to compare alternatives in a meaningful manner.

The same applies when investors compare the performance of different risk assets. Investors in Singapore do invest their funds in different risk assets and with more than one asset management company.

Naturally, there is a tendency to compare returns. Advisers must provide fair, complete and accurate performance information to enable current and potential investors to make meaningful comparisons among alternatives.

The Performance Presentation Standard

CFA Institute, a global professional body for investment management professionals, provides guidance to performance presentation through the Performance Presentation Standard.

The standard requires advisers to provide credible performance information and to avoid misstating performance or misleading clients and prospective clients about the investment performance of advisers or their firms. This standard also encourages full disclosure of investment performance data to clients and prospective clients.

Advisers must give a fair and complete presentation of performance information whenever communicating data with respect to the performance history of individual accounts, composites or groups of accounts, or composites of an analyst or firm's performance results.

Furthermore, advisers should not state or imply that clients will obtain or benefit from a rate of return that was generated in the past.

Whenever advisers provide performance information for which the manager is claiming responsibility, such as for pooled funds, the history must be accurate. Research analysts



PHOTO: PIXABAY

promoting the success or accuracy of their recommendations must ensure that their claims are fair, accurate, and complete.

If the presentation is brief, advisers must make available to clients and prospects, on request, the detailed information supporting that communication. Best practice dictates that brief presentations include a reference to the limited nature of the information provided.

Global Investment Performance Standards (GIPS)

In a bid to help investors make meaningful comparisons, CFA Institute has over the years encouraged the adoption of GIPS. These are globally ac-

cepted standards considered industry best practice for investment performance reporting and presentation. By establishing requirements for consistent and transparent reporting, the GIPS standards empower investors to compare the past performance of asset managers.

Why should investment managers comply with GIPS?

In a nutshell, adoption of GIPS by investment managers:

- Demonstrates commitment to the highest ethical principles for performance reporting. This practice can improve credibility and in turn improve trust in the financial services sector.

- Establishes a basis for fair competition across all markets. The Singa-

pore investor is a global investor who often invests in Singapore risk assets as well as diversifying to global risk assets. A common standard would enable ease of comparison. The same can be said of foreign retail and institutional investors. When they contemplate putting funds into Singapore-based asset managers, it would help their cause when there is a common standard to compare historical returns.

- Helps investment managers compete as asset owners shift more assets toward private equity, private debt, real estate, and hedge funds.

The GIPS Standards have already been adopted by hundreds of organisations around the world, and implemented by many of the top asset management firms.

In Singapore, at the time of writing, these are among the firms that claim compliance with the GIPS Standards – Allianz Global Investors, Amundi, APS Asset Management Pte Ltd, BlackRock, Inc, DWS, Eastspring Investments (Singapore) Limited, Franklin, Fullerton Fund Management Company Ltd, Lion Global Investors Limited, UOB Asset Management Ltd and Nikko AM Global.

Ethics in action

Here is a case to illustrate how the Performance Presentation Standard works. The case is adapted from material developed by CFA Institute.

Ahmad Tarmizi is reviewing the quarterly performance attribution reports for distribution to clients.

Tarmizi works for an investment management firm with a bottom-up, fundamentals-driven investment process that seeks to add value through stock selection.

The attribution methodology currently compares each stock with its sector. The report indicates that the value added in the third quarter of 2021 came from asset allocation and that stock selection contributed negatively to the calculated return.

By running several different scenarios, Tarmizi discovers that calculating attribution by comparing each stock with its industry and then rolling the effect to the sector level improves the appearance of the manager's stock selection activities.

Because the firm defines the attribution terms and the results better reflect the stated strategy, Tarmizi recommends that the client reports should use the revised methodology.

Modifying the attribution methodology without proper notifications to clients fails to meet the requirements of Performance Presentation Standard.

Tarmizi's recommendation is being done solely for the interest of the firm to improve its perceived ability to meet the stated investment strategy. Such changes are unfair to clients and obscure the facts regarding the firm's abilities.

Had Tarmizi believed the new methodology offered improvements to the original model, then he would have needed to report the results of both calculations to the client.

The report should also include the reasons why the new methodology is preferred, which would allow the client to make a meaningful comparison to prior results and provide a basis for comparing future attributions.

■ This column has been adapted from content by CFA Institute and is printed here with permission from CFA Institute. The writers are CFA charterholders who volunteer with the Singapore chapter on advocacy issues with a view towards promoting financial literacy among retail investors.