

PERFORMANCE MEASUREMENT MANAGEMENT

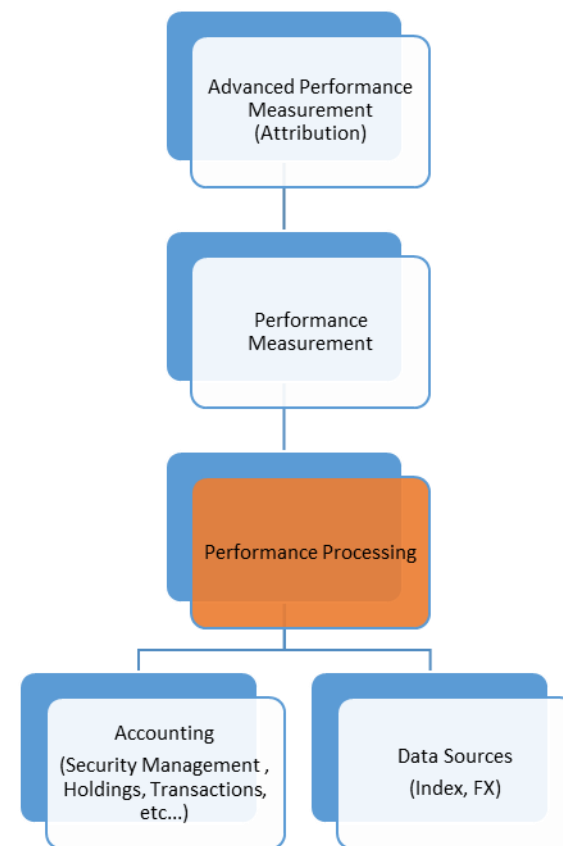
June 2017



Performance Measurement Management

More often than not, the tasks involved in properly managing performance are overlooked. What occurs as a result is that firms are unknowingly using and presenting incorrect performance numbers and analyses. The flow chart presents a generalized overview of **Performance Measurement Management (PMM)**.

An important step in PMM is the **Performance Processing** which properly maps accounting transactions for performance purposes and allows the proper treatment of corporate actions, currency impacts and other.





The following examples are actual situations of incorrect performance measurement management, and show the necessary corrections and the impact on performance

Currency Impact on Cash Returns

Issue: The first two columns presented in **Table 1** show actual performance return (%) in **Base Currency**, however the **Base Currency** presented in the first column shows an incorrect return of -200%.

Reason for Error: Omission of the currency movement in the ending market value accumulated during the month.

Correction: The return is corrected by accounting for the currency impact of \$258.55 USD in the ending market value.

Result: The correct return of 0% is reflected.

Currency Impact on Cash Returns

Table 1: Cash Returns

| 5/31/2013 | In Base Currency | In Base Currency Performance Should Be |
|-------------------------------|---------------------------|---|
| Class/Security | BRITISH POUND STERLING | BRITISH POUND STERLING |
| Class/Security Code | 10040GBP_INTLC4 | 10040GBP_INTLC4 |
| Weight | 0.00 | 0.00 |
| Return (%) | -200.00 | 0.00 |
| Contribution | 0.00 | 0.00 |
| Ending Market Value | 0.00 | 258.55 |
| Beginning Market Value | 0.00 | 0.00 |
| Cash Flow | 258.55 | 258.55 |
| Dollars Earned | -258.55 | 0.00 |
| DW Cash Flow | 129.28 | 129.28 |
| Average Investment | 129.28 | 129.28 |

The correct return of 0% is reflected

The return is corrected by accounting for the currency impact of \$258.55 USD in the ending market value.



Return of Capital

Issue: Treatment of the Return of Capital as a **Cash Withdrawal** rather than as a **Sale**.

Reason for Error: The transaction was incorrectly mapped between accounting and performance which resulted in a return of -6.08%.

Correction: Correctly mapping the Return of Capital transaction from a **Cash Withdrawal** to a **Sale**, thus correctly impacting both security and cash.

Result: The correct return of 7.05% is reflected.

Return of Capital

Table 2: Return of Capital

| 4/30/2013 | Current Performance | Performance should be |
|-------------------------------|--------------------------------|--------------------------------|
| Class/Security | ZURICH FINANCIAL SERVICES AG C | ZURICH FINANCIAL SERVICES AG C |
| Class/Security Code | ZURN.VX_INTLC5 | ZURN.VX_INTLC5 |
| Weight | 1.88 | 1.88 |
| Return (%) | -6.08 | 7.05 |
| Contribution | -0.11 | 0.13 |
| Ending Market Value | 373,352.28 | 373,352.28 |
| Beginning Market Value | 372,745.34 | 372,745.34 |
| Cash Flow | 24,382.18 | -24,382.18 |
| Dollars Earned | -23,775.24 | 24,989.12 |
| DW Cash Flow | 18,286.64 | -18,286.64 |
| Average Investment | 391,031.98 | 354,458.70 |

The correct return of 7.05% is reflected.

Correctly mapping the Return of Capital transaction from a **Cash Withdrawal** to a **Sale**, thus correctly impacting both security and cash.



Stock Dividend

Issue: Treatment of a corporate action as a **Purchase** and not as **Income** for performance purposes, which resulted in an incorrect return 0.13% (base currency).

Reason for Error: Mapping of the stock dividend transaction.

Correction: Transferring the impact from capital (i.e. **Purchase**) to **Income**.

Result: The correct return of 2.33% is reflected.

Stock Dividend

Table 3: Stock Dividend

| 5/31/2013 | Base Currency | Local Currency | Performance should be Base Currency |
|-------------------------------|--------------------------------|--------------------------------|-------------------------------------|
| Class/Security | HONG KONG EXCHANGES AND CLEARI | HONG KONG EXCHANGES AND CLEARI | HONG KONG EXCHANGES AND CLEARI |
| Class/Security Code | 0388.HK_RFPXC5 | 0388.HK_RFPXC5 | 0388.HK_RFPXC5 |
| Weight | 1.37 | 1.37 | 1.37 |
| Return (%) | 0.13 | 0.16 | 2.33 |
| Contribution | 0.00 | 0.00 | 0.00 |
| Ending Market Value | 382,957.49 | 2,972,822.40 | 382,957.49 |
| Beginning Market Value | 382,484.94 | 2,968,312.60 | 382,484.94 |
| Cash Flow | -13.66 | -106.10 | -8,439.44 |
| Dollars Earned | 486.21 | 4,615.90 | 8,911.99 |
| DW Cash Flow | -0.22 | -1.71 | -136.12 |
| Average Investment | 382,484.72 | 2,968,310.89 | 382,484.72 |

Treatment of a corporate action as a **Purchase** and not as **Income** for performance purposes, which resulted in a incorrect return 0.13% (base currency)

Stock Dividend

Table 4: Stock Dividend

| | Current Transaction | | Proposed Procedure | |
|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
| Type | Equity | Equity | Equity | Equity |
| Security | 0388.HK | 0388.HK | 0388.HK | 0388.HK |
| Security Name | HONG KONG EXCHANGES AND CLEARI | HONG KONG EXCHANGES AND CLEARI | HONG KONG EXCHANGES AND CLEARI | HONG KONG EXCHANGES AND CLEARI |
| Transaction Date | 5/31/2013 | 5/31/2013 | 5/31/2013 | 5/31/2013 |
| Transaction Type | PU | PU | PU | IN |
| Transaction Currency | USD | USD | USD | USD |
| Quantity | 251 | 251 | 251 | 251 |
| Capital Amount | 4,213 | 0 | 0 | 0 |
| Income Amount | 0 | 0 | 0 | 4,213 |
| Cash Effect | 4,213 | 0 | 0 | 0 |
| Cash Effect Security | 10040HKD_RFPXC5 | 10040HKD_RFPXC5 | 10040HKD_RFPXC5 | 10040HKD_RFPXC5 |
| Cash Effect Currency Code | HKD | HKD | HKD | HKD |

Corrected by transferring the impact from capital (i.e. **Purchase**) to **Income**.



Spin-Off

Issue: Processing incorrectly the corporate action (spin off of **Mallinckrodt Plc**) which resulted in a large negative return on the parent company (**Covidien Plc**) of -8.74%.

Reason for Error: Missing sale transaction to offset the decrease in market value of the parent company from a performance perspective.

Correction: Generate a sale transaction on the parent company.

Result: The correct return of 0.00% is reflected on the parent company.

Spin-Off

Table 5: Spin-Off

| Daily Return Report (Incorrect Management) | | |
|---|---------------|------------------|
| Date | 2013-07-01 | 2013-07-01 |
| Security | Covidien Plc | Mallinckrodt Plc |
| Begin Market Value | \$304,585 | \$0 |
| End Market Value | \$277,965 | \$26,620 |
| Positive Flows | \$0 | \$26,620 |
| Negative Flows | \$0 | \$0 |
| Total Flows | \$0 | \$26,620 |
| Gross Return | -8.74% | 0.00% |

Processing incorrectly the corporate action (spin off of **Mallinckrodt Plc**) which resulted in a large negative return on the parent company (**Covidien Plc**) of -8.74%.

Spin-Off

Table 6: Spin-Off

| Daily Return Report (Correct Management) | | |
|---|--------------|------------------|
| Date | 2013-07-01 | 2013-07-01 |
| Security | Covidien Plc | Mallinckrodt Plc |
| Begin Market Value | \$304,585 | \$0 |
| End Market Value | \$277,965 | \$26,620 |
| Positive Flows | -\$26,620 | \$26,620 |
| Negative Flows | \$0 | \$0 |
| Total Flows | -\$26,620 | \$26,620 |
| Gross Return | 0.00% | 0.00% |

Corrected by generating a sale transaction on the parent company with the correct return of 0.00% reflected on the parent company

Conclusion

Performance Measurement Management is critical to ensuring the highest quality of information is used by the firm and sent to clients. The impacts of poor management may not seem evident at first but eventually they become apparent and present risks in portfolio management (**strategy risk**) and reporting (**reputational risk**).

It is important to note that although a few examples were presented exclusively at the security level, their impact on performance is significant and felt at all levels. These issues cumulate over time and over all holdings. They impact the following:

- Performance Returns (Alpha)
- Asset Class/Sector impact
- Attribution
- Marketing/ Reporting (reputational risk)
- Erroneous feedback (Impacting front office decisions)



Who was Phocion?

- Athenian statesman from c. 402 BC – c. 318
- Nicknamed "The Good"
- Courage to stand up against popular opinion
- Avoided corruption
- Loyal to the best interests of all Athenians
- Never mistreated anyone
- Never gave insincere counsel

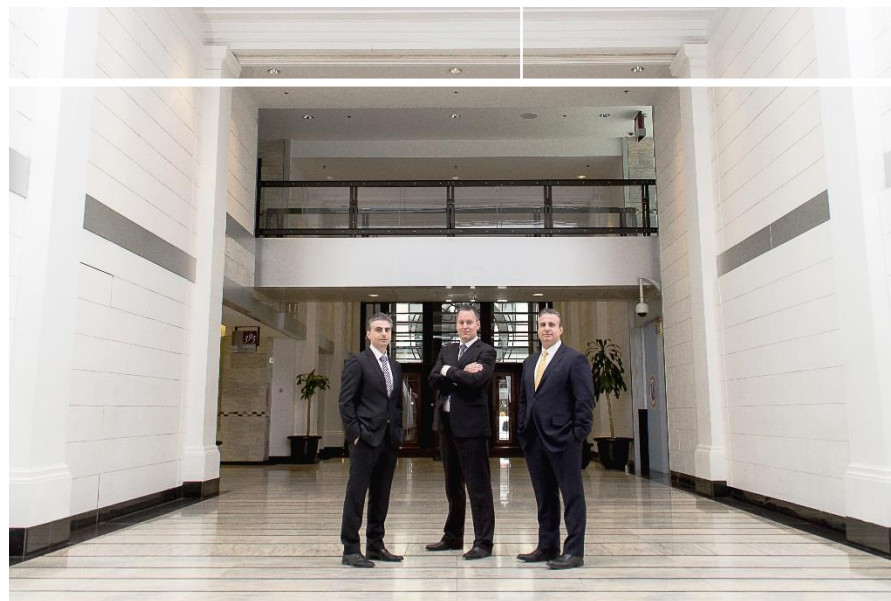


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