Performance Measurement Trends

In this paper, we discuss three major trends in performance measurement for the investment industry. These are the standardization of the performance measurement process through the CFA Institute Global Investment Performance Standards (GIPS), the transition of APAC countries towards a more standardized regulatory framework, and an enhanced demand for managers claiming compliance with GIPS to verify their claims.

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Growing Adoption of GIPS Around the World

In 1987, the CFA Institute proposed a set of standards for investment performance presentation, to allow investors to compare performance across managers. Over the past four years, the number of firms claiming compliance with GIPS has sharply increased. In 2016, 74 of the 100 largest global asset managers claimed GIPS compliance. (Grover 2016) Last year, it rose to 85 of the top 100. (Grover, Out of Top 100 Asset Management Firms Globally, 85 Claim GIPS Compliance 2017) Much of this trend towards GIPS compliance is being driven by asset owners. At the recent CFA Institute Annual Conference in Hong Kong, John Molesphini of eVestment noted a developing change in the institutional investor manager search process. (Molesphini 2018) Asset owners have increasingly shifted from GIPS compliance as a positive screen where investors view GIPS compliance of prospective managers as a bonus, moving instead towards a negative screen where investors are eliminating non-compliant prospective managers from the search process. As institutional investors incorporate quantitative metrics as a first-stage assessment tool of the manager search process, this makes it necessary to ensure a fair comparison of one manager's performance versus another's, which GIPS allows.

East Adapts to Expectations of Western Investors

With the growth of the Asian investment markets, western investors are looking to invest in the Asian markets through local investment managers. This accelerates the need to be able to easily differentiate actual performance from simulated performance, ensure underperforming portfolios haven't been left off manager composite presentations, and other questionable presentation practices which GIPS addresses. This shift is consistent with trends noted by Anju Grover of the CFA Institute Investment Performance Standards Policy Group, as she finds the increase in GIPS compliant firms has stemmed in large part from APAC managers, with a 20% year-over-year increase of compliant managers in the APAC region. (Grover, Out of Top 100 Asset Management Firms Globally, 85 Claim GIPS Compliance 2017) We at Invartis would expect this to continue further, with more AUM gravitating towards GIPS compliant managers.

Local Regulatory Standardization in APAC Helps Drive GIPS, Promote Adoption

APAC has historically lagged investment regulatory aspects compared to US and European frameworks. A large source of that delay has been the diversity of the various markets, as the US and EU respectively have more standardized frameworks that address uniform regulation for all members, whereas that level of unified regulation does not exist for APAC or ASEAN members. However, this trend is changing. Last year, stakeholders and regulatory agencies from various Asian countries started adopting global best practices as the foundation of local regulations, as part of the GIPS 20/20 initiative. In June, self-regulatory authorities in Thailand, Mongolia, and Indonesia adopted elements of CFA best practices for asset managers to apply to their member firms. (Cheung 2017) In August, representatives from 11 APAC nations also gathered in Thailand to brainstorm how local regulatory differences can be addressed to enable the GIPS framework to enhance local policies. (Cheung, GIPS Sponsors in Asia Pacific Brainstorm Ways to Promote the GIPS Standards 2017) We at Invartis expect that APAC countries will continue to incorporate GIPS elements into local regulation, as foreign investors continue to invest in the region.

GIP Compliance Not Enough, Firms Looking for Quality Verification

GIPS itself is voluntary, with investment managers self-asserting their compliance. However, there have been instances of investment managers claiming compliance where regulatory authorities later identified that those managers have not been GIPS compliant. (United States of America Securities and Exchange Commission v. ZPR Investment Management Inc and Max E. Zavanelli 2016) To better protect against these potential instances, investors are increasingly looking for managers to verify their compliance through a third-party verifier. This is particularly key in APAC, given the surge of new firms claiming GIPS compliance, and the fact that GIPS policies can deviate widely from local practices. The verification status, and the reputation of the verification firm, will therefore be something investors will start to question more frequently in the manager search process. At present, peer universe databases such as eVestment and Investment Metrics have data fields to indicate whether a manager claims GIPS compliance. Invartis expects that over the next few years, the verification status and reputation of the verifier will take on a negative screening element to search process, much like how GIPS compliance functions as a negative screen for many managers today. To support this, we would expect that these databases will begin collecting not only whether the manager is GIPS compliant, but also if that claim has been verified and by which verification firm, so that investors can use these elements in their screening process.

Forward Outlook

At Invartis, we have seen increasing demands from our clients to enhance their performance measurement process and move towards GIPS standards. While the above trends are clear, there are additional emerging developments in the performance measurement space. GIPS 20/20 also seeks to address enhancements and standardization in the reporting of alternative investment portfolios, consolidating asset-class specific rules into more uniform rules that can be consistently applied across similar alternative assets. (CFA Institute 2017) This would help increase adoption of GIPS in the alternative investment space, while also easing the burden of compliance for multi-asset managers. However, this requires further consensus, as commentary from NCREIF (NCREIF PREA Reporting Standards Board 2017) and INREV (European Association for Investors in Non-Listed Real Estate Vehicles 2017) indicate that the practicality of such consolidation may be difficult to implement for real-estate investments.

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Contact:

Web: invartisconsulting.com

Mail: hello@invartisconsulting.com

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