



THIRD QUARTER // 2013

Analytical Insights is a quarterly publication providing clients with investment information that can be used in the processes of monitoring global assets.

IN THIS ISSUE

Economic Outlook

Global Reset -
Risk Management

Report of the Quarter

Case Study - Tools
to Help Manage Risk

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Global Risk Solutions
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A MESSAGE FROM DEBRA BAKER

**Debra A. Baker, Managing Director,
Head of Global Risk Solutions, BNY Mellon**

The 2013 year is quickly wrapping up and it has been an extraordinary year for Global Risk Solutions (GRS)! As you know, at the beginning of the year, we vertically aligned all of our Asset Servicing risk services into one group, forming one of the largest and most knowledgeable risk and performance teams in the world. As a result, we have been able to develop and deliver new capabilities that we believe will dramatically impact the way you think about risk and analytics.

- Launched BNY Mellon Risk ViewSM, providing investment transparency across all asset classes and enterprise risk analysis
- Introduced Risk & Compliance service for our EMEA client base to assist with UCITS regulatory reporting requirements
- Developed Fund Fact Sheet reporting adding to our KIID regulatory reporting service

We are going to take this momentum into the new year. The GRS Management Team recently met to discuss strategy and priorities for 2014 and beyond. This is a tremendous group, who are focused on understanding your needs and committed to providing innovative capabilities and industry recognized consultative client service.

- Frances Barney, GRS Consultants – Americas
- George DeGroot, GRS Chief Administrative Officer
- Tim DiNardi, GRS Divisional Information Systems Executive
- John Gruber, GRS Global Product Management
- Fraser Priestley, GRS Consultants – EMEA/APAC
- Lydia Tse, GRS Investment Technology Group Manager
- Steve Wolf, GRS Global Client Service Delivery



Top Row: John Gruber, Steve Wolf, Tim DiNardi, Fraser Priestley.
Bottom Row: Frances Barney, Debra Baker, George DeGroot.
Not pictured: Lydia Tse.

Lastly, I am thrilled to provide you with an update on our current thought leadership project. We have re-engaged Dr. Harry Markowitz, 1990 Nobel Laureate, as co-author of our next research paper focused on risk. After surveying over 100 members of our client base, we will begin to answer the following questions:

- What are the risks that institutional investors are most concerned about now?
- How are institutional investors structuring their risk management process?
- How are regulatory changes affecting risk management and investment processes?

I look forward to sharing the results of our survey and the new Risk paper with you in 2014. We will also share an interview with Dr. Markowitz that was recently conducted by BNY Mellon.

On a personal note, as 2013 comes to a close, I want to wish everyone a happy and safe holiday season.

Best regards,

Debra A. Baker

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REPORT OF THE QUARTER

BNY MELLON RISK VIEWSM

This premium service helps you better understand your exposures and risks inherent within your investment program by addressing different approaches to risk management practices.

- Enhanced investment transparency across all asset classes, including alternatives and derivatives
- Robust enterprise risk analysis capabilities including value-at-risk measures, risk factor stress testing or historical scenario analysis to measure expected losses given a specific time frame and confidence level
- Dynamic and flexible dashboards allow you to create views of portfolios in a manner that is most meaningful to your investment process

BNY Mellon Risk View's enterprise risk summary board reporting includes a series of reports that you can customize for a monthly review or utilize during formal board meetings.

This [sample report](#) was designed to provide the Value-at-Risk and Relative Value-at-Risk of the Total Plan as well as a summary level decomposition of the risk by asset class based on a specific hierarchy. This report is just one of many different ways to decompose the risk of the plan assets. Other options include but are not limited to regions, sector, and countries.

When subscribing to these board reports, you also have access to a series of interactive dashboards that allow you to dynamically view your exposures across all asset classes, review fund liquidity, and generate ad hoc scenario analysis, sensitivity analysis, hypothetical portfolio construction, risk budgeting, and Value-at-Risk decomposition.

For more information on BNY Mellon Risk View, please contact your Global Risk Solutions Consultant.

GLOBAL RISK SOLUTIONS

TOOLS TO HELP MANAGE RISK – CASE STUDY*

CLIENT BACKGROUND

The Public Pension plan mentioned in this case study is based in the US. The plan's market value as of August 31, 2013 was approximately \$30 Billion in mostly traditional asset classes such as Fixed Income and Equity with International exposure only in developed countries. The client currently subscribes to Daily and Monthly Performance, Performance Attribution, Portfolio Analytics, Peer Comparison and Daily and Monthly Compliance.

ISSUES AND GOALS

The client has three active fixed income managers. Because there are higher fees associated with active management, the client wanted to better understand whether additional costs translated into additional returns. The goal was to quantify the managers' bets and strategies to better understand sources of active risk.

OUR SOLUTION

To understand whether active management resulted in better performance we helped the client use our extensive set of tools available on Workbench to not only understand at the total return level but analyze strategies in detail.

*This client result may not be representative of the experience of other clients and is not a guarantee of future performance or success.

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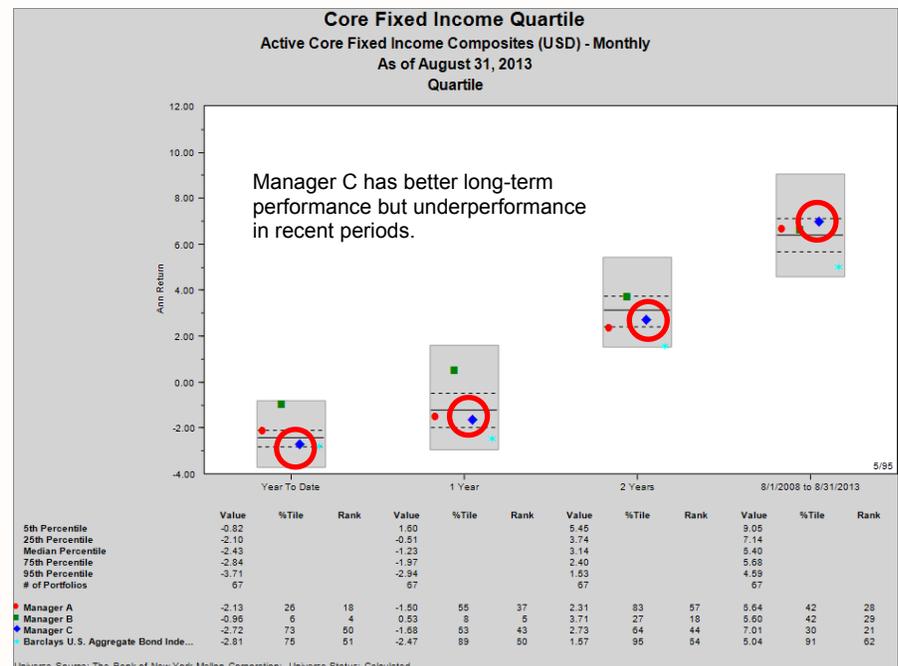
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Figure 1



In Figure 1, the focus was on relative alpha in the *Quartile* report over the recent and longer timeframes. The analysis uncovered that although Manager C has better long-term performance it appears that Manager A and specifically Manager B had outperformed in recent periods. Next we wanted to understand whether returns are justified by risk measures and whether the trends could possibly continue.



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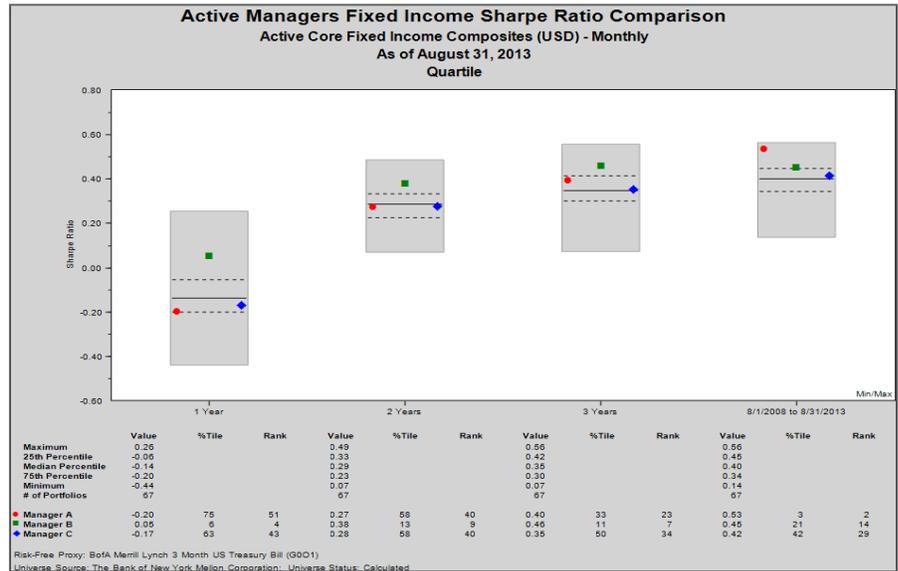
CLIENT BENEFITS

The reports and investment insight helped this client:

- Gain a better understanding of managers' sources of risks and returns.
- Gain a more granular understanding of Managers' bets and decisions through analysis of returns beyond alpha alone.
- View reporting that is not only historically based but that includes detailed analysis of current holdings.

In Figure 2, Manager C's risk adjusted return is lowest over the long-term adding another dimension of analysis compared to alpha alone. In addition, the Sharpe ratio analysis confirms better risk adjusted return over the last three years. In fact by using *Charts (graphics and report writing capability)* it was found that Manager B's Option Adjusted Duration, a measure of fixed income risk, was one of the lowest. This was further confirmed by scenario analysis through the use of *Navigator (a data collection and custom composite builder tool)* by taking out all Manager C from the composite and then measuring the Sharpe ratio. All time periods had better risk-adjusted returns without Manager C than with that portfolio included in the composite.

Figure 2



Ex-Ante returns are impossible to completely forecast, but when analyzing the *Fixed Income Profile* it is possible to extrapolate strategies and probable outcomes. Manager A has a laddered strategy, investing in securities across the term-structure, similar to the benchmark. Manager B placed large bets in shorter-term investments with no option adjusted duration (OAD) beyond 15 years. This strategy has the lowest OAD of 4.16. Conversely, Manager C has larger bets with securities OAD greater than 15 years. Therefore, if the yield curve moves favorable to the short-term then Manager B would be expected to outperform. However, if the long-end of the yield curve outperforms, then Manager C will most likely have higher returns.

Figure 3

UNITED STATES FIXED INCOME PROFILE				
As of August 31, 2013				
UNITED STATES DOLLAR	Manager A	Manager B	Manager C	BC US Aggregate Bonds
Duration Breakdown - Broad Duration - OAD				
Count	246	28	119	352
Exposure/Total MV	17.63%	14.95%	17.17%	8.77%
Contribution to OAD	0.00	0.06	0.02	0.01
Less than 1 Year/Cash Equivalents	205	65	103	2595
1-3 Years	20.01%	30.67%	14.85%	29.23%
3-5 Years	1.04	64	154	1856
5-7 Years	17.42%	19	75	31.56%
7-10 Years	8.49%	12	68	15.77%
10-15 Years	5.55%	21	46	8.88%
15-20 Years	2.19%	1	14	6.16%
20 Yrs and over	0.43%	1	2	4.44%
Other	1.31%	1	1	0.77%
Total	1181	210	598	8518
	100.00%	100.00%	100.00%	100.00%
Fixed Income Profile Number	Laddered	Underweight	Overweight	IX1F00003848

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Contact us and learn more: assetservicingmarketing@bnymellon.com

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10/2013

Policy Summary	
Plan Summary	
Portfolio	Sample Pension
Date	Feb-13
Plan Assets (\$)	\$15,000,000,000
Monthly Plan VaR (%)	-3.66%
RVaR (%)	-0.32%



Asset v. Policy Analysis					
Account Strategy 4	Policy Weights	Assets v Policy		Plan Asset Risk	
		Asset Allocation	% Over/Underweight	VaR	Risk Contribution
Equity LS	10.0%	9.7%	-0.3%	-1.90%	3.43%
Fixed Income	35.0%	27.7%	-7.3%	-1.92%	-0.50%
International Equity	16.0%	15.2%	-0.8%	-7.13%	20.03%
Private Equity	5.0%	5.0%	0.0%	-6.13%	2.25%
Real Assets	10.0%	10.3%	0.3%	-4.23%	6.30%
US Equity Ex L/S	24.0%	29.3%	5.3%	-8.99%	68.49%
Cash	0.0%	3.0%	0.0%	0.00%	0.00%

Asset v Policy

