

Do you know how much risk your manager *really* took?

If your manager's performance report measures risk using only Standard Deviation and Sharpe ratio, you may be missing the real story. These traditional MPT statistics assume that your manager's historical returns have been normally distributed, that is, bell shaped. If, in fact, returns weren't normal, the assessment of your manager's performance could be wrong.

To help you accurately measure your manager's performance, Investment Technologies developed The Expert Performance Analyst.

Let's look at a real-world example using returns for two value managers, MFS and King Investment Advisors, from Effron's PSN database. We'll show how the portfolios stacked up based on two yardsticks--MPT (standard deviation and Sharpe ratio) and Post-Modern Portfolio Theory (downside deviation and Sortino ratio).

MPT Says...

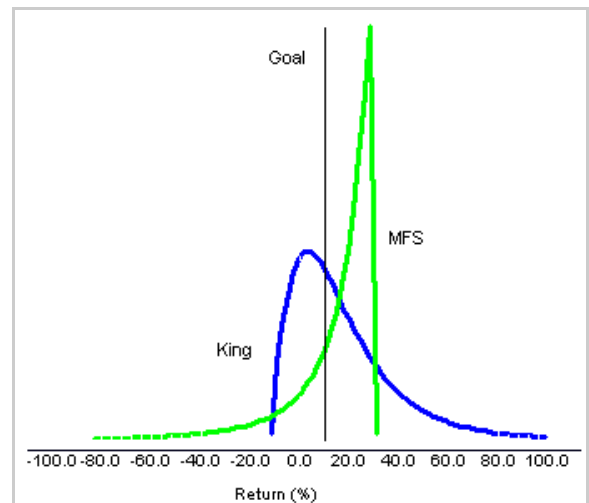
As shown in the table below, the traditional Sharpe Ratio shows MFS substantially outperforming King on a risk-adjusted basis. MFS's 0.92 Sharpe Ratio places it near the top of its style peer group (23

Risk/Return Analysis (10 Years Ending 9/30/2001)		
	King	MFS
Annualized Return	17.6%	15.5%
Traditional Analysis:		
Standard Deviation	23.4%	11.8%
Sharpe Ratio	0.55	0.92
Sharpe PSN Rank (out of 300)	209th	23rd
PMPT Analysis: (10% Goal)*		
Downside Risk	7.7%	21.0%
Sortino Ratio	0.98	0.26
Sortino PSN Rank (out of 300)	30th	181st

out of 300), while King's 0.55 ranks in the bottom third (209 out of 300). Based on this analysis, we would prefer MFS to King, all else being equal.

PMPT Says...

But not so fast! A glance at the chart below suggests that this conclusion may be incorrect. It's clear that both managers' return distributions were anything but normal. King's long tail to the *right* tells us that King had more upside returns than MFS. Conversely, MFS's long tail to the *left* shows that King had more downside returns than MFS.



The bottom line is that King had more *good* volatility and MFS had more *bad* volatility. In fact, MFS had nearly three times as much *true* risk as King (21.0% downside risk versus 7.7%). On a risk-adjusted basis, MFS drops below the PSN Value Universe median (181 out of 300) with a 0.26 Sortino Ratio, while King moves up to near the top of the peer group (30 out of 300).

Using downside risk, King is preferred to MFS.

Get All the Facts from IT

Make sure you know how much risk your manager *really* took with The Expert Performance Analyst. Contact us today at 203/364-9915 or email kferguson@InvestmentTechnologies.com for a free trial subscription and an online demonstration. ■