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UNDEROPTIMIZED DATA STRATEGY?
HERE ARE 6 PORTFOLIO INSIGHTS YOU'RE LIKELY MISSING

INSIGHT

Successful investing depends on turning data into insights. As institutional investment professionals, you have the data: it flows in from custodians, service providers, internal and external research, market news, and a hundred other disparate sources. But, too often, the magnitude of that data becomes noise. How do you make sense of it? How do you combine apparently disjointed components to discover relevance? And – most important of all – how do you leverage those insights across your organization's investment and due diligence teams?

The "hub and spoke" data strategies of the past are no longer sufficient to meet today's needs. They are limited in nature,

> THE "HUB AND SPOKE" DATA STRATEGIES OF THE PAST ARE NO LONGER SUFFICIENT TO MEET TODAY'S NEEDS.

and may hide or obscure vital insights that could be used to drive value across investments. Instead, you need to employ a data strategy that resembles a spiderweb, where secondary, tertiary, and even more distant relationships are taken into consideration along with direct relationships.

Let's take a look at six actionable insights into portfolio performance that a holistic data strategy can unlock for your institution.

ACTIONABLE INSIGHT #1:
MAXIMIZE SFAS LEVEL 1-3 DATA

Consider the data used in Statements of Financial Accounting Standards (SFAS) Levels 1-3 for hedge fund investors. This data is typically captured during annual audits; alternatively, it can be requested on a quarterly or even monthly basis from the investment manager or administrator.

In a traditional analysis, liquidity levels are captured and recorded in a spreadsheet. The back office uses and tracks this data. Sometimes, data may be aggregated from several different sources so that it can be viewed across managers and over time. But, on the whole, the data is not put in the context of the investment and its related performance.

However, by combining SFAS information with performance data coming from the accounting team, custodian, or other data provider, you would be able to compare performance across investment types and understand the relative value of each fund in the group.

TRANSFORMING YOUR DATA STRATEGY

To unlock actionable insights from your data, your data strategy must be:

- **Practical.** Zero in on the data that will ultimately drive decisions and improve processes.

- **Connected.** Get your systems talking to one another, and your personnel and service providers collaborating together.

- **Focused.** Allow personnel to focus on their workflows in the manner that is most efficient for them and the overall organization.

- **Accessible.** Enable relevant data to flow across silo boundaries.

- **Analytical.** Use a feedback loop to assess decisions that have been made and the data used to make those decisions to further improve processes.

For example, in the chart below [1], Last Chance Funds is 80% illiquid. Additionally, you can see that its performance is elevated compared to similar funds, possibly caused by an illiquidity premium. This insight may warrant further review and action by the investment team.

SFAS LEVEL 1 – 3 DATA – COMBINED WITH INVESTMENT DATA

Fund Name	Balance (USD)	Level 1 (Gross)	Level 2 (Gross)	Level 3 (Gross)	QTD	YTD	3-yr Compounded	5-yr Compounded
Alpha Commodity Fund	$1,678,500,708.00	15.000%	45.000%	40.000%	0.945%	0.945%	-0.222%	13.033%
BlackPebble Investments Macro Fund	$1,057,895,506.21	90.000%	10.000%	0.000%	9.896%	14.503%	30.505%	63.787%
King Capital Long Short Equity	$576,517,954.00	25.000%	30.000%	45.000%	-7.245%	-12.260%	-3.849%	3.689%
Last Chance Funds Offshore Fund, Ltd.	$931,349,120.11	10.000%	10.000%	80.000%	9.570%	12.359%	72.279%	74.093%
Louis Capital Emerging Growth Fund L.P.	$341,747.79	87.000%	13.000%	0.000%	-7.791%	-4.693%	-2.074%	24.336%

Figure 1: Combining SFAS Levels 1-3 data with investment data yields deeper insights.

Not only can you see this performance pattern present itself across its peers, but you should also be able to now pull in the redemption terms of your investment to ensure liquidity provisions are in line with the liquidity of the underlying funds.

ACTIONABLE INSIGHT #2:
LEVERAGE ALPHA/BETA TESTING

For a second actionable insight, take a look at alpha/beta testing. Alpha/beta testing shows how a given investment is tracking, but when combined with other data, it can tell you much more.

The example below shows a set of Large Cap managers being tracked against the S&P 500 Index. All have high R2 values, as expected. The fee information is pulled either from stated fees, or from actual costs over rolling periods as reported by the accounting team. From this combined data, you can calculate the Beta Unit Cost (Alpha Adj) by dividing annual fees by its beta and adding back in the annualized alpha. A positive percentage in the Beta Unit Cost (Alpha Adj) column means that you are paying

> ALPHA/BETA TESTING CAN TELL YOU MUCH MORE THAN HOW AN INVESTMENT IS TRACKING.

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1   All charts and examples are fictional. Any resemblance to actual data is not intended and is coincidental.

for beta. A negative percentage means that the manager is actually compensating you for their services based on the outperformance they are generating.

With a data strategy that aggregates and analyzes this information, however, you can go further. For instance, you can:

- **Break the data out** by invested managers and prospects to gain possible improvements in cost-effectiveness.
- **Segregate the data** by investment rationale (e.g., beta or active buckets) to ensure that the manager is performing as expected.
- **Set alerts** by investment types where Beta Unit Cost (Alpha Adj) exceeds a set threshold.

ALPHA / BETA TESTING

Investment Name	Benchmark	LTD Alpha	LTD Beta	LTD R^2	Fees	Beta Unit Cost (Alpha Adj.)
Large Cap Fund 6	S&P 500 TR Index	-0.084%	1.000242	0.976294	0.030%	1.030%
Large Cap Fund 1	S&P 500 TR Index	-0.026%	0.990377	0.960127	0.050%	0.359%
Large Cap Fund 9	S&P 500 TR Index	0.059%	0.999465	0.988049	1.000%	0.285%
Large Cap Fund 4	S&P 500 TR Index	0.026%	1.001966	0.993808	0.500%	0.188%
Large Cap Fund 13	S&P 500 TR Index	0.048%	0.990629	0.985056	0.600%	0.028%
Large Cap Fund 8	S&P 500 TR Index	0.065%	1.024797	0.908974	0.750%	-0.057%
Large Cap Fund 7	S&P 500 TR Index	0.030%	1.002569	0.997909	0.050%	-0.312%
Large Cap Fund 11	S&P 500 TR Index	0.080%	1.034066	0.972582	0.400%	-0.576%
Large Cap Fund 10	S&P 500 TR Index	0.109%	0.862958	0.940239	0.500%	-0.739%
Large Cap Fund 14	S&P 500 TR Index	0.079%	1.000959	0.875615	0.100%	-0.852%
Large Cap Fund 16	S&P 500 TR Index	0.089%	0.909467	0.95145	0.075%	-0.991%
Large Cap Fund 18	S&P 500 TR Index	0.118%	0.916902	0.851723	0.250%	-1.147%
Large Cap Fund 17	S&P 500 TR Index	0.118%	1.011353	0.992928	0.200%	-1.230%
Large Cap Fund 12	S&P 500 TR Index	0.136%	0.99748	0.91215	0.325%	-1.324%
Large Cap Fund 3	S&P 500 TR Index	0.126%	1.264758	0.91485	0.010%	-1.518%
Large Cap Fund 20	S&P 500 TR Index	0.178%	1.050688	0.939697	0.500%	-1.684%
Large Cap Fund 2	S&P 500 TR Index	0.144%	1.010928	0.903855	0.040%	-1.705%
Large Cap Fund 5	S&P 500 TR Index	0.195%	1.009544	0.985159	0.010%	-2.355%
Large Cap Fund 15	S&P 500 TR Index	0.225%	1.206556	0.913641	0.050%	-2.692%
Large Cap Fund 19	S&P 500 TR Index	0.377%	0.975269	0.863738	0.500%	-4.108%
Total:				0.941392	0.297%	

Figure 2: Combining market index data with fee information can yield insights for alpha/beta testing.

ACTIONABLE INSIGHT #3:
IMPROVE PERSONNEL TRACKING

The next insight you can unlock has to do with personnel. Personnel can be tracked from various sources, including Securities & Exchange Commission (SEC) and Form ADV information, back office due diligence, and presentations or due diligence questionnaires (DDQs) from managers. Investment organizations look at this data to ensure that no

material personnel have left and that no significant turnover has taken place. The analysis typically ends there.

Instead, what if you took that information and brought in invested balances and performance data, then calculated the investment team ratio? You would be able to see how resources are dedicated across managers of similar strategies.

In the example below, the highlighted manager has the lowest investment team ratio and is lagging behind its peers quite considerably. It is worth inquiring as to why this might be the case. There may be valid reasons, or there may not. Either way, you can now make a data-based decision about the manager founded on an insight that previously may have been hidden from view.

PERSONNEL TRACKING – COMBINED WITH INVESTMENT DATA

Asset Type	Fund Name	Balance - All Products	Investment Team Ratio %	MTD	QTD	YTD	Rolling 3-yr Compounded	Rolling 5-yr Compounded
Commodities								
	Alpha Commodity Fund	$1,769,465,711.51	44.286%	2.910%	7.257%	6.229%	1.951%	27.661%
Equities								
	All Asset Fund INSTL	$988,938.51	50.000%	0.770%	4.328%	10.306%	14.747%	39.278%
	Complete Capital Value Fund LP	$995,246,583.88	28.846%	0.130%	0.751%	3.809%	4.857%	25.874%
	Down Up Real Estate Fund	$942,325,598.50	47.872%	2.610%	2.799%	9.987%	9.797%	61.925%
	Pioneer Real Estate Fund	$484,092,441.76	45.902%	0.000%	0.180%	3.230%	14.070%	36.767%
	Superb Financial Global Fund II	$1,835,887,499.39	48.387%	3.390%	10.873%	54.086%	46.293%	50.036%
	Theta Partners, L.P.	$420,386,999.24	38.710%	0.000%	0.180%	3.230%	14.070%	36.767%
Equities Total		$4,678,928,061.28	43.286%	1.150%	3.185%	14.108%	17.306%	41.774%
Equity L/S								
	AKJ China Value Fund	$31,450,034.10	15.789%	3.390%	10.873%	54.086%	46.293%	50.036%
	Alpha Small Cap Fund	$18,758,712.48	30.952%	3.090%	5.401%	9.721%	27.509%	
	AV Partners, LP	$17,851,276.12	35.294%	1.750%	4.110%	11.779%	14.274%	18.026%
	CB Asia Emerging Market Fund	$30,604,100.04	50.000%	0.800%	1.486%	7.104%	15.565%	33.674%
	Graystone Investments Technology Fund	$710,895,111.12	53.409%	-1.500%	-1.077%	2.868%	19.119%	36.487%
	King Capital Long Short Equity	$448,593,714.68	24.528%	0.379%	-0.431%	4.323%	6.169%	32.145%
	Long/Short Hedge Fund	$32,171,053.09	50.000%	0.379%	-0.431%	4.323%	6.169%	32.145%
	Orange Energy Fund	$54,875,459.14	48.387%	11.700%	5.871%	52.384%	92.583%	643.121%
	Pioneer 3X Fund	$10,058,697.18	45.902%	2.570%	2.675%	9.660%	9.103%	61.312%
	Theta International	€5,832,118.02	38.710%	1.260%	5.018%	13.332%	18.107%	
Equity L/S Total		$1,360,610,417.40	39.297%	2.382%	3.350%	16.958%	25.489%	113.368%

Figure 3: Combining personnel data with invested balances and performance data lets you calculate investment team ratios, bringing insights into how resources are dedicated across similar-strategy managers.

ACTIONABLE INSIGHT #4:
QUANTIFY OPPORTUNISTIC TRACKING

Opportunistic tracking is another great benefit of a holistic data strategy. Frequently, portfolios will be over- or under-weighted in certain areas based on conviction or opportunity. But how do you know how these conviction trades performed, or how your conviction portfolio performs as a standalone item?

For example, suppose you double an investment size based on conviction. You can certainly back into the performance contribution based on a 50% allocation for the stated time period, but you cannot readily pull out this trade and other conviction trades to see how the conviction portfolio performed on its own merit and how

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it contributed to the overall portfolio. Attribution offers an insight, but depending on how it is calculated, it may not provide the full understanding you need.

This problem can be addressed through asset grouping. Asset groups are portfolio agnostic: they simply give you another way to slice up your data. Suppose, for instance, that you tag the Alpha Small Cap trade as opportunistic in the figure below. You could then place it into the Opportunistic bucket which rolls into the Aggregated Portfolio as well as attach a desired time period.

> ASSET GROUPS ARE PORTFOLIO AGNOSTIC: THEY SIMPLY GIVE YOU ANOTHER WAY TO SLICE UP YOUR DATA.

You can continue to nest these assets within further asset groups for more lenses, as much or as little as you desire. The end result is that you have an opportunistic portfolio that gives you identifiable and quantifiable feedback to pragmatically assess your opportunistic decisions, while still allowing easy access to your aggregated portfolio.
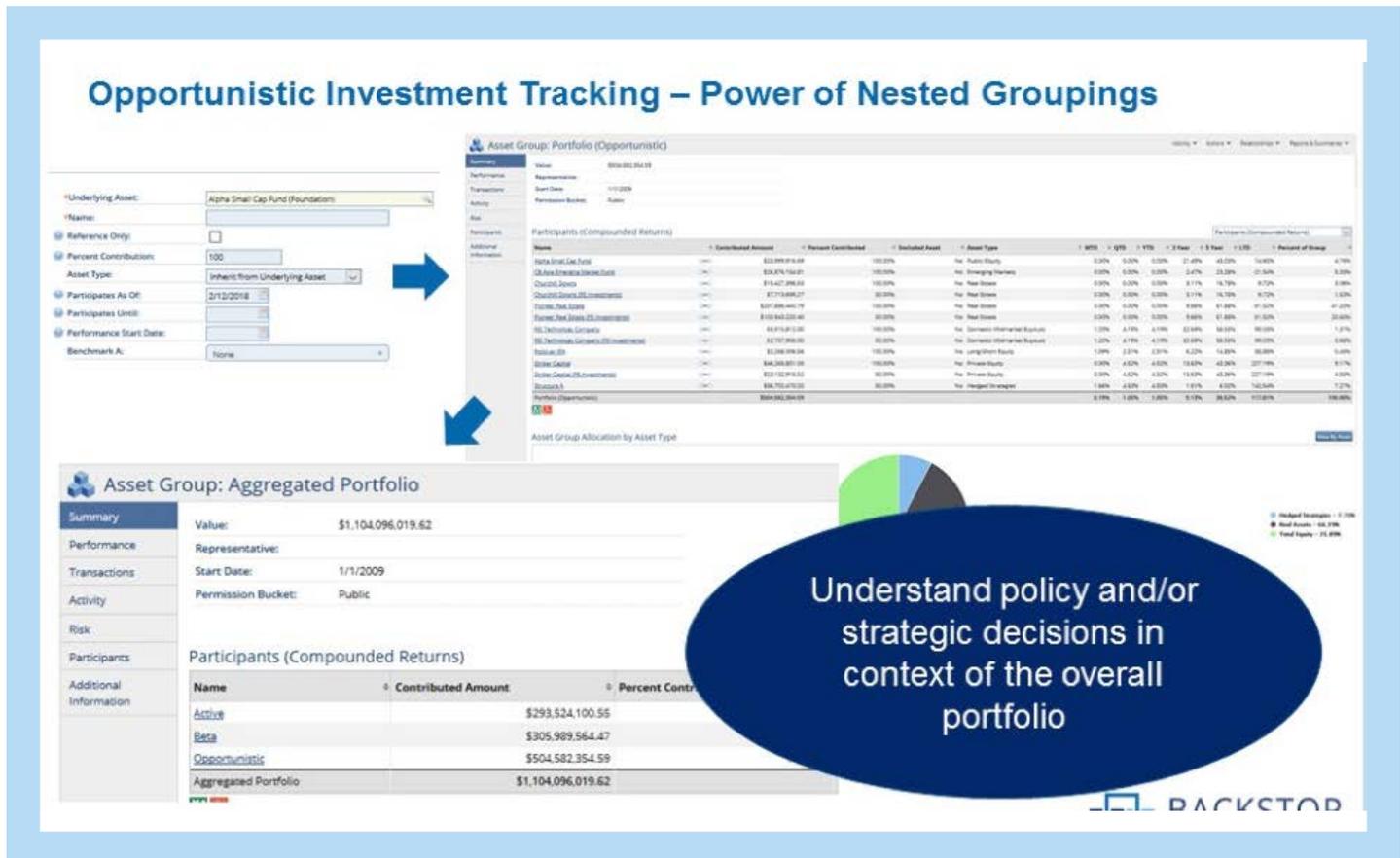

Figure.4: Asset grouping allows you to perform roll-ups that give insight into how your opportunistic decisions are doing.

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ACTIONABLE INSIGHT #5:
EXPAND PRIVATE EQUITY MODELS

Many analysts and portfolio managers continue to use spreadsheets in one form or another – you may be among them. Spreadsheets can be very useful, as they allow columns, inputs, and ratios to be added without programming a database.

Private equity valuation models are a case in point. The problem is that complex spreadsheets are usually not structured in such a way as to leverage the data they contain. By enabling push/pull feeds into these spreadsheets, your analysts can live in their comfortable spreadsheet environment while still allowing investment tracking data to be accessed by their peers for further quality checking and analysis.

- Check on the model output to ensure version control
- Eliminate "fat finger" errors
- Report on changes in the system
- Roll up information quickly across the portfolio
- Understand views and insights across all models
- Identify outliers in assumptions
- Ensure analyst consistency

> STRUCTURE YOUR COMPLEX SPREADSHEETS TO LEVERAGE THE DATA THEY CONTAIN.

ACTIONABLE INSIGHT #6:
UNDERSTAND CONTRIBUTION TO RISK

Finally, a holistic data strategy can provide insights into risk management. When considering portfolio allocation, people are usually well aware of which investments are driving performance, whether good or bad. But it is also important to understand the components contributing to portfolio risk (in this case, defined by volatility), and to dissect that covariance matrix.

For example, suppose you dissect your portfolio covariance matrix based on current portfolio weightings and look at four different time periods. From this holistic view, you see that your contribution-to-risk model is showing 70% of your volatility being contributed by only three investments in the most recent time window. You go back to your initial due diligence work and scorecard and quickly identify that those same three investments were given the lowest rating on your risk scorecard.

You now have the opportunity to assess whether this was what you expected, whether it is what you want going forward, and whether you are taking on enough risk to make a positive difference to the overall portfolio – all of which will impact your future decisions.
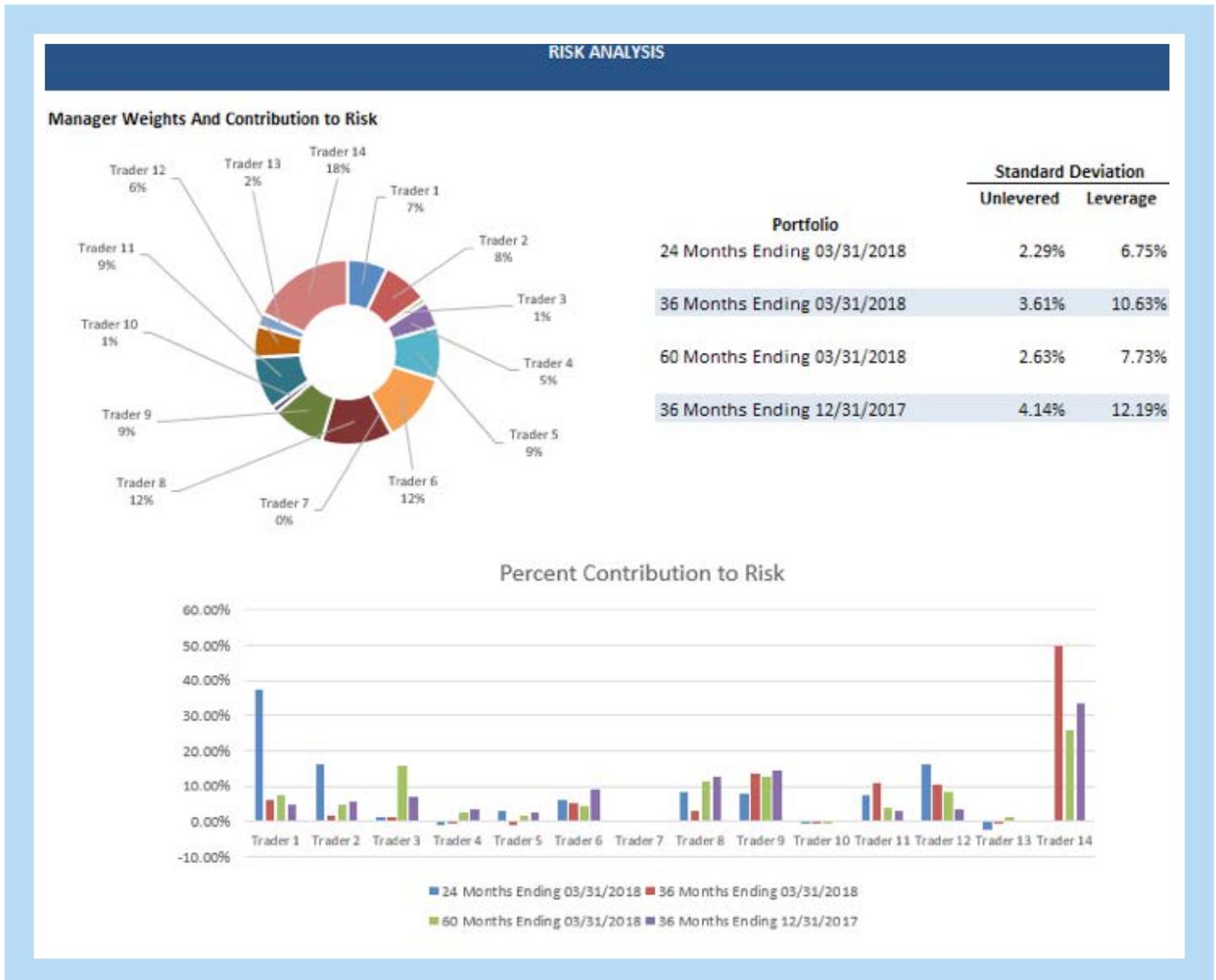
Figure 5: A holistic data strategy gives you different lenses with which to assess contributions to portfolio risk.

TURN INSIGHTS INTO ACTION

A holistic data strategy that considers secondary, tertiary, and even more distant relationships can provide you with limitless insights, many of which can enhance value, boost revenue, and transform your business. The six actionable insights discussed here are just the tip of the iceberg.

You have the data. The insights are there, waiting to be uncovered.

THE NEXT STEP IS UP TO YOU.

IN SUMMARY:

Successful investing depends on turning data into insights. By leveraging a holistic data strategy, you can unlock actionable insights to benefit your customers and your institution.

1. Maximize SFAS Level 1-3 data.
2. Leverage alpha/beta testing.
3. Improve personnel tracking.
4. Quantify performance of conviction trades and portfolios.
5. Expand private equity models for a more holistic view.
6. Understand contributions to risk to dissect the covariance matrix.

ABOUT BACKSTOP SOLUTIONS

At Backstop, we exist to help people make the very most of their time. While some would simply say that time is money, we believe it's bigger than that. To us, time is energy. Time is motivation. Time is success. It's our mission at Backstop to help people use time to its fullest potential in their work, their relationships, and their experiences. We believe that for us and for every one of our clients, every minute matters.

We help our clients in the institutional investment industry maximize their time by removing barriers in their everyday work. We simplify and streamline otherwise time-consuming tasks and processes.

Founded in 2003, Backstop Solutions offers the industry-leading, cloud-based productivity suite to the institutional investment industry, including funds of funds, pensions, investment consultants, private equity, hedge funds, endowments, foundations, and family offices. With over 750 clients, Backstop is the industry standard tool for investment fund managers and institutional asset owners to quickly and easily access, share, and manage the knowledge that's critical to their day-to-day business success.

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