Chandler Asset Management

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Since 1988, Chandler Asset Management has specialized in the management of fixed income portfolios.

Chandler's mission is to provide fully customizable, client-centered portfolio management, which preserves principal, manages risk, and generates income in our clients' portfolios.

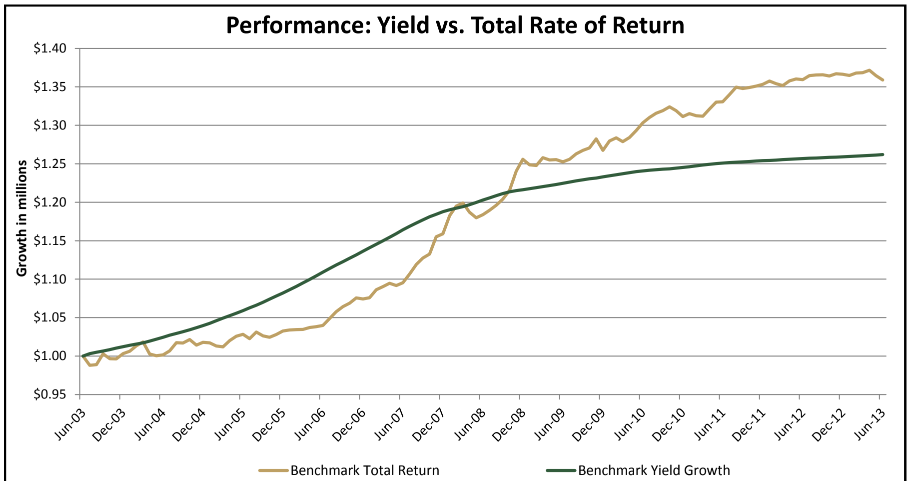
ESTABLISHED 1988

CHANDLER ASSET MANAGEMENT

CELEBRATING 25 YEARS OF SERVICE

Picking the Right Tool to Measure Investment Performance

At Chandler, we specialize in working with clients who seek safety and liquidity foremost from their bond investments. In fact, many of the public agencies we serve are often legally required to rank safety and liquidity ahead of investment yield when managing money on behalf of their constituents.



Source: Bank of America/Merrill Lynch 1-5 US Treasury & Agency Index. Performance is gross of any management or transaction fees. It is not possible to invest directly in an index. Past performance is not indicative of future results.

It's only natural, however, to fix attention on yield. Most of us have experience with yield because we've borrowed money for a car or a home, or because we've put money into savings with the expectation of receiving interest. If you invest in a one-year bank certificate of deposit, for example, you know that you'll receive a set interest rate, as long as you keep your money invested there for 12 months.

Once you know what your yield is likely to be, you can factor the expected cash flow into your budget, whether it's for running a household or a city government.

Comparisons to benchmarks are more than just report cards on investment managers. Ideally, they provide investment discipline and lead to critical questions about how and why a portfolio is performing as it is.

"Yield is very easy to understand," says Jayson Schmitt, CFA, Chandler Senior Vice President and Portfolio Manager. However, he adds, it's just one way to measure performance. Measures of a portfolio are "like tools in a toolbox. They are used for different things."

Ted Piorkowski, CFA, Senior Vice President and Portfolio Manager, says that while yield is an important part of a portfolio's performance, it is limited: "With yield, you don't know how your investment program is working."

For that reason, Chandler relies on an industry standard to measure portfolio performance, known as total rate of return. Total return is defined as interest paid plus capital appreciation, that is, the change in market price of a given security or portfolio. While most people associate changes in market price with stocks, bonds also vary in price as interest rates rise and fall. "Total return measures the value of the portfolio," says Schmitt. "It's about having all the pieces of the puzzle, not just one."

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By calculating the total rate of return on the bond portfolios we manage over time, we can then compare them to industry standards, or benchmarks, that also measure performance using total rate of return. Market indices are commonly used as benchmarks. An index is an unmanaged basket of securities that has specific guidelines and aligns with an overall investment strategy. Financial institutions have created literally hundreds of indices, such as the stock market's widely known Dow Jones Industrial Average Index and S&P 500 Index.

We measure our investment performance against benchmarks that have characteristics similar to our portfolios. These characteristics include:

- Types of bonds, such as US Treasuries, US agencies or corporate securities;
- Creditworthiness, or ability to pay,
- Maturities, the length of time before the bonds are repaid, for example one to three years

We compare the Chandler Short Term Bond composite, our most commonly used investment style, to the Bank of America/Merrill Lynch 1-5 Year US Treasury and Agency Index because it reflects the level of risk and the types of bonds that our public agency clients are authorized to include in their portfolios. Comparisons to benchmarks are more than just report cards on investment managers. Ideally, they provide investment discipline and lead to critical questions about how and why a portfolio is performing as it is.

If the annual total return on a given portfolio is 5% while the benchmark is only 2%, that's not necessarily cause for celebration. It could be a sign that the portfolio is taking on relatively more risk by investing in bonds with longer maturities that exceed the limits set by an investment policy. Or the portfolio could be buying bonds whose issuers are relatively less creditworthy. There's nothing wrong with longer maturities or somewhat lower credit ratings per se, but there would be if the portfolio is veering off-course from its specified requirements.

Conversely, if a portfolio is consistently performing below the benchmark, that could mean the investments are too cautious, that clients are missing out on returns that their risk profiles permit. Those returns could help pay for additional government services or provide greater financial security. No one wants to leave money on the table and we certainly don't want that for our clients.

> "Total return measures the value of the portfolio. It's about having all the pieces of the puzzle, not just one."
>
> - Jayson Schmitt, SVP, Portfolio Manager

Comparing the total rate of returns in the portfolios that we manage to established benchmarks is a best practice that we discuss with our clients when they hire us, says firm founder Kay Chandler, CFA. This practice helps give structure and discipline to investment strategies, so that we can seek to control risks and meet objectives. Our goal, says Chandler, is "to try to have returns consistently better than the benchmark, without taking on more market risk."

Ann Perry

Marketing & Communications Writer

Ann Perry is a writer at Chandler, where she manages the firm's bidding proposals in response to RFPs (Requests for Proposals) from government agencies and institutions seeking financial management services. She also writes newsletters, product commentaries and white papers.