

PREFACE

BACKGROUND

I joined the World Bank in 1992, after completing my PhD at the M.I.T. Sloan School of Management, to work with the derivatives and liability management team. I was fortunate to be associated with Afsaneh Mashayekhi Beschloss and Sudhir Krishnamurthi in this team. In early 1995, Afsaneh was asked to head up the pension investment area and convinced Sudhir and me to join her. The benefit of having no prior experience in asset management is that we started with a clean slate. We visited plan sponsors (corporate and public) and investment managers around the world to adopt best practices and began to question the largely asset-only focus in the industry—possibly because of our liability-based background. In addition, risk management had always been a keen issue for us in managing derivative portfolios—in the asset management area, risk management was treated much more casually.

Afsaneh and Sudhir assembled a relatively unique team to invest the World Bank's pension assets—at one point boasting four PhDs in a staff of seven—and emphasized research and innovation. As Afsaneh's responsibilities evolved to incorporate other internal assets, I was fortunate to be asked to head up the Research and Analytics area for the entire Investment Department. We assembled a talented, enthusiastic team with global experiences. Most of the articles that form the essence of this book are co-authored with colleagues from this team (Kemal Asad-Syed, Masaki Tsumagari, Arturo Balana, Ronald van der

Wouden, Cybele Suarez, and Robert Weary), good testament to the fun we had in questioning conventional wisdom. As the reader will notice, every aspect of managing funds (from establishing investment objectives to evaluating derivatives and leverage) has a new practical or theoretical twist. For example, the M^3 measure and the “luck or skill” measure mark the culmination of many years of thinking on the topic, and the fact that some plan sponsors are evaluating its use is once again a compliment to the fantastic people I have been lucky to work with over the years

PURPOSE OF THE BOOK

The book is designed to help investors, regardless of the institutions they work for, establish formal processes for efficient management of funds. We have tried to integrate best practices worldwide, gained through meetings with plan sponsors and investment managers and our own work on the topics to create material of practical relevance. I have attempted, in putting this book together, to highlight both sides of the investment issue—plan sponsor and investment manager—to facilitate decision-making.

The case study approach is used wherever possible, as practical exposition is more important to fund administrators. Theoretical concepts are either provided in the Appendices or referred to in the text for those who are interested in these aspects. The comments of many plan sponsors are interspersed throughout the book—and the Acknowledgment is testimony to the number of people who have contributed to the final text. In many cases, the “innovation” is a shift in paradigm, rather than a totally different way of doing business. This is most evident in the material on risk management and peer comparison. It is our hope that by addressing the key decisions that sponsors need to make on asset allocation, risk management, and performance evaluation, and demonstrating keys to successful implementation that this book will assist plan sponsors to achieve their objectives more efficiently. It is clear that the state-of-the-art is evolving daily. This book gives a unique perspective of innovative ideas to manage portfolios today.

DISCLAIMER

All information contained in the book are composed of the author’s views and theoretical applications developed throughout the author’s educational and

professional career, and do not represent the views of J.P. Morgan Chase & Co. or any of its affiliates (“JPMC”). They also do not represent the views of the World Bank Group (“WBG”) or any of its affiliates. Accordingly, all views, hypotheses, conclusions, recommendations and errors thereof, reflected in the book are those of the author’s. The author’s ability to write this book in his role with JPMC shall not be construed as an endorsement by JPMC, and any references to JPMC contained in the book are included for general information purposes only. The author’s ability to write this book using insights gained at the WBG shall not be construed as an endorsement by WBG, and any references to WBG contained in the book are included for general information purposes only.