



Zeno AN Solutions Trade Process Peer Group Universes

Featured Peer Universe: Q3 2019 Non-US All Country Managers

Asset manager trading processes often significantly impact overall investment performance. To this end, managers have a fiduciary obligation to both obtain best execution (so as to minimize the impact their trading has on their clients' portfolio returns) and avoid paying excessive commissions. Asset owners, in turn, have a fiduciary obligation to monitor their managers to ensure these legal requirements are achieved.

In early 2014, Zeno AN Solutions ("Zeno"), then known as Zeno Consulting Group, introduced its trade cost Peer Group Universes. Unlike most other trade cost comparisons, Zeno's Peer Group Universes rank managers against other managers charged with the same investment mandate (e.g. Small Cap Growth, Large Cap Value, Non-US All Country etc.). Further, the costs tracked in the universes include not just broker-related costs, but also the trading costs incurred by asset managers "working" their orders over multiple days. Equally important, the universes measure turnover rates, thereby enabling the quantification of how much each manager's trading process impacts their annual investment return.

As such, Zeno views these universes as the next step in the evolution of trade cost analysis; and an important tool in evaluating the degree to which a manager's trading process contributes or detracts from bottom-line performance. Just as Fund fiduciaries use Investment Performance Peer Group Universes to help identify managers with superior stock picking ability, Zeno's Peer Group Universes help evaluate the skill and efficiency with which managers implement those stock picks.

This Quarterly Newsletter highlights the range of trading costs, commissions, turnover, and impact to performance incurred by managers in Zeno's **Non-US All Country** Peer Group Universe.

Non-US All Country - Peer Group Universe

Over the past five plus years, the cost to trade Non-US All Country securities have trended slightly higher. However, while the spread between the Top and Bottom Quartile trading costs remained fairly constant, the spread between the outliers (i.e. 5% versus 95%) has narrowed significantly.

As shown in the table below, over the trailing four-quarters ending September 30, 2019, the median trading costs incurred by Non-US All Country managers was -46 bp; about 10 bp more expensive than five years ago. During this time period, the difference between the more efficient and expensive trading processes (i.e. managers ranking in the 1st vs. 4th Quartiles of the Peer Group), remained 52 bp. However, the spread between the 5th and 95th percentile managers narrowed 66 bp from five years ago, to only 120 bp.

Perhaps most importantly, from an investment perspective, given the turnover rates experienced by Non-US All Country managers (during the four-quarter period ending September 30, 2019), the median impact to annual returns during this period was approximately -36 bp, roughly the same as five years ago. However, the range of the "performance hit" incurred by managers at the extremes (i.e. the 5th and 95th percentiles) ranged from only a couple basis points to over -1.5%!

To put these numbers into context, the median International Fund’s one, three and five-year net returns ending June 30th 2019 were -0.7%, 8.0% and 1.9%, respectively.¹ Clearly, trading costs can eat up a significant portion of the managers’ gross return – often ranging anywhere from 10-30% of a manager’s gross return. From a performance attribution analysis, this is an example of why we encourage clients not to ignore/underestimate the impact of trading on returns.

It should also be noted that the average commission rate paid during this period by Non-US All Country managers was -6 bp, with 4th Quartile commission rates averaging -9 bp or more. As Zeno has been alerting its clients over the past several years, MiFID II as well as other regulatory and market pressures, may be contributing to a drop in global commission rates (as some managers moved to execution-only rates). That in fact appears to have occurred. At this time in 2017 (the last year prior to MiFID II going into effect), the median commission rate for Non-US All Country managers was -7 bp, with 4th Quartile commission rates averaging over -11 bp.

	Non-US All Country				
Ranking	Total Costs (bp)	Impact on Annual Returns (bp)	Turnover (%)	Commissions (bp)	Execution Price vs. VWAP (bp)
Top (25%)	-20	-15	23%	-4	-0
Median (50%)	-46	-36	35%	-6	-3
Bottom (75%)	-72	-62	74%	-9	-6

To review all of Zeno’s Peer Group Universes [click here](#).

Glossary of Terms

Ranking - Displays the results of the managers who ranked in the 25th, 50th, and 75th percentile of their respective peer group universes.

Total Costs - The four-quarter average of total execution costs (sum of multi-day delay, daily market impact and commission costs) paid in order to build/unwind trade orders. The difference between the more efficient vs. more expensive managers can often exceed 100 bp in trading costs.

Performance Impact - The loss of asset value incurred as a result of a manager’s trading activity (calculated by multiplying the manager’s “total cost” by that manager’s turnover). In evaluating the factors contributing to manager returns (i.e. “performance attribution”), “performance impact” describes the impact that trading costs had on a manager’s overall performance.

Turnover - For any given time period, the average of the Buy and Sell trade values (i.e. Buys plus Sells divided by two) executed during that period, divided by the portfolio value at the beginning of that period.

Commissions – Commissions (the explicit fees paid to brokers to execute trades) are typically the smallest, but most controllable part of a manager’s total execution costs – “*The tip of the iceberg.*”

Execution Price vs. VWAP - The difference between the execution price of a manager’s trade, versus the average price paid for that security in the marketplace throughout the full day (“VWAP”). Negative figures indicate that the manager’s executed price was worse than that day’s VWAP.

¹ SPIVA US Scorecard, Mid-year 2019

Zeno AN Solutions helps institutional asset owners to proactively monitor and manage the trading costs and processes of their asset managers. Our clients are solely plan sponsors/pension funds and other asset owners. Our transaction cost analysis services are therefore provided by an independent third party, free from conflicts of interest.

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