Morningstar Direct℠ Cloud

Conducting Total Portfolio Attribution
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Conducting and Analyzing Total Portfolio Attribution

The Total Portfolio Attribution (TPA) capability in Morningstar Direct Cloud allows you to measure the impact of your asset allocation and manager decisions on a client’s account. In this manual, you will learn the following:

- how total portfolio attribution is calculated in Morningstar Direct Cloud
- which asset classes are used for managed investments, and which indexes those asset classes are tied to
- which policies are used for weighting the asset classes, and the specific asset class weighting assigned to each policy, and
- how to view and interpret TPA data for an account, including changing the policy associated with an account.

In TPA, the value of a portfolio manager’s decisions is known as Active Return. Active Return is calculated by adding together the elements described in the following table:

<table>
<thead>
<tr>
<th>Element</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Allocation Effect</td>
<td>Allocation Effect measures an advisor’s intentional deviation from the long-term policy to capitalize on his or her views on different asset classes. Overweighting an asset class that has outperformed the total portfolio is a good decision. The converse is also true.</td>
</tr>
<tr>
<td>Selection Effect</td>
<td>Selection Effect measures an advisor’s decisions to hire and fire managers, and the timing of such events. The manager selection effect is positive when a manager achieves a positive excess return over its benchmark. The converse is also true.</td>
</tr>
<tr>
<td>Misfit</td>
<td>Misfit captures style bias. It occurs when a manager’s benchmark is different than the asset class benchmark. For example, an equity manager is compared to the Russell 1000 index, but the asset class is compared to the S&amp;P 500.</td>
</tr>
</tbody>
</table>

Contribution is another factor to consider when analyzing TPA. Contribution is an absolute analysis of an account’s performance, while TPA is a relative analysis. Contribution is the weight (of a holding) multiplied by its return. Attribution combines the relative weight and relative return versus the benchmark.

Note: To read Morningstar’s full methodology on how TPA is calculated, see this document.
When viewing total portfolio attribution data for accounts, Morningstar Direct Cloud groups investments into the following global broad categories:

- Fixed-Income
- Equity
- Commodities, and
- Money Market.

Note: TPA does not factor in individual stocks and bonds, so if these investments are part of a client’s account, they will appear under “Unclassified” on the Attribution worksheet.

The following table shows the indexes used for each asset class:

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity</td>
<td>Morningstar Gbl Mkts GR USD</td>
</tr>
<tr>
<td>Fixed Income</td>
<td>Morningstar US Core Bd TR USD</td>
</tr>
<tr>
<td>Commodities</td>
<td>Morningstar Lng-Only Cmdty TR USD</td>
</tr>
<tr>
<td>Money Market</td>
<td>Morningstar Cash TR USD</td>
</tr>
</tbody>
</table>

The following default policies can be used when viewing total portfolio attribution data for an account:

- Morningstar Conservative Target Risk
- Morningstar Moderately Conservative Target Risk
- Morningstar Moderately Target Risk
- Morningstar Moderately Aggressive Target Risk, and
- Morningstar Aggressive Target Risk.

The asset allocation breakdown for each policy is detailed in the following table:

<table>
<thead>
<tr>
<th>Policy</th>
<th>Fixed Income</th>
<th>Equity</th>
<th>Commodities</th>
<th>Money Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>Morningstar Conservative Target Risk</td>
<td>68%</td>
<td>20%</td>
<td>9%</td>
<td>3%</td>
</tr>
<tr>
<td>Morningstar Moderately Conservative Target Risk</td>
<td>52%</td>
<td>40%</td>
<td>6%</td>
<td>2%</td>
</tr>
<tr>
<td>Morningstar Moderately Target Risk</td>
<td>34%</td>
<td>60%</td>
<td>4%</td>
<td>2%</td>
</tr>
<tr>
<td>Morningstar Moderately Aggressive Target Risk</td>
<td>19%</td>
<td>80%</td>
<td>1%</td>
<td>0</td>
</tr>
<tr>
<td>Morningstar Aggressive Target Risk</td>
<td>5%</td>
<td>95%</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>
To view the total portfolio attribution for an account, do the following:

1. From the Home page, in the Portfolio Workbooks area, click the **Client Accounts Template**. The Select a portfolio dialog box opens.

2. Click **All Client Accounts**. The Client Accounts Template workbook opens.
Exercise 1: View the total portfolio attribution for an account

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3. Select the **Attribution** worksheet.
4. Be sure the correct account is selected from the focus panel to the left.
5. Click the **border** between the focus panel and the Attribution component to collapse it.

Click here to collapse the focus panel on the left

Remember, unmanaged investments are grouped as “Unclassified”
6. Take note of the Policy Weight% column. If the values here differ significantly from the Actual Weight% values for the account, a different policy might be a better fit for the account. Click the Component Settings icon, and choose a different policy. 

Note: By default, the Morningstar Conservative Target Risk is assigned to each account.

7. Click away from the Component Settings menu to close it.
8. **Scroll right** to see the Active Return value for the account. If the Active Return is positive, it means the asset allocation and selection decisions contributed to a better outcome for the client. If the Active Return value is negative, was it due to allocation decisions, manager selection, or benchmark misfit?

![Table](image)

The Active Return value for this account is strongly negative, and nearly all of this can be attributed to the manager misfit between this small-cap fund and the benchmark.