



## Tighter Fair Value Practices Help Funds Ride Out Volatility

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August 24, 2011

New research shows fund managers have tightened their practices around fair valuation of international equities to be more sensitive to market movements.

In fact, about 36% of funds participating in a recent **Interactive Data** survey say they currently use a “zero trigger” for fair valuation of such securities. A zero trigger requires funds to use fair valuation every day, regardless of whether there is movement in the markets.

The figure is up from 2004, when only about 10% of funds had zero triggers or used fair value procedures on a daily basis, according to the study. Last year, 35% of surveyed funds used a zero trigger.

Funds are also developing more complex triggers for determining when they will fair-value their holdings, according to the survey.

Some firms are now using multiple triggers for the same fund — one that invests in both European and Asian equities, for example. A small number use dynamic or changing triggers, Interactive Data reports. In this scenario, a fund might use a moving average of a certain benchmark, looking at the standard deviation of those movements historically and using that as a trigger.

Interactive Data surveyed 111 mutual fund firms on their fair value practices for international equities and received responses from CFOs, CCOs and valuation team members. The survey was conducted last month, ending July 25.

Driving this trend toward more complex triggers is the desire for a more “security-specific approach” for deciding when to fair-value portfolios, says Rob Haddad, director of evaluated services at Interactive Data.

Funds are required to use fair value prices when market quotations for their portfolio securities are not available or reliable. Heightened volatility in the markets has drawn attention to the importance of fair value practices for funds holding international equities, and setting triggers continues to be a major focus for firms, says Interactive Data.

The increase of funds using a zero trigger over the last seven years may be due in part to increased volatility in the markets, says Haddad, which may have led funds to reexamine the triggers they use through backtesting. With backtesting, funds look at the difference between the fair value price and the next traded price. About 92% of those surveyed said they systematically and regularly review backtesting performance data.

“The higher level of volatility may have influenced funds to take another look [at their triggers] and to examine backtesting to see if it’s helpful,” says Haddad.

Another factor that has probably affected the sharp increase in the number of funds that use zero triggers is simply that firms have gained a greater level of comfort in applying fair value adjustments to equities, says Haddad. Ten years ago it was a new concept for funds to apply adjustments to equity prices, he adds.

Mark Perlow, partner at **K&L Gates**, says he’s also seeing more funds use a zero trigger as well as more complicated triggering strategies.

“The world has gotten more complex and volatile, so it’s natural for trigger levels to become more tailored to the circumstances of a fund and its investments than they had been in the past,” says Perlow.

Haddad says his firm does not expect to see widespread changes to fair value procedures as a result of the most recent market volatility. “We found that many mutual fund clients have been quite comfortable with the fair value procedures they have in place... the systematic review of fair value performance and how it impacts portfolios has given them a sense of comfort.”