

# Preserving Asset Value with Transition Management

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Transition management is used by institutions to implement changes to investment allocations in a project-managed, risk-controlled way. Changes typically arise from benchmark changes, manager changes due to performance, or strategic requirements due to corporate activity. Specific examples of when institutions use transition management are:

- Fund manager changes
- Portfolio liquidation or implementation
- Consolidation of portfolios due to merger activity

## TABLE OF CONTENTS

Why Use a Transition Manager? . . . .	2
How Transition Management Works . .	2

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## Why Use a Transition Manager?

A transition manager takes responsibility for all aspects of a transition, with a view to minimize costs, control risks and reduce the administrative burden to the client, all underscored with the goal of preserving the portfolio's value. The need to control risk, and thus safeguard asset value, is even more evident in today's volatile markets. The transition manager produces comprehensive post-trade analysis, reporting execution performance versus pre-trade benchmarks, thus, providing the client full transparency and accountability.

Relieving clients of the administrative aspects of the transition leaves their staff to continue managing their duties as usual with little disruption.

Transition specialists control costs through trade implementation. While some costs are explicit, such as commissions and taxes, and known prior to transition, they tend to have the lowest impact on the overall value of the investments. The implicit trading costs incurred through market impact (increases by trading faster) and opportunity cost, or volatility (increases by trading more slowly), tend to have the biggest impact on value. The transition manager seeks to minimize the combination of these costs through careful trade strategy design.

Furthermore, in the less transparent over-the-counter markets such as fixed income, information leakage, where details about a potential trade become known in advance of execution, can significantly impact the value of securities traded. At J.P. Morgan, our Transition Management group controls for information leakage by implementing change in an efficient, best execution compliant manner— leveraging technology to access external brokers alongside the deep J.P. Morgan fixed income franchise.

Lastly, using a transition manager enables clearer performance measurement of portfolio managers. The transition manager typically restructures investments within a transition account which ring-fences all costs incurred in the process; the asset manager receives their model portfolio on the date required by the customer so performance starts from the date they receive their model assets. Without a transition manager, a portfolio manager would typically be granted a potentially costly “performance holiday” while purchasing required securities. As a portfolio manager's core strength is security selection and not trading, using a transition manager can dramatically reduce the time required to build a portfolio. Where multiple fund managers are involved, efficiencies are further gained by the transition manager managing risk holistically. The table 1 summarizes these factors.

**Table 1: Service Comparison**

Factors	Fund Manager	Transition Manager
<b>Core Competency</b>	Security selection and portfolio modelling	Efficient portfolio implementation
<b>Timing</b>	Potential timing delays increase opportunity cost	Optimized execution timeframe to minimize opportunity cost and market impact
<b>Reporting</b>	Non-transition specific cost analysis and reporting of implementation	Specific and complete transition cost analysis supported by detailed pre/post trade reporting
<b>Measurement</b>	Accountable for alpha generation or performance versus a benchmark	Accountable for management of risk and cost throughout the transition

## How Transition Management Works

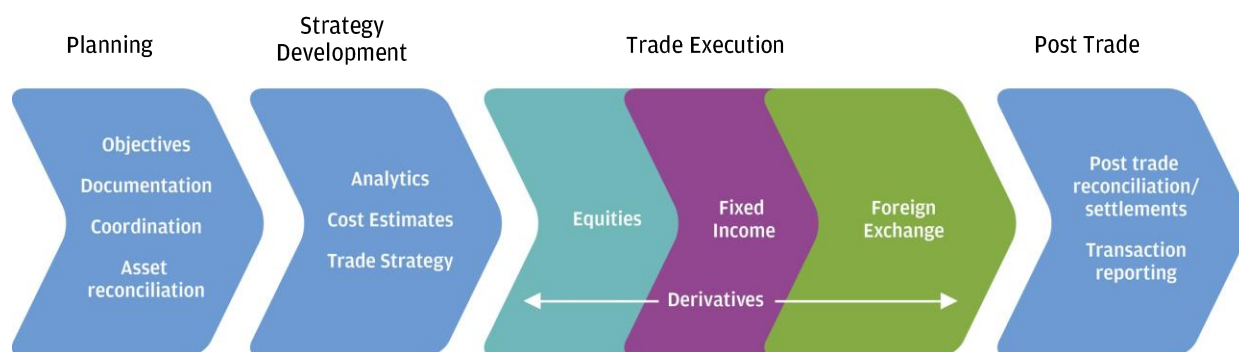
In implementing a transition, the transition manager takes control of the client's “legacy assets” (those securities already held by the client) and executes an optimized trade strategy to restructure these assets into the new, “target” managers' model portfolios that are based on wish lists received from them. Legacy securities desired by the target managers are transferred free of charge, and the remaining securities are traded in a risk controlled way. The transition manager works to maintain market exposure and move to the client's new investment structure in as efficient a way as possible. Derivatives may be employed, for example, as a way to quickly shift the overall portfolio exposure, allowing the transition manager to trade the underlying assets at pace with market liquidity.

The transition process is typically divided into the four stages delineated below:

- During the **Planning** stage, the transition manager coordinates with the client, portfolio managers and custodians to confirm client's transition objectives, verify documentation is complete, ensure relevant custody and trading accounts are opened, and reconcile legacy positions to custodian records. The transition manager produces a detailed project plan that identifies all steps required for the transition, and the party responsible for each.
- During the **Strategy Development** phase of the process, the transition manager performs pre-trade analysis and cost estimates based on the legacy and target security lists, identifies any potential in-kind securities that can be transferred between the legacy and target structures, and develops a risk-minimizing trading strategy for the remaining securities based on the analysis. This analysis containing cost and risk estimates is presented to the client; performance benchmarks are agreed.

- During the **Trade Execution** phase the transition manager implements the trading strategy through a variety of venues, closely monitoring executions and adjusting trading instructions as needed.
- In the **Post Trade** phase, in addition to security settlement, reconciliation, and delivery of assets to the incoming fund manager, the transition manager provides full transaction reporting and performance analysis, comparing transition performance to pre-trade estimates.

While transition managers follow different pricing structures, and some charge an explicit fee for the service, J.P. Morgan does not charge a management fee unless asked to do so. We typically charge a competitive commission based on assets traded.



Already established as the standard process for implementing portfolio changes in the United States, United Kingdom and Australia, as well as among the most sophisticated investors elsewhere, transition management is now seeing greater acceptance by the general investor community as a way to minimize risk, reduce cost and increase operational efficiencies.