

FTfm

Distressed portfolios up for inspection

Impaired assets

Global Workout has answers for investors under duress, writes **Suchita Nayar**

Bank of New York Mellon's advisory business for distressed and illiquid assets has grown rapidly in its debut year.

Set up last May, Global Workout Solutions had amassed \$24bn (£16bn, €18bn) of assets as of March 31. All told, the Boston, Massachusetts, unit expects to be overseeing about \$40bn shortly, including assets in the pipeline and the double counting of some assets common with other businesses of the bank.

It has quickly become a significant component of Standish Asset Management, the bank's fixed income cornerstone that runs \$186bn of assets globally, including some shared mandates. Standish, in turn, is a part of the global franchise of BNY Mellon Asset Management.

The catalyst for Global Workout was the deflating of the credit bubble surrounding the US housing market. This implosion resulted in the near-collapse of the banking system and triggered massive de-leveraging by both financial companies and consumers, leaving many asset classes in need of triage.

"As the credit crisis unfolded, many investors found themselves cornered and had nowhere to turn," says Desmond MacIntyre, president and chief executive of Standish. Commercial paper became illiquid and there was significant performance dispersion in the fixed income space. While most institutions were invested for the long haul, the pain became

too much to bear for some, he says. Furthermore, valuation and pricing anomalies began to appear disconcerting to some.

"We found our large and diverse client base coming to us with problems and wanted assistance to determine whether the assets they held were impaired for the short term or permanently," says Mr MacIntyre, whose overall business has some 400 clients in 37 countries. Amid a backdrop of frozen global markets, the question became: if these assets cannot be sold, what should be done with them?

Herein lay the genesis of Global Workout Solutions, a fiduciary advisor that services stressed, distressed and hard to value assets. And there's no dearth of such paper, in the form of fixed income securities, collateralised debt obligations, structured investment vehicles and securities lending collateral pools, in the current market.

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Additionally, there are illiquid asset-transfers, known as payment-in-kind, that hedge funds and high-yield money market entities have made to redeeming investors.

Global Workout's client roster has expanded to include endowments, family offices, institutional investors, investment consultants and pension funds, as well as banks and insolvency practitioners. Thomas Graf, director of structured products within Standish, oversees the unit with help from 10 investment professionals.



Desmond MacIntyre: 'Investors found themselves cornered and had nowhere to turn'

There are four components of its offering: valuation, risk management, surveillance and liquidation. From a macro perspective, here is how a workout mandate works: the unit would analyse a client's troubled portfolio as part of what Mr MacIntyre calls "a look under the hood". The group would scrutinise models on which assets have been valued and conduct independent pricing verification.

The next step would comprise separating assets that are temporarily impaired from those that are permanently damaged. Depending on the client's investment horizon and end goal, it would establish a multi-year management mandate, including surveillance, for those assets that can be held to maturity with the expectation of a market recovery. Finally, hopeless assets wind up in liquidation, also a process that the unit conducts.

Standish's involvement is not a mere opportunistic exercise to benefit from investors under duress, says Mr MacIntyre, but rather a process aimed at creating tailored, bespoke accounts that can meet the liquidity and

investment needs of clients.

As some credit markets continue to decline or remain frozen, investors face the dilemma and uncertainty of determining the true value of securities they hold, argues Mr MacIntyre. For instance, a broker may quote a price 15 points below that of industry-pricing vendors. Fair value analysis might infer another price altogether. "Our value-add is to put these prices into context and also highlight downside cliff risk and liquidity risk with securities so that clients can optimally manage their exposures," he says.

Looking ahead, Mr Graf says the advisory business continues to see significant inflows from clients who are drawn to it for its independent risk management and proprietary valuation capabilities.

In its marketing pitches, it is telling prospective clients to take charge of portfolio risk by fully understanding today's market reality. Its bottom line is: failing to act on permanently impaired assets can be catastrophic, while moving impulsively on temporarily impaired assets can be equally harmful.

Standish Mellon Asset Management Company LLC ("Standish") is a subsidiary of The Bank of New York Mellon Corporation ("BNYM") and had approximately \$45 billion of discretionary assets under management (AUM) as of March 31, 2009. In addition, Standish managed about \$33 billion on a non-discretionary basis. The Global Workout Solutions Group within Standish has contracted a total \$24 billion (based on net asset values at take-on) in discretionary and non-discretionary business since May 2008. Standish had reported total AUM of \$186 billion as of December 31, 2008. The difference in AUM is the result of a planned corporate restructuring, effective January 1, 2009, that saw the transfer of all cash, indexation, and stable value assets to BNY Mellon Cash Investment Strategies (CIS), a division of The Dreyfus Corporation ("Dreyfus"), an investment adviser. Standish and Dreyfus are wholly-owned subsidiaries of BNYM. These AUM figures also include assets managed by Standish personnel acting as dual officers of Dreyfus and The Bank of New York Mellon, also a subsidiary of BNYM. As of March 31, 2009, Standish had more than 250 clients in 37 countries.