

All you need to know about: **Performance**

“Past performance is not a guide to future performance”

You see this statement written so often in relation to funds yet huge effort is dedicated to communicating investment performance to potential investors – it is a big chunk of what we do too.

Is it true?	Is the statement true? Well, to a large extent, yes. Taken on its own, without any other information to provide some context to the numbers, past performance alone is not much use as an indicator of future performance.
So is all that performance data a waste of space?	We would argue though that performance data can be useful. We believe there are good investment managers and bad investment managers; managers who do better in certain scenarios and funds whose performance is pretty predictable because of what they invest in.
Some background	In part this argument goes back to whether there is any point to “active” investment management at all.
Active vs. passive	Active managers choose a selection of investments and invest a proportion of their portfolio in each investment – thinking about how much money how much money they might lose vs. how much they are likely to make and the likelihood of both of these – usually referred to as “Risk vs. Reward”. Passive managers just buy every available investment, usually in proportion to its size, hoping that, on average, the market will go up.
Academic theory	For a long time a lot of theoretical work assumed that markets were “perfect”. Prices of investments reacted to news; everyone had access to the same news (otherwise you were guilty of possessing inside information), investors would act rationally (all react to the news the same way) and it wasn’t possible to predict what the news would be. Therefore active investors were wasting their time trying to predict the news. You might as well buy a passive investment (especially because the fees charged on passive funds are lower than for active funds).
Real world	But we know the real world doesn’t work that way. Investors aren’t rational. They regularly get overly excited and overly depressed about investments. They don’t all interpret news in the same way and it is possible to second guess what will happen to demand for products and services. Active investing works BUT not every practitioner is good at it.
Short-term vs. long-term	Sifting the good managers from the bad managers is more art than science however. Performance numbers are one, fairly good, indicator. Short-term performance numbers are not much use for this however. Good short-term performance could be the result of one lucky investment. To form an opinion you need longer-term data.
NAV not share price	If you are trying to work out how well a manager is doing, it is important that you look at NAV not share price performance. The share price can shift around

quite a bit as the discount / premium changes. The NAV performance is a measure of the performance of the underlying portfolio.

- Check the manager hasn't changed** It is easy to look at the track record of a fund and get excited about it only to discover that the person or team who generated the performance isn't around any more. We advise you to check that the manager hasn't changed.
- Think about the cycle** It is rare to find a manager that can outperform in all market environments. The market can go through phases where it favours growth companies or defensive companies or inflation-protected securities for example. This can flatter some managers and hurt others depending on their investment style.
- Think about gearing** Investment companies can gear their returns by borrowing money or by altering their structure through the use of things like Zero Dividend Preference Shares. This can flatter performance in upward markets and vice versa. You need to factor this in.
- And remember it is not fool proof** At the end of the day, although we believe past performance can be an indicator of future performance, managers are fallible just like the rest of us. Past performance should not be the only criteria for choosing a fund.