

# FACTS, FIGURES AND HUMANS

Investment research probably brings to mind piles of literature, covering factors like charges, performance, risk ratings and investment objectives. But there are also some human clues investors might pick up on when working out where to put their money. Sara Wilson takes a look.

**H**ow long has the manager been there? How experienced are they? Do they invest their own money in the fund? These are just some of the potential human factors at play when it comes to researching how a fund might perform. But can they really give you any kind of hint on a fund's future prospects?

As you read on, remember, past performance is not a guide to future performance.

## FACTS AND FIGURES

Turn to An investor's guide to data sources on page 4 for some of the more traditional tools you can use to assess a fund's potential.

## FACTOR 1: Skin in the game



Does the manager invest their own money in their funds? This is known as 'skin in the game', and some investors argue that if a fund is good enough for them to invest in, it should be good enough for the manager(s) to do likewise.

Fundsmith's Terry Smith is an example of a high-profile investment manager who invests substantial amounts in his funds, seeing it as aligning his interests with that of shareholders'. He has said that he "wouldn't trust" a manager without skin in the game<sup>2</sup>.

The most recent 'Skin in the game' report by analysts Canaccord Genuity found that 58 chairs or directors of Investment Trusts have personal holdings worth more than £1m, while 67 managers or management teams invest over £1m in their trusts<sup>3</sup>.

But while it can be reassuring for investors to see managers committing financially to their own funds, there's no clear evidence that it boosts performance. Indeed it could be argued that when their own money is at stake there is a risk of managers not being as objective as they should be, or of allowing emotion to influence their decisions.

## FACTOR 2: Manager moves



Research in 2014 by the Cass Business School and the University of Nicosia did find clear evidence that a change of fund manager can impact



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on performance. For instance, when managers exited funds that had been performing well there was a marked deterioration in returns, while underperforming funds typically improved once the manager departed.

The study, which looked at more than 900 UK manager changes between January 1997 and December 2011, concluded that firms had been "relatively successful in replacing bad managers with better managers, but relatively unsuccessful at finding equivalent replacements for their top performing managers"<sup>4</sup>.

### FACTOR 3: Teamwork



A study of Morningstar data for 4,000 US funds by researchers Sergei Sarkissian and Saurin Patel, revealed that those led by teams typically outperformed those led by individuals. They attributed this phenomenon partly to team members keeping a lid on their colleagues' overconfidence, with the effect of keeping trading activity down.

They suggested too that teams of three were most likely to produce good outcomes, pointing to trade-offs between "the benefits of collective wisdom and increasing coordination costs in large groups"<sup>5</sup>.

There is perhaps a lesson for all investors here – asking others for their opinions can result in constructive challenge and help prevent your emotions and investment blindspots from leading you into poor decisions.

### FACTOR 4: Experience



Evidence here is more mixed than you might expect. Another study by Cass compared the records of managers who had been at the helm

for a decade or more with the wider manager population. While the 10-year performance of the former group looked better, there was little difference in the year-to-year performance. But they did find some indication that longer servers had certain traits relevant to positive performance, like low fees, more concentrated portfolios and a bias towards smaller companies<sup>6</sup>.

### FACTOR 5: Gender



The vast majority of fund managers are male, but there's no real evidence this gives them an edge when it comes to running investment funds.

Research by Morningstar last year<sup>7</sup> made it clear the low number of women in the industry is nothing to do with performance. Its main conclusion was that gender is not a factor in performance. But there was some indication investors might be better off if more women were running funds. A test involving picking funds based solely on the manager's gender found there would be better results with all-female teams in both equity and fixed-income asset classes. ■

1. Morningstar – Can Terry Smith Continue Impressive Performance? 09/04/18

2. Citywire – Terry Smith pours £115m into his top performing fund. 21/09/16

3. Investors Chronicle – Does your investment trust have skin in the game? 03/05/18

4. Cass Business School – What impact does a change of fund manager have on mutual fund performance? 07/14

5. Journal of Financial and Quantitative Analysis – To Group or Not to Group? Evidence from Mutual Fund Databases. 29/04/12

6. Cass Business School – New study finds that a fund manager's experience and performance do not always go hand in hand. 11/10/16

7. Morningstar – Female Fund Manager Performance: What Does Gender Have to Do With It? 08/03/18

**Important information:** This general information is provided to support you in making your own investment decisions. It is not a recommendation to buy or sell. Please be aware that the value of investments can fall as well as rise so you could get back less than you invest. Past performance is not a guide to future performance.

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