Fund Management Style - Which is Better?

A common objective of mutual fund investors, though by no means the only one, is for our portfolios to grow in value over time. This is particularly true of equity funds, where we depend on our fund managers to make astute stock selections that, in aggregate, will give us the best chance of adding to our net worth.

Along the way, we get the benefits of diversification, since most funds will normally contain a large number of securities — most often more than we could accumulate on our own.

We also benefit from the professional detachment of fund managers. They look beyond the events of the day which are too often filled with emotional twists that can derail an individual's thought processes. Hopefully, the professionals view current events more dispassionately and make their investment decisions accordingly.

Different Styles

All fund managers strive to do their best to try and maximize returns. But, they do not manage the assets under their care in the same way, of course. For one thing, they tend to adopt one of several "styles" of selecting securities. Some major styles include value, growth momentum and growth at a reasonable price (GARP). GARP managers often seek the middle ground, between value and growth investing.

Value Investing

Perhaps the oldest (and most time proven) style, value investing relies on the principles set down by renowned investor Benjamin Graham. Managers attempt to establish a "fair market value" for a stock, based on valuation factors such as the financial balance sheet, earnings history and outlook, market position, industry-specific factors and management.

Prices of individual stocks often fluctuate around such a fair market value. Overvaluations may occur during periods of enthusiasm. Similarly, under-valuations may result from excess pessimism about the short-term outlook.

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Growth Investing

Growth managers also seek the same returns for their portfolios and are also rigorous in their analysis. However, they tend to emphasize growth prospects as the key driver of investment returns rather than some of the other factors. Projected earnings is also often a key consideration. While a stock may appear expensive to a value proponent, a growth investor may argue that a high growth rate justifies even higher future prices.

Which is Best?

History shows that different styles may outperform at different times in market cycles. Value investors suggest their discipline is less risky, in that the process builds in a downside cushion. However, value investing is not without risk. Prices of some securities will become depressed because the market has noted some operational problem, and they stay depressed. A key skill is to be able to assess the merits of the whole enterprise and keep the risks in context.

If you wish to discuss the different styles of fund management, please don't hesitate to get in touch. We would also be happy to review the criteria we use in choosing the different funds that have been selected for your particular portfolio.