Platypus Asset Management

Fund Manager Insights

‘True-to-label’: avoiding style drift

Every fund has its own stated investment style. Risk management strategies generally combine a variety of styles during portfolio construction, as it is difficult to forecast the top performing style at any point in time. But what happens when funds drift from their stated investment style? And does it even matter?

What is style drift?

Style drift is the divergence of a fund from its stated investment style or objective.# Style drift generally occurs as a result of intentional portfolio investment decisions, or sometimes a change of the fund’s management.

Why does it happen?

Commitment and ability to manage a fund’s assets according to a stated investment style over time is generally viewed as a desirable investment quality. However, managers chasing short-term performance can be tempted to switch to a strategy that is expected to outperform in the short term.

Style drift can happen unintentionally. For example, style drift across market capitalisation can occur for small cap funds when the market is rising and the fund’s stocks are growing. Funds that employ buy and hold strategies are also likely to experience style drift from market capitalisation.

Less common is the drift across investment styles, such as a growth manager increasing their holdings in value or core stocks rather than remaining invested in growth stocks.

What are the dangers of style drift?

Style drift alters risk exposure. If a manager intentionally modifies their investment style as they chase short-term returns, it can change the overall risk return profile of a client’s portfolio. Instead of having a blend of styles, and therefore a diversified risk, a portfolio can end up with a blend of managers all with consistent styles and risk exposures that perform similarly in similar market conditions. This may result in short-term gains, but can be detrimental to the long-term risk-return profile and performance of the portfolio.

If a manager poorly times their shift in style, a client’s overall portfolio will suffer as it will be over-exposed to the wrong style for the market conditions.

Investors diversify their fund styles for a good reason. Style drift unwinds investor intentions at a portfolio level without their knowledge. Given the impact on the risk exposure of a portfolio, style drift is a key reason to review and potentially re-allocate client portfolios.

“We are one of only a handful of genuinely true-to-label growth managers in the Australian market. Our approach is disciplined and unwavering—regardless of economic conditions. We do and always will stand for growth with a capital G.”

DONALD WILLIAMS
Chief Investment Officer

How to check your fund’s style

The simplest way to check for style drift is to look at the fund’s holdings. Style drift can be indicated by:

- a change in company size
- a significant shift in sector weighting
- a decrease in correlation of a fund’s performance with a stated style index; or
- more sophisticated approaches using numerical measures of style drift to classify a portfolio’s style and history.

The returns based style analysis chart overleaf analyses a selection of growth-orientated products within the Mercer Australian Shares (Long Only) manager universe. The chart demonstrates that over the last five years, many managers that have at some stage been considered growth-orientated have drifted towards a blended style.

“Style Drift.” Investopedia US. Web. 31 March 2016.

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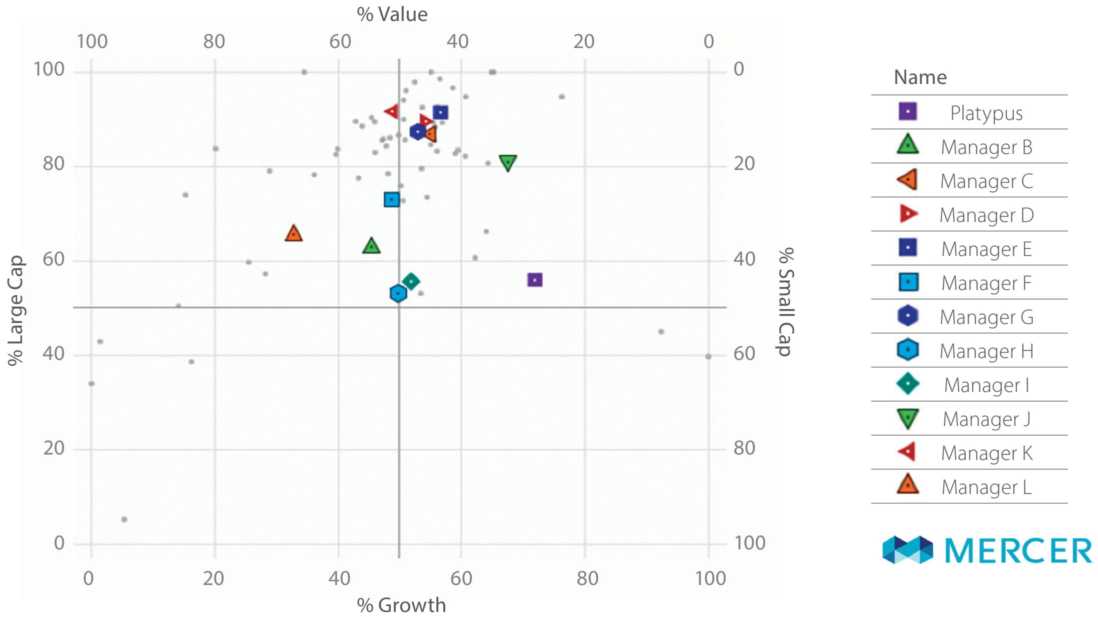
Returns-based style analysis in $A (before fees) over 5 years ending January 2016

Comparison with the Australian (Long Only) universe (monthly calculations)



Source: MercerInsight®.

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Platypus – a 'true-to-label' growth manager

Platypus doesn't pay attention to an index, and makes no apologies for sticking to its growth style of investing—even if growth stocks might be out of favour. The team knows the best investing is done with a long-term perspective.

Consistent with its philosophy, Platypus believe that share price performance over the medium to long term is driven by consistent earnings growth. Companies should exhibit a track record of earnings growth to be considered an investment proposition. The portfolio has a small caps bias, which is a reflection of the durability of growth profiles among smaller companies. The process focuses on absolute returns and, as a result, benchmark weightings are largely ignored.

Investors who are looking for a 'true-to-label' growth manager that has performed consistently have limited options. Platypus provides investors with a portfolio with demonstrably consistent style characteristics and an enviable track record, allowing clients to meet and maintain their overall portfolio objective.

Platypus Australian Equities Fund

Performance as at 31 March 2016	1 mth %	3 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	Since inception[1] % p.a.
Total Return on Wholesale Units	2.05	-5.68	-3.00	10.11	7.92	12.12	6.41
S&P/ASX 300 Accumulation Index	4.78	-2.64	-9.27	5.29	5.45	9.77	4.09
Active Return	-2.73	-3.04	6.27	4.82	2.47	2.35	2.32

Total Returns are calculated after fees and expenses and assume the reinvestment of distributions. Past performance is not a reliable indicator of future performance.
[1]Inception date for performance calculations is 30 April 2006. Retail Units are closed to new investors.