

## The Benefits of a Multi-Manager Investment Solution

When selecting a money manager to invest your assets, it is often tempting to follow the dangerous practice of performance chasing. Many investors simply pick managers based on the previous year's best performers – assuming managers who have delivered strong returns will continue their winning ways. As a result, they tend to sell out of managers at low prices and buy managers at high prices – entrusting their assets to those with the most impressive short-term performance.

In reality, the investment landscape is unpredictable and past performance is an unreliable indicator of future returns. As such, selecting money managers based solely on performance can lead to false expectations as performance will vary over time as investment styles go in and out of favour. Manager performance is cyclical – those who perform well during one market cycle can easily fall behind their peer groups in a subsequent market cycle.

A manager's style continually moves in and out of favour with the market, leading to very distinct cycles of outperformance and underperformance. As a result, investing in just one style and market capitalization can be risky, as the cycles are hard to predict and do not rotate with a particular pattern. One of the best ways to protect against these risks is to implement a multi-manager investment strategy within an investment portfolio. Constructing a multi-manager portfolio involves incorporating money managers with different investment styles and market capitalizations in a complementary manner. This strategy can offer investors increased diversification and performance consistency, with reduced portfolio risk.

Each manager uses unique approaches to decide which stocks to purchase. A manager's investment style will reflect their philosophical views about the key determinants of stock price movements. Managers that share the same ideas about investing are deemed to have a similar style and the characteristics of their portfolio will typically be comparable. The most common styles of investing are Value, Growth and Core. Most other investment styles are variations of these approaches.

*A multi-manager approach represents a key advantage for a managed wealth program such as the Summit and Pinnacle Programs. Single managers do not have access to offsetting management styles to manage portfolio risk. Their portfolios will typically have more risk drag, more unintended bets, and less consistent performance than a multimanager portfolio.*

### The Risks of a Single Manager

Research has shown that no investment style has continually outperformed the market. Historically, when value outperforms the broad market, growth will underperform, and vice-versa. However, the ability to predict when value or growth will be the style that outperforms is difficult at best. As with style, capitalization also shows no predictable pattern. As a result, no single manager is able to consistently outperform year over year. A typical money manager may beat the market 55 percent of the time or less. However, multi-manager combinations of money managers could potentially beat the market more consistently - 60 percent, 65 percent, or even 70 percent of the time.<sup>1</sup>



As such, incorporating complementary money managers with offsetting style and capitalization characteristics in the same portfolio can reduce the style and capitalization risks associated with a single money manager. Take, for example, a U.S. growth manager who specializes in small-cap stocks. Under favourable market conditions, the money manager could generate returns that exceed the overall market. However, if growth stocks or small cap stocks were to go out of favour, as they have historically done, the same money manager could trail the market.

In light of this cycle, over the long term, this manager would have a lower “batting average” relative to the broad market because of inherent style and capitalization risk. No matter how skilled the money manager is, they will always underperform when the investment style or chosen market capitalization is out of favour.

## The Bottom Line

A multi-manager approach represents a key advantage for a managed wealth program such as the Summit and Pinnacle Programs. Single managers do not have access to offsetting management styles to manage portfolio risk. Their portfolios will typically have more risk drag, more unintended bets, and less consistent performance than a multimanager portfolio.

With this in mind, Northern Trust Global Advisors (NTGA), our third party investment management consultant for the Summit and Pinnacle Programs, looks for powerful multi-money manager combinations. No money managers are selected for the Programs in isolation. They are selected to complement and offset the style, capitalization, and investment philosophy of the other money managers that have been selected.

Money managers with opposing styles (or low correlations) will still have common characteristics, such as a solid track record of adding value from stock selection. Combining these managers can neutralize a style bet and can add excess return from stock selection.

NTGA looks for precisely this type of scenario when it conducts searches for money managers. They want money managers who, in combination, improve your market upside capture and reduce your downside-capture relative to what you could achieve through a single money manager alone. For more information on a multi-manager investment strategy or your portfolio, please contact your advisor.

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<sup>1</sup> “The Benefits of Optimization”, Northern Trust Global Advisors, April 2005.

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