



Letter to the Editor re Style Boxes

April 29, 2008

The following letter was received in response to the article [Do Cultural Biases Inhibit Performance?: the Case of Style Boxes](#), by John Minahan, which appeared in the April 22, 2008 issue.

Dear Editor,

We applaud John Minahan for describing what we have heard and seen many times over the years regarding problems with the style grid. These comments raise the question of why the boxes are being used in the first place. As John points out, boxes do a poor job of describing what a manager actually does and often inhibit the pursuit of a well defined and carefully executed investment strategy. We and others have looked into this issue and found that boxes actually lead to inferior investment performance and provide few risk reduction benefits. Indeed, for both improved performance and lower portfolio risk, it is best if the manager ignores boxes entirely and relentlessly pursues a well defined investment strategy.

We believe that the two most important pieces of information regarding an active investment manager are 1) the investment strategy being pursued and 2) how actively and successfully it is being pursued. We refer to this approach as Strategy Based Investing or SBI for short. For the equity version of SBI, we have identified ten strategies for managing equity portfolios: Competitive Position, Economic Conditions, Future Growth, Valuation, Profitability, Market Conditions, Social Considerations, Quantitative, Opportunity, and Risk.

We have surveyed all domestic equity mutual funds (over 9,000 as reported by Lipper), which, ignoring multiple share classes, covers about 2,900 unique funds. We were able to strategy categorize these unique funds. It turns out that Competitive Position is the most popular strategy with Valuation and Future Growth the second and third most popular. We now use strategies for forming peer groups and building portfolios.

The power of looking at managers in this way is that the focus is on what the manager is doing and not on the stocks being held. Many of you probably already do this without realizing it. On the contrary, boxes force you to view the most important aspect of investment management through the opaqueness of the style grid. This is like viewing the world of investing through an out-of-focus pair of binoculars.

Strategy makes it possible to categorize managers correctly which, in turn, allows for the formation of meaningful peer groups. Managers can be evaluated by



strategy to see who is good at that strategy and who isn't. Strategy consistency can be measured, which leads to adult portfolio management rather than playpen management. Adult portfolio management is when managers state their strategy and then are expected to stick to it. Our continuing research reveals that focusing on strategy leads to superior investment portfolios.

Will we witness the dawn of a new world in which managers are no longer constrained by boxes and are free to be strategy consistent in the pursuit of alpha? For investors and advisors, this is a world worth seeking. Thank you John for pushing investors a step closer to this reality.

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[Ed. Note: Strategy Based Investing was the focus of an [article](#) in the September 18, 2007 issue.]

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