



The 5Ws of

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# INVESTMENT

# BENCHMARKS



## WHAT is a benchmark?

A benchmark is a point of reference used to measure something else. For example, if you planted two sunflowers side by side – you could use one as a benchmark to compare them as they grow. Or perhaps you're trying to grow a garden of sunflowers as impressive as your neighbours. Whether or not you deem your efforts good may be relative to the comparison you choose.

In investment management, benchmarks are used to evaluate the performance of a fund or market. Did one fund invested in UK companies (equities) do better than one run by another manager? Or better than the UK market itself?

The latter is often denoted by a country's main index. In the UK, the FTSE 100 (an index of the 100 largest UK companies) is often used.

Indices work as an investment benchmark because they are a sample representative of the market as a whole.



## WHO uses benchmarks?

**Anyone.** Benchmarks are a useful way to measure how your investments have done on a relative basis. However, relative measurements are also like keeping up with the Joneses – if your fund does well but the market does better, you may end up unhappy if you are always comparing your returns to what you *could* have made.



## WHY are benchmarks used?

Benchmarks are used as a tool for reviewing an investment's performance – a point of comparing what you *could* have gained or lost. Did your sunflowers grow taller than your neighbour's or were they worse off? Do you know why?

As your 'neighbour' has grown sunflowers longer, they have historic knowledge of trends that may affect their growth. The same works for index benchmarks. Many have been running for decades. Looking at how they behaved over time may offer some insight on how they might respond to current events.



## WHEN are benchmarks used?

**All the time.** Data is published daily. Benchmarks are in constant use. Although it is important when using a benchmark for comparison that you look at the same time frame – and that your data in the same currency. It is possible to 'cherry pick' a time frame that flatters the performance of an individual fund relative to the benchmark. This may lead to unrealistic expectations.



## WHERE are benchmarks used?

**All over.** A benchmark can be anything but is typically an index. There are *millions* of those used across every investable market and asset class (a broad group of investments with similar financial characteristics) in the world. They can represent a regional market, an asset class specific to that region or a certain size of asset. For instance, there are indices that represent just US small companies, or just global healthcare companies.

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