Why CPI+ is a more meaningful benchmark

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T. Bailey CEO Elliot Farley, Client Portfolio Manager Harry Forman-Hardy and Head of Equities Ben Ridley explain why targeting returns above inflation provides a meaningful long-term objective for T. Bailey's multi-asset funds.

Not all returns are created equal. While some would argue that any investment gain should be considered a success, the T. Bailey Asset Management team looks at things a little bit differently.

The performance of funds, portfolios and investment strategies is typically measured against a benchmark; for example, the S&P 500 or one of the many MSCI or FTSE indexes.

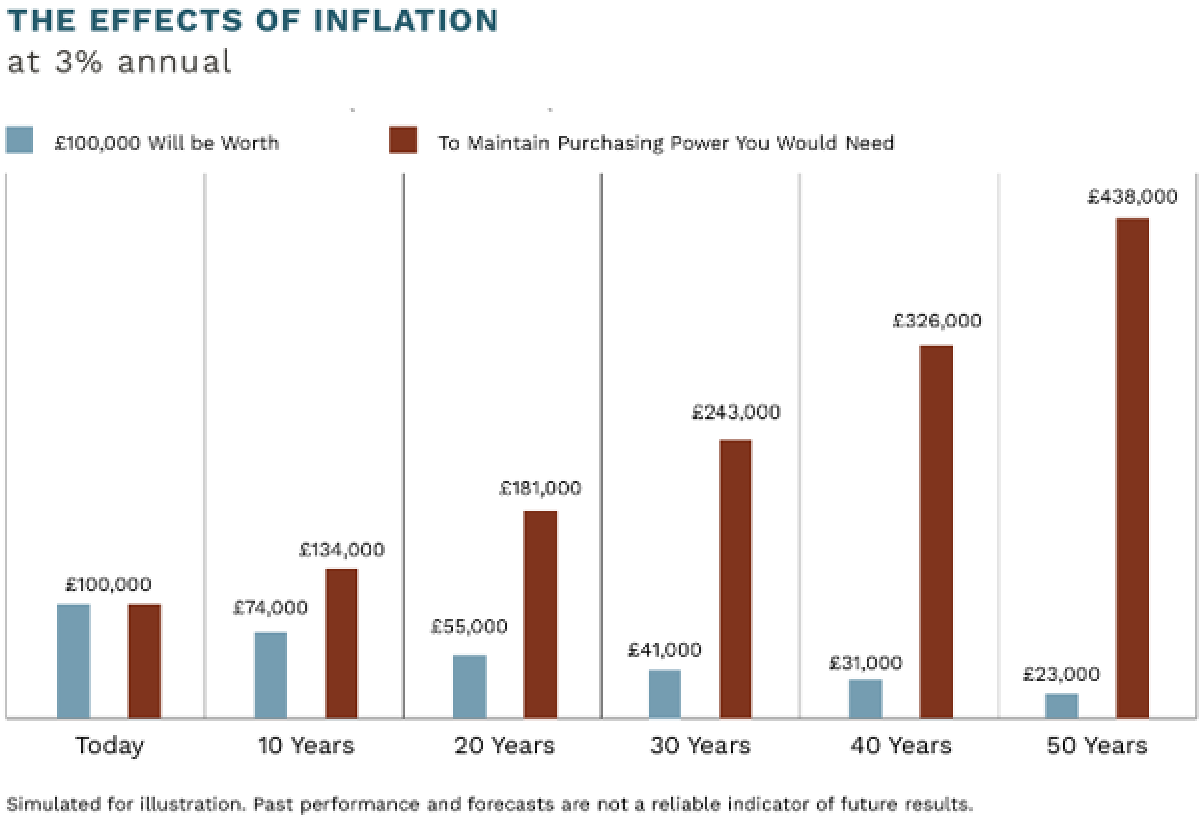
The goal, of course, being to evidence the management team's value-add by delivering better returns than their peers and the market.

But there are two primary challenges with this approach.

Firstly, few end investors truly understand terms such as the IA Mixed Investment 20%-60% Shares sector or the MSCI ACWI, and fund sectors can be very broad, which makes genuine like-for-like comparison difficult.

Secondly, and more importantly, outperforming an index is no guarantee of long-term capital protection or appreciation.

That matters because the T. Bailey multi-asset funds are run on the same long-term approach T. Bailey uses to preserve and grow its founders' own wealth. It's for these reasons that the funds use CPI+ benchmarks, which measure performance against inflation with a target of achieving growth above it.
"You do not want to find, in five or 10 years' time, that what you have saved has less spending power than when you started," says T. Bailey CEO Elliot Farley. "Inflation is a real phenomenon that investors see and feel in their pocket."



Source T. Bailey Asset Management Ltd

Maintaining purchasing power

Benchmarks are useful tools that can help investors compare funds and management styles. But they also have their drawbacks. Adhering to a peer or industry benchmark can encourage short-term thinking, benchmark hugging and a focus on relative rather than absolute outcomes.

Harry Forman-Hardy, Client Portfolio Manager at T. Bailey, says: “If you are benchmarking against an index of peers, a fund could look like it is performing quite well. But the whole index could be below inflation, which means the investor - despite appearances - is actually losing money in real terms.”

No fund manager can ignore inflation, but using a CPI+ benchmark, Forman-Hardy believes, gives “a real focus and clarity of the investment process and allocation decisions and brings everyone closer to the real value of the money invested”.

“There is also an ambition behind CPI+,” he says. “The ‘plus’ element tells the investor that, not only is the manager looking to protect the value of their money in real terms, they are also aiming for meaningful growth on top.”

Realistic but ambitious objectives

Two T. Bailey funds have CPI+ benchmarks:

- Multi-Asset Dynamic Fund - CPI+3%
- Multi-Asset Growth Fund - CPI+4% (given its higher allocation to equities)

Farley notes that some prospectuses can be vague when it comes to outlining the goals of a fund, with statements such as ‘to generate a return’ or ‘to provide income and capital growth’ not uncommon.

“At T. Bailey, we have always set ourselves a challenging hurdle, and inflation itself is a challenge to beat at times,” he says. “But investors need fair compensation for the risks they are taking.”

Farley adds: “We’re not trying to beat inflation every single year, that would be very difficult for anyone to do. We certainly can’t guarantee beating it. Our objective is CPI+ 3% or 4% over rolling five-year periods.

“Inflation drives so much of what is happening in the investment landscape, including what central banks are doing in terms of interest rates, which affects the cost of capital for businesses and what they are able to achieve.

“For us, it is part of the framework for how we build portfolios and consider how asset classes and businesses will perform in different inflation scenarios.”

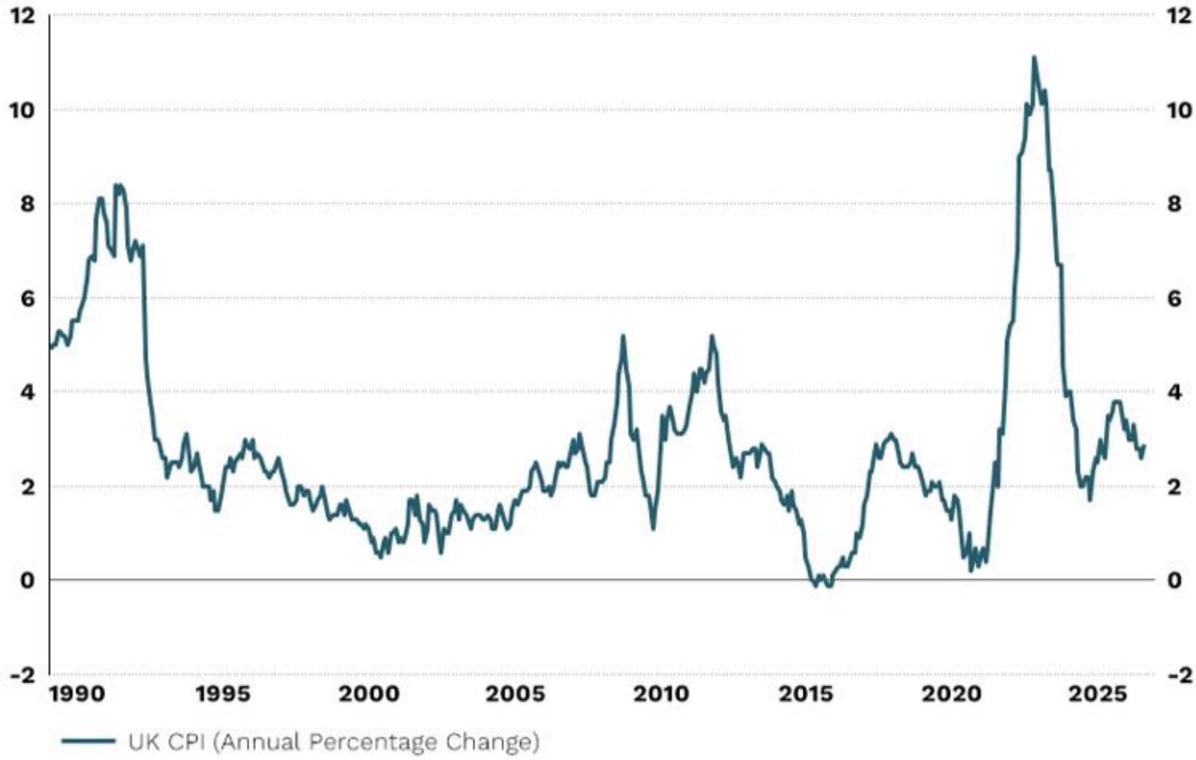
Navigating peaks and troughs

The T. Bailey Multi-Asset Growth Fund has been anchored to a CPI+4% p.a. benchmark since it was launched in 2022, while the T. Bailey Multi-Asset Dynamic Fund used CPI as an internal reference point for real returns since Farley took over running the strategy in 2010 before formally adopting CPI+3% p.a. as its benchmark in 2015.

Since then, it’s fair to say inflation has experienced some highs and lows.

Despite the Bank of England’s efforts to keep inflation at a healthy and manageable 2%, it dipped into negative territory in April 2015 - the first time since official records began in 1996, and, based on comparable historic estimates, the first time since 1960[1]. Just seven years later, the pandemic pushed inflation to a 41-year high of 11.1% in October 2022.

UK CPI: Annual Percentage Change



Source LSEG Workspace

[1] https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/2015-05-19.

Farley says: “Managing the fund through the 2010s was more straightforward in one respect given inflation was lower and less volatile. The trade-off was that returns on cash were low, and income generally was low too, so other areas of the portfolio had to work harder.

“2022 and 2023 were a genuinely challenging period for performance. Inflation rose faster, and to a higher level, than we or most of the market had expected. It's a period we've taken lessons from, and it sharpened our focus on keeping a close eye on volatility and finding ways to access opportunities through different asset classes, which is where the multi-asset approach proved its value.”

Compounding gains, not chasing performance

Before joining T. Bailey in 2024, Head of Equities Ben Ridley always had a traditional benchmark and peer group against which to compare the performance of the funds he managed.

“But coming here, where the multi-asset class funds have CPI+, to me, it really is what advisers and investors want. It hones us, as the investment team, to really think in terms of absolute return.

“With that CPI+ benchmark, the focus is on seeking to preserve capital in real terms over the long term. It’s about a continuous compounding effect rather than chasing performance. We are not here to make our clients a fortune; they are trusting us to grow their assets in line with and above inflation so the next generation and beyond retain purchasing power.”

T.Bailey

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