Clear & Simple Explanations of Key Performance Indicators

Rate of Return (ROR)

Your Investment's Growth in One Simple Number!

Imagine measuring how high your investment climbs over a period — that's ROR for you. It tells you the percentage your investment has grown or shrunk, giving a straightforward picture of its success. It's a quick snapshot of your investment's performance, guiding you on whether you're on the right track toward your financial goals.

Determining whether ROR is favorable typically requires comparison. The first goal is to ensure the number is positive, meaning you've made a return. This needs to be measured over different time periods. To dive deeper, compare your returns against a benchmark and/or similar funds.

Annualized

The Bigger Picture: Your Average Yearly Gains Unveiled!

An annualized rate of return is a measure of how much an investment has changed on average each year during a specific period. It smooths out returns over time, giving you a clearer sense of how the investment performs on an annual basis, even if the actual returns in individual years are volatile.

For example, a 4-year annualized rate of return shows the average yearly return over four years, even if one year had a particularly high or low return. If an investment grows by a total of 40% over four years, the annualized ROR would indicate an average return of 8.78% per year (not just 10% per year), accounting for compounding effects over time.

Annual

Year Over Year: How Did Your Investment Stack Up?

An annual rate of return is the percentage change in investment value over one year (12 months). It represents how much your investment has grown or declined over a specific one-year period, and it can be calculated for any rolling 12-month period, not just the calendar year.

For example, the annual return for 2023 as of June 2024 would measure the performance of your investment from May 2023 to June 2024. This gives a precise reflection of performance over that time span, regardless of the calendar year.

Standard Deviation

Is Your Investment a Smooth Ride or a Wild Rollercoaster?

Think of this as the thrill factor of your investment ride. It measures how wildly your investment returns swing up and down. A higher standard deviation means more risk, as returns vary widely from the average. It's crucial to understanding your investment journey — is it a smooth ride or full of twists?

Standard deviation is a relative measurement. What kind of ride are you comfortable with? If you're okay with volatility, you can often earn a higher return. However, if you need stability to sleep at night, that same standard deviation would be unacceptable.

When presented in comparison with the returns earned for a period, it helps you evaluate whether you're being appropriately compensated for the volatility experienced.

Sharpe Ratio

Are You Getting Paid for the Risks You're Taking?

This ratio tells you the result you're getting for taking on extra risk, beyond what you'd earn in a totally safe investment. A higher Sharpe ratio means you're being rewarded more for each unit of risk. It's like deciding if premium ice cream is worth the extra cost compared to the store brand, considering the taste (return) and the risk (volatility).

For example, Investment A has a Sharpe ratio of 0.5, indicating minimal reward for the risk. Investment B with a ratio of 1.5 suggests you're well-compensated for the risk taken.

Information Ratio

Skill or Luck? How to Tell If You're Really Beating the Market!

This measures how your investment performs against a benchmark, adjusting for the ups and downs of that performance. It's about understanding if beating the market or your chosen benchmark is due to smart decisions or just market fluctuations. A high information ratio indicates that your investment's outperformance is consistent and reliable — akin to consistently beating your friend at chess, showing skill, not just luck.

For example, an information ratio of 0.5 suggests your investment is only slightly outperforming the benchmark, similar to guessing the right answers on a quiz. A ratio of 2.0 shows you're making informed, strategic decisions that lead to significant outperformance, akin to acing an exam through diligent study.

Up Capture

Ride the Market Wave: How Well Are You Seizing Opportunities?

Think of up capture as your investment's ability to ride the waves when the market tide rises. It measures how well your investment performs compared to the market when the market is doing well. If the market goes up by 10% and your investment goes up by 15%, your up capture will be 150. You're not just riding the wave; you're surfing it like a pro, capturing more of the upside than the average. A higher up capture ratio means your investment is doing a great job at seizing opportunities when times are good.

Down Capture

Weathering the Storm: Is Your Investment Shielded from Losses?

On the flip side, down capture is about how your investment fares when the market takes a dive. If you think of a market downturn as a storm, down capture tells you how well your investment can find shelter. It measures your investment's performance relative to the market in these downturns. If the market drops by 10% but your investment only drops by 5%, your down capture will be 50%. Your investment shows resilience, staying drier in the storm. A lower down capture ratio indicates your investment is better at minimizing losses when the market is struggling.