

# Driehaus Emerging Markets Small Cap Growth Fund Commentary

As the calendar turns to 2019, winter is in full swing in Chicago, complete with snow, freezing temperatures, and flight delays out of O'Hare. And true to recent form, our hometown Bulls are already virtually out of postseason contention, thirteen games back from the 8th playoff spot in the NBA's Eastern Conference, while the Bears' Super Bowl hopes were dashed in the first round of the NFL playoffs.

Amid this lull, some friends and I recently turned our sports discussion to a different topic, as one pondered who history will consider the most transformative NBA player. Instinctively, many would point to the likes of Michael Jordan or LeBron James, the two most dominant players of this generation. Historically, a strong argument could also be made for Oscar Robertson, Wilt Chamberlain, and Bill Russell. Shaquille O'Neal's size and strength proved dominant during his prime, resulting in three consecutive NBA titles for the Lakers, and Shaq was named MVP in all three.

However, I was intrigued by the compelling case my friend made for contemporary talents James Harden and Steph Curry. In a string of three recent games, Harden scored 163 points, a total eclipsed only by Michael Jordan and Kobe Bryant, and astonishingly every single one of the points was unassisted. Setting aside for a moment the feat of scoring an average of over fifty points in three consecutive games, the fact that Harden created his own shot so freely has major implications for his team and the game as a whole.

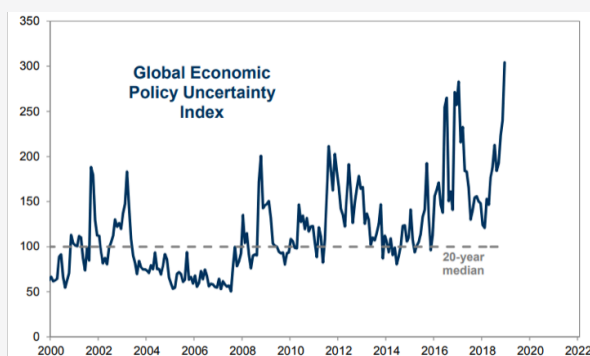
Curry has debatably transformed the game even more than Harden. As a two-time league MVP and three-time champion, Curry's young career has flourished. A sharpshooter from three point range, Curry set the NBA record for most three-pointers made in a season with 272 in the 2012-2013 season. The next year, he broke his own record, making 286. The year after that, he broke it again, making 402! Already, he ranks third in NBA history for all-time made three-pointers.

All of this is great, but what makes Curry truly transformative is his ability to extend the opponent's defense, as evidenced by his incredible knack for shooting extremely long distance three-pointers. The arc of the NBA's three-point line is 23 feet 9 inches from the center of the basket. Curry routinely shoots from 30 to 35 feet, making an incredible 54% of his shots from this distance. In comparison, the average NBA player shoots 35% from three-point range and only 22% from 30 to 35 feet.

While opposing NBA coaches at least found a way to neutralize Shaquille O'Neal (the "Hack a Shaq" strategy was kryptonite to Shaq's Superman interior skills, as he shot an abysmal 53% from the free throw line), Curry looks unstoppable on most nights, particularly when his fellow "Splash Brother" Klay Thompson is also on the floor, a prolific three-point shooter in his own right.

The world political scene is undergoing a similar moment of transformation as the NBA, as policy uncertainty has exploded behind the simultaneous upheaval associated with Brexit, the Gilet Jaunes movement in France, the rise of so-called "strongman" leaders in various countries, and a spiraling geopolitical situation in Venezuela. (Exhibit 1)

**Exhibit 1:**  
**Global Economic Policy Uncertainty Index**



Source: Economic Policy Uncertainty, Goldman Sachs Global Investment Research

Against this backdrop, I was intrigued to hear a quote from an excellent interview of legendary investor Felix Zulauf from November 2017, in which Zulauf predicted that the current populist movement would lead to a 2020 US presidential candidate with a platform to the left of 2016 contender Bernie Sanders. This claim left the interviewer incredulous, and in a prescient moment, Zulauf conceded that we may not even know who this candidate is at the time.

In fact, 29-year-old Alexandria Ocasio-Cortez, known by her initials AOC, was preparing to burst onto the scene with a stunning upset of 10-term incumbent representative Joe Crowley in New York's 14th district. Crowley had been unchallenged by his own party since 2004 and outspent AOC 18-to-1, but lost the primary by a decisive 15 percentage points. AOC then easily defeated Republican nominee Anthony Pappas in the general election to become the youngest woman ever to serve in the US Congress.

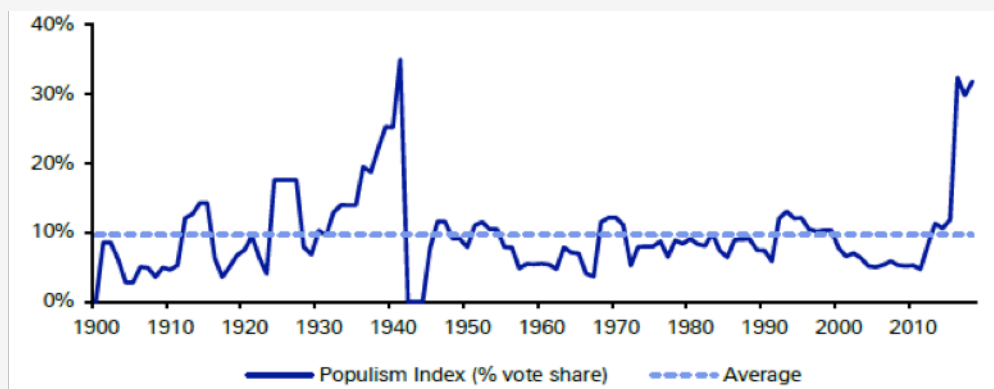
As Democrats took control of the House of Representatives, AOC garnered increasing attention, in large part due to outspoken comments regarding economic and social change. Most notably, on 60 Minutes, she articulated a vision for a "Green New Deal" to be paid for by substantially higher marginal tax rates, noting that "once you get to the tippy tops, on your ten millionth dollar, sometimes you see tax rates as high as 60 or 70 percent."

While Ocasio-Cortez does not meet the constitutional age requirement to run for president, a recent Axios poll found that 74% of Democrats would be interested in voting for her, if she were hypothetically to run. Her 70% "favorable" rating among Democrats was higher than that of Senate Minority Leader Chuck Schumer and slightly lagged House Majority Leader Nancy Pelosi's 75%, suggesting AOC will have significant means to influence the 2020 Democratic platform, despite not being able to run for president.

To be clear, we are not here to opine on politics or predict the outcome of the 2020 US election, but rather to consider the investment implications from these bigger picture trends.

Sticking with the basketball analogy, it is tempting to conclude that AOC, with her 3.5 million social media followers, has changed the game, even as she has barely stepped foot on the court. However, with the shifts toward populism around the world over the past few years, it looks apparent that with or without AOC, this trend was bound to unfold, as Felix Zulauf noted. (Exhibit 2)

**Exhibit 2:  
Populism Index**

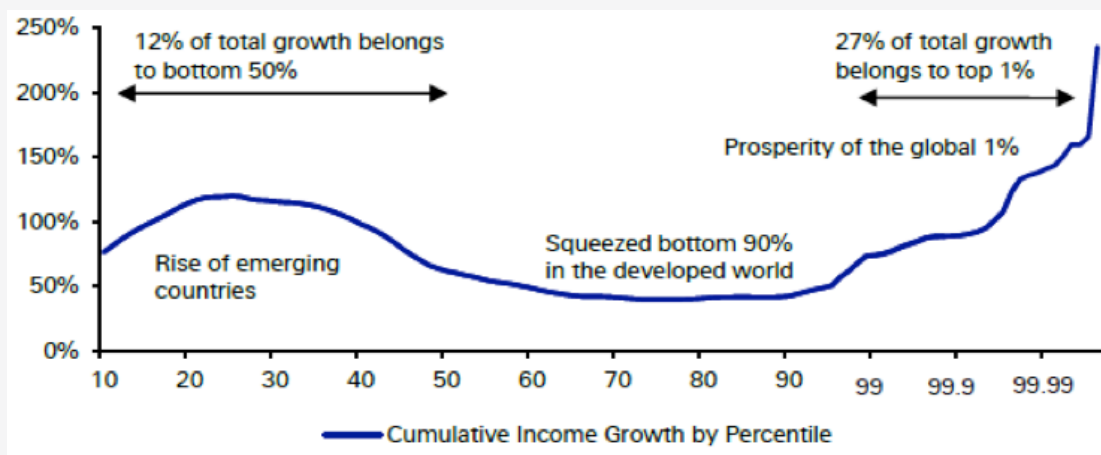


Source: Deutsche Bank

At a time when 26 billionaires own as many assets as the poorest 3.8 billion people in the world, according to a recent study, the political discourse appears set in motion. (Exhibit 3) Weeks after AOC's 60 Minutes comments, 2020 presidential candidate Elizabeth Warren proposed a 2% tax on Americans whose net worth exceeds \$50 million, with an additional 1% tax on billionaires.

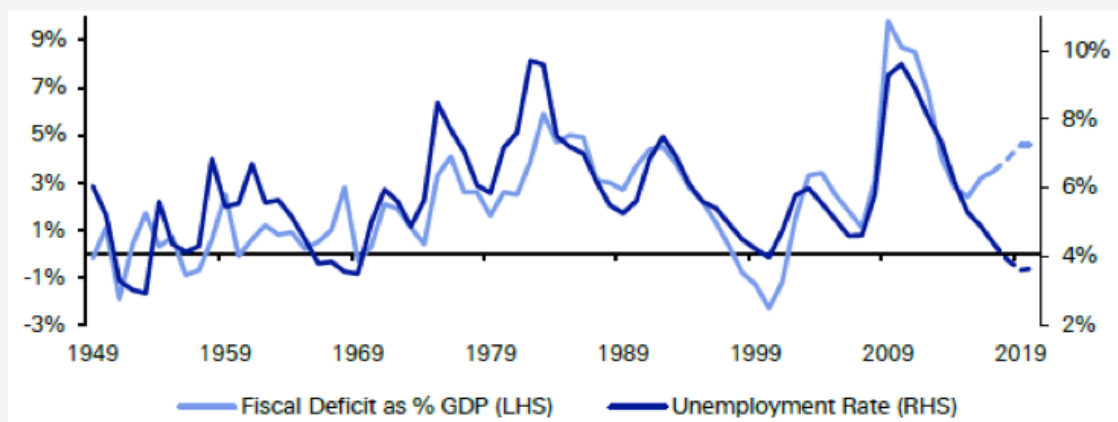
While extreme increases in income tax rates or wealth taxes may be challenging to implement, from both a political and an economic standpoint, increases in fiscal spending look to be further entrenched. This comes at a time when the US fiscal deficit is already widening, the Federal Reserve has been shrinking its balance sheet, and China's once enormous current account surplus could potentially move into deficit. (Exhibit 4)

**Exhibit 3:**  
**Cumulative real income growth by percentile of global income distribution (1980-2016)**



Source: Deutsche Bank

**Exhibit 4:**  
**US fiscal deficit vs. unemployment rate**



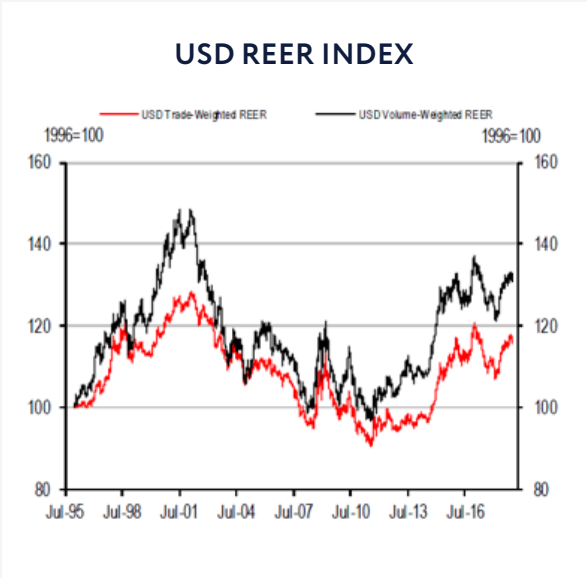
Source: Deutsche Bank

It is striking that against this backdrop, the valuation of the US dollar is near the upper end of its historical range on a real effective basis. At the same time, many emerging market currencies are between 10-25% undervalued on the same measure. (Exhibits 5 and 6)

Amid rising US corporate and government debt levels, we see an increasingly positive case for EM currencies, particularly when considering the valuation starting point depicted above. We expect the improving growth differentials between EM and developed economies, along with the cheap valuations and carry, to catalyze renewed capital inflows to EM. Below, we elaborate on where we are finding these improving growth characteristics and attractive carry within EM.

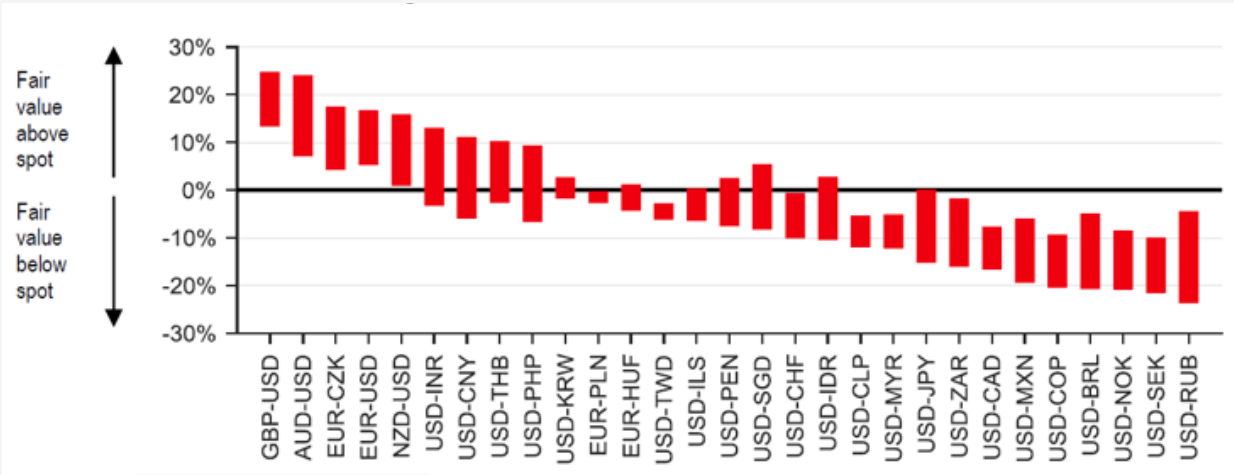
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**Exhibit 5:**  
**US dollar real effective exchange rate**



Source: Bloomberg, HSBC

**Exhibit 6:**  
**Currency valuation ranges**



Source: HSBC, Refinitive Datastream

## Performance Review

The Driehaus Emerging Markets Small Cap Growth Fund, net of fees, returned 7.04% in January, compared to the MSCI Emerging Markets Small Cap Index, net dividend, return of 5.38%<sup>1</sup>. At the sector level, the most significant contributors to returns were communication services

and industrials. Consumer staples and utilities sectors detracted the most value. At the country level, China and Hong Kong contributed most to performance for the month, while South Korea and Thailand were notable detractors from performance.

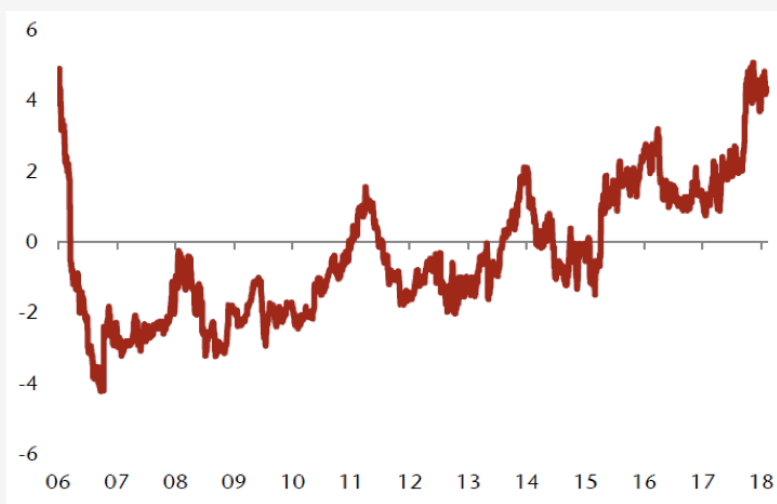
## Positioning and Outlook

The fund remains overweight countries that we believe are best positioned to capture the improving growth differentials described above, along with countries that maintain high carry and scope to benefit from sound policy decisions.

After a period of deteriorating growth, weak consumer confidence, and a challenging regulatory backdrop throughout much of 2018, we see an incrementally

improved backdrop in China as the lagged effect of stimulus filters through to economic activity. Further, as a result of bond index inclusion and substantial inflows from Russia, China has been increasingly successful attracting sources of capital to replace the trade surpluses of the past. Following these strong inflows into Chinese government bonds, the relative attractiveness of mainland equities from a free cash flow perspective is at levels not seen since 2006. (Exhibit 7)

**Exhibit 7:**  
**China free cash flow yield less 10-year bond yield**



Source: FactSet, Jefferies

### <sup>1</sup>Performance Disclosure

The performance data shown represents past performance and does not guarantee future results. Current performance may be lower or higher than the performance data quoted. Principal value and investment returns will fluctuate so that investors' shares, when redeemed, may be worth more or less than their original cost. Performance data represents

the rate that an investor would have earned (or lost), during the given month, on an investment in the Fund (assuming reinvestment of all dividends and distributions). Average annual total return reflects annualized change. **Since Fund performance is subject to change after the month-end, please call (800) 560-6111 or visit [www.driehaus.com](http://www.driehaus.com) for more current performance information.**

Brazil is also positioned to benefit from incrementally better growth in 2019, a development that goes hand in hand with structural reform. After bearing one of the worst economic downturns in the country's history throughout 2014-2015, we see a healthy picture emerging in the banking sector, with improving credit growth and declining non-performing loans. (Exhibit 8 and 9) Approaching critical decisions on pension reform and privatizations, consumer and business confidence could be further bolstered through credible policy actions.

Lastly, while the US dollar stabilized against a broad basket of currencies, EM began to show nascent signs of FX strength in the fourth quarter of 2018, a trend that persisted in January. (Exhibit 10) Factors such as the binary nature of Brexit, the aforementioned social unrest and growth slowdown in Europe, and ongoing stresses in property markets of Australia and Canada, contribute to an uncertain outlook for many G-7 currencies. However, EM arguably maintains a stronger fundamental outlook, driven by the combination of improving growth and historically high carry. (Exhibit 11)

**Exhibit 8:**  
**Loan originations (YoY growth) by Brazilian banks**



Source: BCB and UBS

**Exhibit 9:**  
**Brazil 90-day non-performing loan ratio**



Source: Central Bank and UBS

On a country specific basis, we see dispersion across higher carry currencies in EM, with sound policy supporting the case for countries such as Indonesia, Philippines, and Brazil, while pivotal upcoming elections in India and South Africa could be a precursor to improved growth and reform.

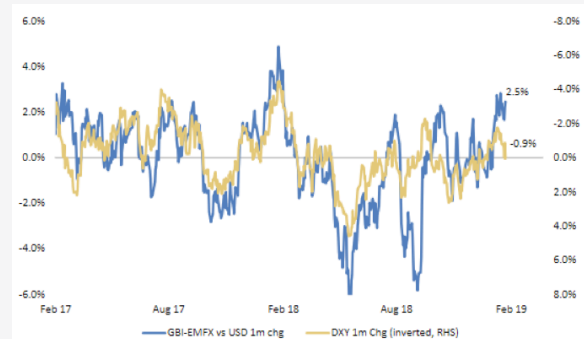
With inflation largely at bay across EM, we see a healthy backdrop for domestic demand, and from a sector perspective, the fund remains overweight the consumer sectors, emphasizing companies that will benefit from expanding market share and rising disposable incomes. Amid the improving macroeconomic backdrop outlined above, we see the EM consumer as particularly well positioned to benefit from these conditions.

Until next month,



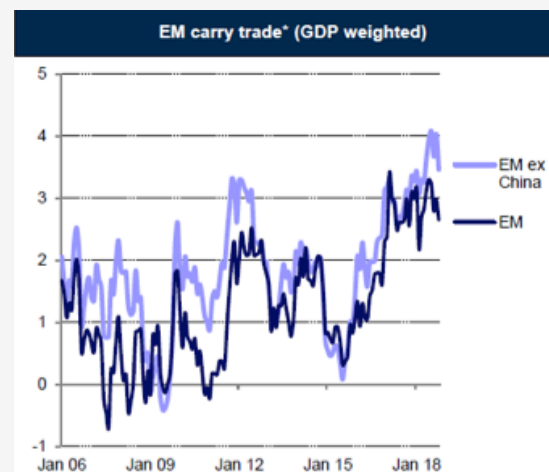
**Chad Cleaver, Lead Portfolio Manager**  
*Driehaus Emerging Markets Small Cap Growth Fund*

**Exhibit 10:**  
**EMFX decoupling from DXY Index**



Source: Central Bank and UBS

**Exhibit 11:**  
**EM maintains historically high carry**



Source: Central Bank and UBS

This material is not intended to be relied upon as a forecast or research. The opinions expressed are those of Driehaus Capital Management LLC ("Driehaus") as of February 14, 2019 and are subject to change at any time due to changes in market or economic conditions. The commentary has not been updated since February 14, 2019 and may not reflect recent market activity. The information and opinions contained in this material are derived from proprietary and non-proprietary sources deemed by Driehaus to be reliable and are not necessarily all inclusive. Driehaus does not guarantee the accuracy or completeness of this information. There is no guarantee that any forecasts made will come to pass. Reliance upon information in this material is at the sole discretion of the reader.

Please consider the investment objectives, risks, fees and expenses of the Fund carefully prior to investing. The prospectus and summary prospectus contain this and other important information about the Fund. To obtain a copy of the prospectus and/or summary prospectus, please call us at (800) 560-6111. Please read the prospectus and summary prospectus carefully before investing.

Driehaus Securities LLC, Distributor



# DRESX Performance Review

## Month-end Performance as of 1/31/19

Fund/Index	MTH	YTD	1 Year	Average Annual Total Return			
				3 Year	5 Year	10 Year	Since Inception <sup>1</sup>
DrieHaus Emerging Markets Small Cap Growth Fund <sup>2</sup>	7.04%	7.04%	-21.73%	-0.03%	-1.77%	9.47%	9.12%
MSCI Emerging Markets Small Cap Index (ND) <sup>3</sup>	5.38%	5.38%	-18.91%	8.43%	2.58%	11.16%	11.59%
MSCI Emerging Markets Small Cap Growth Index (ND) <sup>4</sup>	5.00%	5.00%	-20.22%	4.42%	0.69%	9.85%	10.30%

## Calendar Quarter-end Performance as of 12/31/18

Fund/Index	QTR	YTD	1 Year	Average Annual Total Return			
				3 Year	5 Year	10 Year	Since Inception <sup>1</sup>
DrieHaus Emerging Markets Small Cap Growth Fund <sup>2</sup>	-10.22%	-24.00%	-24.00%	-3.02%	-2.83%	8.08%	8.46%
MSCI Emerging Markets Small Cap Index (ND) <sup>3</sup>	-7.18%	-18.59%	-18.59%	3.68%	0.95%	9.87%	11.11%
MSCI Emerging Markets Small Cap Growth Index (ND) <sup>4</sup>	-8.52%	-19.97%	-19.97%	0.12%	-0.64%	8.70%	9.86%

## Annual Operating Expenses<sup>5</sup>

Gross Expenses	1.47%
Net Expenses	1.45%

The performance data shown above represents past performance and does not guarantee future results. Current performance may be lower or higher than the performance data quoted. Principal value and investment returns will fluctuate so that investors' shares, when redeemed, may be worth more or less than their original cost. The Fund will charge a redemption fee of 2.00% on shares held less than 60 days. Performance data represents the rate that an investor would have earned (or lost) on an investment in the Fund (assuming reinvestment of all dividends and distributions). Average annual total return reflects annualized change, while cumulative total return reflects aggregate change. Contractual fee waivers were in effect from inception to 8/21/2014. Without such fee waivers, performance numbers would have been reduced. Since Fund performance is subject to change after the month-end, please call (800) 560-6111 or visit [www.drieHaus.com](http://www.drieHaus.com) for more current performance information.

<sup>1</sup>Inception Date: 12/1/2008. "Since Inception" is calculated to include performance from the Fund's predecessor limited partnership. <sup>2</sup>The average annual total returns of the DrieHaus Emerging Markets Small Cap Growth Fund include the performance of the Fund's predecessor limited partnership, which is calculated from December 1, 2008 before the Fund commenced operations and succeeded to the assets of its predecessor on August 22, 2011. The predecessor limited partnership was not registered under the Investment Company Act of 1940, as amended ("1940 Act") and thus was not subject to certain investment and operational restrictions that are imposed by the 1940 Act. If the predecessor had been registered under the 1940 Act, its performance may have been adversely affected. The Fund's predecessor performance has been restated to reflect estimated expenses of the Fund. After-tax performance returns are not included for the predecessor limited partnership. The predecessor was not a regulated investment company and therefore did not distribute current or accumulated earnings. <sup>3</sup>The Morgan Stanley Capital International Emerging Markets Small Cap Index (MSCI Emerging Markets Small Cap Index) is a market capitalization-weighted index designed to measure equity market performance of small cap stocks in global emerging markets. Data is in US dollars. The net dividend (ND) index is calculated with net dividend reinvestment. <sup>4</sup>The Morgan Stanley Capital International Emerging Markets Small Cap Growth Index (MSCI Emerging Markets Small Cap Growth Index) is a subset of the MSCI Emerging Markets Small Cap Index and includes only the MSCI Emerging Markets Small Cap Index stocks which are categorized as growth stocks. Data is in US Dollars. The net dividend (ND) index is calculated with net dividend reinvestment. <sup>5</sup>Represents the Annual Fund Operating Expenses as disclosed in the current prospectus dated April 30, 2018 as supplemented on September 17, 2018. It is important to understand that a decline in the Fund's average net assets due to unprecedented market volatility or other factors could cause the Fund's expense ratio for the current fiscal year to be higher than the expense information presented. A shareholder may be required to pay a commission to their financial intermediary. DrieHaus Capital Management LLC, the Fund's investment adviser, has entered into a contractual agreement to waive a portion of its management fee and to reimburse operating expenses to the extent necessary to cap

the DrieHaus Emerging Markets Small Cap Growth Fund's ordinary annual operating expenses (excluding interest, taxes, brokerage commissions, dividends and interest on short sales and other investment-related costs, acquired fund fees and expenses and extraordinary expenses, such as litigation and other expenses not incurred in the ordinary course of the Fund's business), resulting in the current net expense ratio of 1.45% until the earlier of the termination of the investment advisory agreement, by the Board of Trustees or the Fund's shareholders, or October 31, 2021. Pursuant to the agreement, and so long as the investment advisory agreement is in place, for a period not to exceed three years from the date on which the waiver or reimbursement was made, the investment adviser is entitled to reimbursement or previously waived fees and reimbursed expenses to the extent that the Fund's expense ratio remains below the operating expense cap that was in place at the time of the waiver as well as the existing operating expense cap.

The Fund invests in foreign securities, including small and mid cap stocks, which may be subject to greater volatility than other investments. During certain periods, the Fund has benefited from unusually strong market conditions. At times, a significant portion of a Fund's return may be attributable to investments in initial public offerings (IPOs) or concentrations in certain strong performing sectors, such as technology. Returns from IPOs or sector concentrations may not be repeated or consistently achieved in the future. In addition, participating in IPOs and other investments during favorable market conditions may enhance the performance of a Fund with a smaller asset base, and the Fund may not experience similar performance results as its assets grow. **Investments in overseas markets can pose more risks than U.S. investments, and the Fund's share prices are expected to be more volatile than that of a U.S.-only fund.** In addition, the Fund's returns will fluctuate with changes in stock market conditions, currency values, interest rates, foreign government regulations, and economic and political conditions in countries in which the Fund invests. These risks are generally greater when investing in emerging markets. These and other risk considerations are discussed in the Fund's prospectus.

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DrieHaus Securities LLC, Distributor



## SECTOR WEIGHTS (%)

	Fund	Benchmark	Active Weights (%)
Communication Services	3.5	4.2	-0.7
Consumer Discretionary	18.6	14.5	4.1
Consumer Staples	12.9	7.1	5.8
Energy	0.7	1.9	-1.2
Financials	14.9	10.7	4.2
Health Care	3.1	8.6	-5.5
Industrials	15.2	14.5	0.7
Information Technology	9.4	14.1	-4.8
Materials	10.3	11.7	-1.4
Real Estate	4.7	7.8	-3.1
Utilities	0.8	4.9	-4.1
Cash	5.9	0.0	5.9

## COUNTRY WEIGHTS (%)

	Fund	Benchmark		Fund	Benchmark
Argentina	1.8	0.0	Mexico	1.4	3.0
Bangladesh	0.5	0.0	Pakistan	1.0	0.8
Brazil	10.6	7.3	Philippines	2.5	1.0
Cambodia	2.8	0.0	Poland	3.0	1.1
China	17.9	6.7	Russia	1.0	0.8
Cyprus	1.1	0.1	South Africa	7.2	5.6
Egypt	1.0	0.5	South Korea	3.5	18.2
Hong Kong	6.6	4.6	Taiwan	6.8	18.3
India	16.9	14.8	Thailand	1.2	4.0
Indonesia	5.8	2.8	Turkey	1.0	1.4
Kazakhstan	0.6	0.0	Cash	5.9	0.0

TOP 5 HOLDINGS<sup>1</sup> (as of 12/31/18)

Company	Sector	Country	% of Fund
India Grid Trust Units Series - IV	Financials	India	4.1
NagaCorp Ltd.	Consumer Discretionary	Hong Kong	2.7
Li Ning Company Limited	Consumer Discretionary	Hong Kong	2.4
Clicks Group Limited	Consumer Staples	South Africa	2.1
Cyrela Brazil Realty SA Empreendimentos e Participacoes	Consumer Discretionary	Brazil	1.9

## PORTFOLIO CHARACTERISTICS

	Fund	Benchmark	5-year period	Fund	Benchmark
Number of Holdings	84	1,586	Annualized Alpha	-3.49	n/a
Weighted Avg. Market Cap (M)	\$3,250	\$1,180	Sharpe Ratio	-0.20	0.14
Median Market Cap (M)	\$2,502	\$689	Information Ratio	-0.55	n/a
Est. 3-5 Year EPS Growth	20.1%	17.9%	Beta	0.69	1.00
Active Share (3-year avg.) <sup>2</sup>	113.33	n/a	Standard Deviation	11.81	14.24
<b>Market Cap Breakout (%)</b>			Tracking Error	7.86	0.00
< \$5 billion	82.9	99.9	R-squared	0.70	1.00
> \$5 billion	17.1	0.1			

Sources: DrieHaus Capital Management LLC, Factset Research Systems, Inc., eVestment Alliance  
Data as of 1/31/19. Benchmark: MSCI EM Small Cap Index (ND)

<sup>1</sup>Holdings subject to change. <sup>2</sup>Data is calculated monthly.

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**TERMS:** **Active share** represents the share of portfolio holdings that differ from the benchmark index holdings. Average drawdown is the arithmetic average of declines in value during a given period of time. Downside risk is a measure of the average deviations of a negative return series. A large downside risk implies that there have been large swings or volatility in the manager's return series. **Beta** is a measure of a portfolio's volatility. A beta of 1.00 implies perfect historical correlation of movement with the market. A higher beta manager will rise and fall more rapidly than the market, whereas a lower beta manager will rise and fall slower. **Standard deviation** is a measure of the average deviations of a return series from its mean; often used as a measure of portfolio volatility. A large standard deviation implies that there have been large swings or volatility in the manager's return series. **Tracking error** measures the amount of active risk that is being taken by a manager. Tracking error accounts for the deviation away from the benchmark and does not indicate in which direction it occurred, either positive or negative. Source: eVestment Alliance. **Alpha** is the measure of performance on a risk-adjusted basis. Alpha takes the volatility (price risk) of a mutual fund and compares its risk-adjusted performance to a benchmark index. The excess return of the fund relative to the return of the benchmark index is a fund's alpha. **Sharpe ratio** is calculated by finding the portfolio's excess return and then dividing by the portfolio's standard deviation. **Information Ratio (IR)** measures a portfolio manager's ability to generate excess returns relative to a benchmark, but also attempts to identify the consistency of the investor. This ratio will identify if a manager has beaten the benchmark by a lot in a few months or a little every month. The higher the IR the more consistent a manager is and consistency is an ideal trait. **R-squared** is a statistical measure that represents the percentage of a fund or security's movements that can be explained by movements in a benchmark index. For fixed-income securities, the benchmark is the T-bill. For equities, the benchmark is the S&P 500.