TREYNOR RATIOS

vEcoſys

We sometimes hear of an intriguing ratio called Treynor Ratio. What is it?

TREYNOR RATIO

Let me explain…

The Treynor Ratio is also known as the “reward-to-volatility ratio”.

TREYNOR RATIO

It measures the returns a funds gives with respect to its volatility (riskiness).

TREYNOR RATIO

A higher Treynor ratio means that the fund not only performs well but is less risky than the general market.

TREYNOR RATIO

The following example should help you understand the concept of “Treynor Ratio”.

1. **There are two batsmen ‘A’ and ‘B’.**
2. **In a recent match, ‘A’ scored 50 while the average score of his team was 25.**
3. **In another match, ‘B’ scored 100 while the average score of his team was 60.**

Which of them is a better batsman in comparison to their respective team's performance?

TREYNOR RATIO

Applying the "Treynor ratio" principle, lets divide the batsman's score by the team's average score, we get the ratios as follows:-

Ratio for A = 50/25 = 2

Ratio for B = 100/60 =1.67

TREYNOR RATIO

- Although 'B' scores a century, his performance as compared to the overall team's performance was better by 1.67 times whereas 'A' who only scored 50 performed twice as good as the rest of
  his team.

- Hence from this perspective, the performance of the batsman scoring 50 was better than the performance of the batsman scoring a 100 runs.

TREYNOR RATIO

- Thus if two funds A & B have similar returns but A has been more volatile as compared to the market whereas B has been less volatile as compared to the market, the relative performance of B would be better than A, even though otherwise their returns are similar.
- A higher Treynor Ratio indicates that the fund has performed well not only in terms of returns but also in terms of volatility (i.e. it has displayed less riskiness)

TREYNOR RATIO

Hope this lesson has succeeded in further clarifying the concept of 'Treynor Ratio'.

Thinking of Investment

Contact

vEcoSys

DISCLAIMER

The views expressed in this lesson are for information purposes only and do not construe to be any investment, legal or taxation advice. The lesson is a conceptual representation and may not include several nuances that are associated and vital. The purpose of this lesson is to clarify the basics of the concept so that readers at large can relate and thereby take more interest in the product / concept. In a nutshell, Professor Simply Simple lessons should be seen from the perspective of it being a primer on financial concepts. The contents are topical in nature and held true at the time of creation of the lesson. This is not indicative of future market trends, nor is vEcoSys IMF Pvt. Ltd. attempting to predict the same. Reprinting any part of this material will be at your own risk. vEcoSys IMF Pvt. Ltd. will not be liable for the consequences of such action.

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.