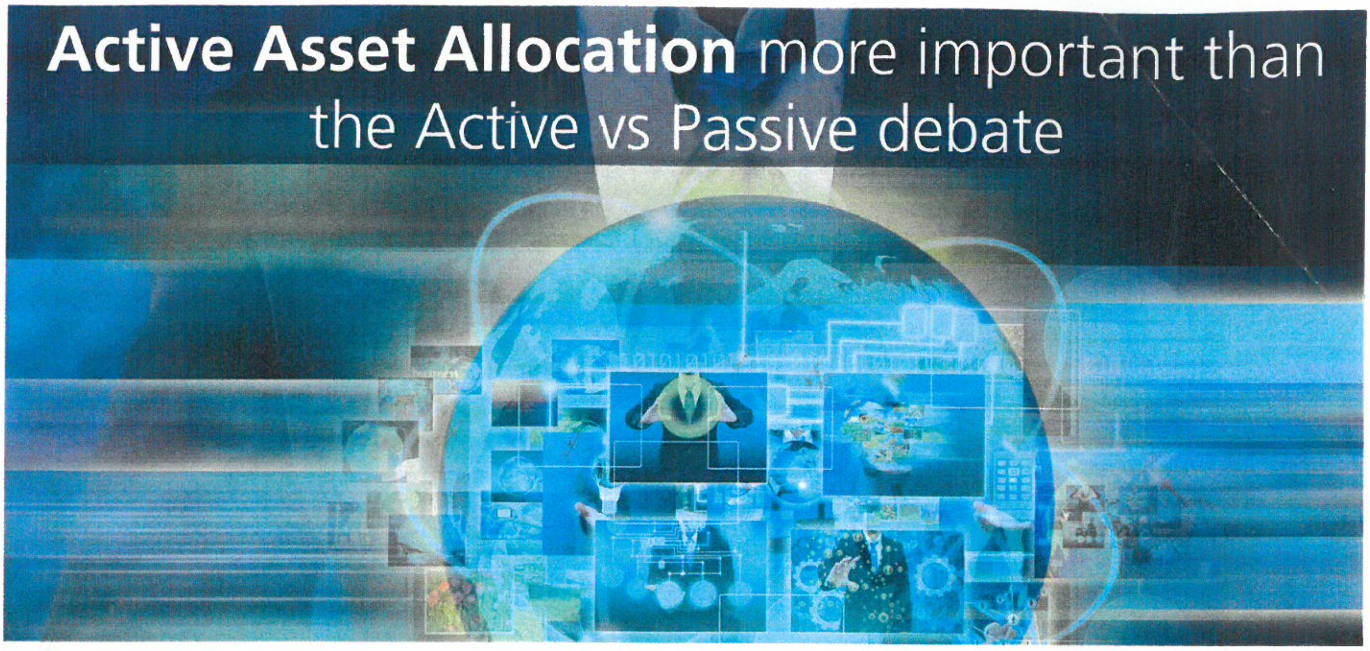
Active Asset Allocation more important than the Active vs Passive debate



Asset allocation decisions should be investors' primary concern as they are the key to determining investment outcomes. There is no single asset allocation that is optimal for an investor over their investing time horizon, whether that investor is an individual saving for a rainy day or a pension scheme investor with a multi-decade investing horizon. Put simply, asset allocation has to be managed; it should never be left to move passively in line with market developments. A combination of good advice, good products and active asset allocation can deliver the best outcomes possible.

The active-passive debate which, in the main, focuses on single asset exposure questions – such as whether I should have an actively or passively managed European equity fund? – tends to side-line the asset allocation question entirely.

But investors should spend more of their time focussing on decisions that have a meaningful impact. Consider the stock market crash in 2007/2008 following the global financial crisis. The S&P 500 Index fell by 57%. Were passive investors excited about the lower costs of their passive equity funds during this fall? Were investors employing active funds thrilled their fund outperformed its benchmark and declined 52% instead of 57%? Actively moving to a more risk-off allocation during periods of severe market stress was the only way to mitigate such declines. The utilisation of active or passive funds was of little consequence if the portfolio allocation was too aggressive. And of course investors who bailed out at the bottom of the crash in March 2009 - as many did – and moved into low risk assets, promising never to touch equities again, missed the near 300% rebound. Being in a passive bond fund with a lower total expense ratio was immaterial!

Furthermore asset allocation is more than determining how much risk to take, it is also about where to allocate that risk. Since the end of the last equity market crash, almost nine years ago, there have been huge divergences between different regional and sector returns from equities. For example, the US market is up c.300% whereas Europe is up c.100%.* The US technology sector is up over 450% (with Apple up 1,325% and Amazon up 1,833%) whilst the energy sector is up around 70%.* Management of these risks and opportunities through active management and successful active asset allocation decisions improves returns for investors.

Whilst the active versus passive fund management decision is important, it is not the main driver of investment returns. The debate is too narrowly focused on the use of active versus passive funds within a single asset portfolio. Picking the best fund, for example a particular global equity fund, is a secondary decision that will count for little if asset allocation decisions are not correctly managed in the first instance.

Zurich has a 30-year unparalleled track-record of outperformance in its range of multi-asset funds, with its newer generation Prisma risk-targeted funds continuing this legacy. This outperformance has been achieved primarily through active asset allocation decisions at key inflection points. Zurich has achieved success in this field by analysing the leading macro-economic themes (GDP growth, PMIs, inflation, interest rates, etc.) as well as employing a disciplined valuation overlay. Zurich's multi-asset funds are currently close to the top of their ranges in equities and the bottom of their duration ranges in government bonds. In Zurich's eyes, passive bonds funds look particularly vulnerable.

Before taking any asset allocation decisions investors need to make the all-important active decision to invest in the first place. Most people invest in order to achieve certain financial goals, with a comfortable retirement being the main one. Investors need to actively plan for retirement. At Zurich we have designed lifestyle investment strategies, such as the Personalised Guide Path (PGP), which help in this regard and allow for flexibility during their investment journey as circumstances change.

Don't be passive about financial planning. The key investment decisions - what to buy, how much, and when - will always require active management and indeed active engagement by the individual investor.

If you'd like to know more about Zurich's active approach to investments, just speak to your local Broker Consultant or visit zurichlife.ie

*Source: Zurich Life, Bloomberg, February 2018

Zurich Life Assurance plc is regulated by the Central Bank of Ireland.

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