

## The systematic decline of active funds

Active funds have been subjected to continuous waves of attack from passive alternatives, and the gist of the argument is that they are in some way inferior to their passive peers. The reasoning is mixed, but the argument's primary drivers are historic underperformance over the past five years, lower fees and fund costs, and high tracking errors vs what investors are expecting.

By [Rupert Hare](#) 17 May 2021



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While these points are valid, they're also often subject to some serious framing by passive funds looking to aggressively capture assets under management (AUM) from other asset managers. They leverage off emotional biases of investors like the anchoring of views on recent performance and a degree of framing bias.

For example, if you tell an investor that a fund is “one of the most expensive in its category”, that sounds rather gloomy on its own. But if you instead tell the investor that “while the fund is one of the most expensive in its category, it has by far the highest performance”, it will frame the fund in a completely different and more positive light. The point is that the most important thing investors can do is to focus on the facts and leverage off them in their judgement.

### Systematic investing

That brings us to the heart of this article, which may at first glance seem like the same topic the industry's been talking about for the past five years – how and why active funds are losing money to passive alternatives. While that may be the case, there's a lesser-known approach that could be a solution for investors and allow them to capture the best of both worlds – known as systematic investing, or process-driven asset-management leveraging off large amounts of data to make investment decisions. The key is to be able to take the best of active investing and combine it with the benefits of passive investing.

Systematic funds require smaller, more specialised teams with a background in both data science and asset management to process large amounts of data – which a traditional manager would require many boots or

the ground for. The translation comes directly into the investor's pocket, with lower fees required to cover fewer analysts.

Lower fees are the surest form of alpha. Looking into the evidence over the last five years for the Association for Savings and Investment South Africa (Asisa) multi-asset high equity category, investors made an additional 0.53% for every 1% saved on fees. So why then is that relationship not one for one? The answer lies in active management lifting that line up at the higher end of the total investment charge (TIC) spectrum through the creation of alpha. In other words, you can indeed get more by paying less, as well as earn more by paying more – both active and passive asset management have their place in a portfolio.

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