Clark Capital Management Group

NavigatorInsights

A Healthy Serving of Active and Passive

What the Investment Industry Can Learn from the Nutrition World

Lately, we've seen a proliferation of articles touting the end of active investing and the beginning of the age of low-cost indexing. I believe that this is exactly the wrong message to send at the wrong time. Long-term investing should be like a well-balanced meal: plenty of protein, vegetables and some healthy carbs too. In our world, it's about healthy allocations of stocks, bonds, and alternatives and a well-balanced mix of investment methodologies, namely active and passive approaches. The overarching goal should be to focus on what really matters: helping the client to achieve his or her personal goals and objectives.

Three Things Investment Professionals Can Learn from the Nutrition World

A Well-Rounded, Personalized Plan Is the Best Bet for Long-Term Success

There are no shortcuts. If someone is looking to lose weight, diet and exercise should be tailored to his or her individual needs in order to improve the likelihood of success. For example, a mainly sedentary, overweight individual should probably not jump right into an extreme exercise plan. Nor should they practice extreme dieting.

Investments are the same way. Without diversification, portfolio risk goes us up and we can be tempted to put all of our assets into a single investment style or the asset class outperforming its peers at a given time. When we search for short cuts, we can easily lose track of the long-term benefits of investing and make bad decisions in the here and now.

It's a Lifestyle, Not a Fad

Fad diets (we've all heard of the grapefruit diet and the cookie diet) leave the body malnourished and can lead to the development of harmful habits.

The same holds true for one's investment allocation. Cutting out one style or type of investment entirely in favor of another can increase risk and derail an investor's long-term plan. A more moderate, diversified approach has a higher likelihood of success. It's all about creating good habits, because bad habits can slowly build up and undermine the chances of achieving one's goals. As Warren Buffet said, "Chains of habit are too light to be felt until they are too heavy to be broken."

My point is that ditching an active approach in favor of a passive approach is shortsighted and vice versa. In our view, ditching an asset class entirely, such as fixed income, and loading up on alternatives may also be shortsighted. We believe healthy mix of both positions the client for a less frenzied experience and reduces the risk of loading up on too much of a good thing.

Knowledge Is Power – Know What You Are Buying and Who You Are Buying It From

The 2008 documentary *Food, Inc.* by filmmaker Robert Kenner shed light on some of the food industry's less savory characteristics — namely corporate farming's loss of integrity, quality and safety in the race to produce more food for less money. He argued that the public didn't really know what they were consuming because they had lost touch with the farmer and the food production process.

In the investment world, it's important to do your research on your manager. Knowing who is managing your assets may help you avoid negative surprises in the future. When researching managers, it may be helpful to ask the following questions: How long have they been in the business? What is the overall firm structure? Has the investment manager had the experience that comes from managing in different market cycles, market regimes and difficulties?

These are all things to consider in addition to the classical risk measures of a manager such as standard deviation, beta and alpha.

Keeping the Focus on What Matters: The Client's Goals and Objectives

The fight between active and passive should not be the focal point of financial planning. Rather, the client should be at the center of every decision.

I would argue that the focus on active vs. passive, or "this-or-that," is a Wall Street rather than a Main Street ideology — which stock to buy, what market to short, how to exploit an opportunity for all it's worth before the markets move into the next big idea.

A client-centered approach doesn't allow for a dichotomy of methodologies or for the distractions that arise from the wholehearted shutting out of either time-tested approach. They complement each other. Case in point, Eugene Fama who advocates passive investing and Robert Shiller, a proponent of active investing, both won Nobel Prizes in the same year.

Outcome-oriented investing supports the theory that good habits lead to long-term success. In the nutrition world, a well-rounded, diversified diet can help increase one's quality of life and extend one's life. In the investment world, a well-rounded, diversified portfolio can help keep clients focused on what matters and increase the likelihood that they will have successful financial outcomes.

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