

The Death of Active Management?

Educated investors are demanding Value Added.

By Mitchell M Maynard, May 2000.

In the last five years indexing has become a chosen method of investment strategy for many do-it-yourself investors. Why are financial advisors not recommending them more often? Money.

Active management has ruled the mutual fund industry for years. It has also had the greatest opportunity to educate the public. The public watches television and reads papers. They are constantly bombarded by advertising telling them that the active management style is the best way to invest. Why has there not been more publicity about indexing? Indexing is cost efficient and the managers don't spend the advertising dollars.

Let's look at the largest active management and passive management mutual fund firms: Fidelity and Vanguard.

Fidelity has built its name around active management. They have developed managed funds for almost every asset class available. They were the original developers of sector funds. They have managers come and go but do they offer superior risk-adjusted funds?

Vanguard has built its name around passive indexing. They have done the same thing that Fidelity has but the thrust is passive indexing. Indexing creates some of the lowest fee expense ratios but do they offer superior risk-adjusted funds?

I ask you how many Fidelity television ads have you seen and compare that to the number of Vanguard ads. If my memory serves me correctly, I have never seen a Vanguard television commercial. John Bogle, Chairman of the Vanguard Group, talk repetitively about saving the shareholder money. There is just no advertising for indexing but at times the largest public fund is an index fund. What is happening?

Active management depends on the extra fees to continue their practice. But what if the active management cannot produce value added? Like dinosaurs they will become extinct. Advisors need to develop a method of money management that can use superior risk-adjusted returns to their clients.