



# Active vs Passive Management

## The Strategic Pursuit of Investment Excellence

August 20, 2024

VP, Co-Chief Investment Officer



Jennifer Hutchins was named Co-Chief Investment Officer in May 2023 and leads the Portfolio Management and Diligence teams. She oversees the planning, execution and success of the Portfolio Management Group and the IMS Select and RMS Select portfolios.

She joined Avantax as an internal support specialist for BMS, a business model that partners CPA firms with experienced financial advisors, from 2007–2008 and returned in 2017 after eight years at H. Beck, Inc., where she held various roles including Senior Product Specialist, Investment Analyst and Vice President of Investments. She started her career in financial planning and wealth management in 2004 as an advisor with A.G Edwards & Sons.

Jennifer received her Bachelor of Arts degree in political science and economics from Christendom College. She has attained the Chartered Financial Analyst® designation, is a member of the CFA Society of Dallas and holds Series 7, 24 and 66 licenses.

- **Purpose:** To help clients as they pursue their goals
- **How:** By selecting the most appropriate investment combinations
- **Question:** Should I use an active fund or ETF or just go passive...



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- **Build Universe of Funds**

- ❖ Active managers with at least one full month of performance in last 10 years
- ❖ Control for survivorship bias
- ❖ ETFs & mutual funds included; index/passive funds excluded
- ❖ Include one passive ETF to represent the index

- **Choose Time Frame**

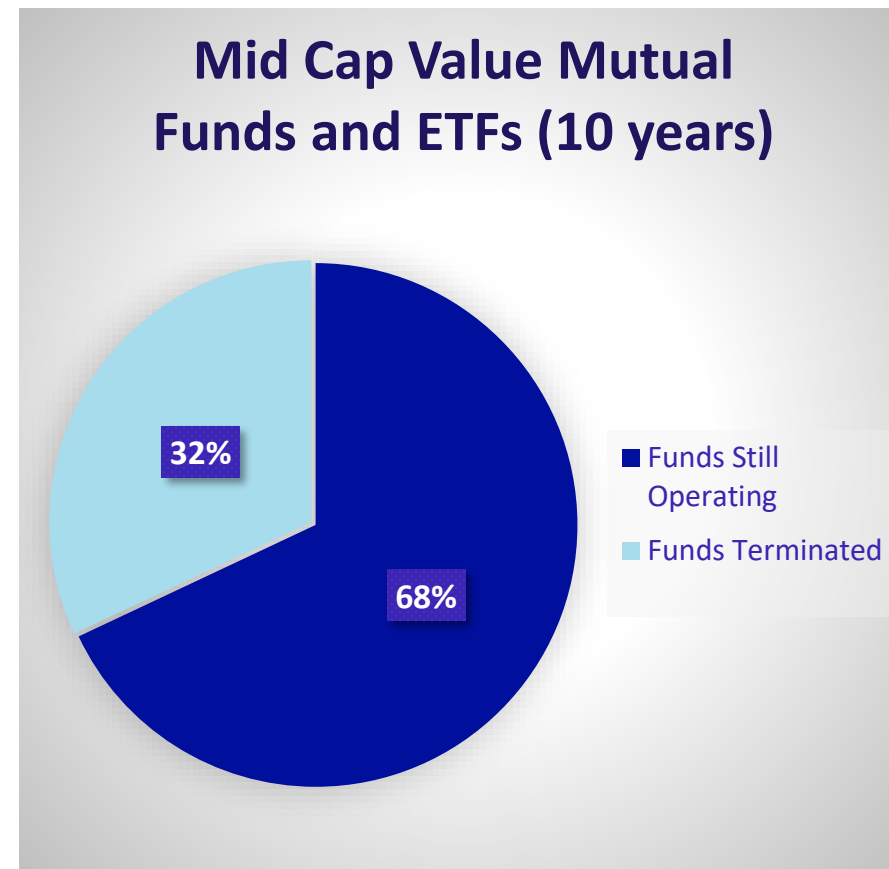
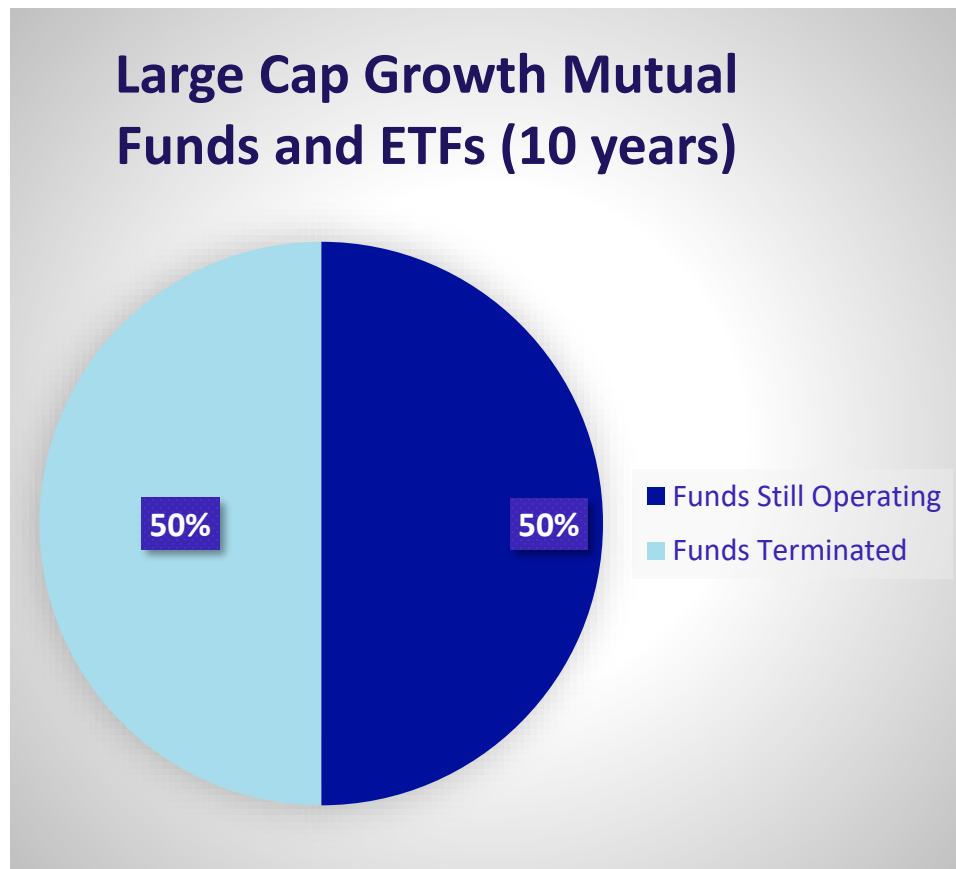
- ❖ non-overlapping 3-year time periods
- ❖ non-overlapping 5-year time periods
- ❖ Rolling time periods
- ❖ Calendar Year Review

- **Evaluate performance of managers vs. index proxy**

- ❖ Identify managers that out(under)performed in period 1, determine what % went on to out(under)perform in period 2, period 3, etc
- ❖ Determine % of managers that consistently outperformed the appropriate benchmark
- ❖ Measure the magnitude of relative out(under)performance for the different groups of managers

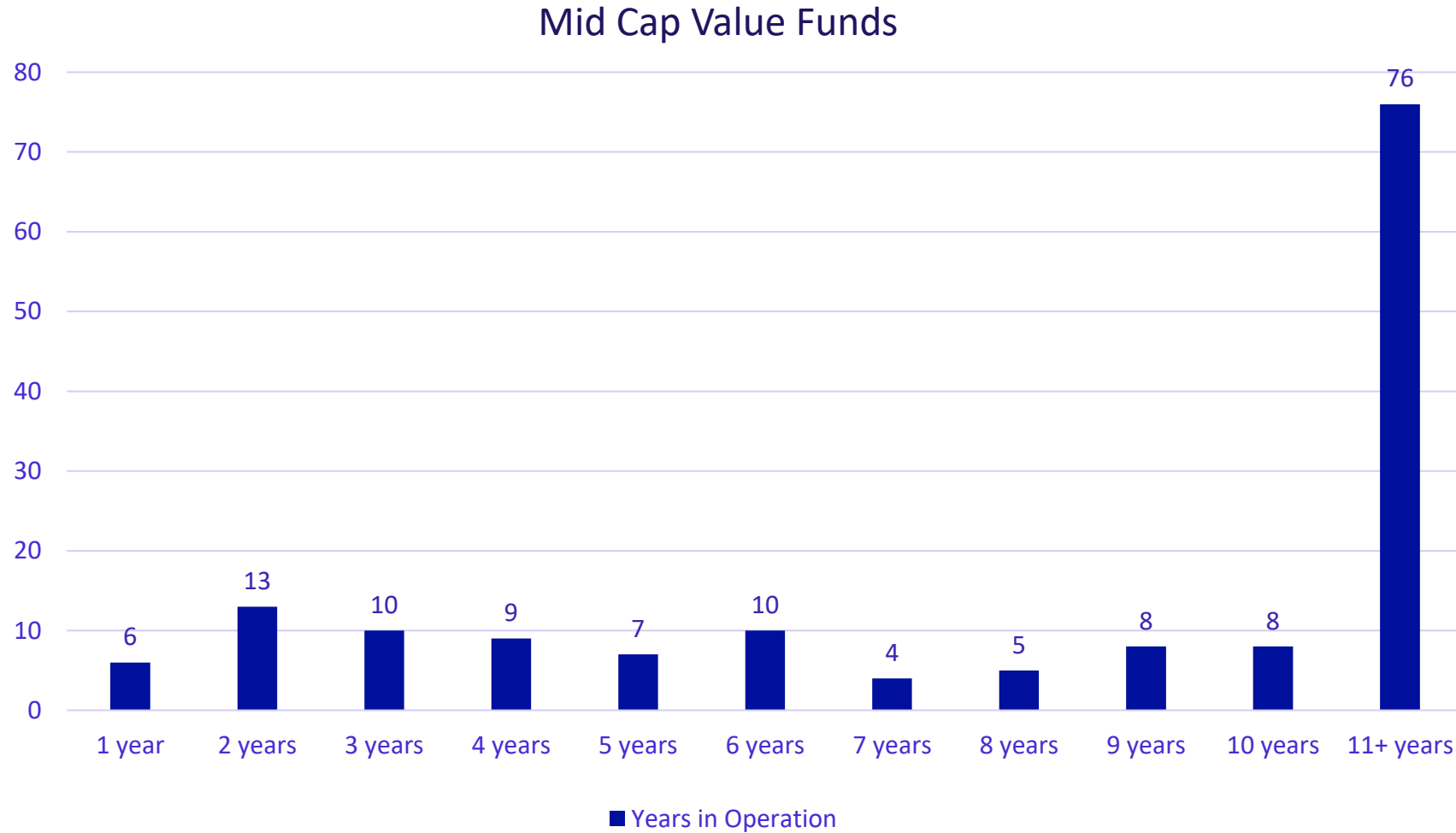
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# ➤ Survivorship Bias



Data Source: Morningstar Direct

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# ► Surviving Fund Returns Versus an Index

## All Survivors (Large Growth) vs. iShares Russell 1000 Growth ETF



3 YEAR PERIODS			5 YEAR PERIODS		
SEPT. 2016 - AUG 2019	SEPT. 2019 - AUG 2022	AVERAGES	SEPT. 2012 - AUG 2017	SEPT. 2017 - AUG 2022	AVERAGES

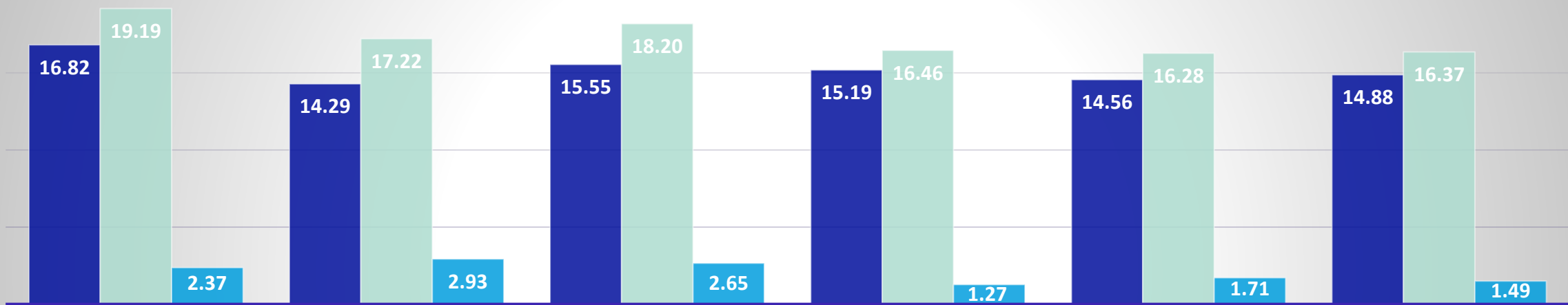
■ Index Return (IWF Annualized)   ■ Average Fund Return (Surviving Funds - Annualized)   ■ Average Over(Under) Performance (Surviving Funds - Annualized)

Data Source: Morningstar Direct

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# ➤ All outperforming funds

## Outperformers vs. iShares Russell 1000 Growth ETF



SEPT. 2016 - AUG 2019

SEPT. 2019 - AUG 2022

AVERAGES

SEPT. 2012 - AUG 2017

SEPT. 2017 - AUG 2022

AVERAGES

3 YEAR PERIODS

5 YEAR PERIODS

■ Index Return (IWF Annualized)

■ Average Fund Return (Outperforming Funds - Annualized)

■ Average Over(Under) Performance (Outperforming Funds - Annualized)

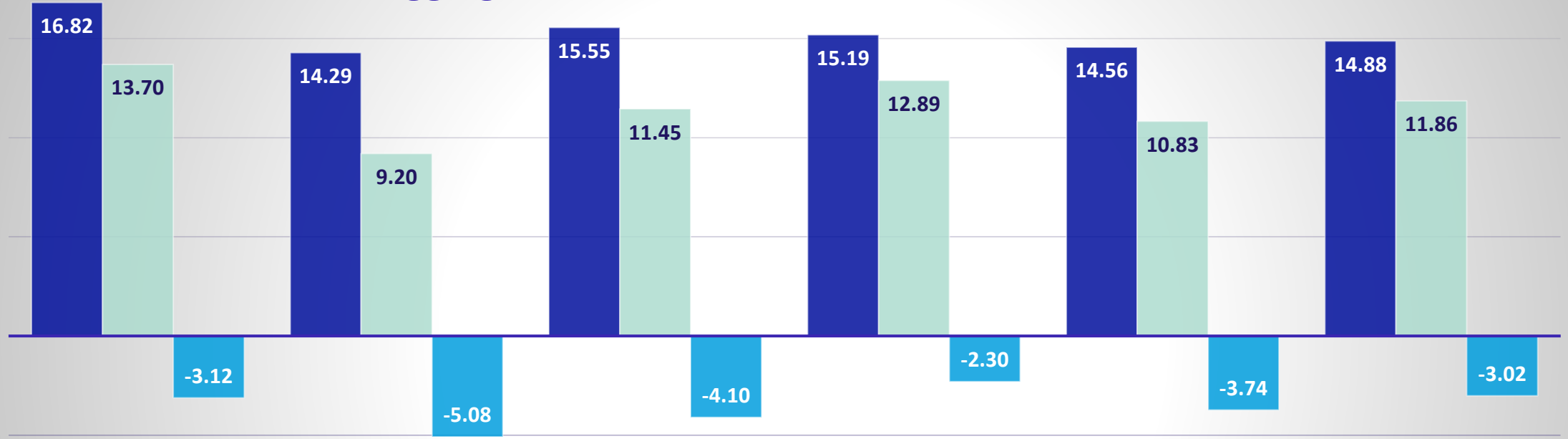
Data Source: Morningstar Direct

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# ➤ All Underperforming Funds

## Lagging Funds vs. iShares Russell 1000 Growth ETF



3 YEAR PERIODS			5 YEAR PERIODS		
SEPT. 2016 - AUG 2019	SEPT. 2019 - AUG 2022	AVERAGES	SEPT. 2012 - AUG 2017	SEPT. 2017 - AUG 2022	AVERAGES
16.82	14.29	15.55	15.19	14.56	14.88
13.70	9.20	11.45	12.89	10.83	11.86
-3.12	-5.08	-4.10	-2.30	-3.74	-3.02

- Index Return (IWF Annualized)
- Average Fund Return (Underperforming Funds - Annualized)
- Average Over(Under) Performance (Underperforming Funds - Annualized)

Data Source: Morningstar Direct

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# Funds Summary

	3 Year Periods			5 Year Periods		
	Sept. 2016 – Aug 2019	Sept. 2019 - Aug 2022	Averages	Sept. 2012 – Aug 2017	Sept. 2017 – Aug 2022	Averages
Index Return	16.82	14.29	15.55	15.19	14.56	14.88
Average Over(Under) Performance (Surviving Funds - Annualized)	-1.35	-4.39	-2.87	-1.34	-3.18	-2.26
Average Over(Under) Performance (Outperforming Funds - Annualized)	2.37	2.93	2.65	1.27	1.71	1.49
Average Over(Under) Performance (Underperforming Funds - Annualized)	-3.12	-5.08	-4.10	-2.30	-3.74	-3.02
	# of Funds	% of Successful Funds	% of Initial Opportuni ty Set	# of Funds	% of Prior Universe	% of Initial Opportunity Set
Eligible Universe	569	--	--	569	--	--
Managers who Survived (full history in both periods)	284	--	90%	260	--	83%
Attrition (Non-Surviving Funds)	32	--	10%	53	--	17%
Survivors who Beat the Index in Prior Period	99	35%	31%	81	31%	26%
Survived + Beat Index in Recent Period	22	8%	7%	21	8%	7%
<b>Survivors who Beat the Index in BOTH Periods</b>	<b>15</b>	<b>15%</b>	<b>5%</b>	<b>10</b>	<b>12%</b>	<b>3%</b>
Chance of Selecting Future Outperformer from Prior Outperformers (Beat Idx in Both Pds X Survival Rate)		14%			10%	
Expected Annualized Out(Under) Performance (Chance of Success X Avg Outperformance)		-3.18			-2.56	
Overall Average Persistence		12%				
Overall Average Expected Outperformance		-2.87				

Data Source: Morningstar Direct

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## ➤ Non-Overlap Periods - Mid Cap Value

Non-overlapping time periods

### **3-year time periods**

January 1, 2015 – December 31, 2017

January 1, 2018 – December 31, 2020

January 1, 2021 – December 31, 2023

### **5 year time periods**

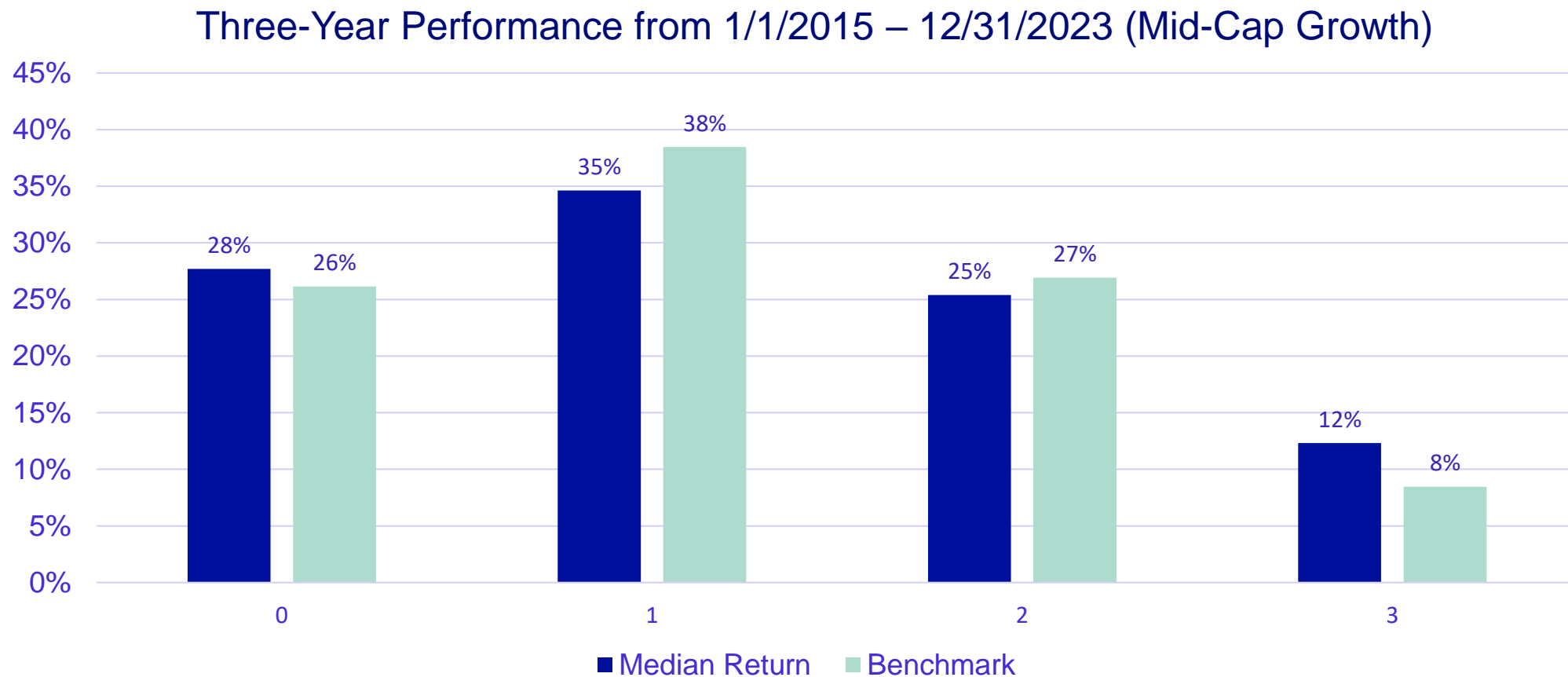
January 1, 2009 – December 31, 2013

January 1, 2014 – December 31, 2018

January 1, 2019 – December 31, 2023

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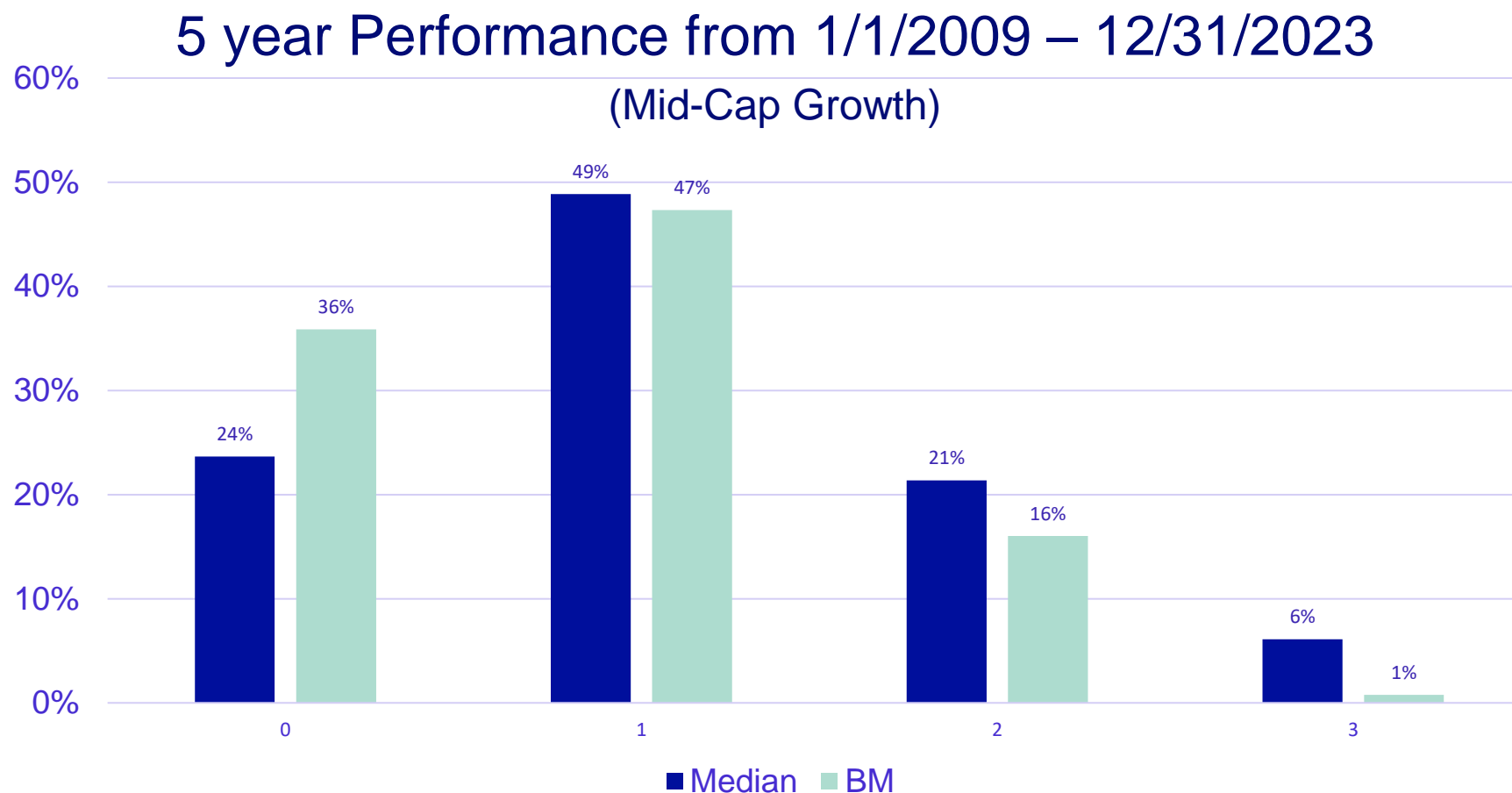
## ► Outperforming Periods (3 years)



Data Source: Morningstar Direct

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## ► Outperforming Periods (5 years)



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## ➤ Rolling Return Periods – Mid Cap Value

Rolling time periods

### **3 year time periods**

First Period - January 1, 1990– December 31, 1992

Final Period - May 1, 2021 – April 30, 2024

377 Time periods

### **5 year time periods**

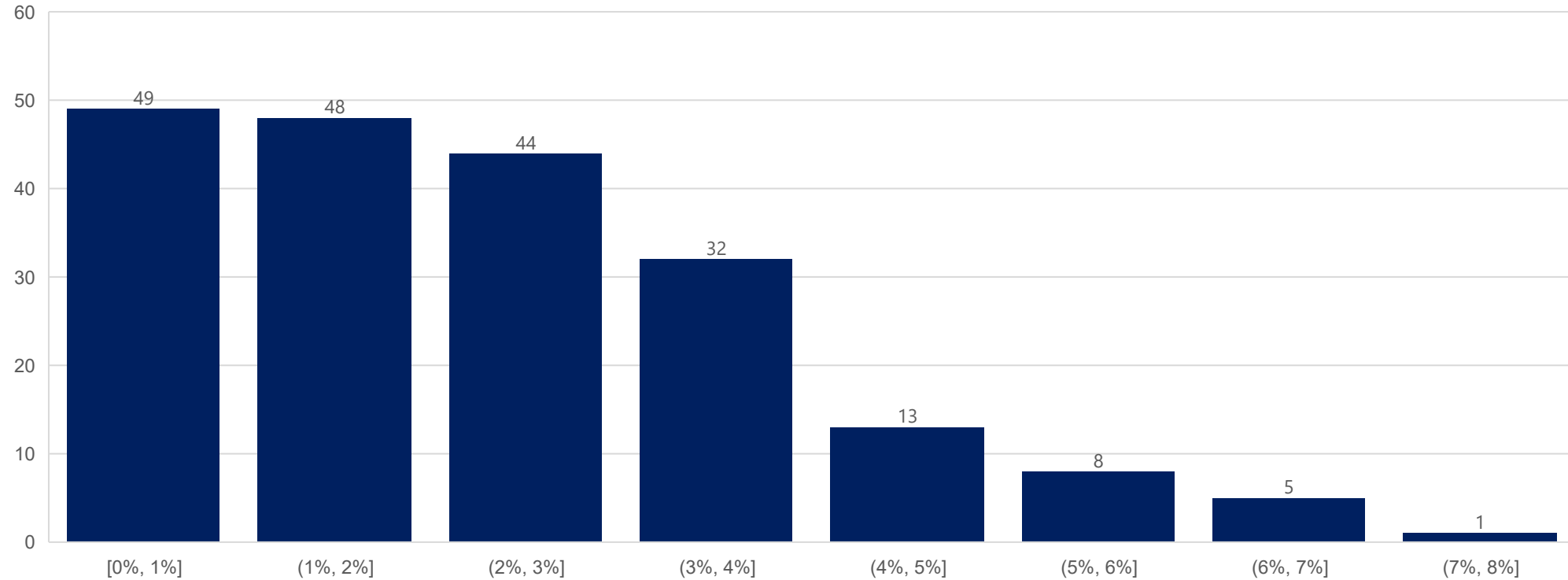
First Period - January 1, 1990– December 31, 1994

Final Period - March 1, 2019 – February 29, 2024

351 Time periods

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## 3 Year Rolling - Average Outperformance (Mid-Cap Growth)



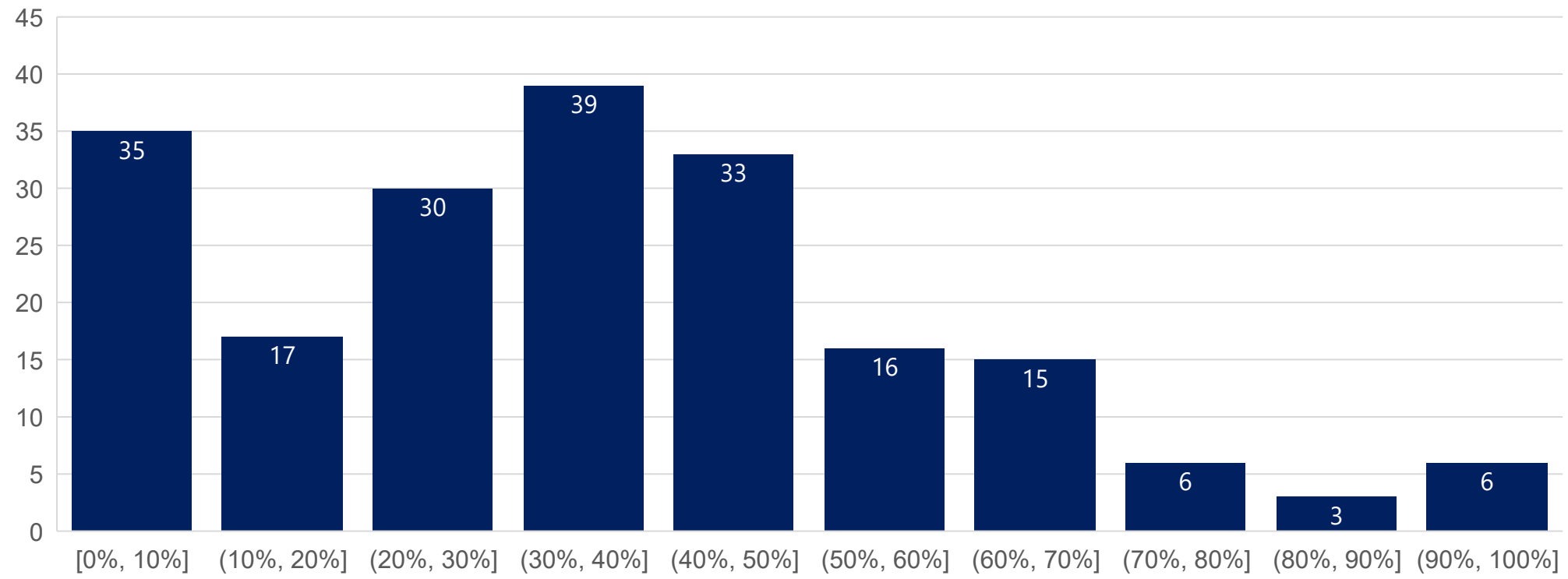
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# ► Results - % Chance of Outperformance

## 3 Year Rolling - % chance of outperformance (Mid-Cap Growth)

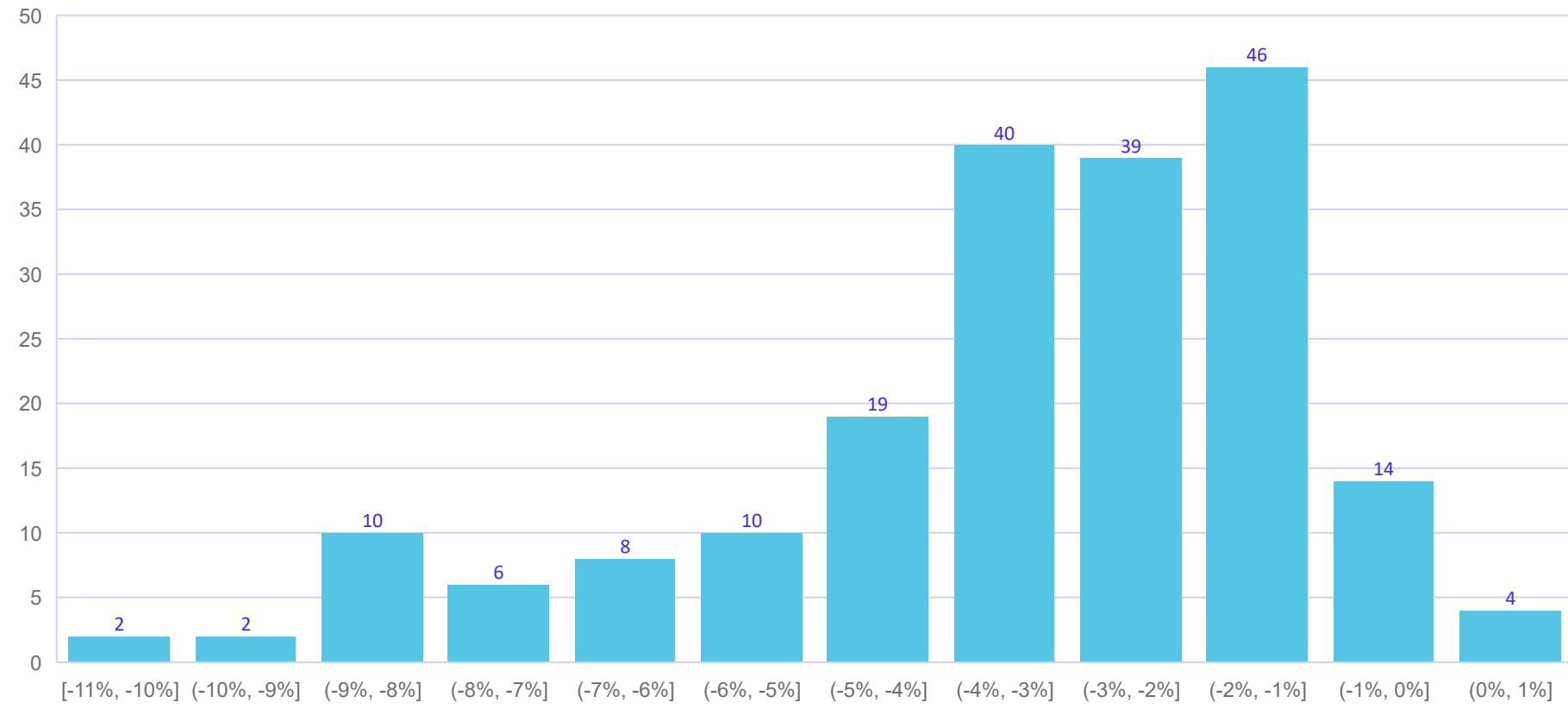


Data Source: Morningstar Direct

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# ▶ Rolling Returns Underperformance (3 years)

## 3 Year Rolling - Average Underperformance (Mid-Cap Growth)

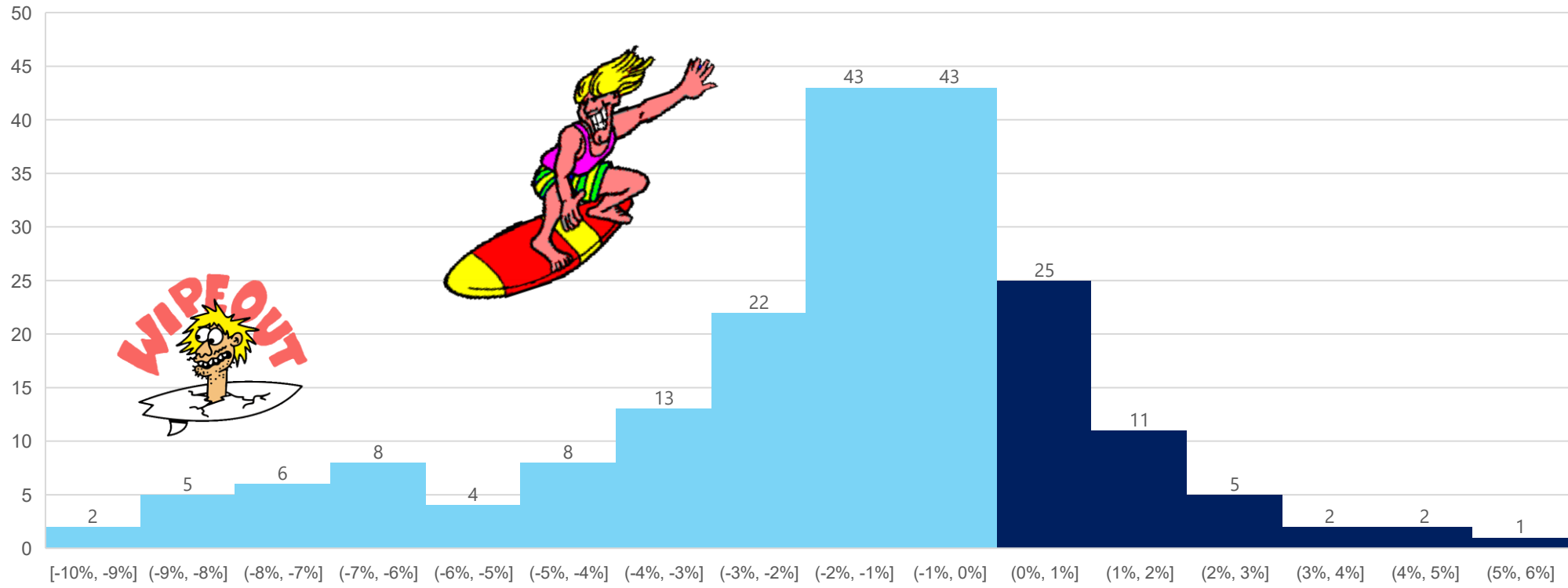


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# Expected Returns Rolling Periods (3 years)

## 3 Year Rolling - Expected Return (Mid-Cap Growth)



Data Source: Morningstar Direct

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- ➔ Review returns over 10+ year period
- ➔ Review number of years funds outperformed benchmark and convert to percentages
- ➔ Scoring system for funds

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## ➤ The Question

**To be passive or not to be passive...that is the question!**

**Or maybe both!**



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## ➤ One Final Thought...

A client asks his adviser, "where should I invest my money?"

The Advisor says, "'Put it on booze. Where else you gonna get 40%?"



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# Thank You!

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# Avantax

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