ProSolution
PRIVATE CLIENTS

This is an addendum to the following blog about passive investment managements – click here.

There has been lots of research that has demonstrated that passive investment returns are higher than active over the long term. Here are just a few:

- Industry expert Robert Arnott, founder of US-based firm Research Affiliates, spent two decades studying the top 200 active US fund managers that have at least $100 million under management. He concluded that from 1984 to 1998, a full 15 years, only eight out of 200 fund managers beat the Vanguard 500 Index. **That is, 96% of active fund managers failed to beat the market over this 15 year period.**

- The median Australian active manager return (after fees) for the 5 years to 2006 was 13.7%. The ASX300 index's return for the same period was 15.9%. That said, the 5 years to 2006 was a very strong bull market. Theoretically, active managers skills should be more obvious in a falling market because let's face it, anyone can make money in a rising market. Let's look at the year ended 30 June 2008. The median active fund manager lost 14.05% in the year to 30 June 2008 compared to the ASX200 which lost 13.75% over the same period according to Mercer (after adjusting for fees per Morningstar).

- Summary of other studies: Sharpe (1991) suggests that the active management will result in more frequent trading and higher research costs than passive management. Milkiel (1996) notes that 70% of all active equity managers underperform the returns of the S&P 500 Index. Bogle (1995) and Gruber (1996) find similar results. Weimers (2000) finds that equity mutual funds outperform the market index, but once expenses and transaction costs are taken into account they are equivalent in performance. Bogle (2000) finds index funds outperform the average equity mutual fund because of the lower management and brokerage costs, sales charges, and tax advantages associated with the index funds. Arnott, Berkin, and Ye (2000) find that the Vanguard 500 Index Fund outperforms the average equity fund. Fortin and Michelson (2002) find that on average index funds outperform actively managed mutual funds for most equity and all bond funds.

> *"The goal of the nonprofessional should not be to pick winners – neither he nor his "helpers" can do that – but should rather be to own a cross section of businesses that in aggregate are bound to do well. A low-cost S&P 500 index fund will achieve this goal."*
> **Warren Buffett – 2013 letter to shareholders**

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