RIAs hedge market risk with actively managed funds

Advisers worry that, as the bull market gets long in the tooth, passive funds may falter

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By **Jeff Benjamin**

As the stock market closes in on a solid 22% gain for the year, marking a near-300% gain from the **2009 low point**, a growing chorus of financial advisers are citing actively managed strategies as a reasonable hedge at this **point in the market cycle**.

An InvestmentNews survey of more than 300 registered investment advisers found that nearly 71% believe active management will outperform passive strategies in 2018.

"It's almost intoxicating as the market climbs higher and higher every day, but what non-professionals don't know may well be their Achilles heel," said Rose Swanger, president of Advise Finance.

"As more people withdrew their investments (during the extended bull market) from active fund management for passive index funds for lower fees and other attributes, they forgot the fundamental weakness of the index fund; that it passively follows the market," she added.

While passively following the market for much of the past nine years would have been a great strategy, some financial advisers are playing the odds that **the good times can't last forever,** and down markets generally favor actively managed strategies.

"I would like to bet [The **Vanguard Group** founder and retired chief executive] John Bogle $1 million that over the next five years active management handily beats passive, and with less risk," said Paul Schatz, president of Heritage Capital.

"I think the cycle for passive is in its final stage and those who flooded into passive strategies will be sorely disappointed," he added.

Mr. Bogle could not be reached for comment.

This year through Wednesday, the **S&P 500 Index** trails the actively managed large-cap growth fund category by six percentage points, according to Morningstar.

"I've always been a believer in active management, and I tell people that have drunk the Kool-Aid of passive management that they don't need a financial planner," said Kashif Ahmed, president of American Private Wealth.

"I don't ever believe in plain-vanilla indexing," he added. "But right now, we're at a point in the market where there needs to be a human being allocating to things that are not so stretched."

Such attitudes of caution are showing up despite a relative absence of calls of doom and gloom from market forecasters.

John Lynch, chief investment strategist at **LPL Financial**, said the S&P 500 is "well positioned to generate strong earnings" in 2018, which he attributes to stronger global growth and lower corporate tax rates.

Mr. Lynch predicts that the benchmark S&P 500 will gain between 8% and 10% in 2018.

Tim Holsworth, president of AHP Financial Services, is among those advisers still not convinced active management is where to be at this point.

"We are taking the attitude of 'show me active is better' before changing much of what we're doing," he said. "The changes we will make going forward will be focusing on allocation, which means staying within the respective risk tolerance of each portfolio."