LONSDALE
Wealth Management

# Passive v active investing

What is the difference between investing in an Active or a Tracker Fund?

## Active Investing

The aim of an actively managed fund is to beat the return from a particular market index or benchmark.

Fund Managers who use an active investment approach aim to either outperform the market by beating a selected index (such as the FTSE 100), outperform their peer group or achieve a specific investment objective.

They seek to do this by using their knowledge and skill to analyse the market. Then they buy shares which they believe are presently undervalued and so have potential to increase in price - or pay dividends over time.

## Passive Investing

Passive investment management is the opposite of active management and will track or closely follow the performance of a particular market index or benchmark such as the FTSE 100.

That is why passive investments are often called Index Funds or Tracker Funds. These have a simple, precise objective; to match a specific index, rather than try to beat it.

*Because you deserve independent advice and support*

| | Active Management | Passive Management |
|---|---|---|
| Approach | **Aims to outperform the market**<br>An active manager selects some shares and other assets in preference to others. | **Tracks a specific index**<br>A passive fund reflects the market or a market sector as a whole, and so does not depend on a manager making the right decisions. |
| Techniques | **Stock-picking**<br>Active managers analyse the market in order to identify and purchase investments that are undervalued (and to sell investments that become overvalued). | **The replication approach**<br>A very straightforward way to match an index. A manager buys the same shares and in the same proportions as they are weighted in the index.<br>**The sampling approach**<br>Useful when the index is very large or complex. Here, a manager uses mathematical models to buy a range of securities that reflect the index in the key risk factors. |
| Key Benefits | **In-depth research and potential for out performance**<br>Using skill to find hidden value and exceptional future growth prospects. | **Diversification**<br>Spreading investments across an entire index.<br>**Low costs**<br>Low research costs and low transaction costs. |
| Key Risks | **May be more expensive**<br>Active management costs tend to be higher which will affect the total returns of the Fund.<br>**May underperform the benchmark**<br>Although it aims to beat the benchmark, this is not guaranteed. | **Total market risk**<br>Your investment reflects the index the fund tracks, so if the market falls so does your fund.<br>**Performance constraints**<br>Index funds are designed to provide returns that closely track their benchmark index, rather than seek outperformance. |

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