PORTFOLIO CONSTRUCTION

Active and Passive Investing — The Long-Run Evidence

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How have active managers performed over the past 20 years?

Active managers have faced challenging years of late. However, our studies show that the long-run evidence on collective active manager performance from several databases appears surprisingly good. Positive average alphas for delegated active managers may reflect true outperformance over 20 years (earned from other active investors), or reporting biases that overstate performance, or some mixture of both.

Are certain investor types, market contexts, or time periods more conducive to good active manager performance?

Further analysis reveals that active management has paid off especially well for large institutional investors; outside the U.S. and more generally in "dusty corners" of financial markets; and at times when common out-of-benchmark tilts fared well. The last point may explain why U.S. equity managers have lagged their benchmarks in the past decade, while many active fixed income managers have outperformed.

Other questions

We also briefly discuss some market implications of the growing shift toward passive. To date, we find only limited measurable impact on market behavior. A companion paper turns to other questions on active versus passive investing, such as the market share between active and passive and the fuzzy boundary between them, as well as implications of the arithmetic of active management.