



## Active/Passive Portfolios

**Ibbotson Associates**

Active or passive? It's a long-running debate in the investment industry. We believe that combining these styles of investing can help to deliver the best of both worlds.

To leverage the strengths of each, we offer a set of portfolios pairing actively managed mutual funds with low-cost, tax-efficient index funds and/or exchange-traded funds (ETFs).



# Understanding the Active/Passive Approach

Traditionally, many approaches to blending active and passive investing used inflexible, fixed ratios or other simple methods. At Ibbotson, we leverage our 30 years of asset allocation expertise and industry-leading research to build a sophisticated framework for combining the best of both styles.

## **Actively Managed Fund Investing**

In this approach to investing, mutual fund managers attempt to achieve higher-than-market returns using a number of techniques including picking individual stocks, rotating among sectors and focusing on particular styles, among others.

At Ibbotson, we use our proprietary methodology to identify promising active managers, analyzing how often a given fund is able to outpace its benchmark. Because we're focused on maintaining a consistent asset allocation within each portfolio we offer, we carefully monitor how closely a fund tracks to its stated goal. Before deciding on an actively managed fund for our portfolios, we'll closely review its expenses, making sure that it charges a reasonable fee for the return it generates.

## **Passively Managed Investing**

The primary goal of passive investing using exchange-traded funds (ETFs) and/or index funds is to achieve performance close to that of a given benchmark at a very low fee. ETFs seek to replicate the overall performance of an index by holding the same security set as a specific

index. However, because ETFs and index funds don't require the same level of security research and analysis as an actively managed mutual fund, they can be very cost-effective investments. Both tend to buy and hold securities longer than actively managed mutual funds do, resulting in lower portfolio turnover and more favorable tax consequences.

## **Combining Active and Passive Approaches**

We seek to use active management where we think it will add the most value, taking into account a portfolio's established risk level while minimizing its expenses. Some asset classes, such as large and small-cap equities, typically offer a talented manager the opportunity to outperform the market. When we invest in those areas, we're likely to select an actively managed fund. However, in asset classes that benefit less from the insights of active managers—such as government bonds—we'll often rely on passively managed investments, granting exposure to those areas at a very low cost.

We carefully monitor the overall risk level of a portfolio when combining active and passive strategies. As a result, those that are more conservative or sensitive to risk have a larger allocation to passively managed investments. In contrast, portfolios relying on higher levels of risk to generate return are often more heavily invested in actively managed funds.

## Building Effective Portfolios

To create each of our offerings, we follow an established portfolio construction process.

- ▶ *Allocate*—We first decide how best to allocate a portfolio among 14 asset classes to ensure that it's diversified and effective. Our methodology considers a portfolio's desired level of risk in order to identify the appropriate strategic mix of stocks, bonds, and other asset classes.
- ▶ *Implement*—Once we've established an asset allocation strategy, we seek the best investments to put our plan into place. We begin with an in-depth quantitative and qualitative assessment of each investment we're considering for a portfolio. Through this research, we identify the combination of passive and active funds that best fulfills each portfolio's target asset allocation.
- ▶ *Optimize*—When a preferred group of passive and active investments is in place, we attempt to maximize the value of a portfolio. As part of this process, we revisit the target asset allocation and investment selection to help minimize the risk of having returns stray from the targets we've established. This helps us ensure that each portfolio offers a stable asset allocation to help meet your investing needs—year in and year out.

## Active/Passive Portfolios



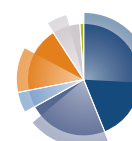
Active/Passive  
20 / 80



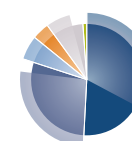
Active/Passive  
40 / 60



Active/Passive  
60 / 40



Active/Passive  
80 / 20



Active/Passive  
95 / 5

	%	A	P	%	A	P	%	A	P	%	A	P	%	A	P
● <b>U.S. Stocks</b>	13	7	6	24	14	10	35	18	17	44	26	18	51	33	18
● <b>International Stocks</b>	5	5	—	10	8	2	16	14	2	23	20	3	29	26	3
● <b>Real Estate REITs</b>	—	—	—	2	—	2	3	—	3	5	5	—	6	6	—
● <b>Bonds</b>	71	29	42	56	25	31	37	20	17	19	11	8	4	4	—
● <b>Alternatives</b>	2	—	2	4	2	2	6	4	2	8	5	3	9	6	3
● <b>Short-Term Reserves</b>	9	—	9	4	—	4	3	—	3	1	—	1	1	—	1
<b>Total</b> Active / Passive	<b>100</b>	<b>41</b>	<b>59</b>	<b>100</b>	<b>49</b>	<b>51</b>	<b>100</b>	<b>56</b>	<b>44</b>	<b>100</b>	<b>67</b>	<b>33</b>	<b>100</b>	<b>75</b>	<b>25</b>

Please note that for illustration purposes, we have grouped the sub-asset allocations together, showing only the six broad asset classes in the portfolios above.

All investments involve risk, including loss of principal. Past performance is no guarantee of future results. ETFs carry certain risks that may adversely affect their net asset value, market price, and/or performance. Because ETFs are not actively managed, their value may be affected by a general decline in the U.S. market segments relating to their underlying indexes. ETFs are traded on national exchanges and therefore are subject to similar investment risks as common stocks.

Diversification does not assure a profit or protect against a loss in a declining market.



*SelectOne*

The Right Choice

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### Working With You

Your financial advisor knows your financial situation, and understands that your needs will change over time. We encourage you to meet with your advisor regularly to ensure that your portfolio continues to reflect your goals and needs. Your advisor will review the recommended solutions to meet your investment and protection needs to help maximize your portfolio's economic value over your lifetime.

Ibbotson helps you and your advisor meet your long-term goals with a series of diversified portfolios based on Morningstar's independent, objective research. Once your plan is in place, we continuously monitor your portfolio as market conditions change, making sure that it remains aligned with your risk and return objectives.