

Opinion

Seven Myths of Asset Management

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The professionalisation of institutional investment has led to the emergence of an entire ‘consulting industry’ over recent years, which itself has introduced certain asset management practices into the marketplace. Are they examples of ‘best practices’ or simply myths?

Myth no. 1: Benchmarking the implementation of the investment strategy is pivotal

Using benchmarks to ensure that the investment implementation is closely monitored is an important part of monitoring, especially when it comes to ensuring that deviations – be they positive or negative – are plausible and understood. An asset manager who consistently underperforms according to the benchmark index for implementing the specified strategy will inevitably be replaced.

However, periodic strategic reviews should actually take precedence over implementation monitoring. As with asset managers, it is essential to distinguish good consultants from their less effective colleagues. The following example clearly illustrates that choosing the right strategy is more important than perfectly implementing a suboptimal one.

Two pension funds with identical risk capacity adopted a new strategy in 2004 and have left it unchanged

over the years. While the Traditional Pension Fund shuns alternative investments, the Progressive Fund has allocated 15% of its portfolio to them. The Progressive Pension Fund incurs significantly higher implementation costs of 0.6% due to the alternative investments, while the Traditional Pension Fund remains at a lower level of 0.15%.¹

After more than twenty years, the controller is pleased to note in his analysis that, after costs, the Progressive Pension Fund has outperformed the market by 0.1 percentage points p.a.; the Board of Trustees celebrates the result. The mood at the Traditional Pension Fund is quite different and there are complaints of an annual underperformance of 0.1 percentage points. But this muted response is unjustified, as the Traditional Pension Fund has in fact pursued a superior strategy, which more than compensates for the suboptimal implementation!

Asset classes	PK progressive	PK traditional
Liquidity	0%	0%
Bonds CHF	35%	35%
Total nominal values	35%	35%
Equities	35%	45%
Equities Switzerland	12%	15%
Foreign Equities	23%	30%
Real Estate Switzerland (2/3 directly, 1/3 indirectly)	15%	20%
Alternative Investments	15%	0%
Raw materials	5%	0%
Hedge funds	5%	0%
Private equity	5%	0%
Total real assets	65%	65%
Total	100%	100%

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Key figures	PK progressive	PK traditional
Volatility of the strategy p.a.	6,76%	6,72%
Return of the strategy p.a.	4,47%	4,87%
Outperformance/underperformance p.a.	0,10%	-0,10%
Portfolio net returns p.a.	4,57%	4,77%

Excluding inflows and outflows, the original assets of CHF 100 million in the Progressive Pension Fund have grown to just under CHF 256 million, while the Traditional Pension Fund has increased by CHF 16 million or

6%. It is better to choose the right route than to navigate the wrong one perfectly! Interestingly, however, institutional investors rarely apply the same rigour to strategic reviews as they do to monitoring implementation.

Myth no. 2: Passive investing reduces the cost of asset management

It is a fact that asset management costs for traditional investments have fallen in recent years. Another fact is that the average costs of 'indexed' investments are lower than those for actively managed mandates. Over the past decade, the share of these more favourable index investments in the total assets held by Swiss pension funds has increased from 22% to 31%.²

It seems logical, therefore, that pension funds should have experienced a decrease in their overall asset management costs as well. But the situation on the ground is actually rather mixed: While a study by the consulting firm c-alm reports a reduction in costs – from 0.56% in 2011 to 0.48% in 2019 – PPCmetrics, another consultancy, finds that asset management costs remained unchanged between 2014 and 2023.³ Interestingly, the

latter found no correlation between asset management costs and fund size across a total asset range of CHF 5 million to CHF 40 billion. These findings are also confirmed by the latest figures.⁴

So what are the reasons? Paradoxically, the indexing of core holdings such as equities and bonds has led many institutional investors to add more active – and often very costly – satellite investments such as infrastructure, commodities, hedge funds and private equity. This has effectively offset the cost savings achieved in core holdings. On average, asset management costs amount to 0.66% for strategies including alternative investments, and 0.31% for those without.⁵ It follows, therefore, that cost reductions stem not from indexing but from foregoing alternative investments.

Myth no. 3: Passive investing reduces the risks

It is true that indexed investing reduces the relative risk. This means that the investment outcome is almost identical to the return of the chosen benchmark. Undoubtedly this is convenient for everyone involved, as 'the market' is responsible for the outcome and no one has to make decisions that might lead to exposure. But the absolute risk – potential asset fluctuations or even losses – can only be managed with active decisions on the selected strategy, benchmark and portfolio structure.

One example: An investor who decides to track equities passively must adhere to the capitalisation

weights of a global stock index. This means that Switzerland would have a weighting of around 2% and the United States over 70%. The latter was still around 50% just a few years ago.

The somewhat higher risk associated with indexed investment solutions arises from their inherently procyclical nature. This may produce concentration risks: Sectors such as technology at the end of the 1990s and today, or countries such as Japan in the late 1980s and the USA today, can take on weightings that contradict the principles of diversification.

The same applies to bonds. The average maturity of

the Swiss Bond Index has increased by 40% since 2009 as a result of low interest rates. Passive investors have

therefore accepted the issuers' maturity decisions – and with them, a higher level of interest rate risk.

Myth no. 4: Additional asset classes improve diversification

The number of asset classes has increased sharply since the turn of the millennium. Still reeling from the painful experiences of the dotcom bubble and the financial crisis, investors were primarily seeking more 'stable' investments. At the same time, providers were forced to develop new offerings in response to shrinking margins in traditional investments. The marketing claim is that alternative investments such as private equity, infrastructure, hedge funds or commodities, in particular, enhance diversification, as they represent 'alternative risk premia' with differing cycles.

An analysis based on the allocations of the average Swiss pension fund⁶ is as enlightening as it is sobering. When the 10% allocation to alternative investments is reassigned to CHF bonds and Swiss equities, twenty years of data show that the resulting return and risk are virtually identical to those of a portfolio including

alternative investments. It becomes clear that variants without alternative investments are more efficient (see table below).

In illiquid assets such as private equity or directly held real estate, the fluctuations merely appear lower because there are no continuously observable market prices. The risks of economic loss are therefore not smaller; most alternative investments are subject to the same economic cycles. Traditional, liquid, transparent and therefore more favourable asset classes can be used to build more efficient portfolios in the long term.

Although a certain degree of diversification is required, it is not expedient to 'blindly' embrace every conceivable asset class. What matters most is that the asset classes included show a return track record supported by publicly available data.

Reflection over twenty years	<i>Allocation of the average pension fund with alternative investments</i>	<i>Allocation without alternative investments same return</i>	<i>Allocation without alternative investments same risk</i>
Number of asset classes	12,0	6,0	6,0
Yield p.a. (in %)	4,5	4,5	4,8
Volatility p.a. (in %)	6,1	5,7	6,1
Worst month (in %)	-8,2	-7,0	-7,1
Best month (in %)	5,8	4,5	4,9

Myth no. 5: Balanced mandates are no longer 'state of the art'

Asset class mandates – that is, individual mandates for Swiss equities, global equities and CHF bonds – are often awarded on the grounds that this allows a specialist to be appointed for each asset class. In practice, however, balanced mandates – where the mixed mandate covers all the asset classes included in the investment strategy – continue to play an important role for pension funds with total assets of up to CHF 1 billion.⁷

There are good reasons for this significance, as mixed mandates offer numerous advantages:

- When working with mixed mandates, all asset managers within a pension foundation implement the same strategy, making them directly comparable.
- Because the total volume in mixed mandates is spread over fewer mandates than in asset class mandates, they tend to be larger and thus generate a significant cost advantage thanks to the degressive fee structure.

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- Moreover, the smaller number of mixed mandates compared with asset class mandates results in lower costs for manager searches and controlling. Only a cynic would draw the opposite conclusion: the preference for asset class mandates might also be due to the opportunities for consultants to earn additional income.
- Asset managers also enjoy greater flexibility through the ability to control cash weightings.

Moreover, mixed mandates can be used for live benchmarking in very large pension foundations that primarily hold asset class mandates: Is the sum of the specialised asset class mandates actually more effective than implementing the strategy through a mixed mandate?

Size of the pension fund	Proportion of mixed mandates in total assets
< 50 million CHF	24%
50 to 100 million CHF	52%
100 to 500 million CHF	42%
500 to 1000 million CHF	34%
1 to 5 billion CHF	17%
> 5 billion CHF	5%

Myth no. 6: The use of investment consultants leads to better investment results

Investment consultants assist pension funds, foundations and companies in choosing their strategy, style (active or indexed investing) and implementation – particularly in selecting asset managers. 73% of pension funds use strategy consultants.⁸ Investment consultants standardise processes, thereby eliminating the most extreme outliers. This helps to prevent disastrous outcomes caused by poor strategies, implementation approaches or asset managers. However, this also comes at the cost of preventing the best results.

From the consultant's perspective, it is rational to 'centre' investment results as a way of safeguarding their reputation. Ultimately, consultants tend to favour a more passive investment style: they may miss opportunities, but will also prevent any disasters. A presentation by the consulting firm PPCmetrics on five-year returns achieved by managers of Swiss equity mandates reveals some interesting insights.⁹

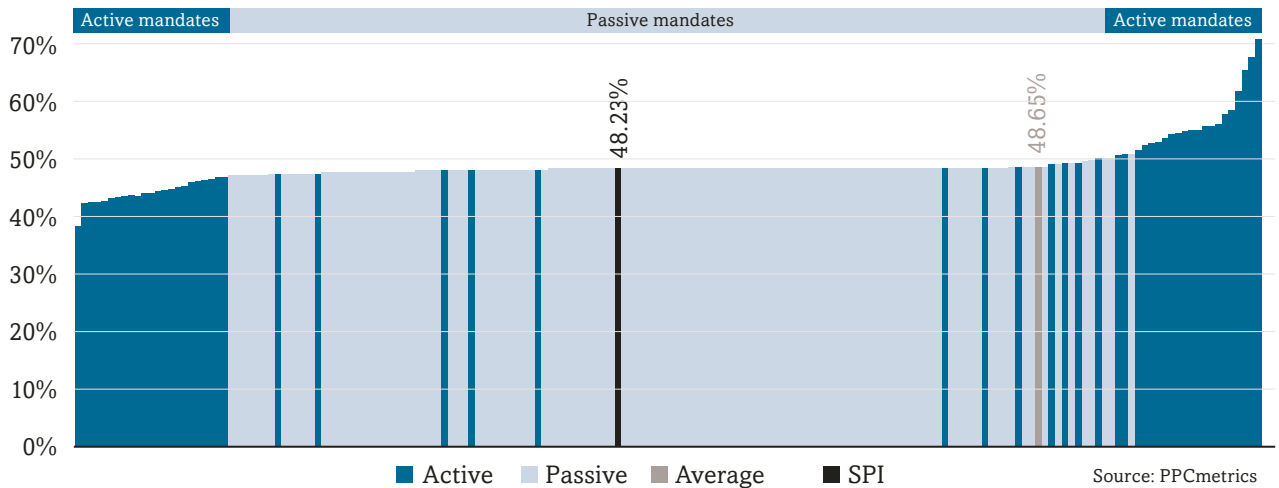
It turns out that active mandates produce both the worst and the best outcomes, while passive mandates cluster around the middle – mirroring the consultants' own preferences.

An investment committee or investor who recognises consultants' tendency to aim for the centre – yet is reluctant to forgo excellent investment solutions and asset managers – must engage actively in the tendering (manager search) and selection process, and clearly define their objectives. For example, it is hardly helpful when tender questionnaires ask about the number of office locations but fail to enquire about paid searches or ongoing legal proceedings. In addition, face-to-face interviews and obtaining references are very time-consuming, but indispensable in the quest for excellence. Merely completing standardised questionnaires is not enough if you want more than just the run-of-the-mill.

The consultancy industry – whether in finance or other sectors – inevitably maintains a certain level of complexity, even when simplification would be possible. After all, complexity creates dependency and dependency translates into future revenues. With this in mind, an investment committee or investor should always prefer simple solutions – thus saving money in the long term and improving investment results.

PPCmetrics Peer Group: Cumulative absolute return

Measurement period: 01/01/2019–12/31/2023



Myth no. 7: Active managers are traders – back and forth empties pockets

There is little doubt that a fair proportion of active managers massively overestimate their own forecasting skills. This often results in excessively active behaviour. Trading in this way inevitably drives up costs, but far less reliably delivers successful returns. The well-documented conclusion is that most active managers fail to add value.¹⁰ Back-and-forth trading empties pockets – a real problem when asset managers or banks earn revenue from trading turnover, as this creates clear disincentives. And the second issue that arises in practice is procyclicality: chasing after the trend empties your pockets as well.

However, if active management is understood as risk management and counter-cyclical control, it can indeed add value over the long term. But if active management is perceived as risk management and countercyclical control, it can definitely yield added value in the long term. Ultimately, it is about making active decisions concerning the portfolio structure: What bond duration is acceptable, what is the maximum proportion of sectors or countries, and are there any weighting limits at the security level? This helps to avoid excessive trading, concentration risks and overly procyclical portfolio developments.

The fact that excessive changes generate unnecessary costs at the stock selection level applies equally to the selection of asset managers. Investors must therefore state unequivocally which characteristics an active manager should possess. Once they have made their selection

carefully and with conviction, they must also allow the manager sufficient time. A two-year period, for example, is too short for a performance assessment. Without exercising the necessary patience, the selection of an asset manager can easily lead to short-sighted actions that incur unnecessary costs. Or to paraphrase Benjamin Graham: “Patience is the investor’s greatest virtue”.

Sources and further reading

- ¹ Data basis according to Thomas Hauser, “Core-Satellite-Ansatz als Rohrkrepierer”, Schweizer Personalvorsorge, May 2024.
- ² Swisscanto, “Pensionskassen Studie”, 2023, p. 39
- ³ c-alm, “Vermögensverwaltungskosten in der 2. Säule”, 2019, p. 15; PPCmetrics, “Sinken Vermögensverwaltungskosten in Zukunft weiter oder ist die Talsohle erreicht?”, May 2024, p. 11
- ⁴ PPCmetrics, Pensionskassen-Jahrbuch, 2025, p. 31
- ⁵ For an allocation according to the UBS Pension Fund Index; refer to Thomas Hauser, “Core-Satellite-Ansatz als Rohrkrepierer”, Schweizer Personalvorsorge, May 2024
- ⁶ Thomas Hauser, “Core-Satellite-Ansatz als Rohrkrepierer”, Schweizer Personalvorsorge, May 2024
- ⁷ Swisscanto, Pensionskassenstudie 2025, p. 42
- ⁸ Swisscanto, Pensionskassenstudie 2025, p. 30
- ⁹ Dr Hansruedi Scherer, Lukas Riesen und Shakitthiyam Vettimayilnathan, “Umsetzung Ak-tien: Wo lohnt sich aktives Management?”, presentation, 3 October 2024
- ¹⁰ Cf., for example, Busse Jeffery A. et al: Performance and persistence in institutional investment management, The Journal of Finance, Vol. LXV, No. 2, p. 765-790, 2010; or Goyal Amit und Sunil Wahal.: The selection and termination of investment management firms by plan sponsors, The Journal of Finance, Vol. LXIII, No. 4, p. 1805- 1847, 2008